

2018 Annual Report – Fédération des caisses Desjardins du Québec

# Here





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### DESJARDINS GROUP ANNUAL REPORT

Visit the website at [desjardins.com/annualreport](https://desjardins.com/annualreport)  
to view the Desjardins Group annual report online.

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This annual report was produced by the Human Resources and Communications Executive Division of Desjardins Group (Corporate Communications Division) and the Finance, Treasury and Administration Executive Division of Desjardins Group (Finance Division).

# Message from management

## Doing what's best for our members and clients: Always the right choice

Our entire cooperative financial group is committed to doing what's best for our members and clients, and that's a game changer. We're updating our management and business practices so members and clients get the advice, products and services they need to achieve optimal financial health.

We're building a stronger member/client culture, and it shows in our Desjardins Group and Federation financial results.

And more and more, we're working as one big nationwide team. We've successfully brought our State Farm agents into the Desjardins fold, and thanks to them and everyone in the Ontario caisses, in our business sectors and support functions and at Aviso Wealth, Desjardins is now a major player in the Canadian financial services industry.

In 2018, the Federation posted surplus earnings before caisse dividends of \$1,350 million, down \$66 million compared to 2017. If we exclude gains posted in the last 2 years, our 2018 surplus earnings are up \$54 million, or 4.6%, over 2017. In 2017, we realized a \$249 million gain net of expenses and taxes on the sale of subsidiaries Western Financial Group Inc. and Western Life Assurance Company, and in 2018, we realized a \$129 million gain net of taxes when we co-created Aviso Wealth.

Last year, we posted an operating income of \$14,129 million, up \$832 million, or 6.3%, compared to 2017. This increase was due largely to growth in both life and health insurance and property and casualty insurance, along with the reinsurance treaty we signed when we acquired State Farm's Canadian operations.

As at December 31, 2018, the Federation's total assets stood at \$157.6 billion, an increase of \$11.8 billion, or 8.1%, from the previous year. This growth was largely due to the increase in securities, including securities borrowed or purchased under reverse purchase agreements as well as net loans and acceptances.

## Performance benefiting members, clients and communities

Thanks to this strong performance, we're investing more in talent acquisition, employee training, service upgrades and our digital shift. These things, together with our excellent capital position, will help us better serve our members and clients.

All across Canada, we're also doing more to support entrepreneurs and community initiatives. We're doing it through our Desjardins Business centres, Desjardins Capital Management Inc., our Créavenir and Desjardins Microcredit to Businesses programs, and our \$100 million fund.

We're also doing it through new initiatives like the Momentum Fund, which provides financial assistance to grow local businesses and create and keep good local jobs.

## Modern, people-focused democratic governance

In today's increasingly complex world, we're bombarded with information on all sides. That's why we're updating the role of director. All our boards of directors now have enhanced group profiles, and directors must complete mandatory training to ensure boards have the requisite skills to fully grasp the challenges they face. These changes will also help us carry out initiatives that are meaningful for our members, clients and communities.



**Guy Cormier**  
President and CEO of Desjardins Group



**Denis Berthiaume**  
Senior Executive Vice-President and Chief  
Operating Officer of Desjardins Group

Finally, we'd like to thank all our employees and elected officers. Your hard work and commitment to doing what's best for our members and clients is really paying off.

Together in 2019, we'll continue to build a strong member/client culture, showcase our cooperative difference and harness the full potential of our cooperative group.

A stylized handwritten signature in black ink, featuring a large loop and a horizontal line extending to the right.

**Guy Cormier**  
President and CEO of Desjardins Group

A handwritten signature in black ink, with the first name 'Denis' clearly legible and a long, sweeping horizontal line at the end.

**Denis Berthiaume**  
Senior Executive Vice-President and  
Chief Operating Officer of Desjardins  
Group

# Strong and distinctive mission, vision and values

## DESJARDINS GROUP'S MISSION

To contribute to improving the economic and social well-being of people and communities within the compatible limits of our field of activity:

- By continually developing an integrated cooperative network of secure and profitable financial services, owned and administered by our members, as well as a network of complementary financial organizations with competitive returns, controlled by our members;
- By educating people, starting with our members, officers and employees, about democracy, economics, solidarity, and individual and collective responsibility.

## VISION

To leverage our position as Canada's leading cooperative financial group to inspire confidence around the world through the commitment of our people, our financial strength and our contribution to sustainable prosperity.

## VALUES

- Money at the service of human development
- Personal commitment
- Democratic action
- Integrity and rigour in the cooperative enterprise
- Solidarity with the community
- Intercooperation

# Fédération des caisses Desjardins du Québec Management's Discussion and Analysis

The *Fédération des caisses Desjardins du Québec* (the Federation) is a cooperative entity of Desjardins Group (hereinafter also referred to as Desjardins). Desjardins Group comprises the Desjardins caisses network in Quebec and Ontario (the caisses), the Federation and its subsidiaries, the *Fédération des caisses populaires de l'Ontario Inc.* and the *Fonds de sécurité Desjardins*.

The role of the Federation is presented in the section "Profile and structure".

The Management's Discussion and Analysis (MD&A) dated February 27, 2019, presents the analysis of the results of and main changes to the Federation's balance sheet for the year ended December 31, 2018, in comparison to previous fiscal years. The Federation reports financial information in compliance with *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings* prescribed by the Canadian Securities Administrators (CSA). Information on the Federation's controls and procedures is presented in the "Additional information" section of this MD&A.

The MD&A should be read in conjunction with the Consolidated Financial Statements, including the Notes thereto, as at December 31, 2018.

Additional information about the Federation is available on the SEDAR website at [www.sedar.com](http://www.sedar.com) (under the *Fédération des caisses Desjardins du Québec* profile), where its Annual Information Form can also be found. More information is available on the Desjardins website at [www.desjardins.com/ca/about-us/investor-relations](http://www.desjardins.com/ca/about-us/investor-relations). None of the information presented on these sites is incorporated by reference into this MD&A.

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## CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

The Federation's public communications often include oral or written forward-looking statements, within the meaning of applicable securities legislation. Such forward-looking statements are contained in this MD&A and may be incorporated in other filings with Canadian regulators or in any other communications. Forward-looking statements include, but are not limited to, comments about the Federation's objectives regarding financial performance, priorities, operations, the review of economic conditions and markets, as well as the outlook for the Canadian, U.S., European and other international economies. Such statements are typically identified by words or phrases such as "believe", "expect", "anticipate", "intend", "estimate", "plan" and "may", words and expressions of similar import, and future and conditional verbs.

By their very nature, such statements involve assumptions, uncertainties and inherent risks, both general and specific. It is therefore possible that, due to many factors, the assumptions made may be incorrect, or that the predictions, forecasts or other forward-looking statements as well as the Federation's objectives and priorities may not materialize or may prove to be inaccurate and that actual results differ materially.

A number of factors, many of which are beyond the Federation's control and the effects of which can be difficult to predict, could influence the accuracy of the forward-looking statements in this MD&A. These factors include those discussed in Section 4.0, "Risk management," such as credit, market, liquidity, operational, insurance, strategic and reputation risk. Additional factors include legal and regulatory risk, environmental and social risk, and the risk related to pension plans.

Additional factors that may affect the accuracy of the forward-looking statements in this MD&A also include factors related to cyber threats, technological advancement and regulatory developments, household indebtedness and real estate market trends, interest rate fluctuations and geopolitical uncertainty. Furthermore, there are factors related to general economic and business conditions in regions in which the Federation operates; monetary policies; the accuracy and completeness of information concerning clients and counterparties; the critical accounting estimates and accounting standards applied by the Federation; new products and services to maintain or increase the Federation's market share; geographic concentration; acquisitions and joint arrangements; credit ratings; and climate change. Additional information on these factors is found in Section 4.0, "Risk management" of this MD&A.

Other factors that could influence the accuracy of the forward-looking statements in this MD&A include amendments to tax laws, unexpected changes in consumer spending and saving habits, talent recruitment and retention for key positions, the ability to implement the Federation's disaster recovery plan within a reasonable time, the potential impact of international conflicts, and the Federation's ability to anticipate and properly manage the risks associated with these factors, despite a disciplined risk management environment.

It is important to note that the above list of factors that could influence future results is not exhaustive. Other factors could have an adverse effect on the Federation's results. Additional information about these and other factors is found in Section 4.0, "Risk management" of this MD&A.

Although the Federation believes that the expectations expressed in these forward-looking statements are reasonable, it cannot guarantee that these expectations will prove to be correct. The Federation cautions readers against placing undue reliance on forward-looking statements when making decisions, given that actual results, conditions, actions or future events could differ significantly from the targets, expectations, estimates or intentions advanced in them, explicitly or implicitly. Readers who rely on these statements must carefully consider these risk factors and other uncertainties and potential events.

The significant economic assumptions underlying the forward-looking statements in this MD&A are described in Section 1.4 "Economic environment and outlook" of this MD&A. These assumptions may also be updated in the quarterly MD&As, in the "Economic environment and outlook" section.

Any forward-looking statements contained in this MD&A represent the views of management only as at the date hereof, and are presented for the purpose of assisting readers in understanding and interpreting the Federation's balance sheet as at the dates indicated or its results for the periods then ended, as well as its strategic priorities and objectives. These statements may not be appropriate for other purposes. The Federation does not undertake to update any oral or written forward-looking statements that could be made from time to time by or on behalf of the Federation, except as required under applicable securities legislation.

## BASIS OF PRESENTATION OF FINANCIAL INFORMATION

The Consolidated Financial Statements have been prepared by the Federation's management in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec, which do not differ from IFRS. The Federation modified certain accounting policies following the adoption of IFRS 9, "Financial instruments", IFRS 15, "Revenue from contracts with customers", and amendments to IFRS 4, "Insurance contracts", on January 1, 2018. For more information about the accounting policies used as well as the accounting policy changes, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

This MD&A was prepared in accordance with the regulations in force on continuous disclosure obligations issued by the CSA. Unless otherwise indicated, all amounts are presented in Canadian dollars (\$) and are primarily from the Federation's Consolidated Financial Statements.

To assess its performance, the Federation uses IFRS measures and various non-IFRS financial measures. Non-IFRS financial measures, other than the regulatory ratios, do not have a standardized definition and are not directly comparable to similar measures used by other companies, and may not be directly comparable to any IFRS measures. Investors, among others, may find these non-IFRS measures useful in analyzing financial performance. They are defined as follows:

#### Average assets – Average loans and acceptances – Average deposits – Average equity

The average balance for these items is used to measure growth. It is equal to the average of the amounts presented in the Consolidated Financial Statements at the end of the previous five quarters, calculated starting from December 31.

#### Adjusted surplus earnings of the Federation before dividends to member caisses

The concept of adjusted surplus earnings is used to exclude specific items in order to present financial performance based on operating activities. These specific items, such as acquisitions and disposals, are unrelated to operations.

The Federation's surplus earnings before dividends to member caisses are adjusted to exclude the following specific items: the gain and expenses, net of income taxes, related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017, as well as the gain, net of income taxes, related to the transaction involving Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P., completed on April 1, 2018, as part of the creation of Aviso Wealth.

The following table presents a reconciliation of surplus earnings before dividends to member caisses as presented in the Consolidated Financial Statements and the adjusted surplus earnings as presented in the MD&A.

(in millions of dollars)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
Presentation of surplus earnings before dividends to member caisses in the Consolidated Financial Statements	\$ 1,350	\$ 1,416	\$ 1,191
<b>Specific items, net of income taxes</b>			
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company	-	(249)	-
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	(129)	-	-
<b>Presentation of the adjusted surplus earnings before dividends to member caisses</b>	<b>\$ 1,221</b>	<b>\$ 1,167</b>	<b>\$ 1,191</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been adjusted to conform to the current period's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

#### Adjusted net surplus earnings – Wealth Management and Life and Health Insurance segment

The net surplus earnings of the Wealth Management and Life and Health Insurance segment are adjusted to exclude the following specific item: the gain, net of income taxes, related to the transaction involving Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investment L.P., completed on April 1, 2018, as part of the creation of Aviso Wealth.

The following table presents a reconciliation of the net surplus earnings of the Wealth Management and Life and Health Insurance segment as presented in the Consolidated Financial Statements, and the adjusted net surplus earnings as presented in the MD&A.

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Presentation of the net surplus earnings of the Wealth Management and Life and Health Insurance segment in the Consolidated Financial Statements	\$ 894	\$ 612	\$ 461
<b>Specific item, net of income taxes</b>			
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	(129)	-	-
<b>Presentation of the adjusted net surplus earnings of the Wealth Management and Life and Health Insurance segment</b>	<b>\$ 765</b>	<b>\$ 612</b>	<b>\$ 461</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

## Adjusted net surplus earnings – Property and Casualty Insurance segment

The net surplus earnings of the Property and Casualty Insurance segment (P&C) are adjusted to exclude the following specific item: the gain and expenses, net of income taxes, related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.

The following table presents a reconciliation of the net surplus earnings of the Property and Casualty Insurance segment as presented in the Consolidated Financial Statements, and the adjusted net surplus earnings as presented in the MD&A.

(in millions of dollars)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
Presentation of the net surplus earnings of the Property and Casualty Insurance segment in the Consolidated Financial Statements	\$ 173	\$ 446	\$ 296
<b>Specific item, net of income taxes</b>			
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company <sup>(3)</sup>	-	(241)	-
<b>Presentation of the adjusted net surplus earnings of the Property and Casualty segment</b>	<b>\$ 173</b>	<b>\$ 205</b>	<b>\$ 296</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been adjusted to conform to the current period's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

<sup>(3)</sup> The difference with the data presented in the table for the adjusted surplus earnings of the Federation before dividends to member caisses is related to intersegment transaction expenses.

## Gross credit-impaired loans/gross loans and acceptances

The gross credit-impaired loans/gross loans and acceptances ratio is used to measure loan portfolio quality and is equal to gross credit-impaired loans expressed as a percentage of total gross loans and acceptances. Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

Table 29 of the Federation's MD&A provides more detailed information on this ratio.

## Loss ratio – Expense ratio – Combined ratio

These ratios are used to measure and analyze the performance of the Property and Casualty Insurance segment's operations.

The loss ratio is equal to incurred claims, net of reinsurance, expressed as a percentage of net premiums earned, excluding the market yield adjustment. Market yield adjustment is defined as the impact of changes in the discount rate on the provisions for claims and adjustment expenses, based on the change in the market-based yield of the underlying assets for these provisions.

The loss ratio is comprised of the following ratios:

- Current year loss ratio, which is the loss ratio excluding catastrophe and major event claims expenses for the current year as well as changes in prior year claims, net of related reinsurance, not including reinstatement premiums, as applicable.
- Loss ratio related to catastrophes and major events, which is the loss ratio including catastrophe and major event claims expenses for the current year, net of reinsurance and including the impact of reinstatement premiums, as applicable.
- Ratio of changes in prior year claims, which is the loss ratio including the effect of changes in prior year claims, net of related reinsurance, not including reinstatement premiums, as applicable.

The expense ratio is equal to operating expenses expressed as a percentage of net premiums earned.

The combined ratio is equal to the sum of the loss ratio and the expense ratio.

The following table presents the calculation of the loss ratio, the expense ratio and the combined ratio, as presented in the MD&A.

(in millions of dollars and as a percentage)	2018	2017	2016
Net premiums	\$ 4,402	\$ 3,896	\$ 3,207
Premiums excluded from the loss ratio <sup>(1)</sup>	-	(61)	(149)
<b>Net premiums considered in the ratio denominators</b>	<b>\$ 4,402</b>	<b>\$ 3,835</b>	<b>\$ 3,058</b>
Claims, benefits, annuities, and changes in insurance contract liabilities	\$ 3,209	\$ 2,555	\$ 1,838
Market yield adjustment (MYA)	45	62	39
Other items excluded from the loss ratio <sup>(1)</sup>	-	(20)	(36)
<b>Claims, benefits, annuities and changes in insurance contract liabilities excluding the MYA</b>	<b>\$ 3,254</b>	<b>\$ 2,597</b>	<b>\$ 1,841</b>
<b>Loss ratio</b>	<b>73.9%</b>	<b>67.7%</b>	<b>60.2%</b>
Non-interest expense	\$ 1,127	\$ 1,099	\$ 1,132
Other expenses excluded from the expense ratio <sup>(2)</sup>	(18)	(114)	(284)
<b>Operating expenses</b>	<b>\$ 1,109</b>	<b>\$ 985</b>	<b>\$ 848</b>
<b>Expense ratio</b>	<b>25.2%</b>	<b>25.7%</b>	<b>27.7%</b>
<b>Combined ratio</b>	<b>99.1%</b>	<b>93.4%</b>	<b>87.9%</b>

<sup>(1)</sup> Due mainly to the life insurance activities of Western Life Assurance Company, the sale of which was completed on July 1, 2017.

<sup>(2)</sup> For 2018: Due mainly to investment management fees and certain other expenses. For 2017 and 2016: Due mainly to the life insurance and insurance product distribution activities of Western Life Assurance Company and Western Financial Group Inc., including expenses related to the sale of these two entities on July 1, 2017.

## Return on equity and adjusted return on equity

Return on equity is used to measure profitability resulting in value creation for members and clients. Expressed as a percentage, it is equal to surplus earnings before dividends to member caisses, excluding the non-controlling interests' share, divided by average equity before non-controlling interests.

The following table presents the reconciliation of return on equity with surplus earnings before dividends to member caisses as presented in the MD&A.

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
Surplus earnings before dividends to member caisses	\$ 1,350	\$ 1,416	\$ 1,191
Non-controlling interests' share	(41)	(43)	(85)
<b>Group's share</b>	<b>\$ 1,309</b>	<b>\$ 1,373</b>	<b>\$ 1,106</b>
Average equity before non-controlling interests' share	\$ 15,210	\$ 14,584	\$ 13,033
<b>Return on equity</b>	<b>8.6%</b>	<b>9.4%</b>	<b>8.5%</b>
<b>Adjusted return on equity<sup>(3)</sup></b>	<b>7.9%</b>	<b>7.8%</b>	<b>8.5%</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been adjusted to conform to the current period's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

<sup>(3)</sup> Takes into account the specific items presented under "Adjusted surplus earnings of the Federation before dividends to member caisses" subsection in this section.

## Income

### Operating income

The concept of operating income is used to analyze financial results. This concept allows for better structuring of financial data and makes it easier to compare operating activities from one period to the next by excluding the volatility of results specific to investments, particularly regarding the extent of life and health insurance and P&C insurance operations, for which a very large proportion of investments are recognized at fair value through profit or loss. The analysis therefore breaks down the Federation's income into two parts, namely operating income and investment income, which make up total income. This measure is not directly comparable to similar measures used by other companies.

Operating income includes net interest income, generated mainly by the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category, net premiums and other operating income such as assessments, service agreements, lending fees and credit card service revenues, income from brokerage and investment fund services, management and custodial service fees, foreign exchange income as well as other income. These items, taken individually, correspond to those presented in the Consolidated Financial Statements.

### Investment income

Investment income comprises net investment income on securities classified and designated as being at fair value through profit or loss, net investment income on securities classified as being at fair value through other comprehensive income, and net investment income on securities measured at amortized cost and other investment income, which are included under "Net investment income" in the Consolidated Statements of Income. Investment income also includes the overlay approach adjustment for insurance operations financial assets. The life and health insurance and P&C insurance subsidiaries' matching activities, which include changes in fair value, gains and losses on disposals and interest and dividend income on securities, are presented with investment income given that these assets back insurance liabilities, which are recognized under expenses related to claims, benefits, annuities and changes in insurance contract liabilities in the Consolidated Financial Statements. In addition, this investment income includes changes in the fair value of investments for the Personal and Business Services segment, recognized at fair value through profit or loss. The presentation of 2017 investment income does not take into account the standards and amendments adopted on January 1, 2018 and is therefore compliant with IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

The following table shows the correspondence of total income between the MD&A and the Consolidated Financial Statements.

(in millions of dollars)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
<b>Presentation of income in the Consolidated Financial Statements</b>			
Net interest income	\$ 1,501	\$ 1,404	\$ 1,303
Net premiums	8,923	8,146	7,263
Other income			
Assessments	392	377	393
Service agreements	742	727	699
Lending fees and credit card service revenues	699	660	575
Brokerage and investment fund services	905	1,030	1,060
Management and custodial service fees	579	514	443
Net investment income <sup>(3)</sup>	170	1,767	1,108
Overlay approach adjustment for insurance operations financial assets	523	N/A	N/A
Foreign exchange income	92	77	70
Other	296	362	140
<b>Total income</b>	<b>\$ 14,822</b>	<b>\$ 15,064</b>	<b>\$ 13,054</b>
<b>Presentation of income in the MD&amp;A</b>			
Net interest income	\$ 1,501	\$ 1,404	\$ 1,303
Net premiums	8,923	8,146	7,263
Other operating income			
Assessments	392	377	393
Service agreements	742	727	699
Lending fees and credit card service revenues	699	660	575
Brokerage and investment fund services	905	1,030	1,060
Management and custodial service fees	579	514	443
Foreign exchange income	92	77	70
Other	296	362	140
<b>Operating income</b>	<b>14,129</b>	<b>13,297</b>	<b>11,946</b>
Investment income			
Net investment income <sup>(3)</sup>	170	1,767	1,108
Overlay approach adjustment for insurance operations financial assets	523	N/A	N/A
<b>Investment income</b>	<b>693</b>	<b>1,767</b>	<b>1,108</b>
<b>Total income</b>	<b>\$ 14,822</b>	<b>\$ 15,064</b>	<b>\$ 13,054</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been reclassified to conform to the current period's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

<sup>(3)</sup> The breakdown of this line item is presented in Note 24, "Net interest income and net investment income", to the Consolidated Financial Statements.

### Credit loss provisioning rate

The credit loss provisioning rate is used to measure loan portfolio quality, and is equal to the provision for credit losses divided by average gross loans and acceptances.

The following table presents the calculation of the credit loss provisioning rate as presented in the MD&A.

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017	2016
<b>Provision for credit losses</b>	<b>\$ 288</b>	<b>\$ 278</b>	<b>\$ 248</b>
Average gross loans	60,309	55,101	51,289
Average gross acceptances	105	69	108
<b>Average gross loans and acceptances</b>	<b>\$ 60,415</b>	<b>\$ 55,170</b>	<b>\$ 51,397</b>
<b>Credit loss provisioning rate</b>	<b>0.48%</b>	<b>0.50%</b>	<b>0.48%</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

## REGULATORY ENVIRONMENT

### Regulatory environment

The Federation's operations are governed in particular by the *Act respecting financial services cooperatives* and the *Act respecting insurance*, which will become the *Insurers Act* in June 2019. The AMF is the main government agency that oversees and monitors deposit-taking institutions (other than banks) and insurance companies that do business in Quebec and are governed by Quebec law, including the Federation and its insurance subsidiaries. Other federal and provincial regulations, in addition to those of regulators, may also govern some operations of Desjardins Group entities, such as the Office of the Superintendent of Financial Institutions (OSFI) related to property and casualty insurance, custodial and trust services and banking services provided by Zaq Bank.

Moreover, Desjardins Group, including the Federation, complies with the minimum regulatory capital requirements issued by the AMF, which reflect the provisions of the Basel III Accord. The Federation manages financial information in compliance with AMF *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings*. The Federation's financial and corporate governance are discussed on page 87 of this MD&A and in the "Corporate governance" section of the Federation's 2018 Annual Report.

In June 2013, the AMF determined that Desjardins Group met the criteria to be designated a domestic systemically important financial institution (D-SIFI), which subjects Desjardins Group to higher capital requirements and enhanced disclosure requirements, among other things, as instructed by the AMF. Since January 1, 2016, Desjardins Group has therefore been subject, as a D-SIFI, to an additional capital requirement of 1% on its minimum capital ratios. Also, based on the recommendations issued by the Enhanced Disclosure Task Force (EDTF) of the Financial Stability Board contained in the document "Enhancing the Risk Disclosures of Banks", Desjardins Group is continuing to integrate all these recommendations into its risk management disclosure framework. Desjardins Group also continues to adapt its disclosure to comply with the principles of risk data aggregation and risk reporting (RDARR), which will strengthen governance as well as risk data aggregation and risk reporting capabilities. Furthermore, Desjardins Group developed a living will, detailing the actions it will take to restore its financial position in the event of a crisis.

It should also be mentioned that Desjardins Bank, National Association, a subsidiary of the Federation incorporated under U.S. federal laws, is supervised by the Office of the Comptroller of the Currency of the United States (OCC), and that the Federation's operations in the United States, as a bank holding company, are subject to the supervisory and regulatory authority of the Board of Governors of the Federal Reserve System. Desjardins Florida Branch, the branch of the Federation operating in the State of Florida and incorporated under U.S. federal laws, is also supervised by the OCC. Desjardins Group is further governed by the U.S. *Bank Holding Company Act* and has the status of Financial Holding Company (FHC) in the U.S. In order to maintain such status, Desjardins Group must continue to meet capital requirements and certain other requirements to be considered "well capitalized" and be deemed "well managed" in accordance with the regulations of the U.S. Federal Reserve (the Fed).

### Changes in the regulatory environment

This section presents matters concerning changes in the regulatory environment that apply to Desjardins Group as a whole, including the Federation and its components.

Desjardins Group closely monitors regulations for financial products and services, as well as new developments in fraud, corruption, tax evasion, protection of personal information, money laundering, terrorist financing and domestic and international economic sanctions in order to mitigate any negative impact on its operations, and aims to comply with best practices in this regard. Additional information on changes in regulatory capital is provided in the "Capital management" section.

#### The Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions

On June 13, 2018, the Quebec National Assembly passed Bill 141, *An Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions* (the Act), which applies to all institutions and intermediaries operating in Quebec's financial sector. The main goal of the Act is to update and modernize the legislative framework for Quebec's financial sector so that the financial institutions that it governs will have all the levers they need to operate in a very competitive environment and governance that is consistent with best practices. The Act affects a series of laws, such as the *Act respecting insurance*, the *Act respecting financial services cooperatives*, the *Act respecting the distribution of financial products and services* and the *Deposit Insurance Act*. The *Act respecting financial service cooperatives* has been amended, among other things, to prescribe the rules for organizing a network of financial services cooperatives and a financial group, and the rules for issuing capital shares and investment shares.

The Act also adds a chapter concerning the *Groupe coopératif Desjardins* (the cooperative group), which comprises the Desjardins caisses in Quebec, the Federation and the *Fonds de sécurité Desjardins*. The chapter aims to strengthen financial solidarity mechanisms within the cooperative group, among other things. In this way, the Act affirms the Federation's mission to look after Desjardins Group's risk management and see to the financial health of the cooperative group and its sustainability. The Federation and the *Fonds de sécurité Desjardins* have additional special powers of supervision and intervention regarding the protection of creditors, including depositors. As well, the Federation may, in accordance with its mission and when it considers that the financial position of the cooperative group so warrants, give written instructions to any caisse or order it to adopt and apply a recovery plan. For its part, the *Fonds de sécurité Desjardins* is required to ensure the distribution of capital and other assets among the components of the cooperative group so that each one can perform its obligations to its depositors and other creditors in full, correctly and without delay. It is required to intervene with a component of the cooperative group each time it appears necessary to do so in order to protect the component's creditors. The *Fonds de sécurité Desjardins* may, in such circumstances, order the assignment of any part of the business of a caisse, order the amalgamation or dissolution of caisses or establish a legal entity to facilitate the liquidation of a caisse's bad assets. Furthermore, the *Fonds de sécurité Desjardins* mutualizes the cost of its interventions between the components belonging to the cooperative group. In addition, if it considers that its financial resources are inadequate to carry out its mission, it may set a special assessment and require any component of the cooperative group to pay it. The revised Act also provides that all the caisses, the Federation and the *Fonds de sécurité Desjardins* may be amalgamated into a single legal entity to be wound up, as these entities cannot be wound up in any other manner.

The amendments to the *Deposit Insurance Act* (to be renamed the *Deposit Institutions and Deposit Protection Act*) provide for new rules for the supervision and control of deposit-taking activities and the activities of authorized deposit-taking institutions, as well as recovery and resolution mechanisms in the event of failure of deposit-taking institutions. Furthermore, the Act introduces a new *Insurers Act* that provides for revised supervision for Quebec insurers. A significant change in this new legislation is to allow insurers to sell insurance over the Internet. A few changes aimed at modernizing the *Act respecting the distribution of financial products and services* were also introduced, such as rules for insurance brokers in offering products and new rules applicable to distributing products without a representative. In addition, in property and casualty insurance, the Act makes it mandatory for divided co-owners to have co-ownership insurance.

Generally speaking, the provisions of the Act applicable to financial services cooperatives came into force on July 13, 2018, one month after assent, but there are several exceptions. Among these, the chapter concerning the cooperative group came into force when the first internal by-law of the cooperative group was adopted, on December 7, 2018. The new provisions of the *Insurers Act*, for their part, will come into force on June 13, 2019 or subsequently, as the case may be, along with a large portion of the amendments to the *Act respecting the distribution of financial products and services*.

Desjardins Group is continuing its work to update its frameworks in order to reflect the new requirements.

#### Rules concerning capital instruments

The Capital Adequacy Requirements (CAR) Guideline of the Office of the Superintendent of Financial Institutions (OSFI) applicable to Canadian financial institutions includes requirements for Non-Viability Contingent Capital as part of regulatory capital. Desjardins Group, under the AMF's guideline on adequacy of capital base standards for financial services cooperatives, is subject to similar rules applicable to non-viability contingent capital in its regulatory capital. However, Desjardins Group has not issued any instrument subject to these rules, given that discussions with the AMF are still underway on how Desjardins Group will apply them. For further information, see the "Capital management" section on page 49.

#### The Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA)

In June 2018, proposals for significant changes to the PCMLTFA and its regulations were published by the Department of Finance Canada. Desjardins Group is participating in work sessions with the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), the Department of Finance Canada and other industry players to discuss these and other changes to the Canadian money laundering and terrorist financing (ML/TF) regime. While preparing for the implementation of these legislative changes, Desjardins Group is continuing to closely monitor developments to assess their impact on its operations.

#### Financial reforms in the U.S.

Should reform initiatives in the U.S. pertaining to financial regulation become a reality, they may affect non-U.S. financial institutions operating in the U.S., including Desjardins Group. The deregulation bill of U.S. Congress and the American regulators has been set in motion, in particular with the enactment of a statute providing some relief concerning certain rules prescribed by the Dodd-Frank Wall Street Reform and Consumer Protection Act and a proposal for a draft regulation simplifying the Volcker rule which deals with proprietary trading and hedge fund ownership interests. Desjardins Group continues to closely monitor developments in these draft reforms, for which the scope and timetable remain uncertain at this time.

#### Recapitalization regime for domestic systemically important banks

On April 18, 2018, the Department of Finance Canada published the final version of three regulations to implement the main features of the Bank Recapitalization (Bail-in) Regime and the OSFI issued the final version of its guideline on Total Loss Absorbing Capacity (TLAC). The introduction of the regulations and the TLAC guideline are intended to ensure that a non-viable domestic systemically important bank (D-SIB) has sufficient loss absorbing capacity to support its recapitalization. These regulations and the TLAC guideline came into force on September 23, 2018. The D-SIBs will be required to issue the ratios specified in the TLAC guideline as of the quarter commencing November 1, 2018 and comply with the requirements of the TLAC guideline no later than November 1, 2021. This regime is not applicable to Desjardins Group because it is regulated by the AMF. Furthermore, the amendments to the *Deposit Insurance Act* (to be renamed the *Deposit Institutions and Deposit Protection Act*) passed by the Quebec government on June 13, 2018, as mentioned above, provide for certain recovery and resolution mechanisms in the event of the failure of deposit-taking institutions. On October 25, 2018, the AMF issued for comment its draft regulations on a bail-in regime for a cooperative group as well as a draft TLAC guideline. The comment period initiated by the AMF ended on November 23, 2018. Desjardins Group will continue to monitor developments in this file and is expecting the adoption and implementation of a recapitalization regime similar to the federal one described above on March 31, 2019.

#### Data confidentiality and security

Data confidentiality and security is a rapidly changing area. In Canada, new provisions of the *Personal Information Protection and Electronic Documents Act* (PIPEDA) came into force on November 1, 2018. They will, in particular, require businesses to give notice of any breaches of security safeguards and impose the keeping of a register. Failure to give notice will result in a fine. It should be noted that in Europe, the *General Data Protection Regulation* (GDPR), which came into force on May 25, 2018, provides for new obligations that apply internationally to entities that control or process the personal data of citizens in the territory of the European Union. Although the impact of this regulation is not considered significant for Desjardins Group, the organization must closely monitor this file since several of its competitors are subject to it in whole or in part. In Quebec, consultations took place concerning amendments to *An Act respecting the protection of personal information in the private sector* (ARPPIS). As a result, Desjardins Group can expect that stricter rules will be adopted, and it is closely monitoring developments to assess the impacts on its operations.

### Pillar 3 disclosure requirements

Desjardins Group continues to monitor changes in financial disclosure requirements under global standards developed by the Basel Committee on Banking Supervision (BCBS). To this end, in January 2015, the Committee issued a new standard related to the third pillar, which aims to enhance comparability across financial institutions, transparency and disclosure with regard to regulatory capital adequacy and risk exposure. In December 2016, the AMF filed an update of its guideline on the adequacy of capital base standards for financial services cooperatives, which includes revised Pillar 3 provisions. Desjardins Group issued a Pillar 3 report for the period ended December 31, 2018, in order to comply. In addition, in March 2017, the BCBS issued the second phase of the revisions to Pillar 3 disclosure. In the fourth quarter of 2018, the AMF presented a draft update of its guideline. The changes would be effective on March 31, 2019 and will include requirements resulting from the second phase of the standard related to Pillar 3, particularly with respect to the leverage ratio, composition of capital and total loss absorbing capacity. For further information, see the "Capital management" section on page 49.

### Capital adequacy requirements for life and health insurers

In October 2016, the AMF issued the new *Capital Adequacy Requirements Guideline (CARLI) – Insurance of persons*. This new regulatory framework replaced the *Capital Adequacy Requirements Guideline (CAR) – Life and Health Insurance* as of January 1, 2018. The subsidiary Desjardins Financial Security Life Assurance Company complies with the requirements of the new guideline.

### Report on Ontario's auto insurance plan

Before the election, in June 2018, of a new majority government in Ontario, the Ontario Finance Minister at the time unveiled the Fair Auto Insurance Plan in December 2017, aimed at making automobile insurance more affordable for drivers and providing better care for accident victims. The Plan was based on a report by David Marshall on the province of Ontario's automobile insurance system, released in April 2017, and provided for the implementation by the government of various initiatives in the short- and medium-term. In spite of the uncertainty surrounding the potential implementation of the recommendations as a result of the change in government, Desjardins Group continues to monitor and support developments in Ontario's automobile insurance system.

### Guideline on granting residential mortgages

In February 2018, the AMF issued the revision of its guideline on granting residential mortgages, which went into effect in March 2018. The AMF's requirements are similar to those of the OSFI, issued in October 2017, which aim to encourage mortgage lenders to remain prudent in their mortgage underwriting practices and set a minimum interest rate or "stress test" for uninsured mortgages. Desjardins Group has already applied these practices since January 1, 2018.

### Modernization of the Canadian payments system

Technological progress and innovation affect the payments ecosystem, which is undergoing major changes. In 2016, Payments Canada launched a multiyear initiative to modernize the Canadian payments system. On December 19, 2018, Payments Canada issued its "Modernization Delivery Roadmap 2018 Update". The activities involve, in particular, the new high-value payments system – Lynx, real-time payments, and retail batch payments. These initiatives are in addition to the one already introduced in 2018, with the implementation of a new credit risk assessment model for the retail payments system in Canada and enhancements to automated funds transfers. Desjardins Group continues to monitor work by the industry, the federal government and Payments Canada.

### Qualified Intermediary Agreement

The U.S. Qualified Intermediary regime allows clients of financial intermediaries to benefit from more streamlined administrative procedures and more readily take advantage of the reduced tax rates allowed under tax agreements concerning taxable U.S. source income. For their part, financial institutions must comply with the sometimes-complex provisions of an agreement established by the U.S. tax authorities. This agreement has undergone several significant changes in the past few years with very short implementation deadlines. Desjardins Group entities that are QIs are continuing their efforts to take the necessary measures to comply with the last agreement issued in January 2017 and monitor future changes.

### Section 871(m) of the U.S. Internal Revenue Code

Section 871(m) of the U.S. *Internal Revenue Code* (IRS) was set up to ensure that non-U.S. investors pay tax on dividend payments on U.S. equity-linked instruments. This regulation, which has been in effect since January 1, 2017, provides for phased-in application of additional regulatory requirements in 2019, 2020 and 2021. Following the IRS's publication of Notice 2018-72 in September 2018, some relief has been provided for applications scheduled for 2019. The applicable regulatory requirements basically deal with subject loan, securities lending and delta-one transactions. Delta one is a ratio that measures the sensitivity of the derivative product to fluctuations in the underlying product price to which it refers. The calculation of delta can apply by individual transaction or combined transactions. The combined transaction rules also apply progressively. The regulatory requirements for non-delta one transactions have been postponed until January 1, 2021, while QSL status (Qualified Securities Lender – described in IRS Notice 2010-46) is maintained until January 1, 2021. The Desjardins Group entities concerned are putting measures in place to apply the regulation and monitor future changes.

### Regulation 93-101, Derivatives: Business Conduct and Regulation 93-102, Derivatives: Registration

In April 2017, the CSA issued draft *National Instrument 93-101 – Derivatives: Business Conduct* and draft *Companion Policy 93-101 Derivatives: Business Conduct* to establish a comprehensive regime for regulating the business conduct of participants in over-the-counter derivatives markets. In June 2018, the CSA published a second version of these drafts for comment. The consultation ended in September 2018. In April 2018, the CSA published for consultation draft *National Instrument 93-102 – Derivatives: Registration* and draft *Companion Policy 93-102 – Derivatives: Registration* for derivatives dealers, derivatives advisers and potentially other derivatives market participants. This consultation also ended in September 2018. The various derivatives market participants are furthermore subject directly or indirectly to a certain number of national and international standards resulting from a regulatory reform that is gradually taking effect. The Desjardins Group entities concerned are closely watching this regulatory development.

### Application of the new framework for European markets in financial instruments

In May 2014, European legislatures adopted a new framework for markets in financial instruments (MIF 2), in the form of the *Markets in Financial Instruments Directive* and the *Markets in Financial Instruments Regulation*. The regulatory requirements related to the MIF 2 directive have been applicable since January 3, 2018 and change the framework for carrying on market activities in Europe. One purpose of the new framework is to strengthen investor protection and make financial markets more resilient and transparent. The Desjardins Group entities concerned are closely monitoring this regulatory development in Canada and the notices issued in this regard by the CSA.

### Report on Climate change-related Disclosure Project

On April 5, 2018, the CSA issued *CSA Staff Notice 51-354, Report on Climate change-related Disclosure Project*. The report summarizes the findings of its project to review the disclosure by reporting issuers of risks and financial impacts associated with climate change, and its plans for future work. The Staff Notice also mentions that the CSA will continue to monitor the quality of issuers' disclosure with respect to climate change-related matters, best practices in the area of climate change-related disclosure and the development of disclosure frameworks. Desjardins Group is closely monitoring regulatory developments in this regard.

Desjardins Group presents a specific disclosure, based on the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), in its annual social and cooperative responsibility report. This disclosure is not incorporated by reference into this MD&A.

## 1.0 Fédération des caisses Desjardins du Québec

### 1.1 Profile and structure

#### WHO WE ARE

The Federation is a cooperative entity which is responsible for assuming orientation, framework, coordination, treasury and development activities for Desjardins Group and acts as a financial agent on Canadian and foreign financial markets. It provides its member caisses—namely 271 member caisses in Quebec and Ontario as at December 31, 2018 with a variety of services, including certain technical, financial and administrative services. The Federation's mission also includes risk management and capital management for Desjardins Group, and it ensures the financial soundness and sustainability of the Desjardins cooperative group, pursuant to the *Act respecting financial services cooperatives*. The cooperative group is comprised of the Desjardins caisses in Quebec, the Federation and the *Fonds de sécurité Desjardins*.

The Federation enables the caisses and other Desjardins Group components to accelerate their development and better respond to the needs of their members and clients. The Federation's structure has been designed to take into account the needs of Desjardins Group's members and clients, as well as the markets in which it operates.

The Federation is, among other things, the treasurer and official representative of Desjardins Group with the Bank of Canada and the Canadian banking system.

The Federation also has the right to participate in the Visa Inc. and MasterCard Inc. payment systems in Canada on behalf of Desjardins Group. In addition, it manages majority interests in joint-stock companies through holding companies.

#### WHAT MAKES US DIFFERENT

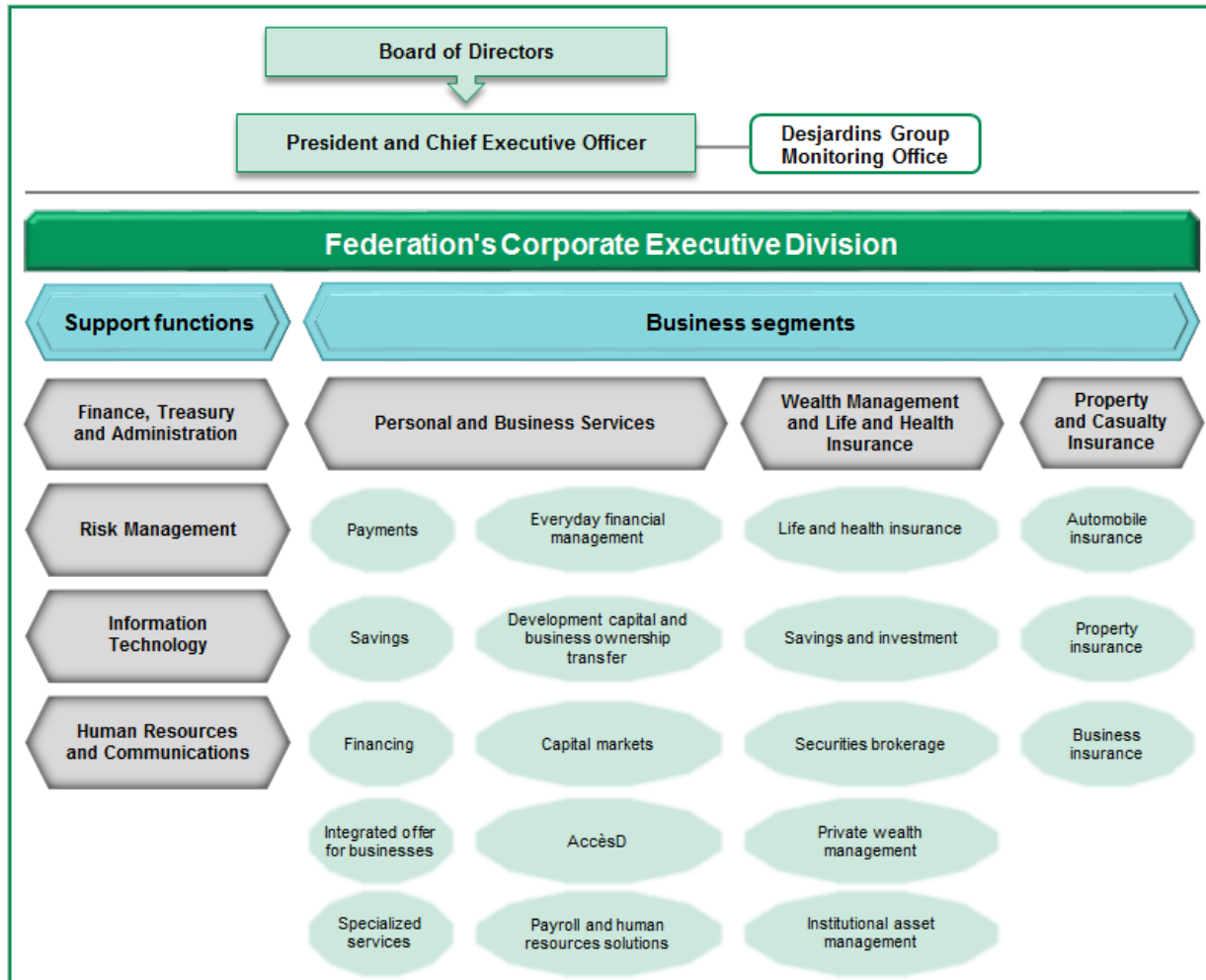
The Federation stands out from other Canadian financial institutions because of the cooperative nature of its component caisses. The resulting mission and values are the driving force for its directors, managers and employees. They are echoed in its orientations, and help it achieve its vision of sustainable prosperity within the communities that Desjardins Group, including the Federation, serves. Since the first caisse was founded in 1900 in Lévis, Desjardins Group has always been a key player in financial education, and it believes that the cooperative business model is more relevant now than ever in a greatly changing world.

Desjardins Group's ambition is to be first in people's hearts. Thanks to its varied distribution channels, numerous intermediary networks and personnel who strive to always work in the interests of members and clients, Desjardins Group stays close to its members and their communities. In order to best meet members' increasingly diverse needs, Desjardins Group pays special attention to the caisse network and its range of service delivery methods. This process is also part of Desjardins Group's continued commitment to the vitality of cooperation at the caisse level in terms of democratic life, representation, education and training, cooperation with other cooperatives and support for community development.

Another hallmark of Desjardins Group is its modern, grassroots-level democratic governance, based on the active participation of directors elected by caisse members. This participation is expressed in working together and in terms of governance. Bodies that address local issues are active in various areas where the caisses are present, and the *Forum de concertation Mouvement* serves a similar purpose at the caisse network level. In terms of governance, the caisses' elected officers participate at the general meeting, at orientation congresses and on the Federation's Board of Directors and its various commissions.

## STRUCTURE OF THE FEDERATION

The Federation's structure has been designed to take into account the needs of Desjardins Group members and clients, as well as the markets in which it operates. The Federation and the caisse network in Quebec and Ontario have the support of three main business segments (Personal and Business Services, Wealth Management and Life and Health Insurance, and Property and Casualty Insurance), which reinforces their ability to build on their products and services.



## The Federation's 2018 highlights

Surplus earnings before dividends	Loans and acceptances outstanding	Assets under management	Tier 1A capital ratio	Total asset growth
<b>\$1,350 million</b>	<b>+ \$3.3 billion</b>	<b>\$66.4 billion</b>	<b>15.7%</b>	<b>+ \$11.8 billion</b>

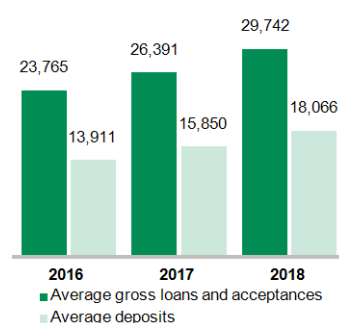
- Surplus earnings before dividends to member caisses down \$66 million, or 4.7%, compared to 2017.
- Increase of \$54 million, or 4.6%, in adjusted surplus earnings<sup>(1)</sup> before dividends to member caisses, compared to 2017.
- Operating income<sup>(1)</sup> of \$14,129 million, up 6.3% compared to 2017.
- Adjusted operating income<sup>(1)</sup> of \$13,997 million, up 7.5% compared to 2017.
- Growth in loans and acceptances outstanding, up \$3.3 billion compared to 2017.
- On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P., leading to the creation of Aviso Wealth.

## 2018 segment highlights

### PERSONAL AND BUSINESS SERVICES

#### Average gross loans and acceptances and average deposits<sup>(1)</sup>

(in millions of dollars)

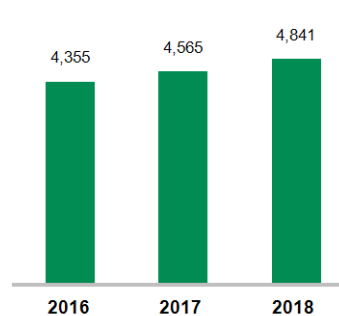


- Leader credit and debit card issuer in Quebec and No. 5 in Canada (based on 2017 outstandings), the segment has issued more than 6.9 million credit cards and 5.7 million debit cards in Canada.
- Growth of 10.6% compared to 2017 in business volume related to credit card products, Accord D, and auto and durables financing.
- Surplus earnings before dividends to member caisses totalled \$301 million, down \$16 million compared to 2017, as a result of a decrease in income from trading and new issues on capital markets as well as expenses related to the winding-up of the Zag Bank's operations.
- Acquisition and set-up of new Canada-wide credit card portfolios.
- Growth of \$3.4 billion compared to 2017 in the entire average portfolio of loans and acceptances.

### WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

#### Written premiums

(in millions of dollars)

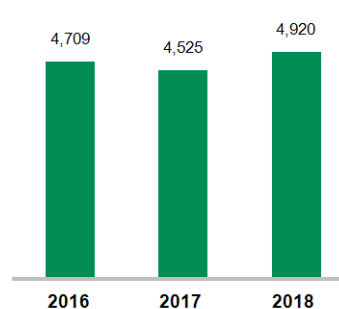


- No. 5 life and health insurer in Canada and No. 2 in Quebec (based on written premiums in 2017).
- No. 2 in Canada and No. 1 in Quebec for market-linked guaranteed investments (based on 2017 assets under management).
- Record net sales of \$3.5 billion for market-linked guaranteed investments, up 70.1% in 2018.
- Desjardins Private Wealth Management named "Best Private Wealth Management Company in Canada" for a third straight year, according to the Global Banking and Finance Review, particularly for its comprehensive range of products and services, its financial soundness and the quality of its customer experience.
- Net surplus earnings of \$894 million, up 46.1%, compared to 2017.
- Adjusted net surplus earnings<sup>(1)</sup> of \$765 million, up 25.0% compared to 2017, related to a more favourable product claims experience and higher income due to the increase in assets under management.
- Gross insurance premiums of \$4.3 billion, up 2.6% compared to 2017.
- Significant growth of 117.2% in net sales for online brokerage in 2018.

### PROPERTY AND CASUALTY INSURANCE

#### Gross written premiums

(in millions of dollars)



- Canada's No. 3 and Quebec's No. 2 property and casualty insurer (based on gross direct premiums written in 2017).
- Underwriting profits for the 26th consecutive year, in spite of automobile insurance material damage coverage under pressure in all geographic markets in 2018.
- Launch of the "Radar" functionality in the mobile application so that insureds can be alerted to severe weather risks for their property.
- Transition to the Desjardins brand for the Canadian operations acquired from State Farm and introduction of a new contract for the exclusive agent network in Ontario, Western Canada and Atlantic Canada.
- Net surplus earnings of \$173 million for the year, down \$273 million due to the gain net of expenses on the sale of subsidiaries in 2017.
- Adjusted net surplus earnings<sup>(1)</sup> down \$32 million, or 15.6%, compared to 2017, on account of the increase in the loss ratio, mainly in automobile insurance.
- Growth of \$506 million, or 13.0%, compared to 2017, in net premiums to total \$4.4 billion.
- Improvement in the expense ratio<sup>(1)</sup> to 25.2% in 2018, compared to 25.7% in 2017.

<sup>(1)</sup> See "Basis of presentation of financial information".

**Table 1 – Financial results and indicators**

For the years ended December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017	2016
Net interest income	\$ 1,501	\$ 1,404	\$ 1,303
Net premiums	8,923	8,146	7,263
Other operating income <sup>(2)</sup>	3,705	3,747	3,380
<b>Operating income<sup>(2)</sup></b>	<b>14,129</b>	<b>13,297</b>	<b>11,946</b>
Investment income <sup>(2)</sup>	693	1,767	1,108
<b>Total income</b>	<b>14,822</b>	<b>15,064</b>	<b>13,054</b>
Provision for credit losses	288	278	248
Claims, benefits, annuities and changes in insurance contract liabilities	6,584	6,795	5,446
Non-interest expense	6,392	6,239	6,022
Income taxes on surplus earnings	208	336	147
<b>Surplus earnings before dividends to member caisses</b>	<b>\$ 1,350</b>	<b>\$ 1,416</b>	<b>\$ 1,191</b>
<b>Adjusted surplus earnings before dividends to member caisses<sup>(2)</sup></b>	<b>\$ 1,221</b>	<b>\$ 1,167</b>	<b>\$ 1,191</b>
<b>Contribution to consolidated surplus earnings by business segment<sup>(3)</sup></b>			
Personal and Business Services	\$ 301	\$ 317	\$ 349
Wealth Management and Life and Health Insurance	894	612	461
Property and Casualty Insurance	173	446	296
Treasury and Other Support to Desjardins Group Entities	(18)	41	85
	<b>\$ 1,350</b>	<b>\$ 1,416</b>	<b>\$ 1,191</b>
<b>Indicators</b>			
Return on equity <sup>(2)</sup>	8.6%	9.4%	8.5%
Adjusted return on equity <sup>(2)</sup>	7.9	7.8	8.5
Credit loss provisioning rate <sup>(2)</sup>	0.48	0.50	0.48

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> See "Basis of presentation of financial information".

<sup>(3)</sup> The breakdown by line item is presented in Note 31, "Segmented information", to the Consolidated Financial Statements.

**Table 2 – Balance sheets and indicators**

As at December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017	2016
<b>Balance sheet</b>			
Assets	\$ 157,560	\$ 145,740	\$ 134,658
Net loans and acceptances	61,997	58,715	52,441
Deposits	58,057	52,149	46,902
Equity	14,553	16,019	14,680
<b>Indicators</b>			
Assets under administration	\$ 382,469	\$ 419,981	\$ 428,106
Assets under management <sup>(2)</sup>	66,359	66,653	59,490
Tier 1A capital ratio	15.7%	17.5%	15.9%
Tier 1 capital ratio	15.7	17.5	15.9
Total capital ratio	15.7	17.5	15.9
Leverage ratio	7.4	7.9	7.4
Gross credit-impaired loans <sup>(3)</sup> /gross loans and acceptances <sup>(4)</sup>	0.56	0.14	0.18

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Assets under management may also be administered by the Federation. When this is the case, they are included in assets under administration.

<sup>(3)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(4)</sup> See "Basis of presentation of financial information".

## 1.2 Significant events in 2018

### Creation of Aviso Wealth

On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction led to the creation of Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and a partnership between the Centrals and The CUMIS Group. A gain of \$129 million, net of income taxes, related to this transaction, was recognized in the Consolidated Statements of Income for the year ended December 31, 2018. Desjardins Group's interest in Aviso Wealth represents an investment in a joint venture and is recognized using the equity method of accounting in the Wealth Management and Life and Health Insurance segment. The results of the subsidiary Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P. were also presented in the Wealth Management and Life and Health Insurance segment.

Additional financial information is presented in Section 2.1 "Impact of significant transactions".

### Zag Bank

On November 5, 2018, Zag Bank announced that it was winding down its operations, and will close down during 2019. This decision is the result of a recent shift in focus by Desjardins Group, following a recent review of its operations in Ontario, the Atlantic Provinces and Western Canada, to concentrate in particular on growing its property and casualty insurance operations, wealth management activities and payment services. Given this focus, having a direct or online bank no longer fits into the long-term strategy of Desjardins Group, Zag Bank's shareholder. The financial impact of this decision was reported mainly in the third and fourth quarters of 2018.

## 1.3 Financial outlook for 2019

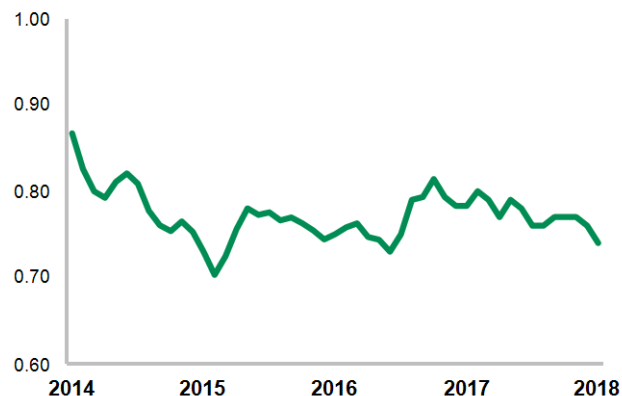
The Federation develops orientations and financial targets in support of Desjardins Group's ambitions. The Federation's actions and achievements are designed to help further the overall financial objectives of Desjardins Group. The financial outlook presented below therefore relates to Desjardins Group's strategic framework.

### FINANCIAL OUTLOOK FOR DESJARDINS GROUP

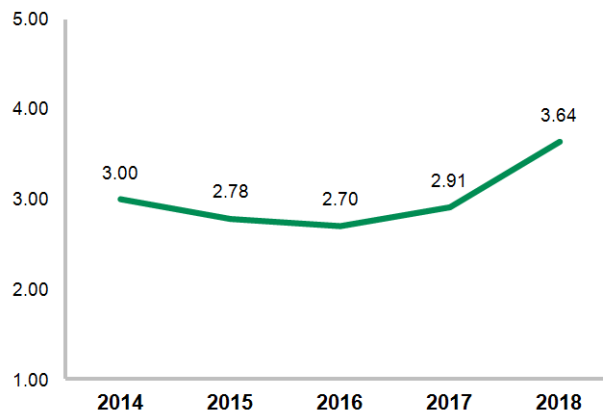
Desjardins Group should continue 2019 on a solid footing, with a level of capitalization that is higher than the average for the Canadian banking industry as well as increasing profitability in an expanding economic environment over the coming year. Stiff competition in the banking sector will place sustained pressure on net interest income, although the rise in interest rates that began in mid-2017 has had a favourable effect. Rigorous cost control and strict capital management will enable Desjardins Group to make significant investments for the benefit of members and communities and adopt innovative concepts to enhance service delivery, with the constant aim of being first in people's hearts and making it easier to do business with Desjardins.

## 1.4 Economic environment and outlook

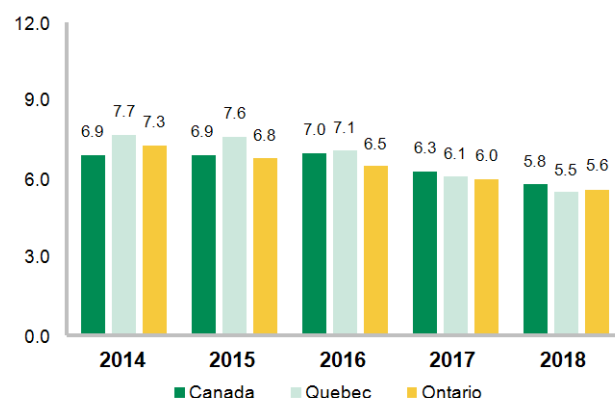
**Changes in the Canadian dollar vs. the U.S. dollar (monthly average)**  
(Canadian dollars/U.S. dollars)



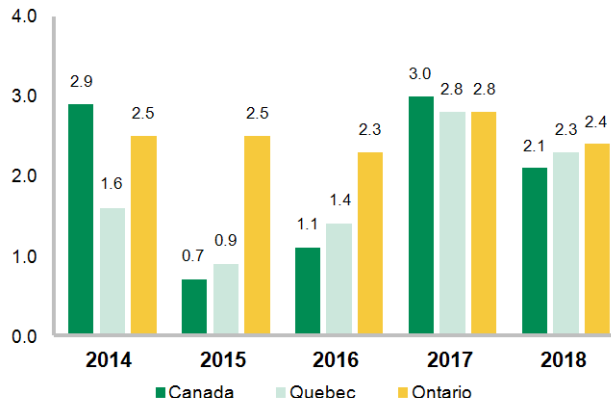
**Changes in the prime rate (annual average)**  
(as a percentage)



**Changes in the unemployment rate (annual average)**  
(as a percentage)



**Annual growth in GDP**  
(as a percentage)



### Global economy

After accelerating sharply in 2017, the international economy continued to expand in 2018. The annual gain in GDP is estimated at 3.7%. This good growth was despite a slowdown in international trade, the result of escalating protectionism that began in the U.S. Furthermore, the growth in several major economies slowed during the year. This was the case in the eurozone, where most confidence indices declined. Euroland's real GDP grew 1.8%, decidedly slower than the 2.5% growth posted for 2017. The Italian budgetary and political problem, the social strains in France and the difficulties in Germany's manufacturing sector have given cause for concern in Europe. In the United Kingdom, the trend is weak, due in particular to uncertainties around Brexit. The Chinese economy is growing at a slightly slower pace, at 6.6% for 2018 compared to 6.8% in 2017. Trade tensions between the U.S. and China have affected the economic environment in China, but also in many emerging countries.

The favourable economic environment and rising inflation led many central banks to continue normalizing monetary policy in 2018. In Europe, the European Central Bank stopped buying financial assets in December 2018, while the Bank of England raised its key interest rates by 0.25%. In North America, the pace of key interest rate hikes accelerated, with the U.S. Federal Reserve (the Fed) announcing four 0.25% increases, compared to three in Canada. Tighter monetary policies and optimistic statements issued by the central banks, particularly in North America, led to higher bond yields in early 2018. The rising interest rates, trade tensions and fears around the health of the global economy brought considerable volatility back to the stock markets. Even the S&P 500 Index, encouraged by tax reform and boosted by corporate earnings, nevertheless incurred two major corrections in 2018, ending the year lower compared to 2017. The year was even more difficult for most of the other stock exchanges. Stock markets in Europe and the emerging economies were held back by trade tensions, political uncertainties and the strength of the U.S. dollar, and the drop in the Toronto Stock Exchange was amplified by lower commodity prices. These factors also led to a weaker Canadian dollar and caused bond rates to fall sharply at the end of 2018.

The global economy should continue to grow in 2019, but economic activity is not expected to accelerate. The trade tensions and concerns about the emerging countries suggest a certain levelling off. In the industrialized countries, demand from the U.S. should partly offset weaker growth in the eurozone. The issue of the divorce between the European Union and the United Kingdom is not yet settled, and the related uncertainties may manifest in the economy. Volatility in the financial markets, concerns about Europe and China and the return of their monetary policies to a virtually neutral orientation should convince the Fed and the Bank of Canada to slow the pace of increases to their key interest rates. The increase in bond rates should also be limited. The return of a more positive sentiment on financial markets could exert some negative pressure on the U.S. dollar. Volatility may well remain high in the stock markets, but strong economic growth and high earnings levels leave hope that the North American indices will outperform their historical averages in 2019. The economic environment should also be quite favourable for commodities and, as a result, for the dollar and Canadian financial assets.

## United States

In the wake of slightly slower growth in early 2018, economic activity in the U.S. accelerated markedly in the spring, and real GDP grew strongly again in the second half of 2018. Above all, the labour market performed very well, with the unemployment rate reaching levels not seen since the end of the 1960s. Salaries also began to rise. This environment was supported by the tax cuts enacted by the Trump administration and Congress at the end of 2017. Confidence remained strong throughout the year despite greater volatility in the financial markets, escalating protectionism, the interest rate hikes and the mid-term elections. Real GDP grew 2.9% in 2018, on the heels of a 2.2% gain in 2017.

The economic environment in the U.S. should continue to be favoured by the budgetary policies implemented in 2018. However, the situation may change due to the risk of political stalemates following the mid-term elections. This became clear with the partial shutdown of the federal government that began at the end of December. Conditions in the labour market should nevertheless continue to improve, which will exert slightly more pressure on salaries and prices. Real GDP should reach 2.6% in 2019. However, the Trump administration's protectionist measures and reprisals by other countries represent significant risks.

## Canada

Following exceptional growth of 3.0% in 2017, Canadian real GDP expanded at a more sustainable rate of around 2.1% in 2018. The slower pace was due mostly to domestic demand. Household spending was not as strong, with slower growth in consumer spending and less residential investment. For the most part this was due to the effects of gradual rising Canadian interest rates and a series of restrictive measures affecting mortgage lending and the housing market. The economy experienced more problems late in the year when the energy sector was hard hit by plummeting oil prices, aggravated in Canada by constraints on the transportation of oil products. The year was also marked by an agreement to replace the North American Free Trade Agreement (NAFTA) with the Canada-United States-Mexico Agreement (CUSMA). This helped reduce uncertainty, opening the way for accelerated non-residential business investment in non-energy sectors.

The 2019 outlook in Canada is for growth near the economy's potential. The problems in the energy sector are expected to continue at the start of the year, as the Alberta government has imposed a significant cut in the province's oil production. The gradual increase in interest rates will also continue to affect consumer spending and the housing market. This being said, several favourable factors are still in place, allowing, among other things, growth in domestic demand to continue at a satisfactory pace. The labour market is strong, with the unemployment rate close to an historic low. Furthermore, demand for new and existing homes remains quite good, and the population is growing relatively quickly, particularly in the 25-to-34-year-old group. Lastly, if CUSMA is ratified as expected, businesses in the non-energy sectors should continue to invest in an environment where full use of production capacity is generating some problems satisfying growing demand. In trade, foreign demand should continue to expand in 2019, but at a slower pace. This will nevertheless foster export growth. The risks nevertheless remain substantial due to the trade wars being waged around the world. In the final analysis, real GDP could grow by 1.8% in 2019.

## Quebec

The Quebec economy grew at a sustained pace in 2018. Real GDP rose by approximately 2.3% for the year, slightly slower than the 2.8% growth posted for 2017. Households continued to be active, driving the residential real estate market. Consumer spending maintained a good pace, with household confidence still high. Existing home sales reached new heights, with prices rising at close to 5.2% in 2018. All the province's regions were swept up in this growth. The Greater Montreal real estate market began to overheat in the fall of 2018, since buyers outnumbered properties for sale. The provincial unemployment rate averaged 5.5% last year, exacerbating the problems many businesses were experiencing recruiting talent. The upward pressure on salaries grew, and employees' hourly compensation increased by approximately 4% last year. Business investment and exports firmed up slightly in 2018, despite the period of uncertainty associated with the NAFTA renegotiations, which continued into the fall.

The Quebec economy is expected to slow somewhat in 2019. The interest rate increases that began in mid-2017 should moderate consumer spending, in particular purchases of big-ticket items that require financing. The residential real estate market will also be affected by higher borrowing costs. Home sales and housing starts can be expected to weaken slightly in 2019, compared to the exceptional market activity of 2018. House prices will rise less quickly due to this market lull and approach 2.5% next year. CUSMA has reduced uncertainty for businesses and will be good for both investment and exports. It remains to be seen whether the tariffs of 25% on steel and 10% on aluminum, which are not part of the new agreement, will be maintained. Quebec's real GDP is expected to grow 2% in 2019, or slightly slower than in 2018.

Changes in the markets in which the Federation operates are described in the corresponding analyses in Section 2.3, "Analysis of business segment results".

## 2.0 Review of financial results

In the charts in this section, the information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

### 2.1 Impact of significant transactions

#### CREATION OF AVISO WEALTH IN 2018

On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction led to the creation of Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and the partnership between the Centrals and The CUMIS Group. For Desjardins Group, the interest in Aviso Wealth represents an investment in a joint venture and is recognized using the equity method of accounting in the Wealth Management and Life and Health Insurance segment. A \$4 million share in Aviso Wealth was recognized in the Consolidated Statements of Income for the year ended December 31, 2018.

The table below presents the operating results of the subsidiary Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P. included in the Federation's financial results for the Wealth Management and Life and Health Insurance segment.

**Table 3 – Impact of the creation of Aviso Wealth**

For the years ended December 31

(in millions of dollars)

	2018	2017	2016
Other operating income <sup>(1)</sup>	\$ 49	\$ 125	\$ 108
<b>Operating income<sup>(1)</sup></b>	<b>49</b>	<b>125</b>	<b>108</b>
Investment loss <sup>(1)</sup>	-	(6)	(7)
<b>Total income</b>	<b>49</b>	<b>119</b>	<b>101</b>
Non-interest expense	49	114	99
Income taxes on surplus earnings	-	1	1
<b>Surplus earnings before dividends to member caisses</b>	<b>\$ -</b>	<b>\$ 4</b>	<b>\$ 1</b>

<sup>(1)</sup> See "Basis of presentation of financial information".

#### SALE OF SUBSIDIARIES IN 2017

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, namely Western Financial Group Inc., a financial services company, and Western Life Assurance Company, a life and health insurance company, to Trimont Financial Ltd., a subsidiary of The Wawanesa Mutual Insurance Company. It should also be recalled that the sale of Western Financial Insurance Company to Economical Insurance was completed on January 1, 2017.

The table below presents the operating results of these three subsidiaries included in the Federation's financial results in the Property and Casualty Insurance segment.

**Table 4 – Impact of the sale of subsidiaries**

For the years ended December 31

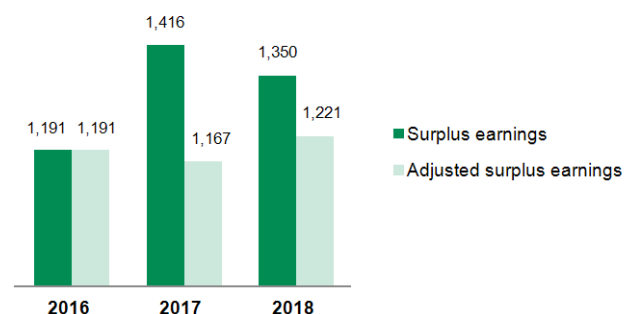
(in millions of dollars)

	2018	2017	2016
Net interest income	\$ -	\$ 3	\$ 5
Net premiums	-	65	213
Other operating income <sup>(1)</sup>	-	97	197
<b>Operating income<sup>(1)</sup></b>	<b>-</b>	<b>165</b>	<b>415</b>
Investment income <sup>(1)</sup>	-	9	6
<b>Total income</b>	<b>-</b>	<b>174</b>	<b>421</b>
Claims, benefits, annuities and changes in insurance contract liabilities	-	22	77
Non-interest expense	-	124	295
Income taxes on surplus earnings	-	9	16
<b>Surplus earnings before dividends to member caisses</b>	<b>\$ -</b>	<b>\$ 19</b>	<b>\$ 33</b>

<sup>(1)</sup> See "Basis of presentation of financial information".

## 2.2 Analysis of 2018 results

**Surplus earnings before dividends to member caisses**  
(in millions of dollars)



**Segment contributions to surplus earnings before dividends to member caisses in 2018**  
(as a percentage)



**Table 5 – Financial results and indicators**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Net interest income	\$ 1,501	\$ 1,404	\$ 1,303
Net premiums	8,923	8,146	7,263
Other operating income <sup>(2)</sup>	3,705	3,747	3,380
<b>Operating income<sup>(2)</sup></b>	<b>14,129</b>	<b>13,297</b>	<b>11,946</b>
Investment income <sup>(2)</sup>	693	1,767	1,108
<b>Total income</b>	<b>14,822</b>	<b>15,064</b>	<b>13,054</b>
Provision for credit losses	288	278	248
Claims, benefits, annuities and changes in insurance contract liabilities	6,584	6,795	5,446
Non-interest expense	6,392	6,239	6,022
Income taxes on surplus earnings	208	336	147
<b>Surplus earnings before dividends to member caisses</b>	<b>\$ 1,350</b>	<b>\$ 1,416</b>	<b>\$ 1,191</b>
<b>Adjusted surplus earnings before dividends to member caisses<sup>(2)</sup></b>	<b>\$ 1,221</b>	<b>\$ 1,167</b>	<b>\$ 1,191</b>
<b>Contribution to consolidated surplus earnings by business segment<sup>(3)</sup></b>			
Personal and Business Services	\$ 301	\$ 317	\$ 349
Wealth Management and Life and Health Insurance	894	612	461
Property and Casualty Insurance	173	446	296
Treasury and Other Support to Desjardins Group Entities	(18)	41	85
	<b>\$ 1,350</b>	<b>\$ 1,416</b>	<b>\$ 1,191</b>
<b>Indicators</b>			
Return on equity <sup>(2)</sup>	8.6%	9.4%	8.5%
Adjusted return on equity <sup>(2)</sup>	7.9	7.8	8.5
Credit loss provisioning rate <sup>(2)</sup>	0.48	0.50	0.48

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> See "Basis of presentation of financial information".

<sup>(3)</sup> The breakdown by line item is presented in Note 31, "Segmented information", to the Consolidated Financial Statements.

## 2018 SURPLUS EARNINGS

For 2018, the Federation reported surplus earnings before dividends to member caisses of \$1,350 million, a decrease of \$66 million, or 4.7%, compared to 2017. Surplus earnings adjusted for specific items, namely the gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in 2018 along with the gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company recognized in 2017, were up \$54 million, or 4.6%, to total \$1,221 million. This increase was mainly due to the more favourable claims experience in life and health insurance and higher income resulting from growth in payment activities and assets under management, mitigated by a higher claims experience in property and casualty insurance. In addition, the reduction in investment portfolio provisions and the impact of the change in the post-retirement benefit plan had a positive effect on non-interest expense.

### Segment contributions to surplus earnings

- Personal and Business Services: **Contribution of \$301 million**, down \$16 million, or 5.0%, compared to 2017.
    - Lower income from trading and new issues on capital markets.
    - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
    - Expenses related to the winding-up of the operations of Zag Bank.
      - Partially offset by:
        - Profit related to the restructuring of Interac Corp.
        - Growth in financing activities related to consumer, credit card and other personal loans.
    - The segment contributed 22.3% to surplus earnings.
  - Wealth Management and Life and Health Insurance: **Contribution of \$894 million**, up \$282 million, or 46.1%, and net surplus earnings adjusted for specific items up \$153 million, or 25.0%, compared to 2017.
    - Higher gains on the disposal of real estate investments in 2018.
    - More favourable claims experience.
    - Higher income from growth in assets under management.
    - Offset by less favourable adjustments to actuarial assumptions in the normal course of business.
    - The segment contributed 66.2% to surplus earnings.
  - Property and Casualty Insurance: **Contribution of \$173 million**, down \$273 million, and net surplus earnings adjusted for specific items down \$32 million, or 15.6%, compared to 2017.
    - Higher claims experience compared to 2017.
    - Impact of the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.
    - Offset by higher investment income.
    - The segment contributed 12.8% to surplus earnings.
- Return on equity was 8.6%**, compared to 9.4% for 2017.
  - Adjusted return on equity was 7.9%**, down compared to 7.8% for 2017.

## OPERATING INCOME

**Table 6 – Operating income**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Net interest income	\$ 1,501	\$ 1,404	\$ 1,303
Net premiums	8,923	8,146	7,263
Other operating income <sup>(2)</sup> (see Table 7)	3,705	3,747	3,380
<b>Total operating income<sup>(2)</sup></b>	<b>\$ 14,129</b>	<b>\$ 13,297</b>	<b>\$ 11,946</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> See "Basis of presentation of financial information".

Operating income totalled \$14,129 million, up \$832 million, or 6.3%, compared to 2017. Excluding the gain of \$132 million before taxes on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in 2018 along with the gross gain of \$278 million on the sale of Western Financial Group Inc. and Western Life Assurance Company recognized in 2017, operating income would have been \$13,997 million, up \$978 million, or 7.5%, compared to 2017.

## Net interest income

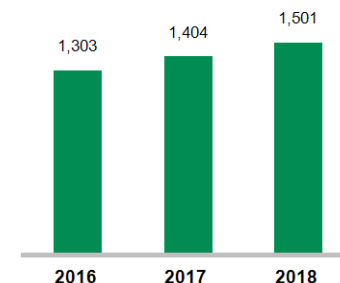
Net interest income is the difference between interest income earned on assets, such as loans and securities, and the interest expense related to liabilities, such as deposits, borrowings and subordinated notes.

It is affected by interest rate fluctuations, funding and matching strategies, as well as the composition of both interest-bearing and non-interest-bearing financial instruments.

- **Net interest income of \$1,501 million**, up \$97 million, or 6.9%.
  - Due to growth in the entire portfolio of loans and acceptances outstanding of \$3.3 billion, or 5.6%, over the year, particularly consumer loans, credit card products and loans to medium-sized businesses and large corporations.

## Net interest income

(in millions of dollars)



## Net premiums

Net premiums, comprising life and health insurance, annuity, and property and casualty insurance premiums, rose by \$777 million, or 9.5%, to total \$8,923 million as at December 31, 2018.

### Wealth Management and Life and Health Insurance segment

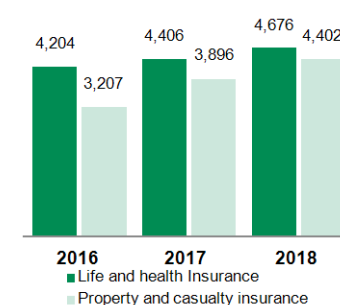
- **Net insurance and annuity premiums of \$4,676 million**, up \$270 million, or 6.1%, due to business growth.
  - Premiums up \$270 million, with annuities accounting for \$165 million, group insurance for \$69 million and individual insurance for \$36 million.

### Property and Casualty Insurance segment

- **Net premiums of \$4,402 million**, up \$506 million, or 13.0%, essentially as a result of the following:
  - Increase of \$367 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, mainly due to the change in the cession rate specified in the treaty, which provides for cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Increase due to growth in the average premium reflecting the current trend in the Canadian property and casualty insurance industry, as well as to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
  - Offset by a decrease in net premiums resulting from the sale of Western Life Assurance Company on July 1, 2017.

## Net premiums<sup>(1)</sup>

(in millions of dollars)



<sup>(1)</sup> The difference between total results and the sum of business segment results is due to intersegment transactions.

## Other operating income

**Table 7 – Other operating income**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
Assessments	\$ 392	\$ 377	\$ 393
Service agreements	742	727	699
Lending fees and credit card service revenues	699	660	575
Brokerage and investment fund services	905	1,030	1,060
Management and custodial service fees	579	514	443
Foreign exchange income	92	77	70
Other	296	362	140
<b>Total other operating income<sup>(3)</sup></b>	<b>\$ 3,705</b>	<b>\$ 3,747</b>	<b>\$ 3,380</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been reclassified to conform to the current year's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

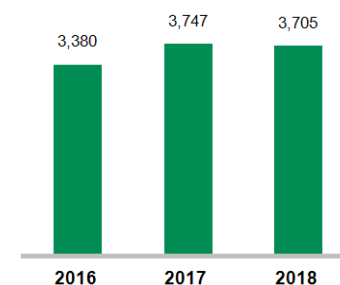
<sup>(3)</sup> See "Basis of presentation of financial information".

Other operating income stood at \$3,705 million for 2018, which is a decrease of \$42 million, or 1.1%, compared to the previous year.

Excluding the gain of \$132 million before taxes on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in 2018 along with the gross gain of \$278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in 2017, other operating income would have been \$3,573 million, up \$104 million, or 3.0%, compared to 2017.

- Income from assessments and service agreements of \$1,134 million, up \$30 million, or 2.7%.
  - Growth in income from the caisses as a result of activities to enhance the service offer for caisse members and clients as well as a higher volume of *AccèsD* transactions.
- Lending fees and credit card service revenues of \$699 million, up \$39 million, or 5.9%.
  - Growth in business volume from payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.
- Income from brokerage and investment fund services of \$905 million, down \$125 million, or 12.1%.
  - Decrease in commission income following the sale of Western Financial Group Inc. and the transaction involving Qtrade Canada Inc.
  - Offset by growth in income from assets under management.
- Management and custodial service fees up \$65 million, or 12.6%.
  - Growth in fees related to assets under management.
- Other operating income of \$296 million, down \$66 million, or 18.2%.
  - Gross gain of \$278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in 2017. Partially offset by the following:
    - Gain before taxes of \$132 million on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in 2018.
    - Decrease in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.

**Other operating income<sup>(1)</sup>**  
(in millions of dollars)



<sup>(1)</sup> See "Basis of presentation of financial information".

## INVESTMENT INCOME

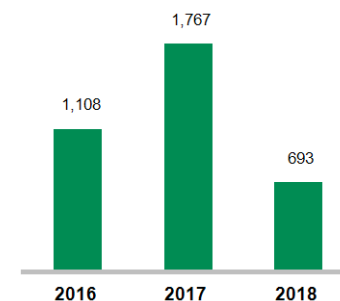
Investment income totalled \$693 million, a decrease of \$1,074 million compared to the previous year.

- Decrease primarily due to fluctuations in the fair value of assets backing liabilities related to life and health insurance operations.
  - Change mostly due to the decrease in the fair value of the bond portfolio related to interest rate fluctuations.
  - Decrease largely offset by the change in actuarial liabilities that in turn led to lower expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
- Lower income from trading activities.
- Smaller change in the fair value of derivative financial instruments, including those associated with the Federation's hedging operations.

Partially offset by the following items:

- Higher dividend income than in 2017, especially on account of reinvested income that included prior-period adjustments.
- Higher gains on disposal of real estate investments in 2018.
- Negative change in the fair value of matched bonds in the Property and Casualty Insurance segment lower than in 2017, chiefly because market interest rates did not rise as much in 2018 as they did in 2017.
- Profit related to the restructuring of Interac Corp.

**Investment income<sup>(1)</sup>**  
(in millions of dollars)



<sup>(1)</sup> See "Basis of presentation of financial information".

## TOTAL INCOME

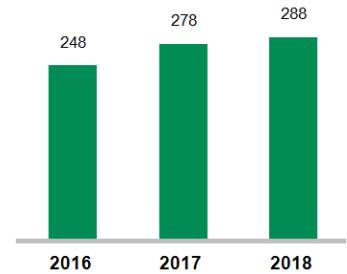
Total income, comprising net interest income, net premiums, other operating income and investment income, amounted to \$14,822 million, a decrease of \$242 million, or 1.6%, compared to 2017.

## PROVISION FOR CREDIT LOSSES

The provision for credit losses totalled \$288 million, up \$10 million, or 3.6%. This increase was mainly the result of growth in outstanding loans as well as the adoption of IFRS 9 as at January 1, 2018. This new standard led to volatility in results following the revision of economic scenarios, the updating of parameters and the migration of borrower ratings. Despite this increase, the Federation continued to present a quality loan portfolio in 2018.

- The credit loss provisioning rate was 0.48% for 2018, compared to 0.50% in 2017.
- The ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.56% as at December 31, 2018, compared to 0.14% a year earlier. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered insignificant.

**Provision for credit losses**  
(in millions of dollars)



## CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE CONTRACT LIABILITIES

Expenses related to claims, benefits, annuities and changes in insurance contract liabilities totalled \$6,584 million, down \$211 million, or 3.1%, compared to 2017.

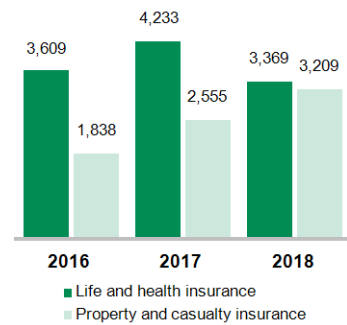
### Wealth Management and Life and Health Insurance segment

- **Cost of claims of \$3,369 million**, down \$864 million, or 20.4%. This decrease was basically the result of the following:
  - Decrease of \$873 million in the actuarial liabilities recognized under "Insurance contract liabilities", which includes the effect of a decrease in the fair value of matched investments.
  - The more favourable product claims experience was offset by less favourable adjustments to the changes to actuarial assumptions made in the normal course of business.

### Property and Casualty Insurance segment

- **Cost of claims of \$3,209 million**, up \$654 million, or 25.6%, mainly due to the following items:
  - Business growth, which led to a higher cost of claims.
  - Increase due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Less positive developments than in 2017 concerning prior-year claims in automobile insurance.
  - The P&C insurers' loss ratio was 73.9% for 2018, compared to 67.7% in 2017.
    - ♦ Higher ratio primarily attributable to less positive developments than in 2017 concerning prior-year claims, (9.9)% vs. (15.0)%, essentially automobile insurance claims.
    - ♦ Higher claims experience for the current year than for 2017: 80.7% vs. 80.1%.
    - ♦ More significant impact of catastrophes and major events compared to 2017: 3.1% vs. 2.6%.

**Claims, benefits, annuities and changes in insurance contract liabilities<sup>(1)</sup>**  
(in millions of dollars)



<sup>(1)</sup> The difference between total results and the sum of business segment results is due to intersegment transactions.

## NON-INTEREST EXPENSE

**Table 8 – Non-interest expense**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Remuneration and other payments	\$ 563	\$ 536	\$ 492
Salaries and fringe benefits			
Salaries	1,862	1,842	1,927
Fringe benefits	377	413	402
	2,239	2,255	2,329
Premises, equipment and furniture, including depreciation	496	514	437
Service agreements and outsourcing	341	322	306
Communications	219	244	265
Other	2,534	2,368	2,193
<b>Total non-interest expense</b>	<b>\$ 6,392</b>	<b>\$ 6,239</b>	<b>\$ 6,022</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

Non-interest expense totalled \$6,392 million for 2018, up \$153 million, or 2.5%, compared to 2017. This increase was mitigated by the following:

- Reduction in investment portfolio provisions.
- Gain due to the impact of the change in the post-retirement benefit plan.

Apart from these favourable items, non-interest expense increased as a result of the following:

- Higher expenses due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
- Business growth, particularly in assets under management.

- **Remuneration and other payments of \$563 million**, up \$27 million, or 5.0%.

- Increase in payments to member caisses as a result of growth in caisse network sales of various Desjardins products.

- **Salaries and fringe benefits of \$2,239 million**, down \$16 million, or 0.7%, compared to 2017, mainly because of the following:

- Gain due to the impact of the change in the post-retirement benefit plan made during 2018.
- Decrease in salaries following the sale of Western Financial Group Inc. and Western Life Assurance Company.
- Offset by higher salaries due to indexing and growth in operations.
- This expense item represented 35.0% of total non-interest expense, lower than the 36.1% recorded in 2017.
- The ratio of fringe benefits to total base compensation was 20.2% in 2018, down compared to 22.4% in 2017, primarily because of the impact of the change in the post-retirement benefit plan made during 2018. For more information, see Note 16, "Net defined benefit plan liabilities" to the Consolidated Financial Statements.

- **Expenses related to premises, equipment and furniture (including depreciation) of \$496 million**, down \$18 million, or 3.5%, compared to 2017, mainly because of the decrease in expenses following the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.

- **Service agreements and outsourcing of \$341 million**, up \$19 million, or 5.9% compared to 2017.

- Increase in expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.

- **Communication expenses of \$219 million**, down \$25 million, or 10.2%, compared to 2017.

- The decrease resulted from the implementation of productivity initiatives.

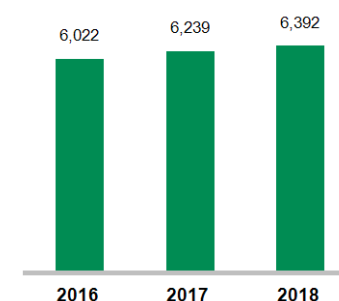
- **Other expenses of \$2,534 million**, up \$166 million, or 7.0%, compared to 2017.

- Increase in expenses due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
- Commitments made under the \$100 million fund program.
- Business growth, particularly in assets under management.
- Increase in expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
- Write-off of certain technology assets in 2018.
- Expenses related to the winding-up of Zag Bank's operations.

Partially offset by the following:

- Reduction in investment portfolio provisions.
- Decrease in expenses due to the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017 as well as the transaction involving Qtrade Canada Inc.

**Non-interest expense**  
(in millions of dollars)



## INCOME TAXES AND INDIRECT TAXES

The Federation is a cooperative financial group, and is considered a private and independent company for tax purposes, unlike the vast majority of other Canadian financial institutions, which are large public corporations. The Federation's entities that are not financial services cooperatives are subject to the large corporation tax regime.

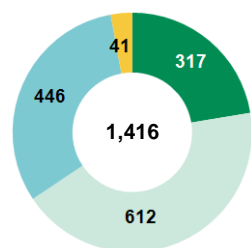
- **Income taxes on surplus earnings before dividends to member caisses of \$208 million**, down \$128 million compared to 2017.
  - Effective tax rate of 13.4% for the year ended December 31, 2018, compared to 19.2% for 2017.
  - If specific items are excluded, the effective tax rate would have been 14.4%, compared to 20.8% in 2017. The lower rate is mainly because of the recovery of taxes related to the remuneration of G capital shares and F capital shares.

Note 26, "Income taxes on surplus earnings", to the Consolidated Financial Statements presents, among other things, a reconciliation of the statutory tax rate and the effective tax rate, expressed in dollars.

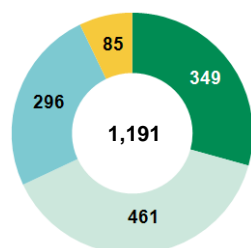
Indirect taxes consist of property and business taxes, payroll and social security taxes, the goods and services tax, and sales taxes. Indirect taxes are included in non-interest expense. For 2018, the Federation's entities paid \$1,141 million in indirect taxes, compared to \$1,049 million in 2017.

## COMPARISON OF 2017 AND 2016

**2017 surplus earnings before dividends to member caisses**  
(in millions of dollars)



**2016 surplus earnings before dividends to member caisses**  
(in millions of dollars)



■ Personal and Business Services  
■ Wealth Management and Life and Health Insurance  
■ Property and Casualty Insurance  
■ Treasury and Other Support to Desjardins Group Entities

For 2017, the Federation posted surplus earnings before dividends to member caisses of \$1,416 million, compared to \$1,191 million for 2016. Surplus earnings adjusted for specific items totalled \$1,167 million, which was down \$24 million, or 2.0%. Return on equity was 9.4%, compared to 8.5% in 2016, while adjusted return on equity was 7.8% in 2017, compared to 8.5% in 2016.

### Segment results

- **Personal and Business Services: Surplus earnings before dividends to member caisses of \$317 million in 2017**, down \$32 million compared to 2016.
  - Increase in the provision for credit losses in 2017 following a recovery of the collective allowance in 2016.
- **Wealth Management and Life and Health Insurance: Net surplus earnings of \$612 million in 2017**, up \$151 million compared to 2016, essentially due to the following:
  - Solid investment performance in 2017.
  - Favourable adjustments to actuarial assumptions made in the normal course of business in 2017.
  - Higher income from growth in assets under management.
  - Offset by a less favourable claims experience in 2017.
- **Property and Casualty Insurance: Net surplus earnings of \$446 million in 2017**, including a gain on the sale of subsidiaries, for an increase of \$150 million compared to 2016.
  - Net surplus earnings adjusted for specific items totalled \$205 million, down \$91 million compared to 2016.
  - Higher claims experience in 2017 than in 2016 and favourable trend in prior-year claims, which were lower than in 2016.

## Consolidated results

- **Operating income of \$13,297 million in 2017**, up \$1,351 million compared to 2016.
  - Net interest income of \$1,404 million in 2017, an increase of \$101 million compared to 2016, mainly on account of growth in the entire portfolio of loans and acceptances outstanding.
  - Net premiums up \$883 million in 2017, mainly because of the following:
    - Increase in net premiums resulting from the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
    - Business growth related to insurance operations in the Wealth Management and Life and Health Insurance segment and the Property and Casualty Insurance segment.
    - Offset by a decrease in net premiums following the sale of Western Life Assurance Company on July 1, 2017 and of Western Financial Insurance Company on January 1, 2017.
  - Other operating income of \$3,747 million, up \$367 million in 2017, essentially due to the following:
    - Gain before taxes of \$278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company.
    - Higher income from assets under management.
    - Growth in business volume from payment and financing activities.
 This increase was partly offset by the following:
    - Decrease in commission income following the sale of Western Financial Group Inc.
    - Increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
- **Investment income of \$1,767 million in 2017**, up \$659 million compared to 2016.
  - Net income on securities at fair value through profit or loss up \$586 million.
    - Increase mainly due to fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
      - Increase mostly offset by the change in actuarial liabilities that in turn led to an increase in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
      - Differences mostly attributable to changes in the fair value of the bond, share and derivatives portfolio.
    - Larger change in the fair value of derivative financial instruments in 2017, including those associated with the Federation's hedging operations.
    - Partly offset by the decline in income from asset-backed term notes (ABTN) activities given that substantially all ABTN were settled in January 2017.
  - Net income from available-for-sale securities up \$70 million, mainly because of higher gains on the disposal of investments in 2017.
  - Net other investment income was \$204 million, stable compared to 2016.
- **Provision for credit losses of \$278 million in 2017**, up \$30 million compared to 2016.
  - In 2016, refining the methodology used in the models for calculating the collective allowance resulted in a recovery of this allowance. However, favourable changes in portfolio risk mitigated this increase.
  - Credit loss provisioning rate of 0.50% as at December 31, 2017, comparable to the rate in 2016.
  - Ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, of 0.14% as at December 31, 2017, down from 0.18% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans.
- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of \$6,795 million**, up \$1,349 million in 2017.
  - Wealth Management and Life and Health Insurance segment: expenses up \$624 million in 2017.
    - Increase of \$425 million in the actuarial liabilities recognized under "Insurance contract liabilities", which included the effect of an increase in the fair value of matched investments.
    - Actuarial liabilities also included the favourable effect of adjustments to actuarial assumptions as well as the less favourable effect of the claims experience.
    - Increase in benefits due to growth in operations.
  - Property and Casualty Insurance segment: expenses up \$717 million in 2017.
    - Increase mainly due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
    - Loss ratio for P&C insurers of 67.7% in 2017, compared to 60.2% in 2016.
      - Higher loss ratio partly due to a less favourable change than in 2016 concerning prior-year claims, (15.0)% vs. (20.2)%, mainly because automobile insurance claims taken over from State Farm as at January 1, 2015 were lower than in 2016.
      - Increased loss ratio also attributable to the higher claims experience for the current year than in 2016, 80.1% compared to 75.8%, primarily in automobile insurance claims in all geographic markets.
    - Offset by catastrophes and major events, which were less significant than in 2016, when there had been two catastrophes caused by hail and the Fort McMurray wildfire in Alberta.
- **Non-interest expense up \$217 million in 2017**, mainly due to the following:
  - The effect of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increased popularity of the BONUSDOLLARS Rewards Program.
  - Business growth, particularly in payment and financing activities and assets under management.
 Partly offset by the following:
  - Decrease in expenses following the sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 as well as Western Financial Insurance Company on January 1, 2017.
  - Effective cost control following the implementation of productivity initiatives that made it possible to limit the increase in non-interest expense in a context of operations growth.

## 2.3 Analysis of business segment results

The Federation's financial reporting is organized by business segments, which are defined based on the needs of Desjardins Group's members and clients, the markets in which it operates, and on its internal management structure. The Federation's financial results are divided into the following three business segments: Personal and Business Services; Wealth Management and Life and Health Insurance; and Property and Casualty Insurance. In addition to these three segments, there is also the Treasury and Other Support to Desjardins Group Entities category. This section presents an analysis of results for each of these segments.

Intersegment transactions are recognized at the exchange amount, which represents the amount agreed upon by the various legal entities and business units. The terms and conditions of these transactions are comparable to those offered on capital markets.

### 2.3.1 Personal and Business Services

#### PROFILE

Personal and Business Services is central to Desjardins Group's operations. This segment is responsible for finetuning a comprehensive, integrated line of products and services designed to meet the needs of individuals, businesses, institutions, non-profit organizations and cooperatives offered through the Desjardins caisse network, its Desjardins Business centres, and specialized teams. This is what makes Desjardins Group a leader in financial services in Quebec and a player on the financial services scene in Ontario as well.

Desjardins's offer includes regular, convenience and savings transactions, payment services, financing, specialized services, access to capital markets, development capital, business ownership transfers and advisory services, and through its distribution network, life and health insurance and property and casualty insurance products.

In addition, members and clients know that they can rely on the largest advisory force in Quebec, made up of dedicated professionals who are there for them at every stage in their life or entrepreneurial growth.

To meet the constantly changing needs of caisse members and clients, the Federation supports the caisse network and its service centres in distributing products and services by optimizing the performance and profitability of the physical and virtual networks through setting up and managing complementary access methods by phone, online, via applications for mobile devices, and at ATMs.

Additional information about the Personal and Business Services segment's principal risks is presented on page 58 of the "Risk management" section of this MD&A.

#### SERVICES

- **Everyday financial management:**
  - Routine transaction services and term savings, as well as specialty services, such as foreign exchange and funds transfers.
- **Integrated business offer:**
  - Customized solutions to support businesses of all sizes in their expansion plans, whether on Quebec, Canadian or international markets.
- **Financing:**
  - **Residential mortgages**, for the purchase of land, new or existing homes and for renovations;
  - **Consumer loans**, such as loans for the purchase of automobiles and durable goods, personal lines of credit, student loans and Accord D financial solutions;
  - **Commercial credit**, which makes it possible to offer financing in the commercial and industrial, agricultural and agri-food, and public and institutional sectors, as well as for commercial and multi-residential real estate.
- **Payment:**
  - Debit, credit and prepaid card payment services for individuals and businesses, merchant payment acceptance services, electronic payment services and both domestic and international funds transfers.
- **AccèsD:**
  - Desjardins Group products and services are available at anytime, anywhere in the world, by phone, online and via applications for mobile devices.
- **Capital markets:**
  - Meeting the financing needs of Canadian corporations, institutions and cooperatives, and providing advisory services for mergers and acquisitions, as well as intermediation and execution services on the stock and fixed income securities markets;
  - Carried out by seasoned sales and trading teams who are supported by a research team that is renowned in the industry for its excellence.
- **Development capital:**
  - Facilitating investment, both directly and through funds, in small and medium-sized enterprises (SMEs) and cooperatives in every region of Quebec;
  - Desjardins Capital Inc., which manages *Capital régional et coopératif Desjardins*, supports the growth of businesses, especially in business ownership transfers;
  - With the backing of a team of specialists operating throughout Quebec, this segment helps to develop and maintain the highest calibre of entrepreneurship in Quebec by providing entrepreneurs with assistance at every stage of their company's growth.
- **Specialized services:**
  - International services, cash management services, custodial and trust services, integrated services for high-net-worth clients as well as payroll and human resources management solutions.

## 2018 ACHIEVEMENTS

- **Interac Flash:** Deployment of contactless technology on Desjardins debit cards.
- **New automated teller machines:** Start of rollout of the touchscreen ATMs that allow envelope-free deposit. More than 400 ATMs have been deployed to date, and rollout will continue throughout 2019.
- **Payment:** Acquisition and set-up of new Canada-wide credit card portfolios.
- **Insufficient funds alert:** Introduction of a new alert to notify members when they do not have the necessary funds in their account to cover a preauthorized payment. More than one million members have signed up for this alert since its launch in February 2018.
- Opening of five **Signature Service** centres in 2018, for a total of 16 to date in different regions of Quebec.
- **Launch of “FondsC”** at all Desjardins Business centres, an initiative aimed at supporting SMEs with financial assistance of up to \$10,000 and encouraging our partner enterprises to initiate new growth projects throughout Quebec.
- Desjardins Capital Inc. and Export Development Canada (EDC) partnered with Siparex Group and Bpifrance to launch the **Transatlantic Fund**, with an envelope of \$120 million to finance the development of European and North American companies and support their growth.
- Desjardins Group **ranked No. 2 among Quebec’s most influential brands** according to the fourth edition of the *Indice Ipsos-Infopresse*.
- **Coollest financial institution:** Based on Léger’s 2018 Youth Study, Desjardins Group is the coolest financial institution according to Quebec millennials.
- Desjardins Group received awards at the PMI Elixir Gala, an event recognizing the best in project management across all industries. The *Approval - Basel Business Credit Risk* and *Support for Agile Approaches by Enhancing Portfolio Management Maturity* were both honoured in the **Palmarès category**.
- Montreal Startup Community Awards – Desjardins Group was a winner: This annual gala recognizes all those who contribute to the development of the Montreal ecosystem for startups. Desjardins Group, through Desjardins Lab, was **honoured as “Corporate Champion of the Year”**.
- The Personal and Business Services segment continued its digital transformation, particularly through the following:
  - **New AccèsD mobile app:** A significant development in the Desjardins mobile app toward a modern and intuitive platform.
  - **Electronic signature:** Large-scale deployment of electronic signature in the caisse network with the addition of consumer financing, deposit, loan insurance products and opening of business accounts.
  - **Online mortgage renewal:** Introduction of 100% online renewal for certain types of mortgages. Introduced gradually with a few caisses, the solution will expand, in 2019, to all caisses, including those in Ontario, for all eligible members and certain mortgage types.
  - Opening of business accounts online and enrolment for **AccèsD Affaires** services greatly simplified, thereby considerably reducing the delay in these processes for the benefit of Desjardins members.

## INDUSTRY

In 2018, the Canadian financial industry comprised some 86 domestic and foreign banking institutions, as well as 523 savings and loan cooperatives, slightly more than 51.8% of which belonged to Desjardins Group.

In the Canadian banking services industry, on-balance sheet and off-balance sheet personal savings outstanding was estimated at \$4,209 billion as at December 31, 2018, for a year-over-year increase of 0.5%, compared to a 7.9% increase a year earlier. This significant slowdown is due to a pullback in stock market activity (an 11.6% drop in the S&P/TSX index in 2018), which affected the value of off-balance sheet savings products (such as investment funds and securities in custody with securities brokers) and reduced the popularity of this riskier type of investment with retail investors. The outstanding volume of loans to individuals was estimated at \$2,165 billion as at the same date, a year-over-year increase of 3.4%, compared to a 5.3% increase observed at year-end 2017. Business financing outstanding was estimated at \$879 billion, a year-over-year increase of 9.1%, compared to an increase of 10.5% as at December 31, 2017.

In Quebec, on-balance sheet and off-balance sheet personal savings outstanding was estimated at \$789 billion at year-end 2018, for nil year-over-year growth, compared to an increase of 8.2% as at December 31, 2017. The slowdown was due to the same factors as for Canada as a whole. The volume outstanding for financing to individuals was estimated at \$387 billion as at the same date, a year-over-year increase of 3.9%, compared to growth of 5.0% at year-end 2017. The volume outstanding for financing to businesses was estimated at \$171 billion as at December 31, 2018, a year-over-year increase of 8.8%, compared to 4.5% growth at the end of 2017.

The major industry players are focusing primarily on client experience, access to services and proactive advice. The fight for market share is therefore very fierce, since all players are adopting strategies aimed at intensifying business relations with their clients and getting to know them better.

Additional information about the economic environment can be found in the “Economic environment and outlook” section of this MD&A.

## 2019 STRATEGIES AND PRIORITIES

The 2019 strategies and priorities of the Personal and Business Services segment are incorporated into Desjardins Group’s strategic priorities and are aimed at helping Desjardins to achieve its ambition of being first in people’s hearts, while working in the best interests of members and clients. The Personal and Business Services segment intends to strengthen its leadership position in financing, savings and, through its distribution network, life and health and P&C insurance products. Capitalizing on the strengths of the entire cooperative group in serving members and clients and increasing their satisfaction will again be Desjardins Group’s key priorities in the coming year. To do so, Desjardins will facilitate interactions with members and clients across all its channels, in particular by streamlining its processes.

Reaching objectives requires the commitment of every director, manager and employee, as well as a high-calibre, comprehensive and integrated offer that is innovative and easy to access. The segment, focused on the financial health of its members, further intends to underscore the cooperative difference by contributing to lasting prosperity in businesses and communities. Its strategy is based on establishing enduring relationships of closeness and trust with members, clients and partners, and on sustainable growth. Its implementation is supported by strong foundations and Desjardins’s long-standing commitments in the regions and in various socio-economic communities.

The Personal and Business Services segment is also continuing to implement its plan to achieve profitable growth in order to remain a major industry player in Quebec while enhancing its productivity by maximizing its synergies with other Desjardins entities and segments.

Another of the segment's priorities is to continue the digital transformation in line with members' and clients' priority life events. In concrete terms, the segment will continue its initiatives to strengthen its relational presence across all channels and spark members' and clients' interest in proactive, value-added advice. The segment also seeks to make members and clients more independent for regular interactions and to continue to simplify products, services and processes from end to end.

## ANALYSIS OF FINANCIAL RESULTS FOR THE PERSONAL AND BUSINESS SERVICES SEGMENT

**Table 9 – Personal and Business Services – Segment results**

For the years ended December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>
Net interest income	\$ 1,144	\$ 1,089	\$ 1,031
Other operating income <sup>(3)</sup>	1,638	1,557	1,420
<b>Operating income<sup>(3)</sup></b>	<b>2,782</b>	<b>2,646</b>	<b>2,451</b>
Investment income <sup>(3)</sup>	46	39	33
<b>Total income</b>	<b>2,828</b>	<b>2,685</b>	<b>2,484</b>
Provision for credit losses	288	274	248
Non-interest expense	2,137	1,972	1,808
Income taxes on surplus earnings	102	122	79
<b>Surplus earnings before dividends to member caisses</b>	<b>301</b>	<b>317</b>	<b>349</b>
Dividends to member caisses, net of tax recovery	-	-	18
<b>Net surplus earnings for the year after dividends to member caisses</b>	<b>\$ 301</b>	<b>\$ 317</b>	<b>\$ 331</b>
Of which:			
Group's share	\$ 301	\$ 317	\$ 325
Non-controlling interests' share	-	-	6
<b>Indicators</b>			
Average gross loans and acceptances <sup>(3)</sup>	\$ 29,742	\$ 26,391	\$ 23,765
Average deposits <sup>(3)</sup>	18,066	15,850	13,911
Credit loss provisioning rate <sup>(3)</sup>	0.97%	1.04%	1.04%
Gross credit-impaired loans <sup>(4)</sup> / gross loans and acceptances ratio <sup>(3)</sup>	1.08	0.28	0.38

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

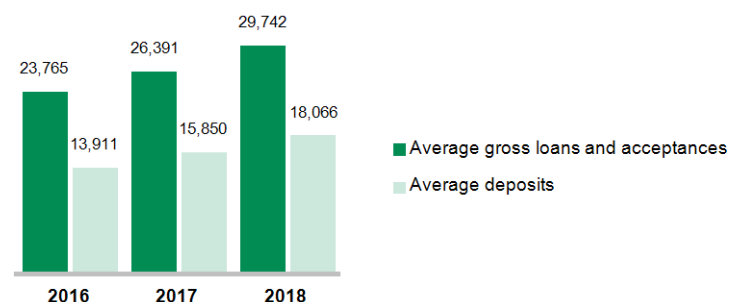
<sup>(2)</sup> Data for 2017 and 2016 have been reclassified to conform to the current year's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

<sup>(3)</sup> See "Basis of presentation of financial information".

<sup>(4)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

### Average gross loans and acceptances and average deposits

(in millions of dollars)



## COMPARISON OF 2018 AND 2017 – PERSONAL AND BUSINESS SERVICES

- **Surplus earnings before dividends to member caisses of \$301 million**, down \$16 million, or 5.0%, essentially due to the following:
  - Lower income from trading and new issues on capital markets.
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses related to the winding-up of the operations of Zag Bank.
 This decrease was partially offset by:
  - Profit related to the restructuring of Interac Corp.
  - Growth in financing activities related to consumer, credit card and other personal loans.
- **Operating income of \$2,782 million**, up \$136 million, or 5.1%.
  - Increase of \$55 million in net interest income mainly as a result of year-over-year growth of \$3.4 billion, or 12.7%, in the entire average portfolio of loans and acceptances outstanding, including consumer loans, credit card products and loans to medium-sized businesses and large corporations.
  - Other operating income of \$1,638 million, up \$81 million, or 5.2%, mainly due to the following:
    - ♦ Growth in business volumes of payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.
    - ♦ Growth in income from caisses as a result of activities to enhance the service offer to the caisse members and clients as well as growth in *AccèsD* transaction volume.
    - ♦ Offset by lower income from new issues on capital markets.
- **Investment income of \$46 million**, up \$7 million, or 17.9%, mainly as a result of:
  - Profit related to restructuring of Interac Corp.
  - Offset by trading income on capital markets.
- **Total income of \$2,828 million**, up \$143 million, or 5.3%.
- **Provision for credit losses of \$288 million**, up \$14 million, or 5.1%, mainly as a result of:
  - Growth in outstandings.
  - Revision of economic scenarios and updating of parameters.
  - Migration of borrower ratings.
  - The adoption of IFRS 9 on January 1, 2018, made the allowance for credit losses more volatile.
- **Non-interest expense of \$2,137 million**, up \$165 million, or 8.4%, chiefly due to:
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses related to the winding-up of Zag Bank's operations.
  - Business growth, especially growth in activities to enhance the service offer to caisse members and clients and in *AccèsD* services.

## 2.3.2 Wealth Management and Life and Health Insurance

### PROFILE

The Wealth Management and Life and Health Insurance segment combines different categories of service offers aimed at growing the assets of Desjardins Group members and clients and helping them protect their financial security. These offers are intended for individuals and businesses, while its group insurance and savings plans meet the needs of employees through their company, or individuals who are part of any other group.

The segment designs several lines of individual insurance (life and health) coverage as well as savings and investment products. In addition to its own products and services, it distributes external savings and investment products as well as securities and private wealth management services. The segment also includes asset management for institutional clients.

One of the greatest strengths of the Wealth Management and Life and Health Insurance segment is its vast and diversified Canada-wide distribution network, which mainly includes:

- Employees of the caisse network and Desjardins Business centres.
- Financial security advisers assigned to caisse members.
- Investment advisers and private managers.
- Exclusive agents and independent partners.
- Actuarial consulting firms and group plan representatives.

To meet members' and clients' needs and preferences, certain product lines are distributed directly via customer care centre, online or through applications for mobile devices. Online services are constantly being finetuned so that they meet clients' changing requirements.

This sector includes the operations of Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. until April 1, 2018, as well as the activities with regard to the interest in Aviso Wealth as of this same date, as mentioned in "Impact of significant transactions".

Additional information about the Wealth Management and Life and Health Insurance segment's principal risks is presented on page 58 of the "Risk management" section of this MD&A.

## SERVICES

- **Insurance for individuals:**
  - Includes products and services offered on an individual basis, or to businesses or groups by way of group plans.
  - These life and health insurance coverages provide peace of mind by reducing the financial impacts that could occur due to illness, disability, accident or death.
- **Savings and investment services:**
  - Include the various investment solutions for individuals and businesses, as well as group retirement savings plans for company employees, or individuals who are part of any other group.
  - The wide array of investment solutions offered, which includes market-linked guaranteed investments (MLGI), exchange traded funds (ETF), guaranteed investment funds and mutual funds with a number of responsible investment products, allow individuals and businesses to find the one best suited to their needs, whether for preparing for retirement, planning a trip or any other financial goal.
- **Securities brokerage services:**
  - Include the distribution of all types of investments, including stock market securities.
  - There are two separate distribution models: the customized services of an investment adviser (full-service brokerage) or online brokerage services for savvy investors who want to trade on their own.
- **Private wealth management services:**
  - Are set out in a constantly updated and integrated offer intended for wealthy clients.
  - The personalized support of private managers includes a number of aspects, such as financial planning, tax and philanthropy optimization as well as portfolio management.
- **Institutional asset management services:**
  - Investment solutions are proposed by a group of investment experts specializing in asset management for institutional clients in order to obtain competitive returns and an attractive risk-return trade-off for them.

## 2018 ACHIEVEMENTS

### Life and Health Insurance

- **Reconfiguring the insurance product portfolio** to simplify and update our offer and propose new solutions for analyzing needs.
- **Complete review of insurance coverage** for serious illnesses, including all types of cancer.
- Launching of a **telemedicine pilot project** with 5,000 participants from one of our group insurance plans.
- **New offer for group insurance plans**, with the possibility of adding therapeutic cannabis.
- Deployment of the **Financial health and well-being zone** on the [desjardinslifeinsurance.com](http://desjardinslifeinsurance.com) website and a new health and well-being platform.

### Wealth Management

- **Enviably results for Desjardins Funds** in terms of total assets according to Strategic Insight: Ranked 1st in Quebec and 11th in Canada.
- **Three new SocieTerra funds** and a new line of eight **Responsible Investment Exchange Traded Funds** (RI ETFs) double the responsible investment products we offer. These RI ETFs are a first in Canada.
- **Three awards for Market-linked guaranteed investments** (MLGIs) from Americas Structured Products & Derivatives Awards. Having received awards for the seventh straight year, Desjardins Group is now the most recognized financial institution for this type of investment in Canada.
- In group retirement savings, Desjardins continues to deploy financial well-being services, including the **launch of a Financial well-being zone**, which helps members to feel confident about their financial future. The secure website provides an adaptive interface for mobile devices; navigation has been simplified and the content has been contextualized.
- In online brokerage, **online accounts and electronic signatures have been launched**, and the website converted to a responsive web design.
- In securities and private wealth management, **statements of account have been simplified and improved, and tax slips have been digitized**.

## INDUSTRY

The wealth management industry and the life and health insurance industry are complementary because their aim is to provide products and services that will increase the net worth of Canadian households and make sure that their financial future is secure.

- **Canadian market:**
  - Wealth Management: At the end of 2017, financial assets of \$4,468 billion were held by Canadian households in various savings and investment products, growing annually at 8.4% on a compound basis, and at 8.2% over the past five years.
  - Life and Health Insurance: Premium income totalled \$110 billion in life and health insurance and in annuities according to 2017 figures, growing by 4.5% over the last five years. About 22 million Canadians have individual or group life insurance for a total of \$4.7 trillion in insurance in force.
- **Competition in Canada:**
  - Wealth Management: A division of all major banking groups, life and health insurance companies and investment funds. Competition is fierce, and players try to outdo one another in terms of ingenuity in order to win over clients and build their loyalty.
  - Life and Health Insurance: Based on 2017 statistics, there are more than 150 insurers, of which 38 are foreign-owned life insurers doing business in Canada. Five insurers monopolize 77.9% of the market, accounting for the high degree of consolidation in this industry. Desjardins Financial Security Life Assurance Company is still a leader in Quebec and ranks fifth in Canada, with written premiums of \$4.6 billion in 2017.
- **Developments and expectations of members and clients:**
  - Given such high and complex needs, financial advisors still play a key role in providing relevant information, making sales and maintaining relationships. Digital offers with virtual and mobile interfaces are increasingly used to cater to certain clients' desire for autonomy.

## 2019 STRATEGIES AND PRIORITIES

The 2019 strategies and priorities of the Wealth Management and Life and Health Insurance segment form part of Desjardins Group's strategic priorities that aim to help Desjardins Group to achieve its ambition of being first in people's hearts. Just like the other Desjardins Group business segments, the Wealth Management and Life and Health Insurance segment works in the interests of its members and clients.

The shift to a member- and client-focused culture is a priority for this segment, for which it plans to pick up the pace. The idea is therefore to optimize its product lines, further automate its processes and accelerate its digital transformation. The resulting efficiency gains will enable it to provide constantly better service to members and clients, which is its *raison d'être*.

Another priority of the Wealth Management and Life and Health Insurance segment is to help actively promote Desjardins Group's cooperative difference. Concretely, it will therefore pursue its initiatives to enhance the financial health and well-being of its members and clients, and to increase its financial literacy efforts with regard to savings and retirement as well as its activities to promote financial health and security management. Additional action would be to maintain its leadership in the area of responsible investing across Canada, thereby promoting the development of a sustainable and responsible economy.

The Wealth Management and Life and Health Insurance segment's third priority is to capitalize on Desjardins Group's strengths as an expansive cooperative group. It will therefore take action to maximize synergies within Desjardins Group, especially for groups and businesses, and to expand its product offer to all Desjardins Group distribution networks and external networks.

In order to successfully carry out the combined actions of these three priorities, this segment can rely on a team of employees and distribution partners who are determined to always better meet the needs of members and clients by providing exemplary and distinctive quality service.

## ANALYSIS OF FINANCIAL RESULTS FOR THE WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE SEGMENT

**Table 10 – Wealth Management and Life and Health Insurance – Segment results**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Net interest income	\$ 4	\$ 1	\$ -
Net premiums	4,676	4,406	4,204
Other operating income <sup>(2)</sup>	1,716	1,514	1,386
<b>Operating income<sup>(2)</sup></b>	<b>6,396</b>	<b>5,921</b>	<b>5,590</b>
Investment income <sup>(2)</sup>	387	1,406	795
<b>Total income</b>	<b>6,783</b>	<b>7,327</b>	<b>6,385</b>
Provision for (recovery of) credit losses	(1)	4	-
Claims, benefits, annuities and changes in insurance contract liabilities	3,369	4,233	3,609
Non-interest expense	2,296	2,329	2,208
Income taxes on surplus earnings	225	149	107
<b>Net surplus earnings for the year</b>	<b>\$ 894</b>	<b>\$ 612</b>	<b>\$ 461</b>
<b>Specific item, net of income taxes</b>			
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	(129)	-	-
<b>Adjusted net surplus earnings for the year<sup>(2)</sup></b>	<b>\$ 765</b>	<b>\$ 612</b>	<b>\$ 461</b>
Of which:			
Group's share	\$ 894	\$ 610	\$ 440
Non-controlling interests' share	-	2	21
<b>Indicators</b>			
Net sales of savings products	\$ 7,908	\$ 8,577	\$ 8,465
Insurance sales	342	523	471
Group insurance premiums	3,301	3,232	3,072
Individual insurance premiums	872	836	796
Annuity premiums	503	338	336
Receipts related to segregated funds	2,026	1,840	2,811

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> See "Basis of presentation of financial information".

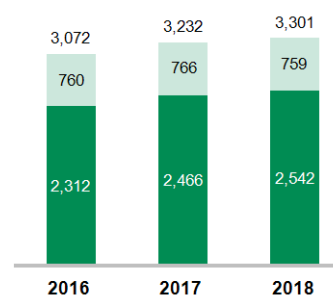
**Table 11 – Expenses attributable to policyholders**

For the years ended December 31

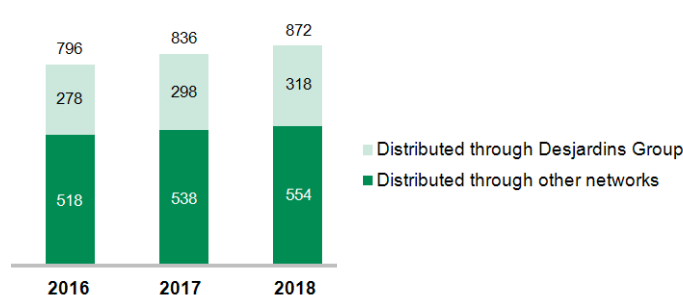
(in millions of dollars)	2018	2017	2016
Insurance and annuity benefits	\$ 3,126	\$ 3,037	\$ 2,904
Change in actuarial liabilities	111	984	559
Policyholder dividends, experience refunds and other	132	212	146
<b>Total</b>	<b>\$ 3,369</b>	<b>\$ 4,233</b>	<b>\$ 3,609</b>

**Group insurance premiums by distribution network**

(in millions of dollars)

**Individual insurance premiums by distribution network**

(in millions of dollars)

**COMPARISON OF 2018 AND 2017 – WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE**

- **Net surplus earnings of \$894 million**, up \$282 million, or 46.1%, and adjusted net surplus earnings of \$765 million, up \$153 million, or 25.0%, mainly as a result of:
  - Higher gains on disposal of real estate investments in 2018.
  - More favourable claims experience.
  - Higher income as a result of growth in assets under management.
  - Offset by less favourable adjustments to actuarial assumptions made in the normal course of business.
- **Operating income of \$6,396 million**, up \$475 million, or 8.0% basically because of:
  - Increase of \$270 million in premiums, of which \$165 million was from annuities, \$69 million was from group insurance and \$36 million, from individual insurance.
  - Other operating income totalled \$1,716 million, up \$202 million, or 13.3%.
    - ♦ Gain on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.
    - ♦ Higher income from growth in assets under management.
    - ♦ Offset by lower income as a result of the aforesaid transaction.
- **Investment income of \$387 million**, down \$1,019 million, or 72.5%.
  - Decrease primarily due to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
    - ♦ Change due mostly to a decrease in the fair value of the bond portfolio as a result of interest rate fluctuations.
    - ♦ Decrease largely offset by the change in actuarial liabilities leading to lower expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
  - Offset by the higher gains on the disposal of real estate investments.
- **Total income of \$6,783 million**, down \$544 million, or 7.4%.
- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of \$3,369 million**, down \$864 million, or 20.4%, essentially as a result of:
  - Decrease of \$873 million in actuarial liabilities under "Insurance contract liabilities", which included the effect of the decline in the fair value of matched investments.
  - The more favourable claims experience for products was offset by the less favourable adjustments related to the changes to actuarial assumptions made in the normal course of business.
- **Non-interest expense of \$2,296 million**, down \$33 million, or 1.4%, mainly because of the following:
  - The transaction involving Qtrade Canada Inc. led to a decrease in expenses.
  - Offset by the higher expenses for assets under management.

## 2.3.3 Property and Casualty Insurance

### PROFILE

The Property and Casualty (P&C) Insurance segment offers insurance products providing coverage for Desjardins Group members and clients against disasters. Since the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017, it includes only the operations of Desjardins General Insurance Group Inc. and its subsidiaries. Desjardins General Insurance Group Inc. offers a personal line of automobile and property insurance products across Canada and also provides businesses with insurance products. Its products are distributed through property and casualty insurance agents in the Desjardins caisse network in Quebec, a number of client care centres (call centres) and Desjardins Business centres, through an exclusive agent network of close to 500 agencies outside Quebec distributing P&C insurance and several other financial products online and via applications for mobile devices.

Desjardins General Insurance Group Inc., which has more than 3,000,000 clients, markets its products to the Canada-wide individual and business market under the Desjardins Insurance and State Farm banners, and to the group market—including members of professional associations and unions, and employers' staff—under The Personal banner. As part of its integration plan for State Farm's Canadian operations, Desjardins Group started to switch from the State Farm banner to the Desjardins Insurance banner on May 1, 2018. The transition will be carried out by December 31, 2019.

Additional information about the Property and Casualty Insurance segment's principal risks is presented on page 58 of the "Risk management" section of this MD&A.

### SERVICES

- **Automobile insurance**, including motorcycle and recreational vehicle insurance:
  - Offers insurance coverage tailored to clients' specific needs and their vehicle features;
  - Also includes the necessary coverage to obtain financial compensation for bodily injury in provinces where such coverage is not provided by a public plan.
- **Property insurance**:
  - Offers owners and tenants insurance coverage to protect their physical property, with all-risk insurance coverage and optional coverages for primary and secondary residences.
- **Business insurance**:
  - Covers the insurance requirements for commercial vehicles, commercial property and public liability for businesses;
  - Service is provided to the following sectors, among others: service firms, retailers and wholesalers, garages, self-employed workers, general or specialized contractors, restaurants, offices, health care professionals, commercial buildings, condominiums and apartment buildings.

### 2018 ACHIEVEMENTS

- Continued streamlining, modernizing and enhancing of the member and client experience:
  - **Improvement of the member and client experience**, in particular by making it easy to purchase home insurance in all regions and business lines and by simplifying automobile claims.
  - Continuation of the digital transformation, in particular by:
    - ♦ Deploying online purchase of auto insurance in Quebec.
    - ♦ Launching online purchase of home insurance for tenants and condo insurance across Canada.
    - ♦ Enhancing its **mobile offer** in a number of ways:
      - Clients can now take photos of damage to their vehicle themselves and send them to a body shop or claims adjuster for an estimate so as to save time and avoid running around.
      - Continue to focus on prevention: In addition to Ajusto (telematics program providing personalized feedback on driving) and Alert (program to prevent water damage in home insurance by using a detector placed close to a potential source of leaks), there is the new **Radar** program, which provides severe weather alerts so steps can be taken to prevent certain damage to a client's home, auto or other property.
      - The functionalities of the P&C Insurance segment's mobile offer, namely the Alert home insurance program and the Ajusto auto insurance program, are being phased into the **Bancassurance Desjardins Mobile Services** app for Quebec members.
- **Integration of State Farm's Canadian operations**: On schedule and almost completed in 2018, with some work to be finalized in 2019. In addition, the State Farm exclusive agent network has been phasing in operations under the Desjardins Insurance banner since May 2018 and the transition should be completed by the end of 2019.
- Continuation of the **program to modernize IT systems** with the new auto rates solution for Ontario, the Atlantic region and the West, and finalizing of the implementation of the business offer for Quebec.

## INDUSTRY

The Canadian P&C insurance industry offers insurance coverage for vehicles, personal and commercial property, and public liability. The Canadian P&C insurance market is a mature market, with an average annual growth rate of 3.3% over the past five years. In 2017, direct premiums written on the Canadian market totalled \$49.8 billion, up 4.1% since 2016, the highest growth rate since 2011. Across Canada, individual insurance accounted for 63.2% of the market, and business insurance accounted for 36.8%. As at December 31, 2017, the P&C Insurance segment ranked third in the Canadian property and casualty insurance market, and it was in second place in the individual insurance market.

The entire auto insurance industry in Canada is now facing challenges associated with profitability resulting from a sharp rise in claims, which reflects in particular the cost of new technologies in motor vehicles and the increase in distractions behind the wheel. The Desjardins Group P&C Insurance segment is proactive regarding these challenges and has implemented an action plan to optimize its profitability in a changing world given the difficult situation. Moreover, this year, the insurance industry was particularly affected by violent winds and tornadoes. According to Insurance Bureau of Canada, the violent winds on May 4, 2018 in southern Ontario and some regions of Quebec caused \$410 million in property damage, with \$380 million of this damage in Ontario. More than 13,000 claims related to this event were filed with Desjardins General Insurance Group (DGIG), for a net cost of reinsurance of about \$54 million, of which \$48 million was essentially for Ontario. In addition, more than 2,000 claims were filed for the tornadoes and high winds that hit the Ottawa–Gatineau region on September 21, 2018, for a net cost of reinsurance of \$38 million for DGIG.

While the Canadian industry is developing at an unprecedented rate, the various industry players are competing simultaneously on several fronts. The Canadian market will continue to develop quickly as in recent years, driven by technological innovations, changes in expectations and consumer behaviour as well as the advent of new business models. These insurers are starting to position themselves in the response to new trends such as InsurTech or the sharing economy, and the Desjardins Group P&C Insurance segment is proactive vis-à-vis these new trends.

## 2019 STRATEGY AND PRIORITIES

The Property and Casualty Insurance segment's 2019 strategies and priorities fall within the scope of Desjardins Group's strategic priorities, and aim to help Desjardins Group attain its goal of being number one in people's hearts.

As a result, in 2019, the segment will continue its efforts to be recognized as a Canadian leader in promoting the member and client experience by adapting its business practices in the interests of its members and clients, by optimizing the performance of its value chain and by modernizing the business line systems. Moreover, in order to affirm Desjardins Group's cooperative difference, the segment intends to continue to modernize its insurance model to enhance added value interactions by capitalizing on analytics and the digital transformation. The segment will also continue to build on the strengths of the expansive cooperative group to which it belongs by accelerating the shift toward Desjardins Mobile Services and by seeking the full potential of the acquisition of State Farm's Canadian operations.

The Property and Casualty Insurance segment will therefore focus its efforts on the following four priorities in 2019:

- Enhance the member and client experience.
- Improve the profitability of the auto product.
- Accelerate the digital transformation for all products and services.
- Acquire, assess, develop and mobilize talent.

## ANALYSIS OF FINANCIAL RESULTS FOR THE PROPERTY AND CASUALTY INSURANCE SEGMENT

**Table 12 – Property and Casualty Insurance – Segment results**

For the years ended December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017	2016
Net interest income	\$ -	\$ 1	\$ 1
Net premiums	4,402	3,896	3,207
Other operating income (loss) <sup>(2)</sup>	(188)	78	(55)
<b>Operating income<sup>(2)</sup></b>	<b>4,214</b>	<b>3,975</b>	<b>3,153</b>
Investment income <sup>(2)</sup>	336	214	206
<b>Total income</b>	<b>4,550</b>	<b>4,189</b>	<b>3,359</b>
Claims, benefits, annuities and changes in insurance contract liabilities	3,209	2,555	1,838
Non-interest expense	1,127	1,099	1,132
Income taxes on surplus earnings	41	89	93
<b>Net surplus earnings for the year</b>	<b>\$ 173</b>	<b>\$ 446</b>	<b>\$ 296</b>
<b>Specific item, net of income taxes</b>			
Gain, net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company <sup>(3)</sup>	-	(241)	-
<b>Adjusted net surplus earnings for the year<sup>(2)</sup></b>	<b>\$ 173</b>	<b>\$ 205</b>	<b>\$ 296</b>
Of which:			
Group's share	\$ 132	\$ 405	\$ 245
Non-controlling interests' share	41	41	51
<b>Indicators</b>			
Gross written premiums <sup>(4)</sup>	\$ 4,920	\$ 4,525	\$ 4,709
Loss ratio <sup>(2)</sup>	73.9%	67.7%	60.2%
Current year loss ratio <sup>(2)</sup>	80.7	80.1	75.8
Loss ratio related to catastrophes and major events <sup>(2)</sup>	3.1	2.6	4.6
Ratio of favourable changes in prior-year claims <sup>(2)</sup>	(9.9)	(15.0)	(20.2)
Expense ratio <sup>(2)</sup>	25.2	25.7	27.7
Combined ratio <sup>(2)</sup>	99.1	93.4	87.9

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> See "Basis of presentation of financial information".

<sup>(3)</sup> The difference between the data presented in the table of the Federation's adjusted surplus earnings before dividends to member caisses is due to intersegment transaction expenses.

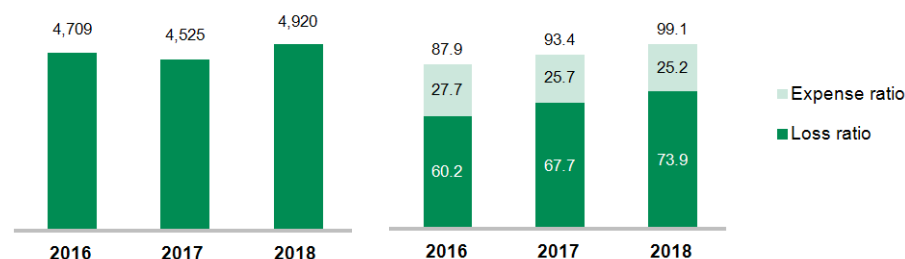
<sup>(4)</sup> Includes the life insurance premiums of Western Financial Group Inc. for 2017 and 2016.

**Gross written premiums**

(in millions of dollars)

**Combined ratio**

(as a percentage of net premiums earned)



## COMPARISON OF 2018 AND 2017 – PROPERTY AND CASUALTY INSURANCE

- **Net surplus earnings of \$173 million**, down \$273 million, and adjusted net surplus earnings, down \$32 million, or 15.6%. essentially due to the following:
  - Higher claims experience than in the previous year.
  - Impact from the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.
  - Offset by higher investment income.
- **Operating income of \$4,214 million**, up \$239 million, or 6.0%.
- **Net premiums of \$4,402 million**, up \$506 million, or 13.0%, primarily as a result of:
  - Increase of \$367 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, mainly due to the change in the cession rate stipulated in the treaty, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Increase due to growth in the average premium reflecting the current trend in the Canadian P&C insurance market, and due to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
  - Offsetting decrease in net premiums following the sale of Western Life Assurance Company on July 1, 2017.
- **Loss of \$188 million, presented under Other operating income (loss)**, while income was recognized in the prior year, for a difference of \$266 million, chiefly because of the following:
  - Gain on the sale of Western Financial Group Inc. and of Western Life Assurance Company, completed on July 1, 2017, and recognized in the corresponding year.
  - Decrease in commission income following the sale of Western Financial Group Inc.
  - Offset by a smaller increase than in 2017 in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations, and arising from the favourable developments in claims taken over.
- **Investment income of \$336 million**, up \$122 million, or 57.0%, basically as a result of the following:
  - Higher dividend income than in 2017, particularly because of the reinvested income, which includes prior-period adjustments.
  - Decrease in the fair value of matched bonds, which was lower than in 2017, mainly due to an increase in market interest rates that was lower in 2018 than in 2017.
- **Total income of \$4,550 million**, up \$361 million, or 8.6%.
- **Cost of claims totalling \$3,209 million**, up \$654 million, or 25.6%, essentially as a result of the following:
  - Business growth leading to a higher cost of claims.
  - Increase due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Change in prior-year claims was not as favourable as in the preceding year in auto insurance.
  - Loss ratio of P&C insurers at 73.9% for 2018, compared to 67.7% in 2017.
    - ♦ Higher loss ratio mainly due to a less favourable change than in 2017 concerning prior-year claims, (9.9)% vs. (15.0)%, mainly in auto insurance.
    - ♦ Claims experience for the current year was higher than in the prior year; namely 80.7% vs. 80.1%.
    - ♦ Impact of catastrophes and major events greater than in the prior year; namely 3.1% vs. 2.6%.
- **Non-interest expense of \$1,127 million**, up \$28 million, or 2.5%, mainly as a result of:
  - Higher expenses due partly to the previously mentioned reinsurance treaty on the charges covered by it and to business growth.
  - Offsetting decrease in expenses resulting from the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.

### 2.3.4 Treasury and Other Support to Desjardins Group Entities category

The Treasury and Other Support to Desjardins Group Entities category includes financial information that is not specific to a business segment. It mainly includes the Federation's treasury activities and those related to financial intermediation between liquidity surpluses and needs of the caisses, as well as orientation and organizational activities for Desjardins Group. This category also includes the operations of Desjardins Capital Inc., as well as Desjardins Technology Group Inc., which encompasses all of Desjardins Group's IT operations. In addition to various adjustments required to prepare the Consolidated Financial Statements, intersegment balance eliminations are classified in this category.

The Federation does not consider an item-by-item comparative analysis of the operations in this category to be relevant given the integration of various consolidation adjustments and intersegment balance eliminations. Consequently, it presents an analysis of these operations based on their contribution to surplus earnings.

**Table 13 – Treasury and Other Support to Desjardins Group Entities**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016
Treasury activities	\$ 52	\$ 113	\$ 110
Activities related to derivatives associated with hedging activities	(33)	89	27
Other <sup>(2)</sup>	(37)	(161)	(52)
<b>Net surplus earnings (deficit) before dividends to member caisses</b>	<b>(18)</b>	<b>41</b>	<b>85</b>
Dividends to member caisses, net of tax recovery	51	44	-
<b>Net surplus earnings (deficit) for the year</b>	<b>\$ (69)</b>	<b>\$ (3)</b>	<b>\$ 85</b>
Of which:			
Group's share	\$ (69)	\$ (3)	\$ 78
Non-controlling interests' share	-	-	7

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Includes support function activities, various adjustments required to prepare the Consolidated Financial Statements, and intersegment balance eliminations.

### COMPARISON OF 2018 AND 2017 – CONTRIBUTION BY TREASURY AND OTHER SUPPORT TO DESJARDINS GROUP ENTITIES TO SURPLUS EARNINGS

- **Net deficit of \$18 million before dividends to member caisses**, compared to net surplus earnings of \$41 million before dividends to member caisses in 2017.
  - **Treasury activities of \$52 million**, compared to a contribution of \$113 million to surplus earnings in 2017, mainly as a result of lower trading income because of high market volatility in 2018.
  - **Activities related to derivatives associated with hedging activities recorded a deficit of \$33 million**, compared to surplus earnings of \$89 million in 2017.
    - Less favourable change in the fair value of swaps in 2018 because the hike in interest rates was not as high as in 2017.
  - **Other activities recorded a \$37 million deficit**, compared to a \$161 million deficit in 2017.
    - Other activities were affected, in 2018 and 2017, by expenses related to the continued implementation of Desjardins-wide strategic projects (in particular, to improve systems and processes as well as to create innovative technology platforms mainly related to the digital transformation), thereby enhancing the member and client experience and improving productivity. Other activities also included contributions from the \$100 million fund as well as payments under the Desjardins Member Advantages program. In addition, certain technology assets were written off.
- The following items partly offset the deficit:
- Decrease in investment portfolio provisions.
  - Income tax recovery related to the remuneration of G capital shares and F capital shares.

## 2.4 Analysis of fourth quarter results and quarterly trends

**Table 14 – Results for the previous eight quarters**

(unaudited, in millions of dollars and as a percentage)								
	2018				2017			
	Q4 <sup>(1)</sup>	Q3 <sup>(1)(2)</sup>	Q2 <sup>(1)(2)</sup>	Q1 <sup>(1)(2)</sup>	Q4 <sup>(2)</sup>	Q3 <sup>(2)</sup>	Q2 <sup>(2)</sup>	Q1 <sup>(2)</sup>
Net interest income	\$ 398	\$ 382	\$ 353	\$ 368	\$ 357	\$ 364	\$ 344	\$ 339
Net premiums	2,246	2,288	2,225	2,164	2,034	2,007	2,099	2,006
Other operating income <sup>(3)</sup>								
Assessments	97	97	99	99	94	93	91	99
Service agreements	193	179	186	184	179	187	194	167
Lending fees and credit card service revenues	177	172	164	186	182	154	153	171
Brokerage and investment fund services	211	216	223	255	245	227	293	265
Management and custodial service fees	138	154	144	143	147	123	125	119
Foreign exchange income	29	15	21	27	22	16	21	18
Other	11	52	163	70	(78)	330	47	63
<b>Operating income<sup>(3)</sup></b>	<b>3,500</b>	<b>3,555</b>	<b>3,578</b>	<b>3,496</b>	<b>3,182</b>	<b>3,501</b>	<b>3,367</b>	<b>3,247</b>
Investment income (loss) <sup>(3)</sup>								
Net investment income (loss)	(42)	(213)	299	126	924	(316)	734	425
Overlay approach adjustment for insurance operations financial assets	258	76	20	169	N/A	N/A	N/A	N/A
	216	(137)	319	295	924	(316)	734	425
<b>Total income</b>	<b>3,716</b>	<b>3,418</b>	<b>3,897</b>	<b>3,791</b>	<b>4,106</b>	<b>3,185</b>	<b>4,101</b>	<b>3,672</b>
Provision for credit losses	63	73	63	89	74	72	59	73
Claims, benefits, annuities and changes in insurance contract liabilities	1,821	1,380	1,727	1,656	2,120	1,000	1,922	1,753
Non-interest expense	1,598	1,598	1,568	1,628	1,651	1,433	1,605	1,550
Income taxes on surplus earnings	6	68	75	59	80	89	100	67
<b>Surplus earnings before dividends to member caisses</b>	<b>228</b>	<b>299</b>	<b>464</b>	<b>359</b>	<b>181</b>	<b>591</b>	<b>415</b>	<b>229</b>
Dividends to member caisses, net of tax recovery	51	-	-	-	44	-	-	-
<b>Net surplus earnings for the period after dividends to member caisses</b>	<b>\$ 177</b>	<b>\$ 299</b>	<b>\$ 464</b>	<b>\$ 359</b>	<b>\$ 137</b>	<b>\$ 591</b>	<b>\$ 415</b>	<b>\$ 229</b>
Of which:								
Group's share	\$ 169	\$ 286	\$ 453	\$ 350	\$ 128	\$ 576	\$ 401	\$ 224
Non-controlling interests' share	8	13	11	9	9	15	14	5
<b>Contribution to consolidated surplus earnings by business segment</b>								
Personal and Business Services	\$ 52	\$ 72	\$ 71	\$ 106	\$ 62	\$ 86	\$ 85	\$ 84
Wealth Management and Life and Health Insurance	183	174	331	206	159	121	189	143
Property and Casualty Insurance	25	70	52	26	48	318	98	(18)
Treasury and Other Support to Desjardins Group Entities	(32)	(17)	10	21	(88)	66	43	20
	\$ 228	\$ 299	\$ 464	\$ 359	\$ 181	\$ 591	\$ 415	\$ 229
<b>Total assets</b>	<b>\$ 157,560</b>	<b>\$ 160,245</b>	<b>\$ 155,685</b>	<b>\$ 151,298</b>	<b>\$ 145,740</b>	<b>\$ 148,020</b>	<b>\$ 144,206</b>	<b>\$ 142,927</b>
<b>Indicators</b>								
Return on equity <sup>(3)</sup>	5.8%	7.1%	11.8%	9.4%	4.5%	15.3%	11.2%	6.5%
Tier 1A capital ratio	15.7	17.0	17.0	16.6	17.5	17.7	15.8	15.2
Total capital ratio	15.7	17.0	17.0	16.6	17.5	17.6	15.8	15.2

<sup>(1)</sup> The information presented for the 2018 quarters reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

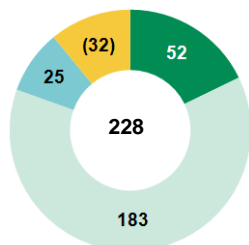
<sup>(2)</sup> Prior-period data have been reclassified to conform to the current year's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

<sup>(3)</sup> See "Basis of presentation of financial information".

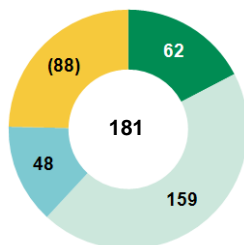
## FOURTH QUARTER CONSOLIDATED RESULTS

For the fourth quarter of 2018, the Federation posted surplus earnings before dividends to member caisses of \$228 million, up \$47 million, compared to the same period in 2017.

**2018 surplus earnings before dividends to member caisses<sup>(1)</sup>**  
(in millions of dollars)



**2017 surplus earnings before dividends to member caisses**  
(in millions of dollars)



■ Personal and Business Services  
■ Wealth Management and Life and Health Insurance  
■ Property and Casualty Insurance  
■ Treasury and Other Support to Desjardins Group Entities

<sup>(1)</sup> The information presented for the three-month period ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

### Contribution of segments to surplus earnings

- **Personal and Business Services: Contribution of \$52 million**, down \$10 million compared to the same period in 2017.
  - Decrease in trading income and income from new issues on the capital market.
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses for the winding-up of Zag Bank's operations.
  - Offset by business volume growth from payment and financing activities.
- **Wealth Management and Life and Health Insurance: Contribution of \$183 million**, up \$24 million compared to the same period in 2017, primarily due to:
  - More favourable claims experience.
  - Higher income from growth in assets under management.
 This increase was partially offset by:
  - Less favourable adjustments to actuarial assumptions made in the normal course of business.
  - Reduction in investment portfolio provisions.
- **Property and Casualty Insurance: Contribution of \$25 million**, down \$23 million compared to the same period in 2017, mainly as a result of:
  - Higher claims experience than in the previous period.
 This decrease was partially offset by:
  - Decrease in contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
  - Higher investment income.
- **Return on equity of 5.8%**, compared to 4.5% for the fourth quarter of 2017.
- **Operating income of \$3,500 million**, up \$318 million, or 10.0%.
- **Net interest income of \$398 million**, up \$41 million, or 11.5%, chiefly as a result of the growth of \$3.3 billion, or 5.6%, for the year in the entire portfolio of loans and acceptances outstanding, which includes financing operations in the area of consumer, credit card and other personal loans, as well as business and government loans.
- **Net premiums of \$2,246 million**, up \$212 million, or 10.4%.
  - **Wealth Management and Life and Health Insurance:** Net insurance and annuity premiums of \$1,134 million, up \$46 million, or 4.2%, compared to the same period in 2017.
    - ♦ Increase of \$34 million in annuity premiums.
    - ♦ Increase of \$7 million in individual insurance premiums.
    - ♦ Increase of \$5 million in group insurance premiums.
  - **Property and Casualty Insurance:** Net premiums of \$1,150 million, up \$167 million, or 17.0%, compared to the same period in 2017.
    - ♦ Increase of \$109 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, mainly as a result of the change in the cession rate stipulated in the treaty, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
    - ♦ Increase due to growth in the average premium and to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
- **Other operating income of \$856 million**, up \$65 million, or 8.2%, due to:
  - Decrease in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
  - Higher income from growth in assets under management.
  - Offset by a decrease in income following the Qtrade Canada Inc. transaction.

- **Investment income of \$216 million**, down \$708 million.
  - Decrease mainly due to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
    - ♦ Difference mostly due to changes in the fair value of the bond portfolio as a result of higher interest rates.
    - ♦ Decrease largely offset by the change in actuarial liabilities that in turn led to a decrease in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
  - Smaller change in the fair value of derivative financial instruments associated with the Federation's hedging operations.
  - Decrease in income generated by trading activities.
  - Offsetting decline in the fair value of matched bonds in the Property and Casualty Insurance segment was less than in the fourth quarter of 2017, due mainly to a lower increase in market interest rates in 2018 than that recorded in the corresponding quarter.
- **Total income of \$3,716 million**, down \$390 million, or 9.5%.
- **Provision for credit losses of \$63 million**, down \$11 million, or 14.9%.
  - Mainly as a result of the updating of parameters.
  - The adoption of IFRS 9 on January 1, 2018 made the allowance for credit losses more volatile.
  - The Federation continued to have a quality loan portfolio.
  - Ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.56%, compared to 0.14% as at December 31, 2017. This increase is due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered insignificant.
- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of \$1,821 million**, down \$299 million, or 14.1%.
  - **Wealth Management and Life and Health Insurance segment:** Expenses totalling \$962 million, down \$551 million, or 36.4%, compared to the same period in 2017, essentially as a result of the following:
    - ♦ Decrease of \$551 million in actuarial liabilities recognized under "Insurance contract liabilities", which included the effect of a decrease in the fair value of matched investments.
    - ♦ More favourable claims experience for products was offset by less favourable adjustments to changes to actuarial assumptions made in the normal course of business.
  - **Property and Casualty Insurance segment:** Claims expenses totalling \$857 million, up \$258 million, or 43.1%, compared to the same period in 2017, mainly due to the following:
    - ♦ Business growth leading to higher claims expenses.
    - ♦ Increase due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
    - ♦ Loss ratio of 70.8% for the fourth quarter of 2018, compared to 59.9% for the corresponding quarter of 2017.
      - Higher ratio due to less favourable developments in prior-year claims than in the fourth quarter of 2017: (10.1)% compared to (22.2)%.
      - Offset by less significant impact of catastrophes and major events in the corresponding quarter of 2017: 0.1% compared to 1.9%.
- **Non-interest expense of \$1,598 million**, down \$53 million, or 3.2%, compared to 2017.
  - Reduction in investment portfolio provisions.
  - Gain due to the impact of the change in the post-retirement benefit plan in fiscal 2018; for more information, see Note 16 "Net defined benefit plan liabilities", to the Consolidated Financial Statements.
  - Lower expenses as a result of the Qtrade Canada Inc. transaction.
 This decrease was partly offset by:
  - Increase in payroll related to indexing and growth in operations.
  - Write-off of some technology assets.
  - Expenses related to the winding-up of Zag Bank's operations.
  - Higher expenses as a result of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increase in expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Remuneration and other payments of \$140 million, up \$7 million, or 5.3%, compared to 2017.
    - ♦ Higher payments to member caisses as a result of the growth in caisse network sales of various Desjardins Group products such as Desjardins Funds.

## QUARTERLY TRENDS

Quarterly income, expenses and surplus earnings before dividends to member caisses are affected by certain trends, including seasonal variations, and by changes in general economic conditions and the capital markets. The Federation's results for the most recent eight quarters were therefore affected by developments in the global, U.S., Canadian and Quebec economies. With expected growth of 2.1% in Canadian real GDP in 2018, compared to 3.0% in 2017, and 2.3% versus 2.8% for Quebec, the Federation's results for the past eight quarters benefited from a growing GDP. Changes in the claims experience and actuarial assumptions may also cause significant variations from quarter to quarter. Lastly, the past eight quarters were affected by the low interest rate environment that continued in 2017 and 2018. However, as of the third quarter of 2017, there were five hikes in Canada's key interest rates as a result of monetary tightening.

## Consolidated surplus earnings

- Trend in surplus earnings before dividends to member caisses was chiefly affected by the change in claims experience from one quarter to the next.
- Growth in income from assets under management throughout 2018.
- Second quarter 2018 results affected by the gain of \$129 million on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P., completed on April 1, 2018, as part of the creation of Aviso Wealth.
- Solid investment performance in the Wealth Management and Life and Health Insurance segment, which contributed to the higher surplus earnings for the second quarter of 2017.
- Fourth quarter of 2017 affected by smaller favourable developments in prior-year automobile insurance claims and a higher claims experience for the current year.
- 2017 third quarter results affected by a gain of \$249 million, net of expenses and after income taxes, on the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.

## Consolidated results

- **Operating income – Upward trend for 2018 and 2017 quarters, except in the fourth quarters.**
  - Operations growth allowed the Federation to grow operating income, in particular premium income.
  - Increase in net premiums due mainly to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Growth in business volume of payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios in 2018, as well as in assets under management.
  - Increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations in the fourth quarter of 2018 and in the fourth quarter of 2017, which reduced operating income.
  - Operating income for the second quarter of 2018 was affected by the gain on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P., completed on April 1, 2018, while income from brokerage and investment fund services was down following this transaction, namely during the last three quarters of 2018.
  - Operating income for the third quarter of 2017 was affected by the gain on the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.
- **Investment income – Fluctuations mainly a result of market volatility leading to changes in the fair value of assets backing liabilities related to life and health insurance operations.** On account of a matching strategy, these fluctuations were offset by a change in actuarial liabilities, the effect of which was reflected in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
- **Provision for credit losses – Slightly up when the 2018 and 2017 quarters are compared, except in fourth quarter 2018.**
  - Explained mainly by the growth in outstandings and the adoption of IFRS 9 as at January 1, 2018. This new standard led to volatility in results following the revision of economic scenarios, the updating of parameters and the migration of borrower ratings.
  - Updating of parameters led to a drop in the provision for credit losses in fourth quarter 2018.
  - Ratio for gross credit-impaired loans, as a percentage of the total portfolio of gross loans and acceptances, has been trending up for the 2018 quarters compared to the 2017 quarters. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered insignificant. The Federation has continued to have a quality loan portfolio.
- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities – Quarterly fluctuations.**
  - Growth in business leading to an increase in claims expenses.
  - All the 2018 quarters were affected by increased claims resulting from the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Expenses mainly affected by a change in the fair value of investments associated with life and health insurance activities in 2018, whose impact was particularly strong in the third quarter of 2017.
  - Expenses affected by the higher loss ratios for property and casualty insurance in 2018.
  - The second and third quarters of 2018 were affected by three catastrophes in all, while the second quarter of 2017 was affected by one catastrophe.
  - Fiscal 2018 was affected by four major events compared to nine in fiscal 2017.
  - 2017 fourth quarter results were affected by a less significant favourable trend in prior-year automobile insurance claims and a higher claims experience for the current year.
- **Non-interest expense – Relatively stable when 2018 and 2017 quarters are compared.**
  - The reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations with regard to the charges covered by the treaty and business growth, particularly growth in payment and financing activities and in assets under management, led to increases in non-interest expense.
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios for the 2018 quarters.
  - Transaction involving Qtrade Canada Inc. was completed on April 1, 2018, reducing non-interest expense for the last three quarters of 2018.
  - Sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017, reducing non-interest expense as of the third quarter of 2017.
  - Remuneration and other payments included in non-interest expense have been rising, when the 2018 and 2017 quarters are compared, because of the increased sales of various Desjardins Group products by the caisse network.

## Surplus earnings from business segments

- **Surplus earnings before dividends to member caisses of the Personal and Business Services segment – Trending down when 2018 and 2017 quarters are compared.**
  - Decline in income from trading and from new issues on capital markets in 2018.
  - Net interest income up on account of growth in the entire average portfolio of loans and acceptances outstanding.
  - Increase in expenses related to the acquisition and set-up of new Canada-wide credit card portfolios, which affected the 2018 quarters.
  - Expenses related to the winding-up of Zag Bank's operations in third and fourth quarters of 2018.
  - Profit on the restructuring of Interac Corp. in first quarter 2018.
- **Net surplus earnings of the Wealth Management and Life and Health Insurance segment fluctuating over the past eight quarters.**
  - More favourable claims experience for almost all business lines, which affected net surplus earnings positively over the last three quarters of 2018 and the first two quarters of 2017.
  - 2018 second quarter results were affected by the \$129 million gain on the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P., which was completed on April 1, 2018.
  - Income growth related to assets under management during 2018.
  - Higher surplus earnings for fourth quarter 2017, mainly due to favourable adjustments to the actuarial assumptions and partly offset by deterioration in claims experience.
  - Solid investment performance, which also contributed to higher surplus earnings in the second quarter of 2017.
- **Net surplus earnings of the Property and Casualty Insurance segment fluctuating over the past eight quarters.**
  - Larger increase in the cost of claims for the 2018 quarters as a result of business growth and the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which affected each quarter.
  - Results for the second and third quarters of 2018 were affected by three catastrophes, namely damage caused by water and winds in April, by wind in May and damage caused by high winds and tornadoes, mainly in the Ottawa and Gatineau regions in September.
  - Smaller increase in the first and fourth quarter of 2018 compared to the 2017 quarters in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
  - 2017 fourth quarter results were affected by less significant favourable developments in prior-year automobile insurance claims and by a higher claims experience for the current year.
  - 2017 third quarter results were affected by a \$241 million gain, net of expenses and after taxes, on the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.
  - The first quarter of 2017 was affected by higher claims experience for the current year because of unfavourable winter weather conditions, with damage caused by water and major snowfalls in Quebec and the windstorm in Ontario.

# 3.0 Balance sheet review

## 3.1 Balance sheet management

**Table 15 – Consolidated Balance Sheets**

As at December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>		2017		2016	
<b>Assets</b>						
Cash and deposits with financial institutions	\$ 2,738	1.7%	\$ 1,731	1.2%	\$ 1,212	0.9%
Securities	49,666	31.5	46,904	32.2	44,937	33.4
Securities borrowed or purchased under reverse repurchase agreements	14,086	8.9	9,377	6.4	7,713	5.7
Net loans and acceptances	61,997	39.3	58,715	40.3	52,441	38.9
Segregated fund net assets	13,234	8.4	13,379	9.2	11,965	8.9
Derivative financial instruments	4,376	2.8	3,772	2.6	3,706	2.8
Other assets	11,463	7.4	11,862	8.1	12,684	9.4
<b>Total assets</b>	<b>\$ 157,560</b>	<b>100.0%</b>	<b>\$ 145,740</b>	<b>100.0%</b>	<b>\$ 134,658</b>	<b>100.0%</b>
<b>Liabilities and equity</b>						
Deposits	\$ 58,057	36.8%	\$ 52,149	35.8%	\$ 46,902	34.8%
Commitments related to securities sold short	10,829	6.9	9,112	6.3	8,196	6.1
Commitments related to securities lent or sold under repurchase agreements	16,233	10.3	10,062	6.9	9,870	7.3
Derivative financial instruments	3,332	2.1	3,677	2.5	2,540	1.9
Insurance contract liabilities	28,764	18.3	28,300	19.4	27,493	20.4
Segregated fund net liabilities	13,212	8.4	13,354	9.2	11,957	8.9
Other liabilities	11,202	7.1	11,679	7.9	11,642	8.7
Subordinated notes	1,378	0.9	1,388	1.0	1,378	1.0
Equity	14,553	9.2	16,019	11.0	14,680	10.9
<b>Total liabilities and equity</b>	<b>\$ 157,560</b>	<b>100.0%</b>	<b>\$ 145,740</b>	<b>100.0%</b>	<b>\$ 134,658</b>	<b>100.0%</b>

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

## TOTAL ASSETS

As at December 31, 2018, the Federation's total assets stood at \$157.6 billion, up by \$11.8 billion, or 8.1%, over the year, compared to growth of \$11.1 billion, or 8.2%, for 2017. This growth was largely due to an increase in securities, including those borrowed or purchased under reverse repurchase agreements, as well as net loans and acceptances.

## CASH AND DEPOSITS WITH FINANCIAL INSTITUTIONS, AND SECURITIES

As at December 31, 2018, the Federation's cash and deposits with financial institutions amounted to \$2.7 billion, an increase of \$1.0 billion, or 58.2%, over the year, compared to an increase of \$519 million, or 42.8%, in 2017. Securities, including those borrowed or purchased under reverse repurchase agreements, totalled \$63.8 billion, for a year-over-year increase of \$7.5 billion, or 13.3%, compared to a volume of \$56.3 billion at the end of 2017, for an increase of \$3.6 billion, or 6.9%. The Federation's market and deposit activities generated this increase.

## LOANS AND CLIENTS' LIABILITY UNDER ACCEPTANCES

As at December 31, 2018, the Federation's outstanding loan portfolio, including acceptances, net of the provision for credit losses, was \$62.0 billion, an increase of \$3.3 billion, or 5.6%, compared to growth of \$6.3 billion, or 12.0%, during 2017. Among the different borrower categories presented in Table 16 are loans to business and government, which accounted for 61.1% of the Federation's total portfolio as at December 31, 2018. The amount outstanding on that date was \$38.2 billion, up \$1.1 billion, or 3.0%, since December 31, 2017 compared to an increase of \$3.6 billion, or 10.8%, a year earlier.

**Table 16 – Loans and acceptances**

As at December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>		2017		2016	
Residential mortgages	\$ 4,626	7.4%	\$ 4,323	7.3%	\$ 3,486	6.6%
Consumer, credit card and other personal loans	19,710	31.5	17,547	29.8	15,720	29.9
Business and government	38,152	61.1	37,043	62.9	33,427	63.5
	62,488	100.0%	58,913	100.0%	52,633	100.0%
Provision for credit losses	(491)		(198)		(192)	
<b>Total loans and acceptances by borrower category</b>	<b>\$ 61,997</b>		<b>\$ 58,715</b>		<b>\$ 52,441</b>	
Loans guaranteed or insured <sup>(2)</sup>	\$ 5,343		\$ 5,609		\$ 5,196	
Loans guaranteed or insured <sup>(2)</sup> as a percentage of total gross loans and acceptances	8.6%		9.5%		9.9%	

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated.

For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Loans fully or partially guaranteed or insured by a public or private insurer or a government.

Consumer, credit card and other personal loans accounted for 31.5% of the Federation's total loan portfolio as at December 31, 2018. These loans increased by \$2.2 billion, or 12.3%, over the year, to total \$19.7 billion at year-end, compared to growth of \$1.8 billion, or 11.6%, as at December 31, 2017. Consumer loans generated most of this growth as a result, in particular, of an increase in loans related to automobile and durable goods financing.

The Federation's outstanding residential mortgages, which accounted for 7.4% of its total portfolio, totalled \$4.6 billion as at December 31, 2018, for an increase of \$303 million, or 7.0%, since December 31, 2017, compared to an increase of \$837 million, or 24.0%, a year earlier.

### Credit quality

Information about the quality of the Federation's loan portfolio is presented in Section 4.2, "Risk management", on pages 67 to 70 of this MD&A.

## DEPOSITS

**Table 17 – Deposits**

As at December 31

(in millions of dollars and as a percentage)	2018					2017		2016	
	Payable on demand	Payable upon notice	Payable on a fixed date	Total		Total		Total	
Individuals	\$ 2,961	\$ 41	\$ 1,103	\$ 4,105	7.1%	\$ 4,353	8.3%	\$ 3,817	8.1%
Business and government	3,274	-	42,724	45,998	79.2	40,963	78.6	36,780	78.5
Deposit-taking institutions	4,448	-	3,506	7,954	13.7	6,833	13.1	6,305	13.4
<b>Total deposits</b>	<b>\$ 10,683</b>	<b>\$ 41</b>	<b>\$ 47,333</b>	<b>\$ 58,057</b>	<b>100.0%</b>	<b>\$ 52,149</b>	<b>100.0%</b>	<b>\$ 46,902</b>	<b>100.0%</b>

As at December 31, 2018, the Federation's outstanding deposits totalled \$58.1 billion, up by \$5.9 billion, or 11.3%, since the end of 2017, compared to an increase of \$5.2 billion, or 11.2%, a year earlier. This increase was largely the result of growth in the Federation's business and government deposits, which accounted for 79.2% of its total outstanding deposit portfolio as at the end of 2018. Business and government loans outstanding amounted to \$46.0 billion as at December 31, 2018, up \$5.0 billion, or 12.3%, since December 31, 2017, compared to an increase of \$4.2 billion, or 11.4%, a year earlier. This increase was largely due to the various securities, including commercial paper and covered bonds, issued on U.S., Canadian and European markets, which supported the growth in Desjardins Group's funding requirements.

Deposits from deposit-taking institutions stood at \$8.0 billion as at December 31, 2018, up \$1.1 billion, or 16.4%, compared to an increase of \$528 million, or 8.4% a year earlier. Deposits from individuals totalled \$4.1 billion at year-end 2018, down \$248 million, or 5.7%, since the end of 2017, compared to an increase of \$536 million, or 14.0%, in 2017.

## INSURANCE CONTRACT LIABILITIES

As at December 31, 2018, the Federation's insurance contract liabilities were \$28.8 billion, up \$464 million, or 1.6%, from December 31, 2017, compared to an \$807 million, or 2.9%, increase observed a year earlier. This growth is partially due to a \$273 million increase in unearned premiums and higher actuarial liabilities as a result of life and health insurance operations, which grew by \$125 million.

Note 15, "Insurance contract liabilities", to the Annual Consolidated Financial Statements provides additional information about these liabilities of the Federation.

## EQUITY

As at December 31, 2018, equity totalled \$14.6 billion, down \$1.5 billion, or 9.2%, since the end of 2017, compared to an increase of \$1.3 billion, or 9.1%, a year earlier. Net surplus earnings after dividends to member caisses, totalling \$1,299 million, were a source of this growth. In addition, the Federation issued F capital shares for proceeds of \$124 million, net of issuance expenses, as well as F capital shares having a value of \$142 million for the payment of interest when a holder has elected to receive remuneration in F capital shares. Payments of \$1,854 million to member caisses as well as remuneration of \$508 million on capital shares, and the impact of changes in accounting policies amounting to \$214 million reduced equity.

Note 21, "Capital stock", to the Annual Consolidated Financial Statements provides additional information about the Federation's capital stock.

## 3.2 Capital management

Capital management is crucial to the financial management of Desjardins Group as a whole, including the Federation. Its goal is to ensure that the capital level and structure of Desjardins Group and its components are consistent with their risk profile, distinctive nature and cooperative objectives. Capital management must also ensure that the capital structure is adequate in terms of protection for members and clients, profitability targets, growth objectives, rating agencies' expectations and regulators' requirements. In addition, it must optimize the allocation of capital and internal capital flow mechanisms, and support growth, development and asset risk management at Desjardins Group.

Desjardins Group advocates prudent management of its capital. Its purpose is to maintain higher regulatory capital ratios than those of the Canadian banking industry and regulatory requirements. Desjardins's prudent capital management is reflected in the quality of the credit ratings assigned by the various rating agencies.

The financial industry is placing more emphasis on sound capitalization of its operations. Now more than ever, rating agencies and the market favour the best-capitalized institutions. These factors argue in favour of a general increase in the level and quality of capital issued by financial institutions. This is also reflected in the enhanced requirements under Basel III implemented on January 1, 2013.

### Desjardins Group's Integrated Capital Management Framework

Broadly speaking, Desjardins Group's Integrated Capital Management Framework includes the policies and processes required to set targets for its capitalization, to establish strategies to ensure that targets are met, to quickly raise capital, to ensure that the components contribute appropriately to capitalization, and to optimize internal capital flow and use procedures.

In addition, the Internal Capital Adequacy Assessment Program (ICAAP) enables Desjardins Group to ensure it has an appropriate level of capital to cover all the significant risks to which it is exposed and to implement capital management strategies that take into account changes in its risk profile.

Desjardins Group has developed a stress-testing program aimed at establishing and measuring the effect of various integrated scenarios, i.e. to simulate various economic scenarios and to assess their financial and regulatory repercussions. This process makes it possible to determine if the minimum capital target, as established in the capitalization plan, is adequate in view of the risks to which Desjardins Group is exposed. Additional information on the ICAAP and the stress-testing program is presented in Section 4.2 "Risk management".

### Regulatory framework and internal policies

Desjardins Group's capital management is the responsibility of the Federation's Board of Directors. To support it with this task, it has mandated the Management Committee, through the Finance and Risk Management Committee, to ensure that Desjardins Group, including the Federation, has a sufficient capital base in light of the organization's strategic objectives and regulatory obligations. The Finance, Treasury and Administration Executive Division is responsible for preparing, on an annual basis, a capitalization plan to forecast capital trends, devise strategies and recommend action plans for achieving capital objectives and targets.

The current situation and the forecasts show that overall, Desjardins Group, including the Federation, has a solid capital base that maintains it among the best-capitalized financial institutions.

The Federation's regulatory capital ratios are calculated according to the AMF's guideline on adequacy of capital base standards applicable to financial services cooperatives (the guideline). This guideline takes into account the global regulatory framework for more resilient banks and banking systems (Basel III) issued by the Bank for International Settlements.

The minimum amount of Tier 1A capital that the Federation must maintain is 8%. In addition, the Tier 1 and total capital ratios must be above 9.5% and 11.5%, respectively. The minimum requirement for the leverage ratio is 3%.

This capital takes into consideration investments made in subsidiaries of the Federation. Some of these subsidiaries are subject to separate requirements regarding regulatory capital, liquidity and financing, which are set by regulatory authorities governing banks, insurers and securities, in particular. The Federation oversees and manages the capital requirements of these entities to ensure efficient use of capital and continuous compliance with the applicable regulation.

In this regard, it should be mentioned that the life and health insurance subsidiaries under provincial jurisdiction are subject to the Capital Adequacy Requirements Guideline (CARLI) issued by the AMF. The property and casualty insurance subsidiaries under provincial jurisdiction must comply with the Guideline on Capital Adequacy Requirements issued by the AMF. The property and casualty insurance subsidiaries under federal jurisdiction must comply with the OSFI's Minimum Capital Test (MCT) Guideline for federally regulated property and casualty insurance companies. Developments in these guidelines are presented in the "Changes in the regulatory environment" section of this MD&A.

For the purpose of calculating capital, Desjardins Financial Corporation Inc., the holding corporation that mainly includes the insurance companies, has been deconsolidated and presented as a partial capital deduction under the rules for significant investments stated in the guideline. Furthermore, Desjardins Financial Corporation Inc. is subject to the AMF's CARLI guideline.

### Regulatory developments

Desjardins Group continues to monitor changes in capital requirements under the global standards developed by the Basel Committee on Banking Supervision (BCBS) and to assess their impact on the capital ratios and the leverage ratio.

On October 25, 2017, the BCBS issued a guideline entitled "Identification and management of step-in risk", aimed at measuring the risk related to the support that a financial institution could give an unconsolidated entity, should such entity find itself in financial distress, even beyond or in the absence of contractual obligations. The proposed framework does not call for capital requirements to be automatically added to those required under present Basel standards. It is scheduled to come into force in 2020.

On December 7, 2017, the BCBS issued a discussion paper on the regulatory treatment of sovereign exposures. Comments on the topic could be sent to the BCBS until March 9, 2018. The BCBS did not obtain a consensus in order to make changes to the treatment of exposures to sovereign risk.

On December 7, 2017, the Group of Central Bank Governors and Heads of Supervision, the BCBS's oversight body, endorsed the outstanding Basel III post-crisis regulatory reforms. The reforms are intended to help reduce excessive variability in risk-weighted assets (RWA) and improve the comparability and transparency of financial institutions' capital ratios by:

- enhancing the robustness and risk sensitivity of the standardized approaches for credit risk, credit valuation adjustment (CVA) risk and operational risk;
- constraining the use of the internal model approaches, by placing limits on certain inputs used to calculate capital requirements under the Internal Ratings-Based (IRB) approach for credit risk and by removing the use of the internal model approaches for the CVA risk and for operational risk;
- adjusting the leverage ratio exposure measurement; and
- replacing the existing Basel I output floor with a more robust risk-sensitive floor based on the revised Basel III standardized approaches.

The BCBS has scheduled the implementation of these reforms for January 1, 2022 and the transitional provisions for applying the output floor based on the revised Basel III standardized approach.

On March 22, 2018, the BCBS issued a consultative document entitled "Revisions to the minimum capital requirements for market risk", which addresses certain issues raised following the publication on January 14, 2016 of the revised version of the minimum capital requirements for market risk. The consultative document includes proposed changes aimed, in particular, at increasing the risk sensitivity of the standardized approach and recalibrating risk weights for interest risk, equity risk and foreign exchange risk. It also proposes changes to the "Simplified alternative to the standardised approach to market risk capital requirements" issued on June 29, 2017. On December 7, 2017, the BCBS had announced that financial institutions should present information using the standardized approach as of January 1, 2022.

On July 16, 2018, the OSFI released a discussion paper on the proposed implementation timetable for the recent Basel III reforms in Canada. The paper also details the OSFI's views on some of the proposed changes. The AMF has not yet expressed its opinion of the timetable for adopting the new reforms.

Finally, in November 2018, the guideline on adequacy of capital base standards for financial services cooperatives issued by the AMF was revised and it is expected to be effective on March 31, 2019. The main changes cover the following elements:

- Introduction of TLAC provisions;
- Revision of the framework for securitization;
- Implementation of the standardized approach for counterparty credit risk (SA-CCR) and the revised capital requirements for bank exposure to central counterparties;
- Raising of the minimum requirement for the leverage ratio to 3.5% for institutions designated as D-SIFI;
- Introduction of provisions regarding the countercyclical buffer;
- Revision of the Pillar 3 standard;
- Introduction of a new output floor for risk-weighted assets: Since the adoption of the Basel III framework in 2008, the AMF has imposed a requirement regarding the capital output floor for institutions that apply the advanced internal ratings-based approach (credit risk or operational risk). This capital output floor was determined according to Basel I requirements rather than the Basel II standardized approach. For the first quarter of 2019, the AMF is proposing a new capital output floor based on the revised Basel III standardized approach.

The "Changes in the regulatory environment" section presents additional details on regulation as it affects all Desjardins Group operations. In addition, this section contains information on the internal recapitalization (bail-in) file, or the TLAC guideline project.

## Compliance with requirements

As at December 31, 2018, the Tier 1A, Tier 1 and total capital ratios, calculated in accordance with Basel III requirements, were all 15.7%. The leverage ratio was 7.4%.

The Federation and its subsidiaries, which are subject to minimum regulatory requirements with respect to capitalization were in compliance with said requirements as at December 31, 2018.

## Regulatory capital

The following tables present the Federation's main capital components, regulatory capital, capital ratios, movements in capital over the year and risk-weighted assets.

**Table 18 – Main capital components**

Total capital			
Tier 1 capital		Tier 2 capital	
	Tier 1A <sup>(1)</sup>	Tier 1B <sup>(1)</sup>	
<b>Eligible items</b>	<ul style="list-style-type: none"> <li>• Reserves and undistributed surplus earnings</li> <li>• Eligible accumulated other comprehensive income</li> <li>• Capital shares</li> </ul>	<ul style="list-style-type: none"> <li>• Non-controlling interests<sup>(2)</sup></li> </ul>	<ul style="list-style-type: none"> <li>• General allowance</li> <li>• Subordinated notes subject to phase-out</li> <li>• Eligible qualifying shares</li> </ul>
<b>Regulatory adjustments</b>	<ul style="list-style-type: none"> <li>• Goodwill</li> <li>• Software</li> <li>• Other intangible assets</li> <li>• Deferred tax assets essentially resulting from loss carryforwards</li> <li>• Shortfall in allowance</li> <li>• Cross-investments<sup>(3)</sup></li> </ul>		
<b>Deductions</b>	<ul style="list-style-type: none"> <li>• Mainly significant investments in financial institutions<sup>(4)</sup></li> </ul>		<ul style="list-style-type: none"> <li>• Investment in preferred shares of a component deconsolidated for regulatory capital purposes</li> <li>• Subordinated financial instrument</li> </ul>

<sup>(1)</sup> The Tier 1A and Tier 1B ratios are the equivalent of the financial institutions' CET1 and AT1 ratios, for financial services cooperatives regulated by the AMF.

<sup>(2)</sup> The amount of non-controlling interests is determined, in particular, based on the nature of the operations and the capitalization level of the investee.

<sup>(3)</sup> Cross-investments in Tier 1A capital of the Desjardins caisse network in Quebec.

<sup>(4)</sup> Represent the portion of investments in the components deconsolidated for regulatory capital purposes (mainly Desjardins Financial Corporation Inc.) that exceeds 10% of capital net of regulatory adjustments. In addition, when the non-deducted balance, plus deferred tax assets net of corresponding deferred tax liabilities, exceeds 15% of the adjusted capital, the surplus is also deducted from this capital. The net non-deducted balance will be subject to risk-weighting at a rate of 250%.

**Table 19 – Regulatory capital**

As at December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017
<b>Tier 1A capital</b>		
Federation's capital shares	\$ 4,767	\$ 4,501
Other capital shares	4,012	4,036
Reserves	271	540
Undistributed surplus earnings	4,754	5,655
Eligible accumulated other comprehensive income	(1)	456
Deductions <sup>(2)(3)</sup>	(3,906)	(6,026)
<b>Total Tier 1A capital</b>	<b>9,897</b>	<b>9,162</b>
Non-controlling interests	-	13
Deductions <sup>(2)</sup>	-	(13)
<b>Total Tier 1B capital</b>	<b>-</b>	<b>-</b>
<b>Total Tier 1 capital</b>	<b>9,897</b>	<b>9,162</b>
<b>Tier 2 capital</b>		
Subordinated notes subject to phase-out	844	1,032
General allowance	271	126
Deductions <sup>(2)</sup>	(1,115)	(1,158)
<b>Total Tier 2 capital</b>	<b>-</b>	<b>-</b>
<b>Total regulatory capital (Tiers 1 and 2)</b>	<b>\$ 9,897</b>	<b>\$ 9,162</b>
<b>Ratios and leverage ratio exposure</b>		
Tier 1A capital ratio <sup>(4)</sup>	15.7%	17.5%
Tier 1 capital ratio <sup>(4)</sup>	15.7	17.5
Total capital ratio <sup>(4)</sup>	15.7	17.5
Leverage ratio <sup>(5)</sup>	7.4	7.9
Leverage ratio exposure	\$ 134,198	\$ 115,915

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> As prescribed by the guideline, when an entity is required to make a deduction from a given capital component but is not adequately provisioned, the difference is deducted from the component of the next highest quality. If Tier 2 capital is insufficient to absorb a deduction, the undeducted portion will be deducted from Tier 1B, and then from Tier 1A, if necessary.

<sup>(3)</sup> Deductions from Tier 1A are comprised of regulatory adjustments (\$499 million in 2018 and \$2,152 million in 2017), of which cross-investments (\$14 million in 2018 and \$1,634 million in 2017), significant investments (\$2,858 million in 2018 and \$3,137 million in 2017), and items that could not be deducted from Tiers 1B and 2 because of insufficient capital in these tiers (\$549 million in 2018 and \$737 million in 2017).

<sup>(4)</sup> As prescribed by the guideline, the capital ratios are expressed as a percentage of regulatory capital to risk-weighted assets.

<sup>(5)</sup> The leverage ratio is calculated by dividing Tier 1 capital by the exposure measure, which is independent of risk and includes 1) on-balance sheet exposures 2) securities financing transaction exposures, 3) derivative exposures, and 4) off-balance sheet items.

In compliance with Basel III requirements, capital instruments that no longer meet the eligibility criteria for capital tiers have been excluded from them effective January 1, 2013, as prescribed. In accordance with the transitional provisions set out in the guideline, instruments that meet certain conditions are being phased out from capital at an annual rate of 10% over a nine-year period that began on January 1, 2013. The subordinated notes issued by Desjardins Capital Inc. are also subject to the 10% amortization. In order to be fully eligible for Tier 2 capital, such notes must meet Non-Viability Contingent Capital (NVCC) requirements. Desjardins Group has not issued any instruments of this type as discussions concerning the application of these regulations by Desjardins Group are still in progress with the AMF.

On March 24, 2018, Desjardins's Annual General Meeting approved the distribution to member caisses of net income of \$60 million in respect of the G capital shares.

On November 13, 2018, the Federation's Board of Directors approved the distribution to member caisses of net income of \$1,847 million in respect of the FIN-5A capital shares. In addition, on December 6, 2018, the Federation's Board of Directors approved the distribution to member caisses of net income of \$60 million and \$26 million, respectively, for G and INV capital shares.

On December 21, 2018, the Federation filed a new short-form prospectus and obtained a receipt allowing it to issue, in the 12 months following the date of the receipt, F capital shares for a maximum amount of \$125 million. This new issue started on January 15, 2019. During 2018, the Federation issued F capital shares for proceeds of \$124 million, net of issuance expenses. It also issued F capital shares for an amount of \$142 million in order to pay interest where a holder elected to receive remuneration in F capital shares.

As at December 31, 2018, the Tier 1A capital ratio was down 182 basis points compared to December 31, 2017. The positive impact of growth in surplus earnings and the issuance of F capital shares was offset by the increase in risk-weighted assets, the transition to IFRS 9 and a decrease in accumulated other comprehensive income.

**Table 20 – Change in regulatory capital**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017
<b>Tier 1A capital</b>		
Balance at beginning of year	\$ 9,162	\$ 7,317
Increase in reserves and undistributed surplus earnings <sup>(2)</sup>	(1,170)	906
Eligible accumulated other comprehensive income	(457)	70
Federation's capital shares	266	374
Other capital shares	(24)	97
Non-controlling interests	-	(32)
Deductions	2,120	430
Balance at end of year	9,897	9,162
<b>Tier 1B capital</b>		
Balance at beginning of year	-	-
Non-controlling interests	(13)	(6)
Deductions	13	6
Balance at end of year	-	-
<b>Total Tier 1 capital</b>	9,897	9,162
<b>Tier 2 capital</b>		
Balance at beginning of year	-	-
Non-controlling interests	-	(6)
Senior notes subject to phase-out	(188)	(168)
General allowance	145	(6)
Deductions	43	180
Balance at end of year	-	-
<b>Total capital</b>	\$ 9,897	\$ 9,162

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Amount including the change in defined benefit pension plan liabilities.

**Risk-weighted assets (RWA)**

The Federation calculates the risk-weighted assets for credit risk, market risk and operational risk. Since March 2009, it has been using the Internal Ratings-Based Approach for credit risk related to retail loan portfolios – Personal. Other exposures to credit risk are measured according to the Standardized Approach. On June 19, 2017, the Federation received the AMF's authorization to use the Standardized Approach for calculating operational risk as of June 30, 2017. On June 29, 2018, the Federation received the AMF's approval to use market risk internal models for trading portfolios while continuing to use the Standardized Approach for foreign exchange risk and commodity risk in the banking portfolio as of September 30, 2018.

As indicated in the table below, risk-weighted assets totalled \$63.1 billion as at December 31, 2018. Of this amount, \$49.1 billion was for credit risk, \$5.4 billion for market risk and \$8.6 billion for operational risk. As at December 31, 2017, risk-weighted assets stood at \$52.4 billion.

Table 21 - Risk-weighted assets

	Internal Ratings-Based Approach		Standardized Approach		Total as at December 31, 2018				Total as at December 31, 2017
(in millions of dollars and as a percentage)	Exposure (1)	Risk-weighted assets	Exposure (1)	Risk-weighted assets	Exposure (1)	Risk-weighted assets	Capital requirement (2)	Average risk weighting rate	Risk-weighted assets
<b>Credit risk other than counterparty risk</b>									
Sovereign borrowers	\$ -	\$ -	\$ 5,777	\$ -	\$ 5,777	\$ -	\$ -	-%	\$ 21
Financial institutions	-	-	41,033	8,210	41,033	8,210	657	20.0	7,601
Businesses	-	-	16,207	15,846	16,207	15,846	1,268	97.8	12,989
Securitized assets	-	-	5	63	5	63	5	1,250.0	75
Equities	-	-	250	334	250	334	26	133.6	241
SMEs similar to other retail client exposures	-	-	2,195	1,686	2,195	1,686	135	76.8	1,288
Mortgages	2,191	281	435	152	2,626	433	35	16.5	329
Other retail client exposures (excluding SMEs)	6,994	3,802	1,056	793	8,050	4,595	368	57.1	3,207
Qualifying revolving retail client exposures	31,499	9,156	-	-	31,499	9,156	732	29.1	8,110
<b>Subtotal - Credit risk other than counterparty risk</b>	<b>40,684</b>	<b>13,239</b>	<b>66,958</b>	<b>27,084</b>	<b>107,642</b>	<b>40,323</b>	<b>3,226</b>	<b>37.5</b>	<b>33,861</b>
<b>Counterparty risk</b>									
Sovereign borrowers	-	-	8	-	8	-	-	-	-
Financial institutions	-	-	2,770	554	2,770	554	45	20.0	343
Businesses	-	-	13	12	13	12	1	92.3	4
Trading portfolio	-	-	1,284	543	1,284	543	43	42.3	374
Credit valuation adjustment charge	-	-	-	-	-	1,459	117	-	910
Additional requirements for banking and trading portfolio	-	-	-	-	264	14	1	-	1
<b>Subtotal - Counterparty risk</b>	<b>-</b>	<b>-</b>	<b>4,075</b>	<b>1,109</b>	<b>4,339</b>	<b>2,582</b>	<b>207</b>	<b>59.5</b>	<b>1,632</b>
Other assets <sup>(3)</sup>	-	-	-	-	14,366	5,722	458	39.8	6,340
Scaling factor <sup>(4)</sup>	-	794	-	-	-	794	64	-	677
<b>Total credit risk</b>	<b>40,684</b>	<b>14,033</b>	<b>71,033</b>	<b>28,193</b>	<b>126,347</b>	<b>49,421</b>	<b>3,955</b>	<b>39.1</b>	<b>42,510</b>
<b>Market risk</b>									
Value at Risk (VaR)	-	575	-	-	-	575	46	-	-
Stressed Value at Risk (SVaR)	-	2,335	-	-	-	2,335	187	-	-
Incremental risk charge (IRC) <sup>(5)</sup>	-	1,732	-	-	-	1,732	139	-	-
Other <sup>(6)</sup>	-	-	-	754	-	754	60	-	1,965
<b>Total market risk<sup>(7)</sup></b>	<b>-</b>	<b>4,642</b>	<b>-</b>	<b>754</b>	<b>-</b>	<b>5,396</b>	<b>432</b>	<b>-</b>	<b>1,965</b>
<b>Operational risk<sup>(8)</sup></b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>8,581</b>	<b>-</b>	<b>8,581</b>	<b>686</b>	<b>-</b>	<b>8,143</b>
<b>Total risk-weighted assets before threshold</b>	<b>40,684</b>	<b>18,675</b>	<b>71,033</b>	<b>37,528</b>	<b>126,347</b>	<b>63,398</b>	<b>5,073</b>	<b>-</b>	<b>52,618</b>
<b>Risk-weighted assets (RWA) after the transitional provisions for the credit valuation adjustment charge<sup>(9)</sup></b>									
RWA for Tier 1A capital	-	-	-	-	-	63,106	5,048	-	52,364
RWA for Tier 1 capital	-	-	-	-	-	63,150	5,052	-	52,409
RWA for total capital	-	-	-	-	-	63,193	5,055	-	52,445
<b>Total risk-weighted assets</b>	<b>\$ 40,684</b>	<b>\$ 18,675</b>	<b>\$ 71,033</b>	<b>\$ 37,528</b>	<b>\$ 126,347</b>	<b>\$ 63,106</b>	<b>\$ 5,048</b>	<b>-%</b>	<b>\$ 52,364</b>

<sup>(1)</sup> Net exposure after credit risk mitigation (net of allowance for expected credit losses on credit-impaired loans other than retail (except for credit card loans) using the Standardized Approach, excluding those using the Internal Ratings-Based Approach, according to the AMF guideline).

<sup>(2)</sup> The capital requirement represents 8% of risk-weighted assets.

<sup>(3)</sup> Other assets are measured using a method other than the Standardized Approach or the Internal Ratings-Based Approach. Other assets include the investments portion below a certain threshold in components that are deconsolidated for regulatory capital purposes (mainly Desjardins Financial Corporation Inc.), the investments portion below a certain threshold in associates as well as the portion of other deferred tax assets below a certain threshold. These three items are weighted at 250% and the deducted portion (namely above a certain threshold) is weighted at 0%. This class does not include the credit valuation adjustment (CVA) charge and additional requirements for the banking and trading portfolios, which are disclosed in the counterparty credit risk section.

<sup>(4)</sup> The scaling factor is a 6.0% calibration of risk-weighted assets measured using the Internal Ratings-Based Approach for credit exposures in accordance with Section 1.3 of the AMF guideline.

<sup>(5)</sup> Additional requirements representing an estimate of default and migration risks of unsecuritized products exposed to interest rate risk.

<sup>(6)</sup> Represents capital requirements calculated using the Standardized Approach for foreign exchange risk and commodity risk in the banking portfolio. It should be noted that since third quarter 2018, the internal models approach has been applied to all trading portfolios, after receiving the AMF's approval. Prior to this period, the Standardized Approach was used for all market risk requirements.

<sup>(7)</sup> Since third quarter 2018, internal models have been used to calculate market risk for trading portfolios in replacement of the Standardized Approach used previously.

The Standardized Approach was used in prior periods. Prior-period data have not been restated.

<sup>(8)</sup> Since second quarter 2017, the Standardized Approach has been used to assess operational risk. The Basic Indicator Approach was used in prior periods.

<sup>(9)</sup> The scaling factors used since January 1, 2014 to account for CVA charge requirements are being phased in to calculate the Tier 1A, Tier 1 and total capital ratios. They were 80%, 83% and 86%, respectively, in 2018 (72%, 77% and 81% in 2017) and will reach 100% for each class of capital by 2019.

### 3.3 Off-balance sheet arrangements

In the normal course of operations, the Federation enters into various off-balance sheet arrangements, including assets under management and under administration on behalf of caisse members and clients, credit instruments, contractual commitments, financial assets held as collateral and other, as well as structured entities, including securitization.

#### ASSETS UNDER MANAGEMENT AND UNDER ADMINISTRATION

As at December 31, 2018, the Federation administered, for the account of its members and clients, assets totalling \$382.5 billion. This represented an annual decrease of \$37.5 billion, or 8.9%, compared to a decrease of \$8.1 billion, or 1.9%, recorded as at December 31, 2017. The decrease was mainly due to the transaction involving Qtrade Canada Inc., as described in Section 1.2 "Significant transactions in 2018". Financial assets placed with the Federation as wealth manager amounted to \$66.4 billion at the close of 2018, for a decrease of \$0.3 billion, or 0.4% on an annual basis, compared to an increase of \$7.2 billion, or 12.0%, a year earlier.

Assets under management and under administration by the Federation are comprised essentially of financial assets in the form of investment funds, securities held in custody and assets accumulated by pension funds. They do not belong to the Federation, but to caisse members and its clients and, as a result, they are not recognized on the Consolidated Balance Sheets. The Wealth Management segment is primarily responsible for the activities related to assets under management and under administration.

**Table 22 – Assets under management and under administration**

As at December 31

(in millions of dollars)	2018	2017	2016
<b>Assets under management</b>			
Institutions and individuals	\$ 13,902	\$ 15,263	\$ 12,205
Investment funds <sup>(1)</sup>	52,457	51,390	47,285
<b>Total assets under management</b>	<b>\$ 66,359</b>	<b>\$ 66,653</b>	<b>\$ 59,490</b>
<b>Assets under administration</b>			
Individual and institutional trust and custodial services	\$ 280,378	\$ 313,517	\$ 326,798
Investment funds <sup>(1)</sup>	102,091	106,464	101,308
<b>Total assets under administration</b>	<b>\$ 382,469</b>	<b>\$ 419,981</b>	<b>\$ 428,106</b>

<sup>(1)</sup> Including Desjardins Funds and Northwest and Ethical Funds until April 1, 2018.

#### CREDIT INSTRUMENTS

In order to meet its members' and clients' financing needs, the Federation enters into various agreements with them for such instruments as credit commitments, indemnification commitments related to securities lending and documentary letters of credit. These products are generally off-balance sheet instruments and may expose the Federation to credit and liquidity risks. These instruments are subject to the Federation's usual risk management rules.

Note 27, "Commitments, guarantees and contingent liabilities", to the Federation's Consolidated Financial Statements provides more detailed information about these credit instruments.

#### GUARANTEES

The Federation also enters into various guarantee and indemnification agreements with its clients in the normal course of operations. These agreements remain off-balance sheet arrangements and include guarantees, standby letters of credit and credit default swaps. Note 27, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements provides information about these off-balance sheet arrangements.

#### ASSETS PLEDGED AND HELD AS COLLATERAL

In the normal course of business, the Federation holds financial assets as collateral as a result of transactions involving securities borrowed or those purchased under reverse repurchase agreements. Note 27, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements provides additional information about assets held as collateral.

## STRUCTURED ENTITIES

The Federation enters into various financial transactions with structured entities in the normal course of operations to diversify its sources of financing and manage its capital. Structured entities are usually created for a unique and distinct purpose, and they frequently have limited activities. These entities may be included in the Federation's Consolidated Balance Sheets if it has control over them. Detailed information concerning significant exposure to structured entities not included in the Federation's Consolidated Balance Sheets is provided below. Note 13, "Interests in other entities", to the Consolidated Financial Statements provides more information about structured entities.

### Securitization of the Federation's financial assets

The Federation participates in the *National Housing Act* (NHA) Mortgage-Backed Securities Program to manage its liquidities and capital. Transactions carried out under this program sometimes require the use of a structured entity, the Canada Housing Trust (CHT), set up by Canada Mortgage and Housing Corporation (CMHC) under the Canada Mortgage Bonds (CMB) Program. Note 8, "Derecognition of financial assets", to the Consolidated Financial Statements provides more information about the securitization of the Federation's loans.

# 4.0 Risk management

The shaded areas and tables marked with an asterisk (\*) in this section contain information about credit, market and liquidity risks in accordance with IFRS 7, "Financial Instruments: Disclosures". They also contain an analysis of how the Federation assesses its risks as well as a description of its risk management objectives, policies and methods. IFRS 7 provides that risk disclosures may be included in the MD&A. Consequently, the shaded areas and tables marked with an asterisk (\*) are an integral part of the Consolidated Financial Statements, as explained in Note 29, "Financial instrument risk management", to the Consolidated Financial Statements.

In the charts for this section, the information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

## 4.1 Risk factors that could impact future results

In addition to the risks presented in Section 4.2 of this MD&A, other systemic or macroeconomic risk factors, which are outside of Desjardins Group's control, including the Federation, may impact its future results. Furthermore, as indicated in the caution concerning forward-looking statements, general or specific risks and uncertainties may cause the actual results of Desjardins Group, including those of the Federation, to differ from those in the forward-looking statements. Some of these risk factors are presented below and therefore the following description applies to Desjardins Group.

## Principal emerging risks

Principal emerging risks are risks or risk factors that could have a significant impact on Desjardins Group's financial health and would likely affect its reputation, the volatility of its results, the adequacy of its capitalization or liquidities, in the event they fully materialize. Among these risks, certain so-called emerging risks are sharply growing risk factors, or ones that are developing unexpectedly, with unanticipated results. Desjardins Group continues to be proactive in identifying and tracking these risks so that it can take the appropriate management measures when required. For example, the external environment is continuously monitored to identify the risk factors and economic and regulatory events that could impact its operations. In addition, regular exchanges between the Risk Management Executive Division, risk officers and the business segments further define the risk factors of greatest concern.

Principal emerging risks	Description
<b>Cyber threats</b>	<p>Risks related to cyber threats have been on the rise for a number of years. Both the aggregation of new services for members and clients and the exposure of online services are becoming increasingly complex and gradually extending to more and more areas and products. In addition, the authors of cyber threats are using increasingly sophisticated methods and strategies for criminal purposes. Consequently, Desjardins Group has been investing for many years in technology to strengthen its cyber defence capabilities in order to detect cyber security incidents as quickly as possible; in its processes, by optimizing them to respond efficiently to incidents; and in its employees, by attracting and training them in order to continue developing its defence methods.</p> <p>Desjardins Group has also optimized its cyber risk transfer strategies by refining its own assurance policies during 2018. There is no indication that Desjardins would be less at risk than other Canadian financial institutions. In the event of a successful cyber attack, Desjardins would be exposed to financial loss, reputational loss, the risk of not achieving its business objectives as well as major disruption in its operations. Desjardins remains vigilant and proactive in identifying and managing such risks by continuing to invest in cyber defence techniques to protect its systems and data, and its members and clients.</p>

Principal emerging risks	Description
<b>Household indebtedness and changes in the housing market</b>	An economic slowdown, which is felt more acutely in times of geopolitical uncertainty, could substantially affect households whose debt levels are still high. This economic situation could lead to a decline in the housing market, which experienced solid growth in 2018, despite higher interest rates and the tighter mortgage granting rules imposed at the start of the year. Nonetheless, Desjardins remain proactive in assisting members and clients who could be affected in the event of such a situation. Desjardins has sound practices in granting and managing mortgage financing, including a stress test involving interest rates for mortgage financing, which should allow it to circumvent this risk.
<b>Technological developments</b>	Innovative technologies are being increasingly taken into consideration and adopted by financial institutions in the context of their digital transformation, as they represent a crucial vector for transforming business processes and models. In addition to the cyber threats risks, use of these technologies exposes financial institutions to other risks relating to system stability, the modernizing of infrastructure, complex environments and system interdependence. Regulators' expectations and the regulatory environment will be increasingly demanding, and financial sector requirements will continue to grow in terms of managing technology risk. The growing presence of FinTech and InsurTech, which offer simple, innovative technology solutions that meet the expectations of members and clients, puts more pressure on traditional financial institutions to adapt. Desjardins Group has been no exception and remains active in managing this operational and strategic risk, among others, by investing in technology and by reviewing and diversifying its products, services and distribution channels to meet the needs of its members and clients.
<b>Regulatory developments</b>	<p>The financial services industry is one of the most tightly monitored and regulated, and industry regulation has been expanding for many years now. This trend is in response to a number of socio-economic phenomena such as the development of new, increasingly complex financial products, ongoing volatility in the securities market, financial fraud, the fight against money laundering and terrorist financing, the fight against tax evasion, compliance with economic sanctions and the protection of personal information.</p> <p>Although Desjardins Group actively monitors and manages regulatory risk, changes in regulation, its complexity and its uncertainty could have an impact on the performance of its operations, its reputation, its strategies and its financial objectives.</p> <p>As an independent supervisory function, the Office of the Chief Compliance Officer, Desjardins Group promotes a proactive approach to compliance by fully integrating it into the organization's regular operations. Maintaining an effective compliance management framework mobilizes significant amounts of technical, human and financial resources.</p>
<b>Interest rate development</b>	<p>The turbulence seen on capital markets at the end of 2018 lowered bond rates. Furthermore, fewer interest rate increases are now expected in 2019 while the global economy is showing signs of weakness.</p> <p>This rate environment puts pressure on financial intermediation margins, resulting in lower interest income and fiercer competition for deposits as a number of investors abandon investment funds for high interest savings accounts and guaranteed capital investment vehicles. This situation also affects Desjardins Group's insurer and pension plan matching activities while liability valuations increase and return on assets decreases. Desjardins Group is still actively involved in its matching strategies and effectively manages these risks.</p> <p>The risk-averse, highly-volatile environment observed in the last two months of 2018 caused a significant widening in credit spreads, as well as a considerable reduction in the general level of interest rates. These elements had very negative repercussions on portfolios intended for long-term strategies aimed at ensuring the stability of these market parameters.</p>
<b>Geopolitical uncertainties</b>	<p>The adoption of protectionist measures by the U.S. administration increased global uncertainty in 2018. New protectionist measures could be decreed in 2019, particularly if the current negotiations between China and the U.S. are not conclusive. For Canada more specifically, there could be some new twists in the United States–Mexico–Canada (USMC) Agreement, which has not yet been accepted by the legislatures concerned. Some of the articles of the agreement could be contested, which would start the negotiating process all over again.</p> <p>The situation in Europe is one of greater political uncertainty. In addition to Brexit, which is marking time, there is the yellow vest crisis in France and the rise of populism. The European economy may slow again in 2019. The likelihood of a recession has also increased.</p> <p>Aware of the strength of global economic integration, Desjardins Group remains vigilant and continues to rely on its robust risk management framework to identify, measure and mitigate risk.</p>

## Other risk factors that could impact future results

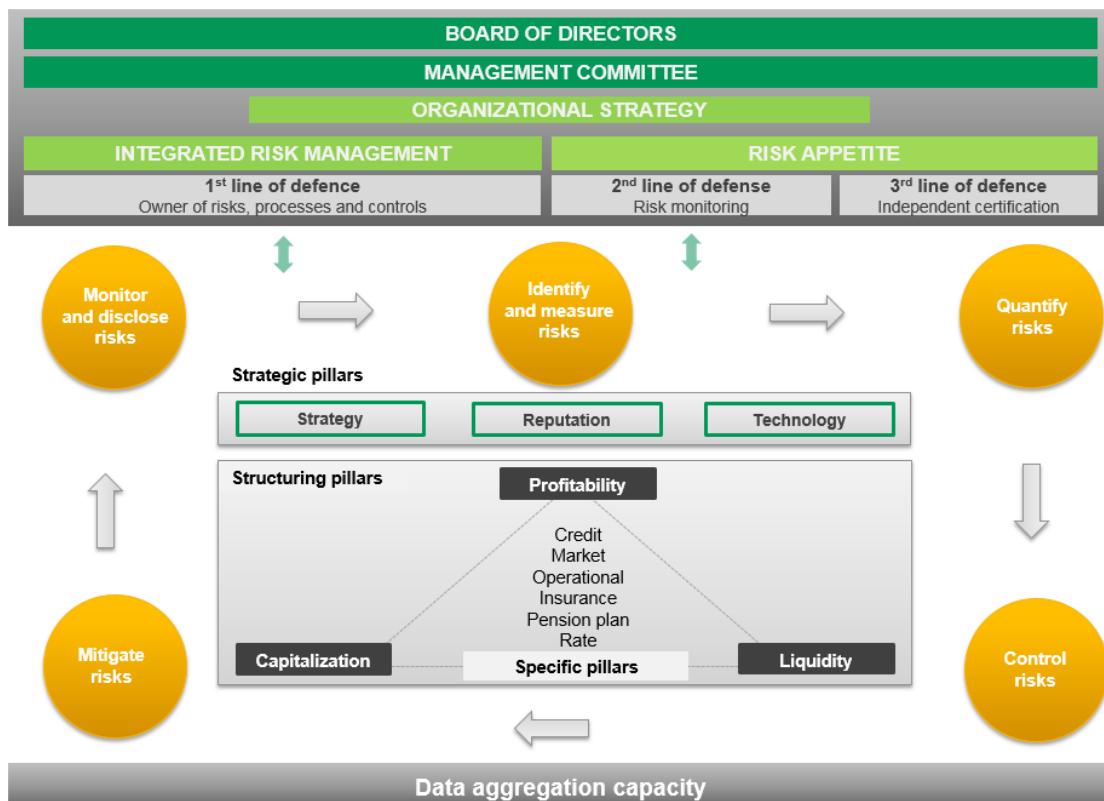
Risk factors	Description
<b>General economic and business conditions in regions in which Desjardins Group operates</b>	General economic and business conditions in the regions in which Desjardins Group operates may significantly affect its income and surplus earnings. These conditions include short and long-term interest rates, inflation, debt securities market fluctuations, foreign exchange rates, the volatility of capital markets, tighter liquidity conditions in certain markets, the level of indebtedness, the strength of the economy, consumer spending and saving habits, and the volume of business conducted by Desjardins Group in a given region.
<b>Monetary policies</b>	The monetary policies of the Bank of Canada and the U.S. Federal Reserve (the Fed), as well as interventions in capital markets, have an impact on Desjardins Group's income. The general level of interest rates may impact Desjardins Group's profitability because interest rate fluctuations affect the spread between interest paid on deposits and interest earned on loans, thereby affecting Desjardins Group's net interest income. Furthermore, considering the current level of indebtedness of Canadian households, higher interest rates could have an adverse effect on consumers' ability to service their debt, leading to an increased risk of loan losses for financial institutions. Desjardins Group has no control over changes in monetary policies or capital market conditions, and it therefore cannot forecast or anticipate them systematically.
<b>Accuracy and completeness of information concerning clients and counterparties</b>	Desjardins Group relies on the accuracy and completeness of the information it has on its clients and counterparties. When deciding to authorize a loan or other transactions with clients or counterparties, Desjardins Group may use information provided by them, including financial statements and other financial information. It may also rely on representations made by clients and counterparties regarding the completeness and accuracy of such information, and on auditors' reports regarding the financial statements. The financial position and income of Desjardins Group could be adversely affected if the financial statements on which it relies fail to comply with accounting standards, are misleading or do not present fairly, in all material respects, the financial position, performance and cash flows of its members, clients and counterparties. Desjardins Group trains its employees and implements procedures to mitigate the risks related to the use of inaccurate, incomplete or fraudulent information from its members, clients or counterparties.
<b>Critical accounting estimates and accounting standards</b>	The Consolidated Financial Statements are prepared in accordance with the IFRS. The accounting policies used by the Federation determine how it reports its financial position and results of operations, and management may be required to make estimates or rely on assumptions about matters that are inherently uncertain. Any change in these estimates and assumptions, as well as in accounting standards and policies, may have a significant impact on the Federation's financial position and results of operations. The significant accounting policies and future accounting changes are described in Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.
<b>New products and services to maintain or increase market share</b>	Strong competitive pressures from Canadian financial institutions and the emergence of new competitors have led Desjardins Group to develop new products and services at a faster pace to maintain or increase its attractiveness as a financial institution with its clients. Developing these new products and services could require large investments by Desjardins or involve risks not identified at the time of their development. Desjardins cannot be certain that the new products and services it offers will result in the anticipated financial benefits.
<b>Geographic concentration</b>	<p>The Federation's operations are heavily concentrated in Quebec. As at December 31, 2018, Desjardins Group's loans to Quebec members and clients therefore accounted for 69.2% of its aggregate loan portfolio. As a result of this significant geographic concentration, its results largely depend on economic conditions in Quebec. Any deterioration in these conditions could adversely impact:</p> <ul style="list-style-type: none"> <li>• past due loans;</li> <li>• problem assets and foreclosed property;</li> <li>• claims and lawsuits;</li> <li>• the demand for products and services;</li> <li>• the value of collateral available for loans, especially mortgages, and by extension, clients' and members' borrowing capacity, the value of assets associated with impaired loans and collateral coverage.</li> </ul>
<b>Acquisitions and joint arrangements</b>	Desjardins Group has implemented a rigorous internal control environment for the acquisition and joint arrangement processes. Nevertheless, its financial or strategic objectives could fail to be met because of unexpected factors such as delays in approval of transactions by regulators or their imposing of additional conditions, the inability to apply the strategic plan in its original form, difficulties in integrating or retaining clients, an increase in regulatory costs, unexpected expenses, or changes in the economic and competitive environment. As a result, synergies, higher income, cost savings, increased market share and other expected benefits may not materialize or may be delayed, thereby impacting Desjardins Group's future surplus earnings.
<b>Credit ratings</b>	The credit ratings assigned to Desjardins Group by rating agencies are instrumental to its access to sources of wholesale funding and the cost of such funding. These ratings may be revised or withdrawn at any time by the agencies. In addition, a significant downgrade to various ratings could raise Desjardins Group's cost of funding, reduce its access to capital markets, and increase additional obligations required by its counterparties.

Risk factors	Description
<b>Climate change</b>	<p>Climate change is an external risk factor that is part of environmental risk. It is defined as an entity's vulnerability to the negative effects of climate change, which could lead to financial losses. It includes:</p> <ul style="list-style-type: none"> <li>physical risks, namely the risks resulting from damage caused by extreme weather events;</li> <li>transition risks, namely the risks related to implementation of measures to ensure environmental transition.</li> </ul> <p>Catastrophes resulting from extreme weather events are unforeseeable and their frequency seems to be growing. The severity of their effects means that they could have a material impact on Desjardins Group's results. Given the nature of their operations, Desjardins's property and casualty insurance subsidiaries are particularly affected by climate change, especially through the catastrophe risk that is an integral part of insurance risk.</p>
<b>Other factors</b>	<p>Other factors that may have an impact on Desjardins Group's future results include changes in tax laws, unexpected changes in consumer spending and saving habits, talent recruitment and retention for key positions, the ability to implement Desjardins Group's disaster recovery plan within a reasonable time, the possible impact of international conflicts on operations, and Desjardins Group's ability to anticipate and manage the risks associated with these factors properly despite a disciplined risk management environment.</p> <p>Desjardins Group cautions the reader that factors other than the foregoing could affect future results. Investors and other stakeholders relying on forward-looking statements to make decisions with respect to Desjardins Group should carefully consider these factors as well as other uncertainties, potential events, and industry factors or other items specific to Desjardins Group that could adversely impact its future results.</p>

## 4.2 Risk management

### Integrated Risk Management Framework

Desjardins Group's objective in risk management is to optimize the risk-return trade-off by developing and applying integrated risk management strategies, frameworks, practices and procedures to all of the organization's business segments and support functions. To this end, Desjardins developed an Integrated Risk Management Framework reflective of its organizational strategy and risk appetite which is aimed, among other things, at giving its senior management and the Federation's Board of Directors an appropriate level of confidence and comfort regarding the understanding and management of the full spectrum of risks associated with the achievement of its objectives. Risk management is a function covering all Desjardins Group's operations, including those of the Federation. Consequently, the following description of risk management applies to Desjardins Group.



## RISK IDENTIFICATION

Desjardins Group considers it important to periodically assess the environment in which it operates and to identify key risks, as well as the aforesaid principal risk factors and emerging risk factors to which it is exposed. Desjardins Group has a risk log that sets out the main categories and subcategories of risks which could affect Desjardins Group. The log is updated at least annually and is used as a basis to make a quantitative and qualitative assessment of risk materiality, to determine Desjardins Group's risk profile and to implement appropriate strategies to mitigate risk.

In the normal course of business, the Federation is exposed to the principal risks shown below, which are covered in specific subsections of this MD&A.

Credit	Market	Liquidity	Operational	Insurance	Strategic	Reputation	Pension plan	Environmental or social	Legal and regulatory
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In addition to strategic, operational, liquidity and reputation risks inherent in operations, the top risks of the Federation's business segments are:

- Personal and Business Services: Credit and market risk
- Wealth Management and Life and Health Insurance: Insurance, market and credit risk
- Property and Casualty Insurance: Insurance and market risk

Strict and effective management of these risks is a priority for Desjardins Group, its purpose being to support its major orientations, particularly regarding its financial soundness as well as its sustained and profitable growth, while complying with regulatory requirements. Desjardins Group considers risk an inextricable part of its development and consequently strives to promote a proactive approach in which each of its business segments, employees and managers is responsible for risk management.

## RISK MEASUREMENT

Desjardins Group uses both quantitative and qualitative techniques to determine its risk exposure. It ensures that an appropriate selection of measurement tools and mitigation techniques are designed and maintained in order to support its business development.

Models play a central role in assessing risk at Desjardins Group and support decision-making in many situations. They are applied to various aspects of risk management. Quantitative models are used for modelling credit risk measurement parameters. They are also used in market risk measurement, economic capital calculations, asset valuation and pricing. Risks are quantified based on both the current economic context as well as on hypothetical stress-testing situations, which are measured for specific risks on a Desjardins-wide integrated basis.

### Desjardins-wide integrated stress testing

Desjardins-wide sensitivity tests and crisis scenarios are used as additional risk analysis tools to measure the potential impact of exceptional but plausible events on, in particular, profitability, liquidity and capital levels. Organization-wide crisis scenarios are developed based on the anticipated economic outlook under unfavourable conditions. In accordance with the second pillar of the Basel Capital Accord, the results of these analyses are a key element of Desjardins Group's internal capital adequacy assessment program and can identify potential vulnerabilities in various operations in relation to risk factors. Desjardins-wide stress testing is conducted annually.

Desjardins Group economists develop a series of potential crisis scenarios annually, based on current economic conditions, on the principal risk factors to which the organization is exposed and on emerging risks. These scenarios are then submitted to senior management for approval of an enterprise-wide assessment. More than 20 macroeconomic variables, including GDP, interest rates, the jobless rate, housing prices, stock indices and inflation, are projected for each of the scenarios and different interest rate curves.

This exercise requires input from various business units and business segments to ensure a global perspective for the analysis as well as consistency among the various estimated impacts. Credit portfolios belonging to the Desjardins caisse network and the Federation are among the large portfolios analyzed. The analysis also covers the two insurance groups, namely Desjardins Financial Security Life Assurance Company and Desjardins General Insurance Group Inc., as well as the Desjardins Group Pension Plan.

The exercise is tied in with Desjardins Group's integrated financial planning, projected over a three-year horizon. The exercise's results are also used to establish capitalization targets and to update risk appetite indicators.

During Desjardins-wide stress testing in 2018, the scenarios developed separately considered the possibility of a long recession in the U.S. combined with a significant real estate correction in Canada, and a global trade war. The results obtained from the assessment of these scenarios show that Desjardins Group's current capitalization levels would be enough to withstand the economic deterioration considered and that its capital ratios would still exceed regulatory limits and its own risk appetite limits.

The results of the exercise are presented annually to various internal committees consisting of Desjardins Group's directors and senior management, namely the Risk Management Commission, the Desjardins Group Finance and Risk Management Committee, the Desjardins Group Management Committee and the Federation's Board of Directors.

In addition to the crisis scenarios studied during its integrated financial planning, Desjardins Group carries out regulatory stress testing based on AMF prescribed assumptions and according to the frequency set by the AMF, generally every two years.

## Governance and model validation

In order to ensure sound governance of the use of Desjardins Group risk models and support the unit monitoring risk models and strategies in its role, activities such as the design, performance monitoring and validation of models for credit risk, market risk, economic capital and stress testing are subject to guidelines that specify the roles and responsibilities of the various parties involved in these activities.

The validation group, which is independent from the units responsible for developing models and the end-user units, is in charge of running the appropriate validation program based on the model's importance. It is responsible for determining the importance level of each of Desjardins Group's risk assessment models. For the most important models, the program consists of a series of points to be validated for evaluating the model on design methodology, including assumptions, reliability and data quality. The program also includes an assessment of the possibility of automatic replication of certain results obtained by the modelling teams and the review of some aspects affecting implementation of the models. In addition, for models used to calculate regulatory capital, validation aims to assess compliance with applicable regulatory requirements. For models of lesser importance, the program has a smaller number of validation points. A model's importance level also dictates how often the model's performance will be validated during its useful life. Even though the governance structure overseeing design and performance monitoring activities includes controls that mitigate the risk that inadequate models are deployed and used, independent validation is the main measure mitigating this risk.

## RISK DISCLOSURE

A risk disclosure report is prepared quarterly and presented to the Desjardins Group Finance and Risk Management Committee, the Desjardins Group Management Committee, the Risk Management Commission and the Federation's Board of Directors. These reports provide relevant information on changes in the principal risks identified as well as on the capital position, particularly capital adequacy in relation to Desjardins Group's risk profile. These reports are regularly updated to include the latest risk management developments.

## RISK APPETITE

As a significant component of the Integrated Risk Management Framework, risk appetite makes it possible to determine the risk type and level that Desjardins is prepared to assume in pursuing its business, financial and strategic objectives. Risk appetite forms an integral part of strategic planning, which makes it possible to guide risk-taking in order to ensure Desjardins Group's stability and sustainability in the case of unfavourable future events that could affect reputation, the volatility of profitability, capital adequacy or liquidities. As a result, risk appetite provides a basis for integrated risk management by promoting a better understanding of the effect of principal risks and emerging risks on Desjardins Group's actual results.

The risk appetite framework reflects Desjardins Group's risk-taking philosophy, mission and values and is based on:

- taking necessary risks to enrich the lives of people and communities, contributing to the development of a sustainable and responsible economy and managing such risks conscientiously;
- protecting Desjardins Group's reputation with its members, clients, communities, regulatory authorities and other stakeholders, while respecting its cooperative values;
- understanding the risks arising from Desjardins Group's operations and engaging in only new activities for which the risks are defined, assessed and understood;
- modernizing Desjardins Group's technologies to adapt to the needs of members, clients and employees in order to simplify their experience;
- thanks to adequate profitability in light of risk exposure, ensuring Desjardins Group's sustainability to be able to give back to members and communities and to meet its commitments to holders of debt securities and equity securities;
- maintaining financial stability within the market by preserving a capitalization level that meets market expectations and complies with regulatory requirements;
- managing liquidities and refinancing activities in order to guard against liquidity risk;
- avoiding excessively large risk concentrations;
- adequately managing operational and regulatory risks.

The risk management function ensures that Desjardins Group's risk profile is in line with its risk appetite. Each quarter, it makes sure that the statements and indicators set by senior management and the Board of Directors are respected, and keeps them informed. In the event a threshold or limit for a risk appetite indicator is exceeded, an immediate investigation is required. The supporting commentary and an action plan, as applicable, are then brought to the attention of the appropriate bodies. The Board of Directors is responsible for approving the risk appetite framework and ensuring that Desjardins Group's financial and strategic objectives are in line with its risk appetite.

The risk appetite framework is reviewed regularly and submitted to the Federation's Board of Directors for approval. The Desjardins Group Risk Management Executive Division relays the main guidelines for risk appetite to the business segments and components, and supports them in implementing these concepts by ensuring consistency in all the indicators, targets, levels and limits with the Desjardins Group framework.

## PROACTIVE RISK MANAGEMENT APPROACH

A proactive risk management approach is one of the cornerstones of Desjardins Group's Integrated Risk Management Framework. It represents all the practices and behaviours of individuals and groups within the organization that condition the collective ability to identify, understand and openly discuss risks and handle present and future risks. Stakeholders, including the Board of Directors, senior management and the Risk Management Executive Division, encourage risk-taking behaviour in line with Desjardins Group's risk management frameworks. A proactive risk management approach promotes open and transparent communication between Desjardins Group's risk management function and its other support functions, business segments and components, while promoting an appropriate risk-return trade-off.

Ethical conduct and integrity are firmly entrenched in Desjardins Group's proactive risk management approach, which relies on the *Desjardins Code of Professional Conduct*. The code sets out the values and principles that Desjardins Group has espoused in order to maintain a high level of integrity.

Other methods used to support the proactive risk management approach and to promote accountability for risk include:

- defining and communicating risk management roles and responsibilities to all line levels in terms of an operations management approach based on the Three Lines of Defence model;
- alignment of strategic decisions and compensation processes with risk-taking;
- the dissemination of risk management frameworks;
- the organizing of risk management training and awareness sessions, bearing in mind the type of risk discussed and the role of the various parties involved.

Risk management and the Integrated Risk Management Framework are based on the following guidelines that provide in particular for:

- the accountability of Desjardins Group's business segments and other functions with regard to the risks inherent to their operations;
- the independence of the risk management function in relation to business segments;
- implementation at every level of the organization in order to obtain a comprehensive vision of risk exposure;
- a procedure aimed at ensuring that risk matters are disclosed and flagged accurately and transparently to senior management in a timely manner;
- the existence and presence of a complete and rigorous process to determine the appropriate capital level based on the risks assumed;
- consideration of risk management in the formulation of strategic plans and business strategies and in the resulting decisions;
- thorough risk assessment prior to launching new products or initiating transactions with a strong financial impact.

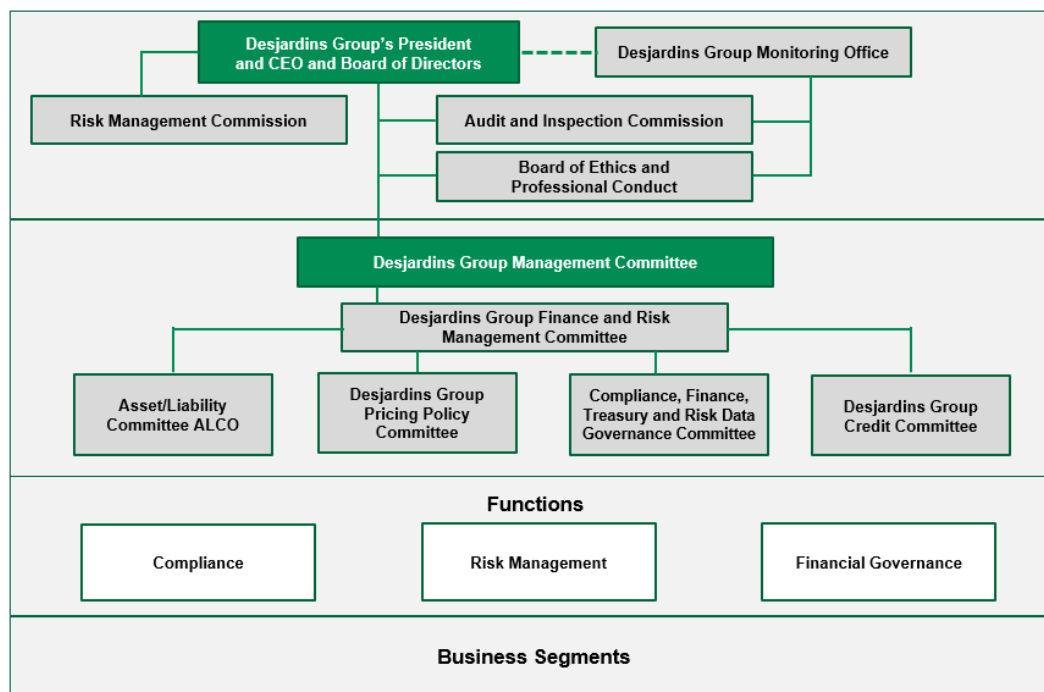
### Compensation in relation to risk management

Desjardins Group has established strict governance with regard to total compensation. The Board of Directors is responsible for the annual changes in the total compensation of senior executives, members of the Management Committee and all employees. In this regard, it establishes an annual salary review, sets the objectives and measures the results of the general incentive plan. Acting as a subcommittee of the Board of Directors, the Human Resources Commission periodically reviews Desjardins Group's position with regard to total compensation so that it can remain competitive.

Incentive plans for senior executives, which are consistent with risk-taking at Desjardins Group, provide, as a general rule, for the medium to long-term deferral of a significant portion of members' annual bonus. The amounts thus deferred can vary annually depending on Desjardins Group's results. This formula encourages key stakeholders to have a long-term vision of Desjardins Group's development, which is beneficial for the organization's members and clients.

## RISK MANAGEMENT GOVERNANCE

The Integrated Risk Management Framework is based on a solid risk governance structure and reflects Desjardins Group's organizational structure as shown below.



The **Federation's Board of Directors** is responsible for guiding, planning, coordinating and monitoring all of Desjardins Group's operations, and in such capacity, it participates actively in overseeing the major risks to which Desjardins Group is exposed. It is in particular responsible for adopting the overall directions and strategies proposed by senior management as well as risk management policies aimed at ensuring sound and prudent management of operations.

The Board is supported in this regard by the Risk Management Commission, the Audit and Inspection Commission, the Board of Ethics and Professional Conduct and the Desjardins Group Management Committee. Further information about these bodies is found in the Corporate Governance section of the Federation's 2018 Annual Report.

The **Desjardins Group Management Committee** makes recommendations to the Board of Directors concerning risk management guidelines and strategies and ensures that they are implemented effectively and efficiently.

The Management Committee relies on the Desjardins Group Finance and Risk Management Committee in performing its duties.

The **Desjardins Group Finance and Risk Management Committee** is responsible for ensuring that the on- or off-balance sheet principal risks to which Desjardins Group is or will be exposed directly or through one or more of its subsidiaries, have been identified and measured, and for assessing the potential impact of identified risks on business strategies.

This committee is supported by the Desjardins Group Credit Committee and the Compliance, Finance, Treasury and Risk Data Governance Committee:

- **The Desjardins Group Credit Committee** approves large credit commitments and monitors activities related to assessing and quantifying credit risk. In its monitoring role, the committee is supported by the model and strategy monitoring unit and by the collective allowance governance committee.
- **The Compliance, Finance, Treasury and Risk Data Governance Committee** provides guidance and exercises authority in establishing and monitoring risk data governance in accordance with Desjardins Group's needs and regulatory requirements. In addition, it prioritizes the actions to improve risk data quality.

The Desjardins Group Finance and Risk Management Committee is also responsible for overseeing and monitoring interest rate and liquidity risk management as well as ensuring compliance with Desjardins Group's pricing policy and the consistency of pricing with Desjardins's strategic objectives and financial targets. These mandates are performed through the **Asset/Liability Committee (ALCO)** and the **Desjardins Group Pricing Policy Committee**.

### Operations management approach based on the Three Lines of Defence model

Risk management governance and the Integrated Risk Management Framework are also based on the Three Lines of Defence model. The Three Lines of Defence encompass complementary responsibilities that are coordinated to support sound and prudent risk management. The management approach based on this model focuses in particular on segregation of tasks and the assignment of complementary roles and responsibilities that are clearly defined between the various parties within the organization in terms of risk management, as the following table illustrates:

Three Lines of Defence model	
<b>First line</b>	
Owner of risks, processes and controls	<ul style="list-style-type: none"> <li>• Identifies and manages process-related risks</li> <li>• Manages its activities in line with the organization's risk appetite</li> <li>• Is responsible for performance of its activities</li> <li>• Designs, implements and maintains effective internal controls</li> <li>• Identifies potential conflict of interest situations and remedies them by adequate segregation of tasks</li> <li>• Produces and reports on its risk profile</li> </ul>
<b>Second line</b>	
Risk monitoring	<ul style="list-style-type: none"> <li>• Establishes risk management frameworks and ensures that they are applied</li> <li>• Monitors and does a critical review of the first line's risk management and the effectiveness of the controls it puts in place</li> <li>• Advises and equips the first line so that it can carry out its responsibilities</li> <li>• Monitors and reports on compliance with risk appetite</li> </ul>
<b>Third line</b>	
Independent certification	<ul style="list-style-type: none"> <li>• Gives an independent opinion on the effectiveness of governance, risk management and internal controls within the organization</li> </ul>

#### 1st Line of Defence

The first line of defence, assumed by process owners, is responsible for the overall performance of the activities assigned to it in the process and for managing the resulting risks.

Consequently, the business sectors ensure day-to-day risk management in compliance with the risk appetite framework, design, implement and maintain effective internal controls, and monitor their risk profile.

#### 2nd Line of Defence

The Risk Management Executive Division is a strategic function whose main purpose is to partner with the business sectors and Desjardins as a whole in their development by identifying, measuring and managing risks. It also ensures that risk management is aligned with Desjardins's risk appetite and business strategy.

In partnership with the business sectors, the Desjardins Group risk management function is responsible for recommending and establishing risk management frameworks, and ensures that the appropriate risk management infrastructure, processes and practices are set up to target all major Desjardins-wide risks.

The Risk Management Executive Division can also rely on the work performed by the compliance and financial governance functions which, based on their separate mandates, help to regulate and manage certain issues inherent to Desjardins Group's operations.

### 3rd Line of Defence

The **Desjardins Group Monitoring Office** is an independent and objective advisory and assurance body that assists Desjardins Group's officers in carrying out their governance, risk management and control responsibilities.

Moreover, it assists the President and Chief Executive Officer of Desjardins Group, and oversees and advises management in its duty to ensure sound and prudent management. In so doing, it contributes to improving Desjardins Group's overall performance and maintaining the confidence of its members, the public and regulatory bodies. The Desjardins Group Monitoring Office includes the internal audit services of Desjardins Group components.

## Basel capital accord

Basel III is an international capital adequacy tool designed to align regulatory capital requirements more closely with risk exposure and to further the continuous development of the risk assessment capabilities of financial institutions.

The Basel III framework is essentially based on three pillars:

- the first pillar sets out the requirements for risk-weighted regulatory capital;
- the second pillar deals with the supervisory review process;
- the third pillar stipulates financial disclosure requirements.

In compliance with the guideline on adequacy of capital base standards, which was adapted to reflect the provisions of Basel III, Desjardins Group uses the Internal Ratings-Based Approach for credit risk related to the retail loan portfolios – Personal. Other exposures to credit risk are currently measured according to the Standardized Approach. On June 19, 2017, Desjardins Group received the AMF's authorization to use the Standardized Approach for calculating operational risk as of June 30, 2017. On June 29, 2018, Desjardins Group received the AMF's approval to use market risk internal models for trading portfolios while continuing to use the Standardized Approach for foreign exchange risk and commodity risk in the banking portfolio as of September 30, 2018. These provisions are used to calculate the Federation's capital ratios, among other things.

Desjardins Group has also set up an internal capital adequacy assessment program (ICAAP). This program is a sound management practice recognized in the industry and is the key element of the second pillar of the Basel Accord. It allows a financial institution to provide for an appropriate level of capital to cover all major risks to which it is exposed, and to implement capital management strategies that follow the changes in its risk profile.

This program is under the responsibility of the Risk Management Executive Division. Capital adequacy is assessed by verifying whether available capital is sufficient to cover the capital required. The units responsible oversee the overall adequacy of Desjardins Group's available capital based on both internal measures of economic capital and the regulatory capital requirements under the first pillar. The results of stress testing exercises are also considered in the capital adequacy assessment.

The internal measure of capital used by Desjardins Group is economic capital, namely the amount of capital that an institution must maintain, in addition to expected losses, to remain solvent over a certain horizon and at a high confidence level. For Desjardins Group, economic capital is assessed over a one-year horizon. A confidence level is selected to meet the objective of maintaining attractive credit ratings. In order to assess the Federation's overall capital adequacy in relation to its risk profile, all significant risks identified through the risk logging process are assessed using internal methodologies to measure economic capital. It should be pointed out that all economic capital methodologies are validated independently to ensure that modelling input and assumptions used allow the assessed risk to be measured appropriately.

## Credit risk

*Credit risk is the risk of losses resulting from a borrower's, guarantor's, issuer's or counterparty's failure to honour its contractual obligations, whether or not such obligations appear on the Consolidated Balance Sheets.*

The Federation is exposed to credit risk first through its direct personal, business and government loans, which accounted for 39.2% of assets on the Consolidated Balance Sheets as at December 31, 2018, compared to 40.3% at the end of 2017. It is also exposed through various other commitments, including letters of credit and transactions involving derivative financial instruments as well as securities transactions.

### CREDIT RISK MANAGEMENT

Desjardins Group upholds its goal of providing efficient service to all its members and clients. To this end, it has developed distribution channels specialized by product and customer base. The various units and components making up these channels are considered centres of expertise and are accountable for their performance in their respective markets, including credit risk management. In this regard, they have specific frameworks to support them, powers of approval, and the corresponding management and monitoring tools. To provide assistance in this area to these units and components, Desjardins Group has set up centralized structures and procedures to ensure that its Integrated Risk Management Framework allows for effective management that remains sound and prudent.

The Risk Management Executive Division has been structured so that it can effectively manage credit risk and provide credit approval, support, quantification and monitoring, and report on credit matters.

#### Framework

A set of policies, guidelines, rules, practices and standards govern all aspects of credit risk management at Desjardins Group. This framework defines the responsibilities and powers of the parties involved, the limits imposed by risk tolerance, the rules governing the assignment and administration of files, and the disclosure rules for Desjardins Group's exposure to credit risks.

All these frameworks govern Desjardins's credit risk management and control activities.

## Assessment of regulatory capital

The AMF has authorized two credit risk assessment approaches to be included in calculating regulatory capital, namely the Standardized Approach and the Internal Ratings-Based Approach. RWA calculations are used to measure the Federation's credit risk, as well as market risk and operational risk. The Federation has adopted the Internal Ratings-Based Approach for credit risk related to loan portfolios of retail clients – Personal. In order to apply this method, it had to make internal estimates to calculate the probability of default (PD), loss given default (LGD) and exposure at default (EAD) on loan products. Other credit risk exposures are measured using the Standardized Approach.

PD is the likelihood of a borrower defaulting on its obligations within a one-year time horizon. For retail customers, behavioural scoring models, estimated using logistic regressions, produce risk levels monthly. The predictive features of these models include in particular borrower and account-specific features such as account age, loan size and delinquency. These models allow proactive management of the portfolio credit risk. However, for regulatory purposes, the PD from scoring models is:

- calibrated by groups of products according to the following drivers: residential mortgages, loans and lines of credit, point-of-sale financing and credit cards.
- adjusted slightly upward (prudential margin) to compensate for the historical volatility of PD.

LGD measures the size of the possible economic loss in the event of the borrower's default. It is expressed as a percentage of EAD. LGD estimates reflect average economic losses by collateral or guarantee type input into an internal history. Economic losses include direct and indirect management costs as well as any recoveries adjusted for the delay between the time of default and the time of the transaction. LGD is adjusted upward to take into account the possible effects of an economic slowdown.

EAD is an estimate of the amount outstanding for a given exposure at the time of default. For on-balance sheet exposures, EAD is equal to the balance at the time of observation. For off-balance sheet exposures, EAD includes an estimate of the additional drawdowns that may occur between the time of observation and the default. Estimates of such possible additional drawdowns reflect the internal history of the average drawdown on revolving credit products between the observation date and the time of default. Finally, EAD of off-balance sheet exposures is adjusted upward to take into account the possible effects of an economic slowdown.

### Differences between the parameters used for accounting and regulatory capital purposes

Loss allowances for expected credit losses for accounting purposes according to IFRS 9 are based primarily on the parameters used to calculate regulatory capital under the Internal-Ratings Based Approach, namely PD, LGD and EAD. However, there are certain differences, and the main ones are presented in the table below:

Regulatory capital		IFRS 9
<b>PD</b>	<ul style="list-style-type: none"> <li>• Estimated using a long-term average for a full economic cycle.</li> <li>• Projected over the next 12 months.</li> <li>• Definition of default associated with an instrument for which payments have been past due for over 90 days, plus certain other criteria.</li> </ul>	<ul style="list-style-type: none"> <li>• Estimated at a point in time for the next 12 months or for the lifetime of the instrument.</li> <li>• Based on past experience, current conditions and relevant forward-looking information.</li> <li>• Will correspond to the definition of default used for regulatory capital purposes.</li> </ul>
<b>LGD</b>	<ul style="list-style-type: none"> <li>• Based on losses that would be expected during an economic downturn.</li> <li>• Subject to certain regulatory floors.</li> <li>• Takes into account all direct and indirect recovery costs.</li> <li>• Discounted to account for the recovery period until default using the discount rate required for regulatory capital purposes.</li> </ul>	<ul style="list-style-type: none"> <li>• Based on past experience, current conditions and relevant forward-looking information.</li> <li>• Excessive conservatism and floors are excluded.</li> <li>• Takes into account only direct recovery costs.</li> <li>• Discounted to account for the recovery period until default using the initial effective interest rate.</li> </ul>
<b>EAD</b>	<ul style="list-style-type: none"> <li>• Corresponds to drawn amounts plus expected use of undrawn amounts before default.</li> </ul>	<ul style="list-style-type: none"> <li>• Based on the expected balance of amounts in default projected over the next 12 months or the lifetime of the instrument based on forward-looking expectations.</li> </ul>
<b>Discounting</b>	<ul style="list-style-type: none"> <li>• No discounting between the date of default and the reporting date.</li> </ul>	<ul style="list-style-type: none"> <li>• Discounted from the date of default to the reporting date using the initial effective interest rate.</li> </ul>

More specifically, credit and counterparty risk exposure includes the following categories:

- Used exposure is the amount of funds invested or advanced to a member or client.
- Unused exposure is the amount of credit in loans or margins that has been authorized, but not yet used after credit conversion factors (CCF) have been applied.
- Repo-style transactions are contractual transactions between two parties, including a retrocession commitment at a pre-set price. Repo-style transactions include repurchase agreement transactions, reverse repurchase agreement transactions, and lending and borrowing of securities that are not outstanding with a central counterparty as well as these same transactions carried out with a non-qualifying central counterparty.
- Over-the-counter (OTC) derivative instruments refer to all OTC derivative financial instruments with different underlying instruments.
- Off-balance sheet exposures include guarantees, commitments, derivatives and other contractual agreements of which the total notional principal amount may not be recognized on the balance sheet.
- The net exposure is calculated after using credit risk mitigation (CRM) techniques, including collateral, guarantees and credit derivatives.

As at December 31, 2018, the EAD was \$138.5 billion before using CRM techniques and \$111.7 billion after using CRM techniques.

## Credit granting

The Risk Management Executive Division assigns approval limits to the various units and components, including the caisse network. The units and components are primarily responsible for approving the files originating from them. However, the Risk Management Executive Division approves any commitments exceeding the approval limits assigned to them. Its approval responsibilities and the depth of the analyses required depend on product features as well as the complexity and extent of transaction risk.

The Risk Management Executive Division also sets commitment limits, namely the maximum commitment that can be granted to a borrower and the related entities. Where required, risk-sharing arrangements can be used, mainly with other caisses or certain Desjardins Group components. Risk-sharing arrangements can also be made with other financial institutions through banking syndicates.

### Retail loans

Retail loan portfolios consist of residential mortgages, personal loans and lines of credit, point-of-sale financing and credit card loans. The Internal Ratings-Based Approach for credit risk is currently used for most of these portfolios.

In general, credit decisions concerning retail customers are based on risk ratings generated using predictive credit scoring models. Credit adjudication and portfolio management methodologies are designed to ensure consistent granting of credit and early identification of problem loans. Desjardins Group's automated risk rating system evaluates the creditworthiness of each member and client on a monthly basis. This process ensures the quick, valid identification and management of problem loans.

Table 23 presents PD tranches in relation to risk levels.

**Table 23 – Probabilities of default of retail clients by risk level\***

Risk levels	PD tranches
Excellent	0.00% - 0.14%
Very low	0.15% - 0.49%
Low	0.50% - 2.49%
Average	2.50% - 9.99%
High	10.00% - 99.99%
Default	100.00%

### Monitoring performance of credit risk assessment models using the Internal Ratings-Based Approach

For portfolios assessed using the Internal Ratings-Based Approach, the Risk Management Executive Division is responsible for the design, development and performance monitoring of models, in accordance with various guidelines on the subject.

Credit risk assessment models are developed and tested by specialized teams supported by the business units and related credit risk management units concerned by the model.

The performance of credit risk parameters is analyzed on an ongoing basis through back testing. This testing is performed on out-of-time and out-of-sample inputs and aims to assess parameter robustness and adequacy. Where a statistically significant overage is observed, prudential upward adjustments are made to reflect an unexpected trend in a segment in particular. These adjustments, allowing a more adequate risk assessment related to the transactions and borrowers, are validated and approved by the units responsible.

More specifically for PD, such back testing takes the form of various statistical tests to assess the following criteria:

- model's discriminating power;
- calibration of the model;
- stability of model results.

Independent validations are also performed on credit risk assessment models. The most critical aspects to be validated are factors allowing appropriate risk classification by level, the adequate quantification of exposures and the use of assessment techniques taking external factors into consideration, such as economic conditions and the credit situation, and lastly, alignment with internal policies and regulatory provisions.

The model approval procedure and reporting are regulated by different bodies depending on the type and size of the approval in question. As a result, new models and significant changes to existing models are approved by the next higher committee than the one that is informed of the annual model performance monitoring results and authorizes any resulting recommendations.

The table below shows the quality of the retail loan portfolio by asset class using the Internal Ratings-Based Approach.

**Table 24 – Exposure to credit risk of retail loan portfolios<sup>(1)\*</sup>**

As at December 31

	2018				2017
	EAD				
(in millions of dollars)	Exposures related to residential mortgage loans	Qualifying revolving retail client exposures	Other retail client exposures	Total	Total
Excellent	\$ 568	\$ 10,054	\$ 17	\$ 10,639	\$ 9,636
Very low	604	12,232	311	13,147	12,689
Low	915	6,817	2,681	10,413	9,345
Average	85	1,126	3,639	4,850	4,257
High	13	1,163	281	1,457	1,337
Default	6	107	65	178	152
<b>Total</b>	<b>\$ 2,191</b>	<b>\$ 31,499</b>	<b>\$ 6,994</b>	<b>\$ 40,684</b>	<b>\$ 37,416</b>

<sup>(1)</sup> Exposures depend on the regulatory scope, which excludes insurance operations.

The table below presents the quality of the retail loan portfolio subject to the Standardized Approach by risk tranche.

**Table 25 – Exposures to retail clients by risk tranche<sup>(1)\*</sup>**

As at December 31

	2018								2017
	Risk tranches								
(in millions of dollars)	0%	20%	35%	50%	75%	100%	Other	Total	Total
Residential mortgages	\$ -	\$ -	\$ 435	\$ -	\$ -	\$ -	\$ -	\$ 435	\$ 411
Other retail client exposures (except for SMEs)	-	-	-	-	1,946	1	-	1,947	1,505
<b>Total</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 435</b>	<b>\$ -</b>	<b>\$ 1,946</b>	<b>\$ 1</b>	<b>\$ -</b>	<b>\$ 2,382</b>	<b>\$ 1,916</b>

<sup>(1)</sup> Exposures depend on the regulatory scope, which excludes insurance operations.

#### Loans to businesses, sovereign borrowers and financial institutions

These loans include retail loans, loans to sovereign borrowers and public bodies, loans to the housing sector and loans to other businesses. Work is in progress to switch these portfolios to the Internal Ratings-Based Approach.

The following table presents the credit quality of the portfolio of loans and acceptances to businesses, sovereign borrowers and financial institutions by risk tranche.

**Table 26 – Exposures to businesses, sovereign borrowers and financial institutions by risk tranche<sup>(1)\*</sup>**

As at December 31

	2018								2017
	Risk tranches								
(in millions of dollars)	0%	20%	35%	50%	75%	100%	Other	Total	Total
Sovereign borrowers	\$ 5,815	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 5,815	\$ 931
Financial institutions	-	47,475	-	21	-	4	-	47,500	34,805
Businesses	-	222	-	653	-	15,303	298	16,476	12,491
SMEs similar to other retail client exposures	-	-	-	-	2,067	113	15	2,195	1,581
<b>Total</b>	<b>\$ 5,815</b>	<b>\$ 47,697</b>	<b>\$ -</b>	<b>\$ 674</b>	<b>\$ 2,067</b>	<b>\$ 15,420</b>	<b>\$ 313</b>	<b>\$ 71,986</b>	<b>\$ 49,808</b>

<sup>(1)</sup> Exposures depend on the regulatory scope, which excludes insurance operations.

### Retail clients, small residential rental properties and small commercial rental properties

Credit scoring systems based on proven statistics are used to assess the risk of credit activities involving these client bases.

These systems were designed using the behavioural history of borrowers with a profile or characteristics similar to those of the applicant in order to estimate the transaction risk.

Such systems are used for initial approval as well as for the monthly reassessment of borrowers' risk level. Ongoing updates allow for proactive management of the portfolios' credit risk.

The performance of these systems is periodically analyzed and adjustments are made regularly to measure transaction and borrower risk as adequately as possible. The units responsible for developing scoring systems and the underlying models ensure that adequate controls are set up to monitor their stability and performance.

### Other segments

The granting of credit is based on the detailed analysis of a file. Each borrower's financial, market and management characteristics are analyzed using a credit risk assessment model designed from internal and external historical data, taking into account the size of the business, the special characteristics of the main industry in which the borrower operates, and the performance of comparable businesses.

In order to determine the model to be used, a segment is assigned to each borrower based on the borrower's main industry and some other features. A quantitative analysis based on financial data is supplemented by an assessment of qualitative factors by the person in charge of the file. Once this analysis is finished, each borrower is assigned a credit risk rating representing the borrower's risk level.

The use of scoring results has been expanded to other risk management and governance activities such as establishing analysis requirements and the required decision-making level, determining the different types of follow-up activities, as well as assessing and disclosing portfolio risk quality.

### **Credit risk mitigation**

When a loan is granted to a member or client, the Federation may obtain collateral to mitigate the borrower's credit risk. Such collateral normally takes the form of assets such as capital assets, receivables, inventory, equipment, securities (government securities, equities, etc.) or cash.

For some portfolios, programs offered by various organizations, in particular Canada Mortgage and Housing Corporation (CMHC) and *La Financière agricole du Québec*, are used in addition to customary collateral. As at December 31, 2018, guaranteed or insured loans represented 8.6% of the Federation's total gross loans, compared to 9.5% at the end of 2017. As a result of these additional measures, the residual credit risk is minimal for loan portfolios with such collateral. In order for enhanced credit offered by a guarantor to be considered a credit risk mitigation technique, the guarantor must meet certain specific criteria to allow this.

Frameworks adapted to each type of collateral contain the requirements for appraising collateral, its legal validity and follow-up. The type of collateral as well as the value of the assets encumbered by such collateral are established on the basis of a credit risk assessment of the transaction and the borrower, depending in particular on the borrower's PD. Such an assessment is required whenever any new loan is granted in accordance with the Federation's frameworks. When an outside professional, such as a chartered appraiser or an environmental assessment firm, is required to determine the value of the collateral, the selection of the professional and the mandate must comply with the necessary requirements in the frameworks. Considering that the collateral is used to recover all or part of the unpaid balance of a loan in the event of the borrower's default to make payment, the quality, the legal validity and the ease with which the collateral can be realized are determining factors in obtaining a loan.

In order to ensure that the value of the collateral remains adequate, it must be periodically updated. The frequency of reappraisals depends in particular on the risk level, the type of collateral or certain triggering events such as a deterioration in the borrower's financial position or the sale of an asset held as collateral. The decision-making level is responsible for approving the updated value of the collateral, if applicable.

During the year ended December 31, 2018, no major change was made to the credit risk mitigation policies, and the quality of assets held as collateral did not change significantly.

### **Loan debt relief**

In managing loan portfolios, the Federation may, for financial or legal reasons, change the original terms and conditions of a loan granted to a borrower experiencing financial difficulty and therefore prevented from discharging his obligations. Such changes may include an interest rate adjustment, the deferral or extension of principal and interest payments or the waiver of a tranche of the principal or interest.

### **File monitoring and management of higher risk files**

Credit practices govern the monitoring of loans. Files are reassessed on a regular basis. Requirements regarding review frequency and depth increase with a higher PD or the size of potential losses on receivables. The officer in charge of the file monitors high risk loans using various intervention methods. A positioning, which must be authorized by the appropriate decision-making level, is required to be performed for files with irregularities or increased risk as well as for files in default.

The unit in charge of the financing is primarily responsible for monitoring files and for managing higher risks. However, certain tasks or files may be outsourced to the Federation's intervention units specializing in turnarounds or recovery. Supervision reports produced and submitted periodically to the appropriate bodies make it possible to monitor the position of high-risk borrowers as well as changes in the corrective measures put in place. In addition, a report accounting for credit activities, covering changes in credit quality and financial issues, is submitted quarterly to the management of the component concerned.

## Default situations

### Identification of default

In accordance with the AMF guideline on adequacy of capital base standards, the following two criteria are used to identify a default situation:

- Quantitative criterion: A borrower's payments are past due by more than 90 days.
- Qualitative criterion: The Federation believes that a borrower is unlikely to repay his debt in full unless the appropriate action is taken, such as realization on a collateral or guarantee, if any.

These criteria are applicable to all clients.

### Impact of default

The impact of a default consists of associating the identified default on exposure to all the same borrower's commitments as well as to other entities in its borrower group. Such impacts vary according to the type of client base.

For individuals, the Federation does not pass on the default.

For retail businesses, small residential rental properties and small commercial rental properties, the default is passed on only to the borrower's exposures to commitments with the same entity within the scope of Desjardins Group. For the application of this criterion, the caisse network is considered one and the same entity.

For non-retail businesses, public bodies, financial institutions and sovereign borrowers, the default is entirely passed on through all the borrower's commitments in the scope of Desjardins Group. The default may also be passed on to other entities forming part of its borrower group according to a case-by-case analysis.

### Removing default

When default is recognized in terms of the quantitative criterion, it may be removed immediately for clients that are retail businesses, small residential rental properties, small commercial rental properties and individuals. If not, it is generally removed within a minimum of three to six months if certain conditions set out in the credit risk guidelines are met.

## Monitoring of portfolio and reporting

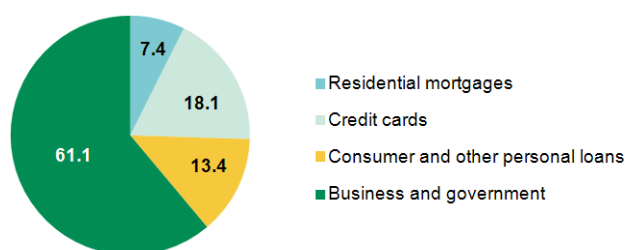
The Risk Management Executive Division oversees the management of all risks to which the organization is exposed, including credit risks. The operating methods require ongoing monitoring of the credit risks to which the Federation is exposed, as well as periodic reporting on portfolio quality to the appropriate bodies.

## BREAKDOWN AND QUALITY OF LOAN PORTFOLIO

The following chart presents the distribution of loans and acceptances by borrower category.

### Breakdown of loans and acceptances

As at December 31, 2018  
(as a percentage)



Loans by borrower category and by industry are presented in the table below. As at December 31, 2018, the main sectors of the business loan portfolio were finance and insurance, manufacturing and real estate, which accounted for 81.6% of the business loan portfolio amounting to \$36.5 billion. The main industries are the same as they were as at December 31, 2017.

**Table 27 – Loans by borrower category and by industry**

As at December 31

(in millions of dollars)	2018 <sup>(1)</sup>		2017		2016	
	Gross loans	Gross credit-impaired <sup>(2)</sup> loans	Gross loans	Gross impaired <sup>(2)</sup> loans	Gross loans	Gross impaired <sup>(2)</sup> loans
Residential mortgages	\$ 4,626	\$ 10	\$ 4,323	\$ 8	\$ 3,486	\$ 2
Consumer, credit card and other personal loans	19,710	200	17,547	72	15,720	82
Public bodies <sup>(3)</sup>	1,446	-	1,910	-	1,037	-
Business						
Agriculture	189	15	125	-	196	1
Mining, oil and gas	275	-	258	-	201	-
Utilities	660	-	379	1	321	-
Construction	1,114	118	730	-	644	1
Manufacturing	1,922	2	1,193	2	902	5
Wholesale trade	501	-	384	-	258	-
Retail trade	322	-	478	-	480	1
Transportation	563	-	468	-	436	-
Information industry	359	-	218	-	196	-
Finance and insurance	26,243	-	26,804	-	24,254	-
Real estate	1,662	-	1,810	-	3,510	1
Professional services	234	-	166	-	169	-
Management of companies	237	-	168	-	87	-
Administrative services	30	-	13	-	39	-
Education	42	-	-	-	6	-
Health care	207	-	126	1	42	-
Arts and entertainment	134	-	79	-	91	-
Accommodation	50	-	36	-	89	1
Other services	305	-	147	-	206	-
Other businesses	1,497	3	1,520	-	252	1
<b>Total business loans</b>	<b>\$ 36,546</b>	<b>\$ 138</b>	<b>\$ 35,102</b>	<b>\$ 4</b>	<b>\$ 32,379</b>	<b>\$ 11</b>
<b>Total loans</b>	<b>\$ 62,328</b>	<b>\$ 348</b>	<b>\$ 58,882</b>	<b>\$ 84</b>	<b>\$ 52,622</b>	<b>\$ 95</b>

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(3)</sup> Including loans to governments.

The following tables present the aging of gross loans that are past due but not credit-impaired.

**Table 28 – Gross loans past due but not credit-impaired<sup>(1)</sup>**

As at December 31, 2018 <sup>(2)</sup>	1 to 29 days	30 to 59 days	60 to 89 days	90 days or more	Total
Residential mortgages	\$ 43	\$ 3	\$ -	\$ 11	\$ 57
Consumer, credit card and other personal loans	679	126	57	-	862
Business and government	2	-	-	-	2
	<b>\$ 724</b>	<b>\$ 129</b>	<b>\$ 57</b>	<b>\$ 11</b>	<b>\$ 921</b>

As at December 31, 2017	1 to 29 days	30 to 59 days	60 to 89 days	90 days or more	Total
Residential mortgages	\$ 43	\$ 4	\$ -	\$ 8	\$ 55
Consumer, credit card and other personal loans	559	104	48	-	711
Business and government	21	1	-	-	22
	<b>\$ 623</b>	<b>\$ 109</b>	<b>\$ 48</b>	<b>\$ 8</b>	<b>\$ 788</b>

<sup>(1)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

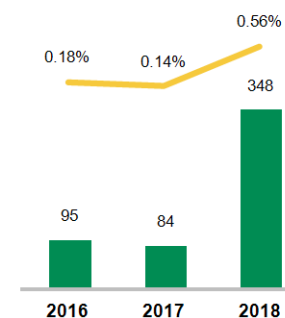
<sup>(2)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

On January 1, 2018, the Federation adopted IFRS 9, "Financial Instruments", which replaces IAS 39, "Financial Instruments: Recognition and Measurement". Contrary to the approach of IAS 39, which was based on an incurred credit loss impairment model, IFRS 9 is based instead on an expected credit loss impairment model. The impairment model under IFRS 9 is therefore more forward-looking in nature. For more information, see Note 2, "Basis of presentation and significant accounting policies" to the Consolidated Financial Statements.

According to Note 7, "Loans and allowance for credit losses" to the Consolidated Financial Statements, the allowance for credit losses as at December 31, 2018 stood at \$491 million, up \$293 million compared to December 31, 2017. This increase was mainly the result of growth in outstanding loans and the adoption of IFRS 9 as at January 1, 2018. This new standard led to volatility in results following the revision of economic scenarios, the updating of parameters and of the migration of borrower ratings.

Gross credit-impaired loans outstanding are now the loans included in stage 3 of the impairment model. The ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.56% as at December 31, 2018, contrary to 0.14% as at December 31, 2017. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered insignificant. The allowance for credit losses on credit-impaired loans totalled \$121 million as at December 31, 2018, for a provisioning rate on credit-impaired loans of 34.7%.

**Gross credit-impaired loans and gross credit-impaired loan ratio<sup>(1)</sup>**  
(in millions of dollars and as a percentage)



<sup>(1)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

Tables 29 and 30 present the gross credit-impaired loans by Federation borrower category and the change in the gross credit-impaired loan balance.

**Table 29 – Gross credit-impaired<sup>(1)</sup> loans by borrower category**

As at December 31

(in millions of dollars and as a percentage)	2018 <sup>(2)</sup>					2017		2016	
	Gross carrying amount					Gross impaired loans	Net impaired loans	Gross impaired loans	Net impaired loans
	Gross loans and acceptances	Gross credit-impaired loans		Allowance for credit losses on credit-impaired loans	Net credit-impaired loans				
Residential mortgages	\$ 4,626	\$ 10	0.22%	\$ 5	\$ 5	\$ 8	\$ 3	\$ 2	\$ 2
Consumer, credit card and other personal loans	19,710	200	1.01	110	90	72	49	82	60
Business and government	38,152	138	0.36	6	132	4	-	11	6
<b>Total</b>	<b>\$ 62,488</b>	<b>\$ 348</b>	<b>0.56%</b>	<b>\$ 121</b>	<b>\$ 227</b>	<b>\$ 84</b>	<b>\$ 52</b>	<b>\$ 95</b>	<b>\$ 68</b>

<sup>(1)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

**Table 30 – Change in gross credit-impaired loans<sup>(1)</sup>**

As at December 31

(in millions of dollars)	2018 <sup>(2)</sup>	2017	2016
<b>Gross impaired loans at the beginning of the year under IAS 39</b>	<b>\$ 84</b>	<b>\$ 95</b>	<b>\$ 85</b>
Impact of adopting IFRS 9 as at January 1, 2018	125	N/A	N/A
<b>Gross credit-impaired loans at the beginning of the past year under IFRS 9</b>	<b>209</b>	<b>N/A</b>	<b>N/A</b>
Gross credit-impaired loans since the past year	777	441	466
Reinstatement to non credit-impaired status	(306)	(225)	(205)
Write-offs and recoveries	(286)	(278)	(281)
Other changes	(46)	51	30
<b>Gross credit-impaired loans at the end of the year</b>	<b>\$ 348</b>	<b>\$ 84</b>	<b>\$ 95</b>

<sup>(1)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

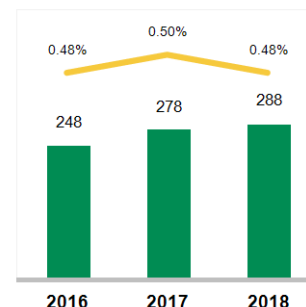
<sup>(2)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

## Provision for credit losses

The Federation's provision for credit losses totalled \$288 million for 2018, up \$10 million compared to 2017. This increase was mainly the result of growth in outstanding loans and the adoption of IFRS 9 as at January 1, 2018. This new standard led to volatility in results following the revision of economic scenarios, the updating of parameters and the migration of borrower ratings. The credit loss provisioning rate was 0.48% at the end of 2018, slightly down from a ratio of 0.50% recorded as at December 31, 2017.

Additional information about the credit risk related to the recognition and measurement of the allowance for credit losses is presented in Note 2, "Basis of presentation and significant accounting policies", and Note 7, "Loans and allowance for credit losses", to the Consolidated Financial Statements.

**Provision for credit losses and credit loss provisioning rate**  
(in millions of dollars and as a percentage)



## Counterparty and issuer risk

*Counterparty and issuer risk is a credit risk relative to different types of securities, derivative financial instrument and securities lending transactions.*

The Risk Management Executive Division establishes a risk rating for each counterparty and issuer before authorizing an exposure limit. The rating comes from internal models or is based on rating agencies (DBRS, Moody's, Standard & Poor's and Fitch) recognized by the AMF and the OSFI. Risk ratings are also used as parameters in calculating capital requirements for counterparty and issuer risk. Desjardins Group's exposure limits are established on the basis of its risk appetite framework and its Tier 1A capital. These amounts are then allocated to various components based on their needs. Limits may also apply to certain financial instruments, if considered relevant.

A large proportion of Desjardins Group's risk exposure is to the different levels of government in Canada, Quebec public and parapublic entities and major Canadian banks. For most of these counterparties and issuers, the credit rating is A- or higher. Desjardins Group's exposure to U.S. and European financial institutions is low, and its exposure to sovereign debt is concentrated in Canada and the United States.

In its derivative financial instrument and securities lending transactions, which include repurchase agreements, reverse repurchase agreements and securities borrowing and lending, Desjardins Group is exposed to counterparty credit risk.

Desjardins Group uses derivative financial instruments primarily for asset and liability management purposes. Derivative financial instruments are contracts whose value is based on an underlying asset, such as interest rates, exchange rates or financial indices. The vast majority of Desjardins Group's derivative financial instruments are traded over the counter with a counterparty and include forward exchange contracts, currency swaps, interest rate swaps, credit default swaps, total return swaps, forward rate agreements, and currency, interest rate and stock index options. Other instruments are exchange-traded contracts, consisting mainly of futures and swaps traded through a clearing house. They are standard contracts executed on established stock exchanges or well-capitalized clearing houses for which the counterparty risk is very low.

The credit risk associated with derivative financial instruments traded over the counter refers to the risk that a counterparty will fail to honour its contractual obligations toward Desjardins Group at a time when the fair value of the instrument is positive for Desjardins. This risk normally represents a small fraction of the notional amount. It is quantified using two measurements, namely replacement cost and the credit risk equivalent. Replacement cost refers to the current replacement cost of all contracts with a positive fair value. Credit risk equivalent is equal to the sum of this replacement cost and the potential credit exposure. Desjardins Group also limits counterparty risk exposure by entering into master agreements called International Swaps and Derivatives Association (ISDA) agreements, which define the terms and conditions for the transactions. These agreements provide for netting to determine the net exposure in the event of default. In addition, a Credit Support Annex can be added to the master agreement in order to request the counterparties to pay or secure the current market value of the positions when such value exceeds a certain threshold, which has been set at zero for its main counterparties. The value of these different measures and the impact of the Federation's master netting agreements is presented in Note 19, "Derivative financial instruments and hedging activities", to the Consolidated Financial Statements.

Desjardins Group also limits its risk by doing business with counterparties that have a high credit rating. Note 19, "Derivative financial instruments and hedging activities", to the Consolidated Financial Statements presents derivative financial instruments for the Federation by credit risk rating and type of counterparty. Based on replacement cost, this note indicates that substantially all of the Federation's counterparties have credit ratings ranging from AAA to A-. Furthermore, by purchasing hedges through credit derivatives, such as credit default swaps and total return swaps, Desjardins Group can transfer credit risk to a counterparty or hedge itself against various types of risk.

Securities lending transactions are regulated by Investment Industry Regulatory Organization of Canada participation agreements. Desjardins Group also uses netting agreements with its counterparties to mitigate its credit risk exposure and requires a percentage of collateralization (a pledge) on these transactions.

Desjardins Group accepts from its counterparties only financial collateral that complies with the eligibility criteria set out in its policies. These criteria allow for the timely realization of collateral, if necessary, in the event of default. The types of collateral received and pledged by Desjardins Group are mainly cash and government securities.

Additional information about the Federation's credit risk is presented in Note 5, "Offsetting financial assets and liabilities", Note 19, "Derivative financial instruments and hedging activities", and Note 27, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.

## Market risk

Market risk refers to the risk of changes in the fair value of financial instruments resulting from fluctuations in the parameters affecting this value, in particular, interest rates, exchange rates, credit spreads and their volatility.

Desjardins Group is exposed to market risk through its trading activities, which result primarily from short-term transactions conducted with the intention of profiting from current price movements or to provide arbitrage revenue. Desjardins Group is also exposed to market risk through its non-trading activities, which group together mainly asset/liability management transactions in the course of its traditional banking activities as well as investment portfolios related to its insurance operations. Desjardins Group and its components have adopted policies that set out the principles, limits and procedures to use in managing market risk.

## GOVERNANCE

Desjardins Group's components are primarily structured into different legal entities to deliver products and services that can be distributed to Desjardins Group members and clients. These legal entities manage financial instruments exposed to market risk and are subject to different regulatory environments such as the banking, securities brokerage, wealth management, life and health insurance and property and casualty insurance industries. The board of directors of these entities delegate to various committees the responsibility of setting up systems and procedures to establish measures adapted to their operations and regulatory environments. These measures, together with the appropriate follow-up procedures, are incorporated into their respective policies and guidelines. The function of the Risk Management Executive Division is to monitor these measures and ensure compliance with the said policies. The main measures used and their follow-up processes are described below.

## MANAGEMENT OF MARKET RISK RELATED TO TRADING ACTIVITIES – VALUE AT RISK

The market risk of trading portfolios is managed on a daily basis under a specific policy. This policy specifies the risk factors that must be measured and the limit for each of these factors as well as the total. Tolerance limits are also provided for various stress testing. Compliance with these limits is monitored daily and a market risk dashboard is produced on a daily basis and sent to senior management. Any limit exceeded is immediately analyzed and the appropriate action is taken.

The main tool used to measure this risk is "Value at Risk" (VaR). VaR is an estimate of the potential loss over a certain time interval at a given confidence level. A Monte Carlo VaR is calculated daily on the trading portfolios, using a 99% confidence level and a holding horizon of one day (holding horizon scaled up to 10 days for the purpose of regulatory capital calculations). It is therefore reasonable to expect a loss exceeding the VaR figure once every 100 days. The calculation of VaR is based on historical data for a one-year interval.

In addition to aggregate VaR, Desjardins Group also calculates an aggregate stressed VaR (SVaR). It is calculated in the same way as aggregate VaR, except for the use of historical data. Therefore, instead of using the interval of the past year, the aggregate SVaR takes into account the historical data for a crisis period of one year from September 2008.

The incremental risk charge (IRC) supplements the VaR and SVaR measures and represents an estimate of default and migration risks of unsecuritized products held in the trading portfolio, exposed to interest rate risk, and measured over a one-year horizon at a 99.9% confidence level.

Table 31 presents the aggregate VaR and the aggregate SVaR for trading activities by risk category as well as the incremental risk charge (IRC). Equity price risk, foreign exchange risk, interest rate risk and specific interest rate risk are the four risk categories to which the Federation is exposed. These risk factors are taken into account in measuring the market risk of the trading portfolio. They are reflected in the VaR table presented below. The definition of a trading portfolio meets the various criteria defined in the Basel Capital Accord.

**Table 31 – Market risk measures for the trading portfolio\***

(in millions of dollars)	As at December 31, 2018				As at December 31, 2017			
	Average		High		Average		High	
Equities	\$ 1.0	\$ 0.4	\$ 1.0	\$ 0.2	\$ 0.5	\$ 0.3	\$ 1.6	\$ 0.1
Foreign exchange	0.5	0.5	1.2	0.1	0.4	0.3	1.8	-
Interest rate	2.4	4.1	6.0	2.0	2.1	3.0	5.1	1.8
Specific interest rate risk <sup>(1)</sup>	5.9	7.1	9.7	3.6	4.3	5.2	8.2	2.5
Diversification effect <sup>(2)</sup>	(6.9)	(7.8)	N/A <sup>(3)</sup>	N/A <sup>(3)</sup>	(5.1)	(5.7)	N/A <sup>(3)</sup>	N/A <sup>(3)</sup>
<b>Aggregate VaR</b>	<b>\$ 2.9</b>	<b>\$ 4.3</b>	<b>\$ 6.1</b>	<b>\$ 2.1</b>	<b>\$ 2.2</b>	<b>\$ 3.1</b>	<b>\$ 5.1</b>	<b>\$ 2.0</b>
<b>Aggregate SVaR</b>	<b>\$ 16.0</b>	<b>\$ 16.0</b>	<b>\$ 26.1</b>	<b>\$ 8.8</b>	<b>\$ 11.1</b>	<b>\$ 11.9</b>	<b>\$ 19.7</b>	<b>\$ 8.2</b>
<b>Incremental risk charge (IRC)</b>	<b>\$ 75.2</b>	<b>\$ 76.9</b>	<b>\$ 98.7</b>	<b>\$ 43.0</b>	<b>\$ 54.1</b>	<b>\$ 104.8</b>	<b>\$ 211.3</b>	<b>\$ 54.1</b>

<sup>(1)</sup> Specific risk is the risk directly related to the issuer of a financial security, independent of market events. A portfolio approach is used to distinguish the specific risk from the general market risk. This approach consists of creating a sub-portfolio that contains the positions involving the specific risk of the issuer, such as provinces, municipalities and companies, and a sub-portfolio that contains the positions considered to be without issuer risk, such as governments in the local currency.

<sup>(2)</sup> Refers to the risk reduction related to diversification, namely the difference between the sum of the VaR of the various market risks and the aggregate VaR.

<sup>(3)</sup> The highs and lows of the various market risk categories can refer to different dates.

The average of the trading portfolio's aggregate VaR was \$4.3 million for 2018, up \$1.2 million compared to 2017, mainly as a result of an increase in the average of the interest rate VaR. As for the average of the aggregate SVaR, it was \$16.0 million for 2018, up \$4.1 million compared to 2017. The average of the incremental risk charge was \$76.9 million, down \$27.9 million compared to 2017.

Aggregate VaR and aggregate SVaR are appropriate measures for a trading portfolio but they must be interpreted by taking into account certain limits, in particular the following ones:

- these measures do not allow future losses to be predicted if the actual market fluctuations differ markedly from those used to do the calculations;
- these measures are used to determine the potential losses for a one-day holding period, and not the losses on positions that cannot be liquidated or hedged during this one-day period;
- these measures do not provide information on potential losses beyond the selected confidence level of 99%.

Given these limits, the process of monitoring trading activities using VaR is supplemented by stress testing and by establishing limits in this regard.

## Back testing

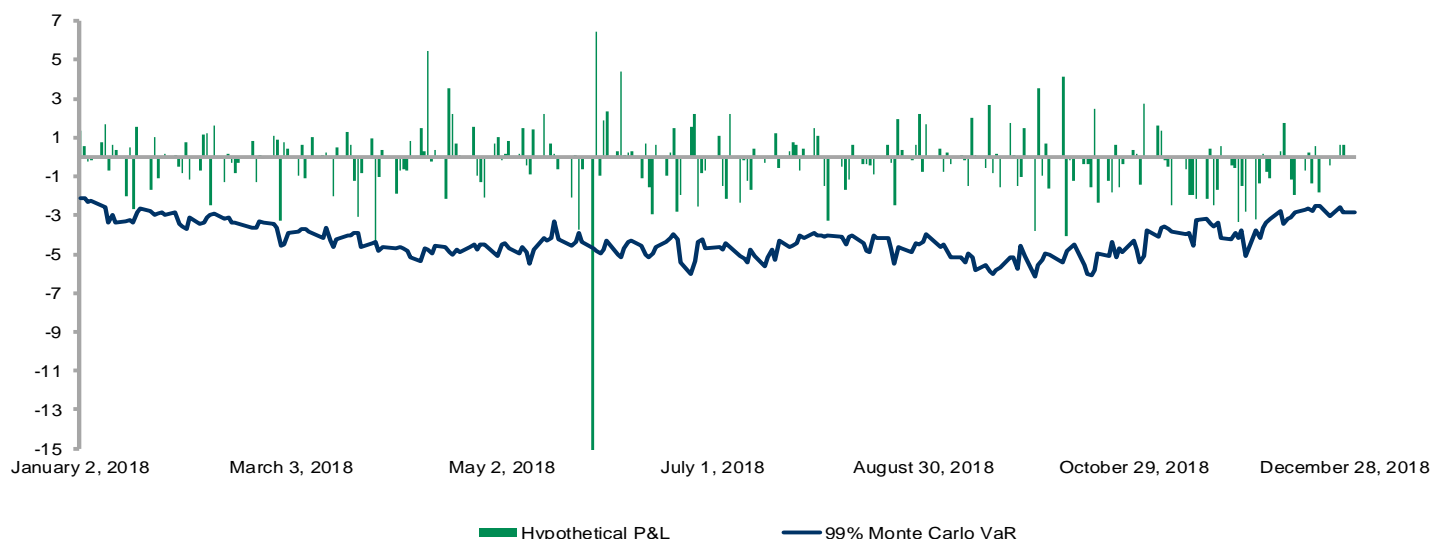
Back testing, which is a daily comparison of the VaR with the profits and losses (P&L) on portfolios, is conducted to validate the VaR model used by ensuring that hypothetical results correspond statistically to those of the VaR model. In addition, an independent modelling validation unit works on the model every year.

Desjardins Group performs back testing daily, applying a hypothetical P&L and an actual P&L to its trading portfolios. The hypothetical P&L is calculated by determining the difference in value resulting from changes in market conditions between two consecutive days. The portfolio mix between these two days remains static.

The following chart presents changes in VaR for trading activities as well as hypothetical P&L related to these activities for 2018. Hypothetical P&L was exceeded twice during the year on March 27 and May 28, respectively. As for actual P&L compared to VaR, no overage was observed for Desjardins Group if income from commissions and subscriptions was included in actual P&L. However, two overages were observed if such income from commissions and subscriptions was not included in actual P&L. In spite of these overages, the VaR model remains adequate.

## VaR compared to hypothetical P&L for trading activities

(in millions of dollars)



## Stress testing

Certain events that are considered highly unlikely and that could have a significant impact on trading portfolios may occur from time to time. These events are at the tail-end of the distribution and are the result of extreme situations. Use of a stress-testing program is required to assess the impact of these potential situations.

The stress-testing program used for trading portfolios includes historical, hypothetical and sensitivity scenarios based, for instance, on events such as 9/11 or the 2008 credit crisis. Using such stress testing, changes can be monitored in the market value of positions held depending on various scenarios. Most stress-testing is predictive. For a given stress test, shocks are applied to certain risk factors (interest rates, exchange rates, commodities) and the effects of these shocks are passed on to all the risk factors taking historical correlations into account. The running of each stress test is considered to be independent of the others. In addition, certain stress testing is subject to limit tracking. Stress-testing results are analyzed and reported daily using a dashboard, together with VaR calculations, in order to detect vulnerability to such events. The stress-testing program is reviewed periodically to ensure that it is kept current.

## STRUCTURAL INTEREST RATE RISK MANAGEMENT

Desjardins Group is exposed to structural interest rate risk, which represents the potential impact of interest rate fluctuations on net interest income and the economic value of equity. This risk is the main component of market risk for Desjardins Group's traditional banking activities other than trading, such as accepting deposits and granting loans, as well as for its securities portfolios used for long-term investment purposes and as liquidity reserves.

Interest rate sensitivity is based on the earlier of the repricing or the maturity date of the assets, liabilities and derivative financial instruments used to manage structural interest rate risk. The situation presented reflects the position only on the date indicated and can change significantly in subsequent years depending on the preferences of Desjardins Group members and clients, and the application of policies on structural interest rate risk management.

Some Consolidated Balance Sheet items are considered non-interest-rate-sensitive instruments, including investments in equities, non-performing loans, non-interest-bearing deposits, non-maturity deposits with an interest rate not referenced to a specific rate (such as the prime rate), and equity. As dictated in its policies, Desjardins Group's management practices are based on prudent assumptions with respect to the maturity profile used in its models to determine the interest rate sensitivity of such instruments.

In addition to the total sensitivity gap, the main structural interest rate risk factors are:

- the trend in interest rate level and volatility;
- the changes in the shape of the interest rate curve;
- member and client behaviour in their choice of products;
- the financial intermediation margin;
- the optionality of the various financial products offered.

In order to mitigate risk factors, sound and prudent management is applied to optimize net interest income while minimizing the negative incidence of interest rate movements. The established policies describe the principles, limits and procedures that apply to structural interest rate risk management. Simulations are used to measure the effect of different variables on changes in net interest income and the economic value of equity. These policies specify the structural interest rate risk factors, the risk measures selected, the risk tolerance levels and the management limits as well as the procedures in the event that limits are exceeded. Structural interest rate risk is assessed at the required frequency according to portfolio volatility (daily, monthly and quarterly).

The assumptions used in the simulations are based on an analysis of historical data and on the effects of various interest rate environments on changes in such data. These assumptions concern changes in the structure of assets and liabilities, including modelling for non-maturity deposits and equity, in member and client behaviour, and in pricing. Desjardins Group's Asset/Liability Committee (ALCO) is responsible for analyzing and approving the global matching strategy on a monthly basis while respecting the parameters defined in structural interest rate risk management policies.

Table 32 presents the potential impact before income taxes, with regard to structural interest rate risk management associated with banking activities, of a sudden and sustained 100 basis point increase or decrease in interest rates on net interest income and the economic value of equity for the Federation. The impact related to insurance activities is presented in Note 1 of this table.

**Table 32 – Interest rate sensitivity (before income taxes)<sup>(1)</sup>**

As at December 31

(in millions of dollars)	2018		2017	
	Net interest income <sup>(2)</sup>	Economic value of equity <sup>(3)</sup>	Net interest income <sup>(2)</sup>	Economic value of equity <sup>(3)</sup>
Impact of a 100-basis-point increase in interest rates	\$ (21)	\$ 51	\$ (8)	\$ -
Impact of a 100-basis-point decrease in interest rates <sup>(4)</sup>	19	(54)	9	-

<sup>(1)</sup> Interest rate sensitivity related to insurance activities is not reflected in the amounts above. For these activities, a 100-basis-point increase in interest rates would result in a \$215 million decrease in the economic value of equity before taxes as at December 31, 2018, and a \$226 million decrease as at December 31, 2017. A 100-basis-point decrease in interest rates would result in an increase of \$222 million in the economic value of equity before taxes as at December 31, 2018, and of \$205 million as at December 31, 2017. Additional information is provided in the "Interest rate risk management" section of Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements.

<sup>(2)</sup> Represents the interest rate sensitivity of net interest income for the next 12 months.

<sup>(3)</sup> Represents the sensitivity of the present value of assets, liabilities and off-balance sheet instruments.

<sup>(4)</sup> The results of the impact of a decrease in interest rates take into consideration the use of a floor to avoid negative interest rates.

## FOREIGN EXCHANGE RISK MANAGEMENT

*Foreign exchange risk arises when the actual or expected value of assets denominated in a foreign currency is higher or lower than that of liabilities denominated in the same currency.*

In certain specific situations, Desjardins Group and its components may become exposed to foreign exchange risk, particularly with respect to the U.S. dollar and the euro. This exposure mainly arises from their intermediation activities with members and clients, and their financing and investment activities. A Desjardins Group policy on market risk has set foreign exchange risk exposure limits, which are monitored by the Risk Management Executive Division. To ensure that this risk is properly controlled, Desjardins Group and its components also use, among other things, derivative financial instruments such as forward exchange contracts and currency swaps. Desjardins Group's residual exposure to this risk is low because it reduces its foreign exchange risk by using derivative financial instruments.

## PRICE RISK MANAGEMENT

In its non-trading activities, Desjardins Group is exposed to price risk, related mainly to components that operate in insurance and their investment portfolios. *Price risk is the risk of potential loss resulting from a change in the market value of assets (shares, commodities, real estate properties, index-based assets) but not resulting from a change in interest rates or foreign exchange rates, or in the credit quality of a counterparty.*

### Management of price risk related to real estate activities

The insurance components may be exposed to changes in the real estate market through the properties they own, whose market value may fluctuate. They manage this risk using policies that set out diversification limits such as geographic limits and limits for real estate property categories. Each real estate investment is subject to an annual professional appraisal to determine its market value in accordance with the standards prescribed by regulatory authorities.

### Management of price risk related to stock markets

The insurance components may also be exposed to price risk related to stock markets, particularly through the equity securities and derivative financial instruments they hold as well as the minimum guarantees provided under segregated fund contracts, whose value is affected by market fluctuations. They manage this risk using the different limits set in policies and a hedging program to mitigate the effect of market volatility. For additional information, see Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements.

## Liquidity risk

*Liquidity risk refers to Desjardins Group's capacity to raise the necessary funds (by increasing liabilities or converting assets) to meet a financial obligation, whether or not it appears on the Consolidated Balance Sheets.*

Desjardins Group manages liquidity risk in order to ensure that it has timely and cost-effective access to the funds needed to meet its financial obligations as they become due, in both routine and crisis situations. Managing this risk involves maintaining a sufficient level of liquid securities, ensuring stable and diversified sources of financing, monitoring indicators and having a contingency plan in the event of a liquidity crisis.

Liquidity risk management is a key component of the overall risk management strategy. Desjardins Group and its components have established policies describing the principles, limits, risk appetite thresholds as well as the procedures that apply to liquidity risk management. These policies are reviewed on a regular basis to ensure that they are appropriate for the operating environment and prevailing market conditions. They are also updated to reflect regulatory requirements and sound liquidity risk management practices. Given that the insurance companies are subject to specific regulatory requirements, they manage their liquidity risks based on their own needs while following Desjardins Group guidelines. The securities held by these components are not taken into account in the valuation of Desjardins Group's liquidity reserves, since they cannot be used by Desjardins Group's Treasury to generate liquidity for other components.

Desjardins Group's Treasury ensures stable and diversified sources of institutional funding by type, source and maturity. It uses a wide range of financial products and borrowing programs on various markets for its funding needs. Through these operations, the funding needs of Desjardins Group components can be satisfied under conditions comparable to those offered on capital markets.

Furthermore, Desjardins Group issues covered bonds and securitizes CHMC-insured loans in the course of its normal operations. Desjardins Group is also eligible for the Bank of Canada's various intervention programs and loan facilities for Emergency Lending Assistance advances.

The implementation of Basel III strengthens international minimum liquidity requirements through the application of a liquidity coverage ratio (LCR), a net stable funding ratio (NSFR) and the use of Net Cumulative Cash Flow (NCCF). Under its liquidity risk management policy, Desjardins Group already produces these two ratios as well as the NCCF, and reports them on a regular basis to the AMF. The effective date of the regulatory requirements concerning the NSFR has been postponed to January 1, 2020, and Desjardins Group intends to comply with the NSFR requirements once they become effective.

Applying the calculation rules established by the Basel Committee on Banking Supervision and incorporated in the AMF's Liquidity Adequacy Guideline, Desjardins Group's average LCR was 122.1% for the quarter ended December 31, 2018, compared to 120.0% for the previous quarter. The AMF requires that the ratio be greater than or equal to 100% in the absence of stressed conditions. This ratio is proactively managed by Desjardins Group's Treasury, and an appropriate level of high-quality liquid assets is maintained for adequate coverage of the theoretical cash outflows associated with the standardized crisis scenario within the Basel III framework. Desjardins Group's main sources of theoretical cash outflows are a potential serious run on deposits by members of Desjardins caisses and a sudden drying-up of the short-term institutional funding sources used on a day-to-day basis by Desjardins Group.

### Liquidity risk measurement and monitoring

Desjardins Group determines its liquidity needs by reviewing its current operations and evaluating its future forecasts for balance sheet growth and institutional funding conditions. Various analyses are used to determine the actual liquidity levels of assets and the stability of liabilities based on observed behaviours or contractual maturities. Maintaining liquidity reserves of high-quality assets is required to offset potential cash outflows following a disruption in capital markets, or events that would restrict its access to funding or result in a serious run on deposits.

The minimum liquid asset levels to be maintained by Desjardins Group are specifically prescribed by policies. Daily management of these securities and the reserve level to be maintained is centralized at Desjardins Group Treasury and is subject to monitoring by the Risk Management function under the supervision of the Finance and Risk Management Committee. Securities eligible for liquidity reserves must meet high security and negotiability criteria and provide assurance of their adequacy in the event of a severe liquidity crisis. The securities held are largely Canadian government securities.

In addition to complying with regulatory ratios, a Desjardins-wide stress testing program has been set up. This program incorporates the concepts put forward by the Basel Committee on Banking Supervision in “Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring”. The scenarios, based on a downgrade of Desjardins Group combined with a shock on capital markets, make it possible to:

- measure the extent, over a one-year period, of potential cash outflows in a crisis situation;
- implement liquidity ratios and levels to be maintained across Desjardins Group;
- assess the potential marginal cost of such events, depending on the type, severity and level of the crisis.

The calculations are performed daily to ensure compliance with the liquidity levels to be maintained based on the acute stress scenarios.

#### Liquidity risk indicators

The purpose of monitoring liquidity indicators daily is to quickly identify a lack of liquidity, whether potential or real, within Desjardins Group and on capital markets. Warning levels subject to an escalation process are established for each of these indicators. If one or more indicators trigger a warning level, the Desjardins Group Finance and Risk Management Committee is immediately alerted. This committee would also act as a crisis committee should the contingency plan be put into action.

This plan lists the sources of liquidity available in exceptional situations. In addition, it lays down the decision-making and information process based on the severity level of a potential crisis. The aim of the plan is to allow quick and effective intervention in order to minimize disruptions caused by sudden changes in member and client behaviour and potential disruptions in capital markets or economic conditions. Furthermore, in the event of a crisis extensive enough to question Desjardins Group's creditworthiness, a living will has been prepared to enable the crisis committee to draw on a broader range of liquidity sources to deal with the situation.

## SOURCES OF FINANCING

Core funding, which includes capital, long-term liabilities and a diversified deposit portfolio, is the foundation upon which the Federation's liquidity position depends. The solid base of deposits from member caisses combined with wholesale funding, diversified in terms of the programs used as well as the staggering of contractual maturities, allows high regulatory liquidity ratios to be maintained while ensuring their stability. The deposits of member caisses are presented on the Consolidated Balance Sheets, under “Deposits – Deposit-taking institutions” and accounted for 4.5% of total consolidated liabilities as at December 31, 2018, compared to 3.9% a year earlier. Total deposits, including wholesale funding, presented on the Consolidated Balance Sheets amounted to \$58.1 billion as at December 31, 2018, up \$5.9 billion since December 31, 2017. Additional information on deposits is found in Section 3.1 “Balance sheet management” of this MD&A.

### Financing programs and strategies

As Desjardins Group's treasurer, the Federation meets the needs of the organization's members and clients. Its first priority is to implement appropriate strategies to identify, measure and manage risks, which strategies are regulated by policies. In 2018, the Federation succeeded in maintaining a liquidity level sufficient to meet Desjardins Group's needs through its strict treasury policy, solid institutional financing and the contribution of the caisse network. Short-term wholesale financing is used to finance very liquid assets while long-term wholesale financing is mainly used to finance less liquid assets and to support reserves of liquid assets.

In order to secure long-term financing at the lowest cost on the market, the Federation maintains an active presence in the federally-guaranteed mortgage loan securitization market under the *National Housing Act* (NHA) Mortgage-Backed Securities Program. In addition, to ensure stable financing, it diversifies its sources from institutional markets. It therefore regularly resorts to the capital markets when conditions are favourable, and makes public and private issues of term notes on Canadian, U.S. and European markets as required.

The main programs currently used by the Federation are:

**Table 33 – Main financing programs**

As at December 31, 2018

Financing program	Maximum authorized amount
Medium-term notes (Canadian)	\$10 billion
Covered bonds (multi-currency)	\$10 billion
Short-term notes (European)	€3 billion
Short-term notes (U.S.)	US\$15 billion
Medium-term notes (multi-currency)	€7 billion

The following table presents the remaining term to maturity of wholesale funding.

**Table 34 – Remaining contractual term to maturity of wholesale funding**

As at December 31

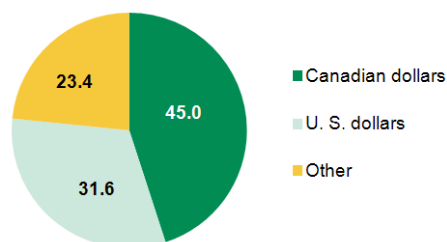
(in millions of dollars)	2018								2017
	Less than 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Total – Less than one year	1 to 2 years	Over 2 years	Total	Total
Bearer discount notes	\$ 2,508	\$ 284	\$ 3	\$ 3	\$ 2,798	\$ -	\$ -	\$ 2,798	\$ 2,802
Commercial paper	5,019	3,262	1,589	3,304	13,174	-	-	13,174	9,276
Medium-term notes	-	-	-	1,728	1,728	4,724	4,205	10,657	11,030
Mortgage securitization	65	318	511	803	1,697	1,104	7,019	9,820	9,164
Covered bonds	-	1,564	-	1,563	3,127	1,562	1,170	5,859	4,517
Subordinated notes	-	-	-	-	-	879	499	1,378	1,388
<b>Total</b>	<b>\$ 7,592</b>	<b>\$ 5,428</b>	<b>\$ 2,103</b>	<b>\$ 7,401</b>	<b>\$ 22,524</b>	<b>\$ 8,269</b>	<b>\$ 12,893</b>	<b>\$ 43,686</b>	<b>\$ 38,177</b>
Including:									
Secured	\$ 65	\$ 1,882	\$ 511	\$ 2,366	\$ 4,824	\$ 3,545	\$ 8,688	\$ 17,057	\$ 15,069
Unsecured	7,527	3,546	1,592	5,035	17,700	4,724	4,205	26,629	23,108

The Federation's total wholesale funding presented in the table above was carried out by the Federation, except for the subordinated notes, which were issued by Desjardins Capital Inc. Total wholesale funding was up \$5.5 billion compared to December 31, 2017, mainly because of an increase in commercial paper and covered bonds.

In addition, the Federation diversifies its financing sources in order to limit its dependence on a single currency. The chart "Wholesale funding by currency" presents a breakdown of borrowings on the markets and subordinated notes by currency. These funds are obtained primarily through short- and medium-term notes, mortgage securitization, covered bonds and subordinated notes.

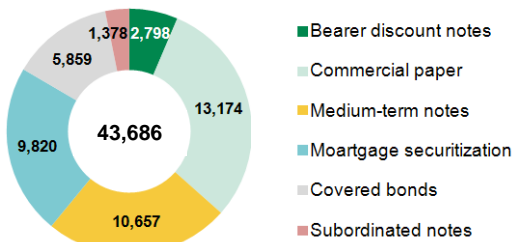
#### Wholesale funding by currency

As at December 31, 2018  
(as a percentage)



#### Wholesale funding by category

As at December 31, 2018  
(in millions of dollars)



Moreover, the Federation participated in new issues under the NHA Mortgage-Backed Securities Program for a total amount of \$2.4 billion for the year. During the same period, it also completed an issue of covered bonds on the European market for a total amount of 750 million euros and an issue of 1.0 billion euros under its multi-currency medium-term note program. In addition, the Federation launched three issues for a total of \$1.8 billion under its Canadian medium-term note program. Note also that on January 30, 2019, the Federation launched a new issue totalling 750 million euros under its covered bond program.

Outstanding notes issued under the Federation's medium-term financing programs amounted to \$26.3 billion as at December 31, 2018, compared to \$24.7 billion a year earlier. The outstanding notes for these issues are presented under "Deposits – Business and government" in the Consolidated Balance Sheets. Desjardins Capital Inc.'s senior notes outstanding totalled \$1.4 billion as at December 31, 2018, unchanged from a year earlier. Furthermore, to round out its financing and increase its capital base, in 2018, Desjardins Group, through the Federation, issued F capital shares for proceeds, net of issuance costs, of \$124 million, as well as F capital shares having a value of \$142 million for the payment of interest when the holder has elected to receive remuneration in F capital shares.

Overall, these transactions made it possible to adequately meet the liquidity needs of Desjardins Group, to better diversify its sources of financing and to further extend their average term.

## CREDIT RATINGS OF SECURITIES ISSUED

Desjardins Group's credit ratings affect its ability to access sources of funding on capital markets, as well as the conditions of such funding. They are also a factor considered in certain Desjardins Group transactions involving counterparties.

Rating agencies assign credit ratings and related ratings outlooks based on their own proprietary methodology, which includes a number of analytical criteria, including factors that are not under Desjardins Group's control. The rating agencies evaluate Desjardins Group primarily on a combined basis and recognize its capitalization, its consistent financial performance, its significant market shares in Quebec and the quality of its assets. Consequently, the credit ratings of the Federation, a reporting issuer, and of Desjardins Capital Inc., a venture issuer, are backed by Desjardins Group's financial strength.

During 2018, the credit ratings and outlooks for the securities issued by Desjardins Group remained unchanged and were affirmed by the rating agencies Moody's, Standard & Poor's (S&P), DBRS and Fitch.

Following the publication, on April 18, 2018, of the final version of regulations to implement the main features of the Bank Recapitalization (Bail-in) Regime by the Department of Finance Canada and of the final version of the TLAC guideline by the OSFI, DBRS, Moody's and S&P issued press releases mentioning several decisions concerning the credit ratings of Canadian domestic systemically important banks (D-SIBs). Since this "bail-in" regime does not apply to Desjardins Group, which is regulated by the AMF, DBRS, Moody's and S&P did not mention Desjardins in their press releases.

The ratings outlooks for Desjardins Group from S&P and Fitch are stable, but DBRS's and Moody's outlooks are negative. The negative ratings outlook assigned to Desjardins Group by DBRS and Moody's is due to uncertainty about the implementation of a "bail-in" regime for Desjardins Group. However, Moody's ratings outlook for Desjardins Capital Inc. is stable.

The Federation and Desjardins Capital Inc. have first-class credit ratings that are among the best of the major Canadian and international banking institutions.

**Table 35 – Credit ratings of securities issued**

	DBRS	STANDARD & POOR'S	MOODY'S	FITCH
<i>Fédération des caisses Desjardins du Québec</i>				
Short-term	<b>R-1 (high)</b>	<b>A-1</b>	<b>P-1</b>	<b>F1+</b>
Medium- and long-term, senior	<b>AA</b>	<b>A+</b>	<b>Aa2</b>	<b>AA-</b>
<i>Desjardins Capital Inc.</i>				
Medium- and long-term, senior	<b>AA (low)</b>	<b>A</b>	<b>A2</b>	<b>A+</b>

Desjardins Group regularly monitors the additional level of obligations its counterparties would require in the event of a credit rating downgrade for the Federation and Desjardins Capital Inc. This monitoring enables Desjardins Group to assess the impact of such a downgrade on its funding capabilities and its ability to perform transactions in the normal course of its operations as well as ensure that it has the additional liquid assets and collateral necessary to meet its obligations. Currently, Desjardins Group is not obliged to provide additional collateral in the event of its credit rating being lowered three notches by one or several credit rating agencies.

## CONTRACTUAL MATURITIES OF ON-BALANCE SHEET ITEMS AND OFF-BALANCE SHEET COMMITMENTS

Table 36 presents assets and liabilities recorded on the Consolidated Balance Sheets and off-balance sheet commitments at their carrying amount and classified according to their residual contractual maturities. The classification of maturities is an information source with regard to liquidity and financing risk, but it differs from the analysis performed by the Federation to determine the expected maturity of the items for liquidity risk management purposes. Many factors other than contractual maturity are taken into consideration to measure expected future cash flows and liquidity risk.

The value of the credit commitments presented in this table represents the maximum amount of additional credit that the Federation could be required to grant if the commitments were fully used. The value of guarantees and standby letters of credit correspond to the maximum cash outflows that the Federation could be required to make in the event of complete default of the parties to the guarantees, without taking any possible recovery into account. These commitments and guarantees do not necessarily represent future liquidity needs, because a large portion of these instruments will expire or be cancelled without giving rise to any cash outflows.

Note 15, "Insurance contract liabilities", provides additional information on the contractual maturities of actuarial liabilities and provisions for claims and adjustment expenses.

**Table 36 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments\***As at December 31, 2018<sup>(1)</sup>

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
<b>Assets</b>										
Cash and deposits with financial institutions	\$ 2,435	\$ 308	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (5)	\$ 2,738
<b>Securities</b>										
Securities at fair value through profit or loss <sup>(2)</sup>	167	718	1,409	977	1,470	2,947	8,471	16,332	4,423	36,914
Securities at fair value through other comprehensive income <sup>(2)</sup>	1,594	767	755	255	293	1,261	3,607	2,556	43	11,131
Securities at amortized cost	1,124	172	196	89	2	1	5	32	-	1,621
Securities borrowed or purchased under reverse repurchase agreements	13,728	311	47	-	-	-	-	-	-	14,086
<b>Loans</b>										
Residential mortgages <sup>(3)</sup>	46	19	102	110	274	547	2,210	1,306	12	4,626
Consumer, credit card and other personal loans <sup>(3)</sup>	52	65	165	189	279	1,061	5,229	5,298	7,372	19,710
Business and governments <sup>(3)</sup>	7,148	1,962	1,704	1,243	1,406	5,626	10,527	1,798	6,578	37,992
Allowance for credit losses	-	-	-	-	-	-	-	-	(491)	(491)
Segregated fund net assets	-	-	-	-	-	-	-	-	13,234	13,234
Clients' liability under acceptances	124	36	-	-	-	-	-	-	-	160
Premiums receivable	178	64	13	3	-	-	-	-	2,120	2,378
Derivative financial instruments	235	391	191	359	215	919	1,843	213	10	4,376
Amounts receivable from clients, brokers and financial institutions	1,455	1	-	-	-	-	-	-	31	1,487
Reinsurance assets	38	76	77	70	68	198	390	1,041	-	1,958
Investment property	-	-	-	-	-	-	-	-	943	943
Property, plant and equipment	-	-	-	-	-	-	-	-	811	811
Goodwill	-	-	-	-	-	-	-	-	121	121
Intangible assets	-	-	-	-	-	-	-	-	389	389
Deferred tax assets	-	-	-	-	-	-	-	-	896	896
Other assets	297	95	75	3	12	9	26	5	1,958	2,480
<b>Total assets</b>	<b>\$ 28,621</b>	<b>\$ 4,985</b>	<b>\$ 4,734</b>	<b>\$ 3,298</b>	<b>\$ 4,019</b>	<b>\$ 12,569</b>	<b>\$ 32,308</b>	<b>\$ 28,581</b>	<b>\$ 38,445</b>	<b>\$ 157,560</b>

See page 81 for footnotes.

**Table 36 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)\***As at December 31, 2018<sup>(1)</sup>

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
<b>Liabilities and equity</b>										
<b>Deposits</b>										
Individuals <sup>(4)</sup>	\$ 659	\$ 101	\$ 33	\$ 28	\$ 42	\$ 90	\$ 142	\$ 3	\$ 3,007	\$ 4,105
Business and governments <sup>(4)</sup>	7,926	5,480	2,142	3,575	3,872	7,396	10,200	2,129	3,278	45,998
Deposit-taking institutions <sup>(4)</sup>	149	151	377	105	169	691	1,852	13	4,447	7,954
Acceptances	124	36	-	-	-	-	-	-	-	160
Commitments related to securities sold short <sup>(5)</sup>	19	490	136	38	1	780	4,316	5,049	-	10,829
Commitments related to securities lent or sold under repurchase agreements	16,233	-	-	-	-	-	-	-	-	16,233
Derivative financial instruments	128	148	163	119	156	656	1,704	248	10	3,332
Amounts payable to clients, brokers and financial institutions	2,078	4	-	-	-	-	-	-	2,023	4,105
Insurance contract liabilities	430	783	929	847	800	1,853	4,286	16,289	2,547	28,764
Segregated fund net liabilities	-	-	-	-	-	-	-	-	13,212	13,212
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	1,578	1,578
Deferred tax liabilities	-	-	-	-	-	-	-	-	254	254
Other liabilities	2,298	407	288	30	15	95	102	42	1,828	5,105
Subordinated notes	-	-	-	-	-	879	-	499	-	1,378
Total equity	-	-	-	-	-	-	-	-	14,553	14,553
<b>Total liabilities and equity</b>	<b>\$ 30,044</b>	<b>\$ 7,600</b>	<b>\$ 4,068</b>	<b>\$ 4,742</b>	<b>\$ 5,055</b>	<b>\$ 12,440</b>	<b>\$ 22,602</b>	<b>\$ 24,272</b>	<b>\$ 46,737</b>	<b>\$ 157,560</b>
<b>Off-balance sheet commitments</b>										
Credit commitments <sup>(6)</sup>	\$ 3,792	\$ 138	\$ 687	\$ 571	\$ 1,052	\$ 2,469	\$ 7,778	\$ 496	\$ 90,432	\$ 107,415
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	2,474	2,474
Commitments under lease contracts	4	7	11	11	10	38	94	167	-	342
Documentary letters of credit	-	1	-	-	-	-	-	-	-	1
Guarantees and standby letters of credit	18	79	78	191	374	12	16	75	4	847
Credit default swaps	-	-	-	-	-	-	537	-	-	537

See page 81 for footnotes.

**Table 36 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)\***

As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
<b>Assets</b>										
Cash and deposits with financial institutions	\$ 1,343	\$ 378	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 10	\$ 1,731
<b>Securities</b>										
Securities at fair value through profit or loss <sup>(2)</sup>	45	541	1,152	835	2,112	2,195	7,181	15,881	1,712	31,654
Available-for-sale securities <sup>(2)</sup>	2,361	515	815	299	265	1,098	3,957	2,663	3,277	15,250
Securities borrowed or purchased under reverse repurchase agreements	8,982	257	123	15	-	-	-	-	-	9,377
<b>Loans</b>										
Residential mortgages <sup>(3)</sup>	39	49	227	93	120	505	1,934	1,350	6	4,323
Consumer, credit card and other personal loans <sup>(3)</sup>	41	84	196	209	273	1,128	4,473	4,472	6,671	17,547
Business and governments <sup>(3)</sup>	6,579	2,364	1,270	1,378	1,465	5,432	8,753	3,318	6,453	37,012
Allowance for credit losses	-	-	-	-	-	-	-	-	(198)	(198)
Segregated fund net assets	-	-	-	-	-	-	-	-	13,379	13,379
Clients' liability under acceptances	31	-	-	-	-	-	-	-	-	31
Premiums receivable	173	62	13	3	-	-	-	-	1,847	2,098
Derivative financial instruments	99	115	174	159	162	699	2,228	136	-	3,772
Amounts receivable from clients, brokers and financial institutions	1,519	3	-	-	-	-	-	-	41	1,563
Reinsurance assets	35	71	72	63	60	213	423	1,038	227	2,202
Investment property	-	-	-	-	-	-	-	-	817	817
Property, plant and equipment	-	-	-	-	-	-	-	-	780	780
Goodwill	-	-	-	-	-	-	-	-	121	121
Intangible assets	-	-	-	-	-	-	-	-	466	466
Deferred tax assets	-	-	-	-	-	-	-	-	746	746
Other assets	443	68	109	2	5	8	21	-	1,532	2,188
Assets of the disposal group held to be transferred	-	-	-	-	-	-	-	-	881	881
<b>Total assets</b>	<b>\$ 21,690</b>	<b>\$ 4,507</b>	<b>\$ 4,151</b>	<b>\$ 3,056</b>	<b>\$ 4,462</b>	<b>\$ 11,278</b>	<b>\$ 28,970</b>	<b>\$ 28,858</b>	<b>\$ 38,768</b>	<b>\$ 145,740</b>

See page 81 for footnotes.

**Table 36 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)\***

As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
<b>Liabilities and equity</b>										
<b>Deposits</b>										
Individuals <sup>(4)</sup>	\$ 42	\$ 75	\$ 122	\$ 72	\$ 76	\$ 238	\$ 497	\$ 3	\$ 3,228	\$ 4,353
Business and governments <sup>(4)</sup>	9,246	3,768	1,703	1,653	2,134	5,383	12,019	1,602	3,455	40,963
Deposit-taking institutions <sup>(4)</sup>	685	192	279	186	200	687	1,840	6	2,758	6,833
Acceptances	31	-	-	-	-	-	-	-	-	31
Commitments related to securities sold short <sup>(5)</sup>	155	595	114	108	21	1,366	2,225	4,526	2	9,112
Commitments related to securities lent or sold under repurchase agreements	10,062	-	-	-	-	-	-	-	-	10,062
Derivative financial instruments	156	126	191	172	166	558	2,166	142	-	3,677
Amounts payable to clients, brokers and financial institutions	2,628	1	-	-	-	-	-	-	1,618	4,247
Insurance contract liabilities	412	732	897	834	766	1,885	4,121	16,379	2,274	28,300
Segregated fund net liabilities	-	-	-	-	-	-	-	-	13,354	13,354
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	1,741	1,741
Deferred tax liabilities	-	-	-	-	-	-	-	-	204	204
Other liabilities	1,923	427	347	8	9	60	81	741	1,198	4,794
Liabilities of the disposal group held to be transferred	-	-	-	-	-	-	-	-	662	662
Subordinated notes	-	-	-	-	-	-	898	490	-	1,388
Total equity	-	-	-	-	-	-	-	-	16,019	16,019
<b>Total liabilities and equity</b>	<b>\$ 25,340</b>	<b>\$ 5,916</b>	<b>\$ 3,653</b>	<b>\$ 3,033</b>	<b>\$ 3,372</b>	<b>\$ 10,177</b>	<b>\$ 23,847</b>	<b>\$ 23,889</b>	<b>\$ 46,513</b>	<b>\$ 145,740</b>
<b>Off-balance sheet commitments</b>										
Credit commitments <sup>(6)</sup>	\$ 3,569	\$ 110	\$ 149	\$ 225	\$ 397	\$ 2,957	\$ 7,031	\$ 243	\$ 80,604	\$ 95,285
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	2,024	2,024
Commitments under lease contracts	4	7	11	11	11	41	102	212	-	399
Documentary letters of credit	-	-	-	-	1	-	-	-	-	1
Guarantees and standby letters of credit	38	70	37	201	226	-	13	78	4	667
Credit default swaps	-	-	-	-	-	-	540	-	-	540

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated.

For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Equity securities are classified under "No stated maturity".

<sup>(3)</sup> Amounts repayable on demand are classified under "No stated maturity".

<sup>(4)</sup> Deposits payable on demand or after notice are considered as having "No stated maturity".

<sup>(5)</sup> Amounts are presented by remaining contractual maturity of the underlying security.

<sup>(6)</sup> Includes personal lines of credit, lines of credit secured by real or immovable property and credit card lines for which the amounts committed are unconditionally revocable at any time at the Federation's discretion.

## Operational risk

*Operational risk is the risk of inadequacy or failure attributable to processes, people, internal systems or external events and resulting in losses, failure to achieve objectives or a negative impact on reputation.*

Operational risk is inherent to all of Desjardins Group's activities, including management and control practices in other risk areas (credit, market, liquidity, etc.) as well as activities carried out by a third party. This risk may lead to losses mainly resulting from theft, fraud, damage to tangible assets, non-compliance with legislation or regulations, systems failures, unauthorized access to computer systems, cyber threats, or problems or errors in process management. To maintain this risk at an acceptable level, an operational risk management framework has been developed and deployed throughout the organization. The framework includes the usual practices for sound management of operations and is based on the three lines of defence model, clearly defining the roles and responsibilities in risk and operations management.

### OPERATIONAL RISK MANAGEMENT FRAMEWORK

The purpose of the operational risk management framework is to identify, measure, mitigate and monitor operational risk as well as make interventions and disclosures for operational risk in accordance with operational risk appetite and the frameworks adopted by the Board of Directors. It is supported by guidelines setting out operational risk management foundations. At the same time, the operational risk management framework connects with the other areas of risk.

The operational risk management framework is reviewed annually to ensure its adequacy and its relevance based on Desjardins Group's risk profile and developments in industry practices.

### GOVERNANCE

Risk management governance emphasizes accountability and effective risk oversight. Operational risk is governed by a set of policies, directives and rules. These frameworks are reviewed periodically to ensure consistency with the Integrated Risk Management Framework approved by the Board of Directors.

Reporting is done on a regular basis to the committees that provide risk management oversight so that their members can assess Desjardins Group's operational risk exposure.

### Approaches to identifying, measuring and monitoring operational risk

With respect to the operational risk management framework, the following table illustrates the tools and methods used to identify, measure and monitor operational risk.

Description	
<b>Risk identification and measurement</b>	A standard inventory of operational risks to which Desjardins Group is exposed has been prepared and is used as the basis for determining the most significant operational risks and evaluating the effectiveness of the mitigation measures in place to reduce them. The risk and control assessments, carried out on a periodic basis, can be related to projects, products, systems, processes and activities, as well as to strategic initiatives and important new products. Consideration of internal and external events (losses, audit findings, etc.) is an integral part of these assessments. When the results indicate operational risk exposures that exceed the established tolerance level, action plans are prepared to reduce exposure to an acceptable level.
<b>Collection of data on operational losses</b>	The collection of internal data on operational losses is carried out to list and quantify losses according to predetermined thresholds. Operational losses are indexed in a database. Through analysis, causes are better understood, trends are determined, and corrective measures are taken when necessary. In addition, external operational risk events in the industry are monitored to detect potential or emerging risks and increase risk management at Desjardins Group, if need be. The main trends identified through analysis of operational losses are reported to the various committees on a regular basis. During 2018, operational losses were consistent with the limits set for risk appetite by senior management and the Board of Directors. Contingent liabilities, including the impact of litigation, are presented in Note 27, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.
<b>Key risk indicators</b>	To monitor their risk profile and track developments in it, the business segments and support functions establish operational risk indicators to help them proactively monitor any increase in their exposure to the most significant risks and act accordingly when the tolerance level is reached.

## Description

<b>Specialized risk assessment programs</b>	Complementing the operational risk management framework are certain programs that are the responsibility of specialized groups. These programs supervise specific risks and track them using their oversight process. They are as follows: <ul style="list-style-type: none"> <li>- Financial disclosure risk management;</li> <li>- Technology risk management;</li> <li>- Business continuity risk management;</li> <li>- Third party risk management;</li> <li>- Risk management related to fraud;</li> <li>- Regulatory risk management;</li> <li>- Risk management related to governance and data quality.</li> </ul>
<b>Risk-sharing insurance programs</b>	Desjardins Group has developed insurance programs to give itself additional protection against material operational losses. These programs offer protection based on the business segment's needs, the institution's risk tolerance, as well as emerging risks on the market.
<b>Calculation of capital exposed to operational risk</b>	Since second quarter 2017, Desjardins Group has used the Standardized Approach to calculate its operational risk in the form of regulatory capital exposed to operational risk.

## Insurance risk

*Insurance risk refers to the risk that events may turn out differently from the assumptions used when designing, pricing or measuring actuarial reserves for insurance products, and that profitability of these products may be affected.*

Desjardins Group is exposed to insurance risk in the course of its life and health and property and casualty insurance operations.

Insurance risk for the life and health insurance subsidiaries is composed of the following elements:

- mortality risk: Potential loss resulting from an increase in the mortality rate of insureds;
- longevity risk: Potential loss resulting from an increase in the life expectancy of insureds;
- morbidity/disability risk: Potential loss resulting from a decline in the state of health of insureds;
- policyholder behaviour risk: Potential loss resulting from unfavourable policyholder behaviour in keeping their policy in force or exercising any options specified in policies;
- expense risk: Potential loss resulting from an increase in the level of expenses.

Insurance risk for the property and casualty insurance subsidiaries is composed of the following elements:

- underwriting risk: Potential loss resulting from an increase in the frequency or severity of losses (e.g., fire, theft, water damage, vandalism) covered by the insurance products offered, which mainly cover physical damage to property, bodily injury as well as liability of insureds (civil, legal, etc.);
- catastrophe risk: Potential loss resulting from an increase in the frequency or severity of catastrophes covered by insurance policies;
- reserve risk: Potential loss resulting from inadequate provisions or actuarial reserves.

Identifying, assessing and mitigating the risks associated with new insurance products and changes made to existing ones are part of a thorough product approval process. All risks at the insurance subsidiaries, including insurance risk, are managed in accordance with their Integrated Risk Management Policy, in line with Desjardins Group's Integrated Risk Management Framework. The process of logging risks under this policy makes it possible to identify all risks likely to affect the subsidiary concerned that should be the subject of governance and a framework, as well as to maintain a register of all such risks and assess them using the appropriate method.

The subsidiaries are responsible for the risk they generate, including insurance risk. Each one has its own specific governance structure. Insurance risk is governed by several policies that clearly set out the roles and responsibilities of the different parties concerned so that they can comply with the various regulatory guidelines. The subsidiaries also have a robust infrastructure that includes the appropriate tools for ensuring the availability, integrity, completeness and aggregation of all the data necessary for sound insurance risk management.

Insurance risk arises from potential errors in projections concerning the many factors used to set premiums, including future returns on investments, underwriting experience in terms of claims experience, mortality and morbidity, and administrative expenses. These projections are essentially based on actuarial hypotheses that must be consistent with the standards of practice in effect in Canada. The insurance subsidiaries also adopt strict pricing standards and policies and perform spot checks to compare their projections with actual results. Insurance product design and pricing are reviewed on a regular basis. Some product pricing may be adjusted depending on the accuracy of projections.

In addition, the subsidiaries limit their losses through reinsurance treaties that vary based on the nature of the activities, and also through additional reinsurance protection with respect to large-scale catastrophic events.

To reduce reinsurance risk, the insurance subsidiaries do business with many reinsurers that meet financial strength criteria, most of which are governed by the same regulatory authorities as the subsidiaries. Such reinsurance treaties do not release the subsidiaries from their obligations toward their policyholders but do mitigate the risks to which they are exposed.

The subsidiaries comply with the standards for sound management practices established by the regulatory bodies that govern them and test their financial soundness using unfavourable scenarios and measure the effect of such scenarios on their capitalization ratio. These tests include stress testing, including the standardized acute stress scenarios required from time to time by regulators, as well as dynamic capital adequacy testing. Test results showed that capital was adequate in each case.

Each insurance sector subsidiary provides independent reports and assessments of its exposure to different risks to its Board of Directors as well as to the appropriate levels at Desjardins Group. They report in particular on changes in material risks and the effectiveness of the procedures in place to mitigate them, the results of risk analyses, and the main assumptions and findings from the stress testing.

The activities specific to the insurance subsidiaries expose them, in addition to insurance risk, to other types of risk, notably the risks identified in Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements, as well as other risk factors identified in Section 4.1 "Risk factors that could impact future results".

## Strategic risk

*Strategic risk refers to the risk of loss attributable to an inability to adapt to a changing environment because of failure to act, an inappropriate strategic choice or the inability to effectively implement strategies.*

It is first up to senior management and the Board of Directors to address, define and monitor developments in the strategic orientations of Desjardins Group according to its risk appetite and the consultation processes specific to Desjardins. Events that could compromise the achievement of Desjardins Group's strategic objectives are systematically and periodically monitored by the board of directors and senior management. Business segments and support functions identify and periodically assess events and risks that could prevent the achievement of strategic objectives, and report thereon to the appropriate bodies.

Organizational development plans are assessed in light of the organization's risk appetite framework to ensure that such initiatives are in line with the organization's strategic plan. Furthermore, this plan is updated annually to take market developments into account, in particular major trends in the industry and action taken by competitors.

## Reputation risk

*Reputation risk is the risk that a negative perception by the stakeholders, whether or not justified, of Desjardins Group's practices, actions or lack of action could have an unfavourable impact on its income and equity, and the trust that it inspires.*

A reputation is of critical importance, and reputation risk cannot be managed separately from other risks. Therefore, managing reputation risk in all its business segments is a constant concern for Desjardins Group. In this regard, Desjardins Group seeks to ensure that all employees are constantly aware of the potential repercussions of their actions on Desjardins's reputation and image. Desjardins Group considers it essential to foster a proactive approach to risk management in which integrity and ethical conduct are fundamental values.

Desjardins Group has defined a management framework, and roles and responsibilities with regard to reputation risk. This framework is in addition to various processes already in place to identify, measure and govern this risk, such as the previously mentioned operational risk management initiatives, the regulatory compliance program, ethical requirements, and reputation risk assessment as part of new initiatives and the introduction of new products. All these aspects aim to promote sound reputation risk management. All officers and employees are required to perform their duties in accordance with these principles and Desjardins Group's values.

## Pension plan risk

*Pension plan risk is the risk of loss resulting from pension plan commitments made by Desjardins Group for the benefit of its employees. This risk basically arises from rate, price, foreign exchange and longevity risks.*

The organization's main pension plan is the Desjardins Group Pension Plan (DGPP). The Federation, through its Board of Directors, is the sponsor of the DGPP and, as such, acts as the representative for all Desjardins Group employers. The Desjardins Group Retirement Committee, which is composed of members of the Board of Directors of the Federation and representatives of active participants and retirees, is the administrator of the DGPP. It is responsible for managing pension fund assets and administering the benefits promised by the plan. It sees to it that the rules specified in the plan are applied and ensures legal compliance as well as sound governance of the plan. In this regard, it has developed policies and an internal by-law as required under the *Supplemental Pension Plans Act*.

To properly manage DGPP risks, the Desjardins Group Retirement Committee has set up a Risk Management Advisory Committee. This committee, under the responsibility of the Desjardins Group Retirement Committee, is tasked with analyzing the main risks associated with management of DGPP operations. In this regard, it examines the integrated risk profile and the asset allocation strategy every year. It also issues opinions on new investments which are submitted to the Investment Committee. In addition, a risk management dashboard for the DGPP, made up of risk indicators identified in the profile, is updated quarterly.

## Environmental or social risk

*Environmental or social risk results from an environmental event or social issue during Desjardins Group's operations or its financing, investment or insurance activities, which could lead to financial loss or harm its reputation.*

Regarding environmental risk, potential financial losses could be incurred as a result of higher costs or the impairment of an asset because of an internal risk, namely a risk generated by an entity and having a negative impact on the environment, or an external risk, namely an event caused by the environment and having a detrimental effect on the entity. Climate change is identified as an external risk factor and defined in Section 4.1 "Risk factors that could impact future results".

In addition, business relations with entities whose operations could involve social, environmental or governance issues could lead to reputation risk.

In order to mitigate environmental or social risk, and to uphold its commitment to contribute to the development of a sustainable and responsible economy, Desjardins Group has incorporated Environmental, Social or Governance (ESG) factors into all of its business decisions. Tools and reference materials are being developed to support business segments. An ESG orientation committee, a subcommittee of Desjardins Group's Management Committee, has been set up to recommend orientations and promote a cohesive approach within the organization.

Since sustainable development is an integral part of Desjardins's strategic priorities, Desjardins Group has developed a sustainable development policy for all its operations, incorporating orientations for the development of a sustainable and responsible economy as part of the strategic alignment of its risk appetite framework.

Furthermore, Desjardins Group maintains its leadership in sustainable development through a number of integrated initiatives in its Strategic Plan and its performance management, particularly by setting targets for reducing its carbon footprint and gradually integrating these targets into its performance objectives. It is also continuing the innovative development of products and services, focused on sustainable development, for its members and clients. All these initiatives may be consulted in its annual social and cooperative responsibility report based on Global Reporting Initiative (GRI) indicators. This report is not incorporated by reference in this MD&A.

In addition, recognizing the major impact of climate change on the environment, society and the economy, Desjardins Group periodically updates its analysis of climate change risks and reports to senior management on the importance of each risk identified and the actions to be taken to mitigate such risks. Its strategy and management of these risks are also disclosed to the CDP (formerly known as the Carbon Disclosure Project) as well as in a specific climate change report based on the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) and forming an integral part of the annual social and cooperative responsibility report.

## Legal and regulatory risk

*Legal and regulatory risk refers to the risk associated with Desjardins Group's non-compliance with the obligations arising from the interpretation or application of legislative and regulatory provisions or contractual commitments, which could affect its operations, reputation, strategies and financial objectives.*

Legal and regulatory risk entails, *inter alia*, effectively preventing and handling possible disputes and claims that may lead in particular to judgments or decisions by a court of law or regulatory body that could result in orders to pay damages, financial penalties or sanctions. Moreover, the legal and regulatory environment is evolving quickly and could increase Desjardins Group's exposure to new types of litigation. In addition, some lawsuits against Desjardins Group may be very complex and be based on legal theories that are new or have never been verified. The outcome of such lawsuits may be difficult to predict or estimate until the proceedings have reached an advanced stage, which may take several years. Class action lawsuits or multi-party litigation may feature an additional risk of judgments with substantial monetary, non-monetary or punitive damages. Plaintiffs who bring a class action or other lawsuit sometimes claim very large amounts and it is impossible to determine Desjardins Group's liability, if any, for some time. Legal liability or an important regulatory measure could have an adverse effect on the current activities of Desjardins Group, its results of operations and its financial position, in addition to damaging its reputation. Even if Desjardins Group won its court case or was no longer the subject of measures imposed by regulatory bodies, these situations could harm its reputation and have an adverse impact on its financial position, due in particular to the costs associated with such proceedings, and its brand image.

The financial services industry is one of the most strictly regulated and monitored sectors. In recent years, the regulations governing the industry have expanded significantly in response to numerous socio-economic phenomena such as the development of new, increasingly complex financial products, the continuing volatility in the securities industry, financial fraud, the fight against money laundering and terrorist financing, and the fight against tax evasion, to mention but a few. In addition to federal (Canada and the U.S.) and provincial government requirements, the regulatory environment also includes organizations such as the AMF, the Canadian Securities Administrators, the OSFI, the Financial Transactions and Reports Analysis Centre of Canada, the Mutual Fund Dealers Association of Canada, and the Investment Industry Regulatory Organization of Canada. Complying with important legislative and regulatory provisions, such as those for the protection of personal information, laws and regulations governing insurance, the *Foreign Account Tax Compliance Act*, the Standard for Automatic Exchange of Financial Account Information in Tax Matters, the *Dodd-Frank Wall Street Reform and Consumer Protection Act* and the Basel accords, requires considerable technical, human and financial resources and also affects the way Desjardins Group manages its current operations and implements its business strategies.

As an independent supervisory function, the Office of the Chief Compliance Officer of Desjardins Group fosters a proactive approach to compliance by fully integrating compliance into the organization's current operations. It is responsible for developing, updating and maintaining the compliance management framework, which is based on the identification and monitoring of regulatory obligations and the functional units subject to them. Regulatory developments and their impact on operations are therefore monitored and evaluated on an ongoing basis by the compliance function in cooperation with the Office of the Chief Legal Officer, and strategies are implemented as required to mitigate them. The compliance function provides support to managers in charge of business segments and support functions so that they can effectively manage their risks, by developing an appropriate framework and documentation, acting in an advisory capacity, setting up training programs and conducting periodic inspections of operations. The Desjardins Group Monitoring Office provides an independent assessment of the effectiveness of the compliance management framework. Lastly, Desjardins Group has set up a formal reporting process related to compliance for its senior management and various decision-making bodies. In addition, to maintain its reputation for integrity as well as the confidence of its members and clients, the market and the general public, Desjardins Group has developed a code of professional conduct applicable to all its officers and employees and to all its components. This overall management of compliance provides reasonable assurance that Desjardins Group's operations are carried out in compliance with applicable regulations. Despite all these efforts, Desjardins Group may not be able to predict the exact impact of regulatory developments and appropriately implement strategies to respond. It could then sustain an adverse impact on its financial performance, its operations and its reputation. For further information, refer to the "Regulatory environment" section of this MD&A.

Bill 141, mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions, was passed on June 13, 2018. The chapter concerning the *Groupe coopératif* (the cooperative group) came into force when the first internal by-law of the cooperative group was passed on December 7, 2018. The new provisions of the *Insurers Act* will come into force on June 13, 2019, or subsequently, as the case may be, along with a large portion of the amendments to the *Act respecting the distribution of financial products and services*. For further information, see pages 10 and 11 in the "Changes in the regulatory environment" section, which presents changes in the regulations applicable to Desjardins Group.

## 4.3 Additional information related to certain risk exposures

The tables below provide more details about more complex financial instruments that carry a higher risk.

**Table 37 – Asset-backed securities**

As at December 31

(in millions of dollars)	2018		2017	
	Notional amounts	Fair value	Notional amounts	Fair value
Financial asset-backed and mortgage-backed securities <sup>(1)</sup>	\$ 138	\$ 140	\$ 146	\$ 148

<sup>(1)</sup> None of the securities held is directly backed by subprime residential mortgage loans. Further to the adoption of IFRS 9 on January 1, 2018, these securities are presented under "Securities at fair value through profit or loss" and "Securities at fair value through other comprehensive income" on the Consolidated Balance Sheets.

As at December 31, 2017, they were presented under "Securities at fair value through profit or loss" and "Available-for-sale securities".

**Table 38 – Leveraged finance loans and subprime loans**

As at December 31

(in millions of dollars)	2018	2017
Leveraged finance loans <sup>(1)</sup>	\$ 81	\$ 149
Alt-A mortgage loans <sup>(2)</sup>	18	19
Subprime residential mortgage loans <sup>(3)</sup>	2	1

<sup>(1)</sup> Leveraged finance loans are defined as loans to large corporations and finance companies whose credit rating is between BB+ and D, and whose level of indebtedness is very high compared to other companies in the same industry.

<sup>(2)</sup> Alt-A mortgages are defined as loans to borrowers with non-standard income documentation. These loans are presented in the Consolidated Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

<sup>(3)</sup> These loans are defined as loans to borrowers with a high credit risk profile. Subprime residential mortgages are recorded in the Consolidated Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

## 5.0 Additional information

### 5.1 Controls and procedures

The Federation complies with certain requirements of the regulations prescribed by the Canadian Securities Administrators (CSA) respecting continuous disclosure obligations, oversight of independent auditors, certification of financial disclosures, and audit committees.

Therefore, during 2018, the Federation carried out work so that it could provide certification as at December 31, 2018 of the design and effectiveness of its disclosure controls and procedures, as well as of its internal control over financial reporting.

#### DISCLOSURE CONTROLS AND PROCEDURES

In accordance with the CSA guidance in National Instrument 52-109, the President and CEO as well as the Executive Vice-President, Finance, Treasury and Administration and Chief Financial Officer (CFO) designed, or caused to be designed, disclosure controls and procedures, which are supported in particular by a process for periodic certification of financial disclosures in annual and interim filings. All information collected as part of the financial governance process is reviewed on a quarterly and annual basis by the members of the Desjardins Group Disclosure Committee and of the Audit and Inspection Commission, who play a lead role in overseeing and assessing the adequacy of disclosure controls and procedures.

As at December 31, 2018, the Federation's management assessed the design and effectiveness of its disclosure controls and procedures. Based on the results of this assessment, the President and CEO, and the CFO concluded that disclosure controls and procedures were adequately designed and effective. These controls and procedures are designed to provide reasonable assurance that the information presented in annual, interim or other reports filed or transmitted under securities legislation is recorded, processed, summarized and reported within the time periods prescribed by such legislation. These controls and procedures are also designed to warrant that such information is assembled and disclosed to the Federation's management, including its signing officers, in accordance with what is appropriate to make timely decisions regarding disclosure.

#### INTERNAL CONTROL OVER FINANCIAL REPORTING

The Federation's management caused an adequate internal control over financial reporting process to be designed and has maintained it. This process is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS.

The design and effectiveness of internal control over financial reporting were assessed in accordance with the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control – Integrated Framework (2013) for financial controls and in accordance with the Control Objectives for Information and Related Technologies (COBIT) framework for IT general controls.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements on a timely basis. Management's assessment of the controls provides only reasonable, not absolute, assurance that all the problems related to control which could give rise to material misstatements have been detected.

The assessment of the design and effectiveness of internal control over financial reporting was performed by the Federation's management under the supervision of the President and CEO, and of the CFO. Based on the results of this assessment, these senior officers concluded that as at December 31, 2018, internal control over financial reporting was adequately designed and effective, and did not contain any material weakness. These controls provide reasonable assurance regarding the reliability of the Federation's financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS.

#### CHANGE IN INTERNAL CONTROL OVER FINANCIAL REPORTING

During the year ended December 31, 2018, the Federation did not make any changes to its internal control over financial reporting that had materially affected, or may materially affect, its operations. On January 1, 2018, the adoption of IFRS 9, "Financial Instruments", IFRS 15, "Revenue from Contracts with Customers", and the amendments to IFRS 4, "Insurance Contracts", did not materially affect its internal control over financial reporting.

Various other aspects of corporate governance are examined in more detail in section "Corporate governance" of the Federation's 2018 Annual Report.

### 5.2 Related party disclosures

In the normal course of operations, the Federation offers financial services to related parties, including its associates and other related companies, and enters into agreements for operating services with them. It also pays its key management personnel compensation under normal market conditions.

The Federation and its subsidiaries carry out transactions with related parties, primarily member caisses. Services provided to the member caisses include various technical, administrative and financial services, for which income, such as assessments and fees, are collected. At the same time, the member caisses receive remuneration from the Federation on products and services such as credit cards, payroll services and investment fund and financial engineering services. The Federation also acts as treasurer, thereby allowing the member caisses to borrow or lend liquidities. Member caisses and the Federation also enter into swap contracts.

Through Desjardins Investments Inc., the Federation receives management fees as manager for Desjardins Funds in exchange for the following services: accounting, record keeping, custody of securities, portfolio management and transfer agent services. Through Desjardins Trust Inc., the Federation also receives fees as fund depositary. Finally, it receives management income from pension plans and interest expense paid to the Desjardins Group Pension Plan.

Furthermore, the Federation provides its financial products and services, under normal market conditions, to its directors, its key management personnel and the persons related to them.

The Federation has set up a process to obtain assurance that all transactions with its officers and the persons related to them have been carried out as arm's-length transactions and in compliance with the legislative framework for its various components.

Additional information about related party transactions is presented in Note 32, "Related party disclosures", to the Annual Consolidated Financial Statements.

## 5.3 Critical accounting policies and estimates

A description of the accounting policies used by the Federation is essential to understanding the Consolidated Financial Statements as at December 31, 2018. The significant accounting policies are described in Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements. Some of these policies are of particular importance in presenting the Federation's financial position and operating results because they require management to make judgments as well as estimates and assumptions that may affect the reported amounts of some assets, liabilities, income and expenses, as well as related information. The significant accounting policies that required management to make difficult, subjective or complex judgments, often involving uncertainties, are discussed below.

### STRUCTURED ENTITIES

A structured entity is consolidated when it is controlled by the Federation. Management must make significant judgments when it assesses the various elements and all related facts and circumstances as a whole to determine whether control exists, especially in the case of structured entities.

A structured entity is an entity that has been designed so that voting rights or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: restricted activities, a narrow and well-defined objective, insufficient equity to permit it to finance its activities without subordinated financial support, or financing in the form of multiple contractually linked instruments issued to investors.

Additional information about structured entities is presented in Note 13, "Interests in other entities", to the Consolidated Financial Statements.

### DETERMINATION OF THE FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value measurement of financial instruments is determined using a three-level hierarchy, reflecting the importance of the inputs used for the measurements. Level 1 denotes measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities, while level 2 designates valuation techniques based primarily on observable market data. Level 3 concerns valuation techniques not based primarily on observable market data.

There is little subjectivity in the determination of the fair value of financial instruments, especially securities and commitments related to securities sold short, obtained from quoted prices on active markets. This fair value is based on the quoted price within the bid-ask spread that is most representative of fair value in the circumstances.

If there are no quoted prices on active markets, fair value is determined using models that maximize the use of observable inputs and minimize the use of unobservable inputs. In such cases, fair value estimates are established using valuation techniques such as cash flow discounting, comparisons with similar financial instruments, option pricing models and other techniques commonly used by market participants, if these techniques have been demonstrated to provide reliable estimates. Valuation techniques rely on assumptions concerning the amount and timing of estimated future cash flows and discount rates that are mainly based on observable data, such as interest rate yield curves, exchange rates, credit curves and volatility factors. When one or several material inputs are not observable on the market, fair value is determined mainly based on internal inputs and estimates that take into account the characteristics specific to the financial instrument and any factor relevant to the measurement. For complex financial instruments, significant judgment is used in determining the valuation technique to be used and in selecting inputs and adjustments associated with this technique. Due to the need to use estimates and make judgments when applying many valuation techniques, fair value estimates for identical or similar assets may differ between entities. Fair value reflects market conditions on a given date and may not be representative of future fair values. It should not be considered as being realizable in the event of immediate settlement of these instruments.

### Loans

The fair value of performing loans is determined by discounting expected contractual cash flows using market interest rates charged for similar new loans at the reporting date and takes estimated prepayments into account, adjusted to take into account credit losses on the loan portfolio. Changes in interest rates and in the creditworthiness of borrowers are the main causes of changes in the fair value of loans held by the Federation, which result in a favourable or unfavourable difference compared to their carrying amount.

## Deposits

The fair value of fixed-rate deposits is determined by discounting expected cash flows using market interest rates currently being offered for deposits with substantially the same term and takes estimated prepayments into account. The fair value of deposits with floating-rate features or with no stated maturity is assumed to be equal to their carrying amount.

## Subordinated notes

The fair value of subordinated notes is based on brokers' quotes.

## Derivative financial instruments

The fair value of derivative financial instruments is determined using pricing models that incorporate current market prices and the contractual prices of the underlying instruments, the time value of money, interest rate yield curves, credit curves and volatility factors. This fair value is presented without taking into account the impact of legally enforceable master netting agreements. However, the Federation adjusts the measurement of these instruments based on credit risk, and such adjustments reflect the financial ability of the counterparties to the contracts and the creditworthiness of the Federation, as well as credit risk mitigation measures such as legally enforceable master netting agreements. Note 19, "Derivative financial instruments and hedging activities" describes the type of derivative financial instruments held by the Federation.

## Financial instruments whose fair value equals their carrying amount

The carrying amount of certain financial instruments that mature in the next 12 months is a reasonable approximation of their fair value. These financial instruments include the following items: "Cash and deposits with financial institutions", "Securities borrowed or purchased under reverse repurchase agreements", "Clients' liability under acceptances", "Premiums receivable", "Amounts receivable from clients, brokers and financial institutions", some items included in "Other assets – Other", "Acceptances", "Commitments related to securities lent or sold under repurchase agreements", "Amounts payable to clients, brokers and financial institutions" and some items included in "Other liabilities – Other".

Additional information on the fair value of financial instruments is presented in Note 4, "Fair value of financial instruments", to the Consolidated Financial Statements.

## DERECOGNITION OF FINANCIAL ASSETS

A financial asset is derecognized from the Consolidated Balance Sheets when the contractual rights to the cash flows from the asset expire, when the contractual rights to receive these cash flows are retained but the Federation has the obligation to pay them to a third party under certain conditions, or when the Federation transfers the contractual rights to receive the cash flows and substantially all the risks and rewards of ownership of the asset have been transferred.

When substantially all the risks and rewards of ownership of the transferred financial asset are retained by the Federation, such asset is not derecognized from the Consolidated Balance Sheets and a financial liability is recognized, when appropriate.

When substantially all the risks and rewards related to a financial asset are neither transferred nor retained, the Federation derecognizes the financial asset over which it does not retain control and recognizes an asset or a liability representing the rights and obligations created or retained in the asset transfer. If control of the financial asset is retained, the Federation continues to recognize the asset in the Consolidated Balance Sheets to the extent of its continuing involvement in said asset.

When a financial asset is derecognized in its entirety, a gain or a loss is recognized in the Consolidated Statements of Income for an amount equal to the difference between the carrying amount of the asset and the value of the consideration received.

Management must use its judgment to determine whether the contractual rights to the cash flows have expired, have been transferred or have been retained with an obligation to pay them to a third party. With respect to the transfer of substantially all the risks and rewards of ownership of the assets, management evaluates the Federation's exposure before and after the transfer as well as the changes in the amount and timing of the net cash flows of the transferred asset. Lastly, management must make judgments to determine whether it controls the financial asset and to measure retained rights.

Additional information about the derecognition of financial assets is presented in Note 8, "Derecognition of financial assets", to the Consolidated Financial Statements.

## IMPAIRMENT OF FINANCIAL INSTRUMENTS

### *Accounting policies applicable since January 1, 2018*

Under IFRS 9, at each reporting date, the Federation recognizes a loss allowance for expected credit losses for debt instruments classified as at amortized cost or as at fair value through other comprehensive income, as well as certain off-balance sheet items, namely loan commitments and financial guarantees, which are not measured at fair value through profit or loss. This allowance is estimated based on an impairment model that comprises three different stages:

- Stage 1: For financial instruments that have not had a significant increase in credit risk since initial recognition and are not considered credit-impaired financial assets, a loss allowance amounting to 12-month expected credit losses is recognized.
- Stage 2: For financial instruments that have had a significant increase in credit risk since initial recognition but are not considered credit-impaired financial assets, a loss allowance amounting to the lifetime expected credit losses is recognized.
- Stage 3: For financial assets considered credit impaired, a loss allowance amounting to the lifetime expected credit losses continues to be recognized.

Financial instruments may, over their life, move from one impairment model stage to another based on the improvement or deterioration in their credit risk and the level of expected credit losses. Instruments are always classified in the various stages of the impairment model based on the change in credit risk between the reporting date and the initial recognition date of the financial instrument and an analysis of evidence of impairment.

### **Determination of significant increases in credit risk**

To determine whether, at the reporting date, credit risk has significantly increased since initial recognition, the Federation bases its assessment on the change in default risk over the expected life of the financial instrument, which requires significant judgment.

To this end, the Federation compares the PD of the financial instrument at the reporting date with its PD at the date of initial recognition. In addition, it considers reasonable and supportable information indicating a significant increase in credit risk since initial recognition, including qualitative information and information about future economic conditions to the extent that it affects the assessment of the instrument's PD. The criteria used to determine a significant increase in credit risk vary depending on the type of clients and are mainly based on a relative change combined with an absolute change in the PD. They also include absolute PD thresholds and certain other criteria. All instruments that are more than 30 days past due are transferred to Stage 2 of the impairment model.

### **Definition of default and credit-impaired financial asset**

The definition of default used in the impairment model corresponds to the definition used for internal credit risk management purposes and for regulatory purposes. It considers relevant quantitative and qualitative factors. In particular, a loan is in default when contractual payments are over 90 days past due. A financial asset is considered credit-impaired when it is in default, unless the detrimental impact on the estimated future cash flows is considered insignificant.

### **Measurement of the loss allowance for expected credit losses**

The loss allowance for expected credit losses reflects an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, and takes into account reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Generally, the loss allowance for expected credit losses represents the present value of the difference between cash flows that are due, or the amount of the commitment that may be used under the terms and conditions of the contract, and total cash flows that the Federation expects to receive. For credit-impaired financial assets, expected credit losses are calculated based on the difference between the gross carrying amount of the asset and estimated cash flows.

The measurement of the loss allowance for expected credit losses is estimated for each exposure at the reporting date and is based on the result of multiplying the three credit risk parameters, namely PD, loss given default (LGD) and exposure at default (EAD). The result of this multiplication is then discounted using the effective interest rate. The parameters are estimated using an appropriate segmentation that considers common credit risk characteristics. For financial instruments in Stage 1 of the impairment model, credit risk parameters are projected over a maximum horizon of 12 months, while for those in Stage 2 or Stage 3, they are projected over the remaining life of the instrument.

To determine the credit risk parameters, financial instruments are aggregated based on their common credit risk characteristics.

The loss allowance for expected credit losses also considers information about future economic conditions. To incorporate forward-looking information relevant to the determination of significant increases in credit risk and the measurement of the loss allowance for expected credit losses, the Federation uses the econometric models for credit risk projection. These models estimate the impact of macroeconomic variables on the various credit risk parameters. The Federation uses three scenarios to determine the loss allowance for expected credit losses and assigns to each scenario a probability of occurrence. It may also make adjustments to take into account the relevant information that affects the measurement of the loss allowance and that has not been incorporated into the credit risk parameters.

For credit-impaired financial assets that are individually material, measuring the loss allowance for expected credit losses does not require using credit risk parameters. It is instead based on an extensive review of the borrower's situation and the realization of collateral held. The measurement represents a probability-weighted present value, calculated using the effective interest rate, of cash flow shortfalls that takes into consideration the impact of various scenarios that may materialize and information about future economic conditions.

## Key data and assumptions

Determining the loss allowance for expected credit losses under IFRS 9 is based on a set of assumptions and methodologies specific to credit risk and changes in economic conditions. Significant judgment must therefore be exercised to determine the loss allowance for expected credit losses. The main items affecting its measurement are the following:

- changes in the borrowers' credit risk rating or probability of default;
- incorporation of forward-looking information;
- estimated life of revolving credit facilities.

### Changes in the borrowers' credit risk rating or probability of default

The borrowers' credit risk rating is the foundation of the credit risk assessment model. The rating of a borrower is directly related to its estimated PD. Many variables are taken into consideration in credit risk assessment models. Changes in the borrowers' credit risk rating have an impact on determining significant increases in credit risk, as this is mainly based on the change in the borrower's PD, and measuring the loss allowance for expected credit losses. Changes in the credit risk rating may increase or decrease the loss allowance for expected credit losses. Generally, a deterioration in a borrower's credit risk rating gives rise to an increase in the allowance, while an improvement results in a decrease in the allowance.

### Incorporation of forward-looking information

The Federation uses three different scenarios to determine the loss allowance for expected credit losses, namely a base scenario, an upside scenario and a downside scenario. Projections for each scenario are provided for a four-year horizon. The macroeconomic variables projected under each scenario and the related probability of occurrence have a significant impact on determining significant increases in credit risk and measuring the loss allowance for expected credit losses. The models vary depending on the portfolios and include one or several of the following main variables: gross domestic product, unemployment rate, the Consumer Price Index, housing prices, the corporate credit spread and the S&P/TSX index. The macroeconomic variable projection and the determination of the probabilities of occurrence of the three different scenarios are reviewed quarterly.

The incorporation of forward-looking information may increase or decrease the loss allowance for expected credit losses. Generally, an improvement in the outlook will give rise to a decrease in the allowance, while a deterioration will result in an increase in the allowance.

### Estimated life of revolving credit facilities

The expected life of most financial instruments is equal to the maximum contractual term during which the Federation is exposed to credit risk, including extension options that may be exercised solely by the borrower. The exception to this rule concerns revolving credit facilities, which consist of personal and business lines of credit and credit card loans, for which their life must be estimated. To determine the life of revolving credit facilities, the Federation determines the period over which there is exposure to credit risk but for which expected credit losses would not be mitigated by normal credit risk management actions, and considers the following:

- the period over which it was exposed to credit risk on similar financial instruments;
- the length of time for defaults to occur on similar financial instruments following a significant increase in credit risk;
- the credit risk management actions that it expects to take once the credit risk on the financial instruments has increased.

The determination of the estimated life of revolving credit facilities has a significant impact on estimating the loss allowance for expected credit losses, mainly for revolving credit facilities in Stage 2 of the impairment model. Generally, an increase in the estimated life of revolving credit facilities gives rise to an increase in expected credit losses.

Additional information about loans and the allowance for credit losses, in particular a sensitivity analysis of the allowance for credit losses, is presented in Note 7, "Loans and allowance for credit losses" to the Consolidated Financial Statements.

## **Accounting policies applicable before January 1, 2018**

Under IAS 39, at the reporting date, the Federation assessed whether there was any objective evidence that a financial asset or a group of financial assets was impaired.

### **Allowance for credit losses on loans**

Under IAS 39, objective evidence of impairment resulted from a loss event that had occurred after the loan was granted but before the reporting date and that had an impact on the estimated future cash flows of loans.

The impairment of a loan or a group of loans was determined by estimating the recoverable amount of these financial assets. The allowance was equal to the difference between this amount and the carrying amount. To determine the estimated recoverable amount of a loan, the Federation discounted the estimated future cash flows at the effective interest rate inherent to the loan. When the amounts and timing of future cash flows could not be estimated with reasonable reliability, the estimated recoverable amount was determined using the fair value of the collateral underlying the loan, net of expected costs of realization, or the observable market price for the loan. The collateral could vary depending on the type of loan.

The allowance for credit losses on loans represented management's best estimate for loan impairment at the reporting date. As part of its evaluation, management had to make judgments to determine the data, assumptions and estimates to be used, including determining when a loan was considered credit-impaired and the amount that could have been recovered. Changing these estimates and assumptions would have had an impact on the allowance for credit losses and the provision for credit losses for the year.

The allowance for credit losses related to credit-impaired loans was measured either individually or collectively for loans that were not individually material, while the allowance for credit losses was measured collectively for non-credit impaired loans.

### Individual allowances

The Federation first reviewed its loan portfolios on a loan-by-loan basis to assess credit risk and determined whether there was any objective evidence of impairment for which a loss should have been recognized in the Consolidated Statements of Income. Loan portfolios for which there was no objective evidence of impairment were included in groups of financial assets having similar credit characteristics and were subject to a collective allowance.

### Collective allowance on credit-impaired loans

Certain consumer, credit card and other personal loan portfolios comprised a large number of homogeneous balances that were not individually material. A collective allowance was established on such loans based on the portfolio's historical net loss rate.

### Collective allowance

The method used by the Federation to determine the collective allowance took into account the risk parameters of the various loan portfolios, in particular through the integration of sophisticated credit risk models. These collective allowance models took into account certain factors such as PD, LGD and EAD. These parameters were based on historical losses and determined according to the category and risk rating of each loan. The measurement of the collective allowance relied heavily on management's judgments and depended on management's assessment of current credit quality trends with respect to business segments, the impact of changes in its credit policies, and economic conditions.

Additional information about loans and the allowance for credit losses is presented in Note 7, "Loans and allowance for credit losses" to the Consolidated Financial Statements.

### **Available-for-sale securities**

Under IAS 39, securities classified in the "Available-for-sale" category were examined at the reporting date to determine whether there was any objective evidence that they were impaired. In measuring the impairment loss, the Federation took into account many factors specific to each investment and all the factors that could have indicated such a loss. Factors considered included, but were not limited to, a significant or prolonged decline in fair value, significant financial difficulties of the issuer, a breach of contract, the increasing probability that the issuer would enter bankruptcy or a restructuring and the disappearance of an active market for the financial asset in question. Management also used its judgment to determine when to recognize an impairment loss.

The Federation individually assessed debt securities classified as "Available-for-sale", including preferred shares with characteristics and behaviour similar to those of debt instruments, to determine whether there was any objective evidence of impairment. For equity securities classified in the "Available-for-sale" category, the objective evidence also included a "significant" or "prolonged" decline in fair value below cost.

Additional information about the recognition of available-for-sale securities under IAS 39 and fair value measurement is presented in Note 3, "Carrying amount of financial instruments", and Note 4, "Fair value of financial instruments", to the Consolidated Financial Statements.

## **IMPAIRMENT OF NON-FINANCIAL ASSETS**

The Federation assesses at the reporting date whether there is evidence that an asset may be impaired. An impairment loss is recognized when the carrying amount of the asset exceeds its recoverable amount.

The recoverable amount represents the higher of the fair value less costs of disposal and the value in use. Fair value represents the best estimate of the amount that could be obtained from the sale of the asset in an arm's-length transaction between knowledgeable and willing parties. The value in use is calculated using the most appropriate method, generally by discounting recoverable future cash flows.

Estimating the recoverable amount of a non-financial asset to determine whether it is impaired also requires that management make estimates and assumptions. Any change in these estimates and assumptions could impact the determination of the recoverable amount of non-financial assets and, therefore, the outcome of the impairment test. The main estimates and assumptions used in calculating the recoverable amount are future cash flows estimated based on internal financial forecasts, expected future earnings, the growth rate and the discount rate.

### **Goodwill and intangible assets with indefinite useful lives**

Goodwill and intangible assets with indefinite useful lives are tested for impairment once a year and when there is possible evidence of impairment.

The impairment test for goodwill and intangible assets with indefinite useful lives is performed based on the recoverable amount of the asset or each cash-generating unit (CGU) (or each group of CGUs) to which goodwill or the intangible asset with an indefinite useful life applies. Significant judgments must be made to estimate the data taken into account in the model used to determine the recoverable amount of each intangible asset with an indefinite useful life or each CGU.

When the recoverable amount of the asset or the CGU is less than the carrying amount, an impairment loss is recognized in the Consolidated Statements of Income for the year and is first recorded as a reduction of the intangible asset with an indefinite useful life or, in the case of a CGU, as a reduction of the goodwill allocated to the CGU (or group of CGUs) and then as a reduction of the other identifiable assets of the CGU (or group of CGUs) pro rata on the basis of their carrying amount in the unit. The allocation of an impairment loss to the assets of a CGU (or group of CGUs) must however not result in their carrying amount being lower than the highest of the following amounts: fair value of the assets less costs to sell, their value in use, and zero. Goodwill impairment losses cannot be reversed.

Note 11, "Goodwill and intangible assets", to the Consolidated Financial Statements provides further information about the impairment of non-financial assets.

## INSURANCE CONTRACT LIABILITIES

### Life and health insurance contract liabilities

Life and health insurance contract liabilities consist of actuarial liabilities, benefits payable, provisions for claims not reported, provisions for dividends and experience refunds as well as policyholder deposits.

Actuarial liabilities represent the amounts which, together with estimated future premiums and net investment income, will provide for all the life and health insurance subsidiaries' commitments regarding estimated future benefits, policyholder dividends and related expenses. The appointed actuary of each of these subsidiaries is required to determine the actuarial liabilities needed to meet its future commitments. These actuarial liabilities are determined using the Canadian Asset Liability Method (CALM), in accordance with Canadian accepted actuarial practices, and they are equal to the value in the Consolidated Balance Sheets of the assets that back them.

### Property and casualty insurance contract liabilities

Property and casualty insurance contract liabilities consist of unearned premiums, provisions for claims and adjustment expenses.

Unearned premiums represent the portion of premiums remaining to be earned at the reporting date.

The provisions for claims and adjustment expenses related to the insurance policies of the property and casualty insurance subsidiaries are estimated using actuarial techniques that consider best estimate assumptions, taking into account currently known data, which are regularly reviewed and updated. Any resulting adjustment is recognized in the Consolidated Statements of Income for the year in which the revision occurs. The provision for claims and adjustment expenses is reported on a discounted basis using the rate of return of the underlying assets, with a margin for adverse deviations.

Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements provides information about accounting for the various life and health and property and casualty insurance contract liabilities, the main assumptions used and the impact on profit or loss of changes to assumptions.

## PROVISIONS

Provisions are liabilities of uncertain timing or amount. A provision is recognized when the Federation has an obligation (legal or constructive) as a result of a past event, the settlement of which should result in an outflow of resources embodying economic benefits, and when a reliable estimate can be made of the amount of the obligation. The amount of the obligation is discounted where the effect of the time value of money is material.

Provisions are based on management's best estimate of the amounts required to settle the obligations on the reporting date, taking into account the relevant risks and uncertainties. As these estimates are forward-looking in nature, management must use its judgment to forecast the timing and amount of future cash flows. Actual results may differ significantly from these forecasts.

## CONTINGENT LIABILITIES

In the normal course of its business, the Federation is involved in various litigation and legal proceedings.

Additional information about contingent liabilities is presented in Note 27, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.

## INCOME TAXES ON SURPLUS EARNINGS

The income tax expense on surplus earnings recognized in the Consolidated Statements of Income comprises the current and deferred tax expense on operating surplus earnings as well as the income tax consequences of remuneration on capital stock and dividends when certain conditions are met. The total income tax expense includes the income tax expense on surplus earnings recognized in the Consolidated Statements of Income as well as current and deferred taxes on items recognized outside profit or loss directly in the Consolidated Statements of Comprehensive Income or the Consolidated Statements of Changes in Equity.

The total income tax expense is based on the expected tax treatment of the transactions. To determine the current and deferred portions of these income taxes, management must make judgments to establish assumptions concerning the dates on which deferred income tax assets and liabilities will be reversed. Significant judgment must be used to interpret the relevant tax legislation in order to determine the income tax expense. If the Federation's interpretation differs from that of taxation authorities or if the reversal dates do not correspond to the forecasted dates, the provision for income taxes on surplus earnings may increase or decrease in subsequent years.

Note 26, "Income taxes on surplus earnings", to the Consolidated Financial Statements provides additional information on income taxes on surplus earnings.

## DIVIDENDS TO MEMBER CAISSES

Dividends to member caisses recognized in the Consolidated Statements of Income reflect management's best estimate. They are based on a resolution of the Board of Directors to recommend to the General Meeting that their payment be approved. The annual dividends are determined on the basis of the distribution of the surplus earnings that the Annual General Meeting of the Federation has approved. Transfers to the reserves are recognized when approved by the member caisses. Dividends to member caisses are allocated to Treasury and Other Support to Desjardins Group Entities.

## EMPLOYEE BENEFITS

The Federation participates in a pension plan and a supplemental pension plan through Desjardins Group's defined benefit group plans. It offers the majority of its employees a defined benefit pension plan and a defined benefit supplemental pension plan. The Federation also offers a post-retirement benefit plan that provides medical, dental and life insurance to retiring employees and their dependents. However, during the fourth quarter of 2018, Desjardins Group notified its employees of amendments to this plan that would come into effect on January 1, 2019. As of that date, Desjardins Group will no longer fund the post-retirement benefit plan for employees who retire, except for employees who meet, as at January 1, 2019, certain criteria allowing them to keep their rights under the current plan. These criteria are based on age and the number of years of participation in the plan.

The Federation participates in defined benefit group pension plans whose risks are shared by entities under common control. The Federation's share in the cost recognized and the net liability for the defined benefit group pension plans of Desjardins Group is mainly determined based on funding rules, as described in the plan's by-laws. The main Desjardins Group pension plan is funded by both employee and employer contributions, which are based on the financial position and the funding policy of the plan. Employers' contributions are determined using a percentage of the assessable payroll for their employees participating in the plan.

The Federation's share in the cost of the group post-retirement benefit plan of Desjardins Group is determined based on the number of active insureds of the Federation as a percentage of the total number of active insureds for Desjardins Group as a whole. The method to determine the share was reviewed during the year and is now based on eligible insureds.

Note 16, "Net defined benefit plan liabilities", to the Consolidated Financial Statements provides further information on accounting for defined benefit plans and on the sensitivity of the key assumptions.

## 5.4 Future accounting changes

Accounting standards and amendments issued by the IASB but not yet effective as at December 31, 2018 are presented below. Regulatory authorities have stated that early adoption of these standards and amendments will not be permitted, unless they indicate otherwise.

### IFRS 16, "LEASES"

In January 2016, the IASB issued IFRS 16, "Leases", which will replace the current standard, IAS 17, "Leases", and related interpretations. IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. Under IFRS 16, a lease is a contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

IFRS 16 introduces a single recognition model for the lessee, thereby eliminating the current distinction between operating and finance leases. The lessee must recognize on the Consolidated Balance Sheets a lease liability corresponding to the present value of the remaining lease payments as well as a right-of-use asset measured at the amount of the lease liability, plus or minus certain adjustments, if any. An interest expense and a depreciation charge relating to the lease liability and the right-of-use asset, respectively, must be recognized and presented separately in the Consolidated Statements of Income. Leases with terms of 12 months or less and low-value leases will continue to be recognized as a lease expense based on the terms of the lease. In addition, the Federation will apply the practical expedient which allows not to separate non-lease components from lease components for a contract.

For the lessor, the standard does not provide for any significant changes except for enhanced disclosures.

The Federation will have to adopt IFRS 16 as at January 1, 2019 on a retrospective basis. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 16 will be recognized in the opening Consolidated Balance Sheet. The Federation decided not to restate comparative periods upon adopting the provisions of IFRS 16. Consequently, the retrospective impact of applying IFRS 16 will be recognized in the Consolidated Balance Sheet as at January 1, 2019, which is the effective date of the new standard. In addition, the Federation elected to apply the following transitional expedients proposed in the standard as at the date of transition:

- The right-of-use asset will be equal to the amount of the lease liability adjusted by the amount of prepaid lease payments.
- Existing contracts at the date of transition will not be reassessed to determine whether they are, or contain, a lease under IFRS 16.

The Federation believes that adopting IFRS 16 will result, on January 1, 2019, in the recognition of a right-of-use asset of approximately \$330 million and a lease liability of the same amount, as well as a decrease of about 8 basis points in regulatory capital ratios.

### IFRS 17, "INSURANCE CONTRACTS"

In May 2017, the IASB issued IFRS 17, "Insurance Contracts", which will replace the current standard, IFRS 4, "Insurance Contracts". IFRS 17 sets out the recognition, measurement, presentation and disclosure requirements applicable to all insurance contracts.

IFRS 17 requires that insurance contract liabilities be measured using a general model based on current value. This model uses assumptions as at the reporting date to estimate the amount, timing and uncertainty of future cash flows and takes into account market interest rates and the impact of insurance contract holder options and guarantees.

In addition, under IFRS 17, profits on the sale of insurance policies will no longer be recognized upon initial recognition, but will instead be deferred as separate liabilities and recognized in profit or loss over the contract term as services are provided.

The Federation is currently assessing the impact of adopting IFRS 17, which will be effective for annual periods beginning on or after January 1, 2021. In November 2018, the IASB tentatively decided to defer the effective date of IFRS 17 to the annual periods beginning on or after January 1, 2022.

## CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING

In March 2018, the IASB issued the “Conceptual Framework for Financial Reporting”, which replaces the current version of the conceptual framework. The “Conceptual Framework for Financial Reporting” includes new concepts, updates the definitions and recognition criteria for assets and liabilities and clarifies some key concepts. The Federation is currently assessing the impact of adopting this new framework, which will be effective for annual periods beginning on or after January 1, 2020.

## 5.5 Five-year statistical review

**Table 39 – Consolidated Balance Sheets**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016	2015	2014
<b>ASSETS</b>					
<b>Cash and deposits with financial institutions</b>	<b>\$ 2,738</b>	<b>\$ 1,731</b>	<b>\$ 1,212</b>	<b>\$ 1,006</b>	<b>\$ 1,232</b>
<b>Securities</b>					
Securities at fair value through profit or loss	<b>36,914</b>	31,654	31,005	28,715	24,846
Available-for-sale securities	<b>N/A</b>	15,250	13,932	14,400	11,616
Securities at fair value through other comprehensive income	<b>11,131</b>	N/A	N/A	N/A	N/A
Securities at amortized cost	<b>1,621</b>	N/A	N/A	N/A	N/A
	<b>49,666</b>	46,904	44,937	43,115	36,462
<b>Securities borrowed or purchased under reverse repurchase agreements</b>	<b>14,086</b>	9,377	7,713	8,046	10,143
<b>Loans</b>					
Residential mortgages	<b>4,626</b>	4,323	3,486	2,861	2,367
Consumer, credit card and other personal loans	<b>19,710</b>	17,547	15,720	14,697	13,827
Business and government	<b>37,992</b>	37,012	33,416	33,330	29,891
	<b>62,328</b>	58,882	52,622	50,888	46,085
Allowance for credit losses	<b>(491)</b>	(198)	(192)	(180)	(163)
	<b>61,837</b>	58,684	52,430	50,708	45,922
<b>Segregated fund net assets</b>	<b>13,234</b>	13,379	11,965	9,781	8,695
<b>Other assets</b>					
Clients' liability under acceptances	<b>160</b>	31	11	376	858
Premiums receivable	<b>2,378</b>	2,098	1,961	1,665	1,130
Derivative financial instruments	<b>4,376</b>	3,772	3,706	4,879	3,153
Amounts receivable from clients, brokers and financial institutions	<b>1,487</b>	1,563	2,541	2,041	1,751
Reinsurance assets	<b>1,958</b>	2,202	2,582	1,964	785
Investment property	<b>943</b>	817	806	669	551
Property, plant and equipment	<b>811</b>	780	769	745	655
Goodwill	<b>121</b>	121	471	472	472
Intangible assets	<b>389</b>	466	690	660	569
Deferred tax assets	<b>896</b>	746	724	678	599
Other	<b>2,480</b>	2,188	2,140	1,852	1,689
Assets of the disposal group held to be transferred	<b>-</b>	881	-	-	-
	<b>15,999</b>	15,665	16,401	16,001	12,212
<b>TOTAL ASSETS</b>	<b>\$ 157,560</b>	<b>\$ 145,740</b>	<b>\$ 134,658</b>	<b>\$ 128,657</b>	<b>\$ 114,666</b>

See the next page for the footnote.

**Table 39 – Consolidated Balance Sheets (continued)**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017	2016	2015	2014
<b>LIABILITIES AND EQUITY</b>					
<b>LIABILITIES</b>					
<b>Deposits</b>					
Individuals	\$ 4,105	\$ 4,353	\$ 3,817	\$ 2,518	\$ 2,055
Business and government	45,998	40,963	36,780	38,925	33,535
Deposit-taking institutions	7,954	6,833	6,305	6,479	5,532
	<b>58,057</b>	<b>52,149</b>	<b>46,902</b>	<b>47,922</b>	<b>41,122</b>
<b>Other liabilities</b>					
Acceptances	160	31	11	376	858
Commitments related to securities sold short	10,829	9,112	8,196	5,464	6,304
Commitments related to securities lent or sold under repurchase agreements	16,233	10,062	9,870	9,283	13,021
Derivative financial instruments	3,332	3,677	2,540	2,478	2,194
Amounts payable to clients, brokers and financial institutions	4,105	4,247	4,659	4,713	3,713
Insurance contract liabilities	28,764	28,300	27,493	26,734	19,435
Segregated fund net liabilities	13,212	13,354	11,957	9,776	8,706
Net defined benefit plan liabilities	1,578	1,741	1,478	1,548	1,576
Deferred tax liabilities	254	204	247	218	201
Other	5,105	4,794	5,247	4,674	3,245
Liabilities of the disposal group held to be transferred	-	662	-	-	-
	<b>83,572</b>	<b>76,184</b>	<b>71,698</b>	<b>65,264</b>	<b>59,253</b>
<b>Subordinated notes</b>	<b>1,378</b>	<b>1,388</b>	<b>1,378</b>	<b>1,884</b>	<b>2,564</b>
<b>TOTAL LIABILITIES</b>	<b>143,007</b>	<b>129,721</b>	<b>119,978</b>	<b>115,070</b>	<b>102,939</b>
<b>EQUITY</b>					
Capital stock	8,779	8,537	8,066	7,505	7,050
Undistributed surplus earnings	4,764	5,674	4,781	3,977	3,290
Accumulated other comprehensive income	(9)	458	393	265	386
Reserves	271	540	524	507	440
<b>Equity – Group's share</b>	<b>13,805</b>	<b>15,209</b>	<b>13,764</b>	<b>12,254</b>	<b>11,166</b>
<b>Non-controlling interests</b>	<b>748</b>	<b>810</b>	<b>916</b>	<b>1,333</b>	<b>561</b>
<b>TOTAL EQUITY</b>	<b>14,553</b>	<b>16,019</b>	<b>14,680</b>	<b>13,587</b>	<b>11,727</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 157,560</b>	<b>\$ 145,740</b>	<b>\$ 134,658</b>	<b>\$ 128,657</b>	<b>\$ 114,666</b>

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

**Table 40 – Consolidated Statements of Income**

For the years ended December 31

(in millions of dollars)	2018 <sup>(1)</sup>	2017 <sup>(2)</sup>	2016 <sup>(2)</sup>	2015	2014
<b>Interest income</b>					
Loans	\$ 2,597	\$ 2,070	\$ 1,866	\$ 1,762	\$ 1,595
Securities	230	195	182	167	188
	<b>2,827</b>	<b>2,265</b>	<b>2,048</b>	<b>1,929</b>	<b>1,783</b>
<b>Interest expense</b>					
Deposits	1,159	783	660	598	593
Subordinated notes and other	167	78	85	128	135
	<b>1,326</b>	<b>861</b>	<b>745</b>	<b>726</b>	<b>728</b>
<b>Net interest income</b>	<b>1,501</b>	<b>1,404</b>	<b>1,303</b>	<b>1,203</b>	<b>1,055</b>
<b>Net premiums</b>	<b>8,923</b>	<b>8,146</b>	<b>7,263</b>	<b>7,006</b>	<b>6,018</b>
<b>Other income</b>					
Assessments	392	377	393	339	304
Service agreements	742	727	699	760	684
Lending fees and credit card service revenues	699	660	575	547	533
Brokerage and investment fund services	905	1,030	1,060	1,037	970
Management and custodial service fees	579	514	443	385	374
Net investment income	170	1,767	1,108	1,210	2,457
Overlay approach adjustment for insurance operations financial assets	523	N/A	N/A	N/A	N/A
Foreign exchange income	92	77	70	74	70
Other	296	362	140	250	323
	<b>4,398</b>	<b>5,514</b>	<b>4,488</b>	<b>4,602</b>	<b>5,715</b>
<b>Total income</b>	<b>14,822</b>	<b>15,064</b>	<b>13,054</b>	<b>12,811</b>	<b>12,788</b>
<b>Provision for credit losses</b>	<b>288</b>	<b>278</b>	<b>248</b>	<b>302</b>	<b>265</b>
<b>Claims, benefits, annuities and changes in insurance contract liabilities</b>	<b>6,584</b>	<b>6,795</b>	<b>5,446</b>	<b>5,431</b>	<b>6,303</b>
<b>Non-interest expense</b>					
Remuneration and other payments	563	536	492	471	428
Salaries and fringe benefits	2,239	2,255	2,329	2,221	1,907
Premises, equipment and furniture, including depreciation	496	514	437	397	351
Service agreements and outsourcing	341	322	306	327	251
Communications	219	244	265	254	233
Other	2,534	2,368	2,193	2,063	1,957
	<b>6,392</b>	<b>6,239</b>	<b>6,022</b>	<b>5,733</b>	<b>5,127</b>
<b>Operating surplus earnings</b>	<b>1,558</b>	<b>1,752</b>	<b>1,338</b>	<b>1,345</b>	<b>1,093</b>
Income taxes on surplus earnings	208	336	147	208	198
<b>Surplus earnings before dividends to member caisses</b>	<b>1,350</b>	<b>1,416</b>	<b>1,191</b>	<b>1,137</b>	<b>895</b>
Dividends to member caisses	70	60	25	-	9
Tax recovery on dividends to member caisses	(19)	(16)	(7)	-	(2)
<b>Net surplus earnings for the year after dividends to member caisses</b>	<b>\$ 1,299</b>	<b>\$ 1,372</b>	<b>\$ 1,173</b>	<b>\$ 1,137</b>	<b>\$ 888</b>
Of which:					
Group's share	\$ 1,258	\$ 1,329	\$ 1,088	\$ 957	\$ 825
Non-controlling interests' share	41	43	85	180	63

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> Data for 2017 and 2016 have been reclassified to conform to the current year's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.

**Table 41 – Selected financial measures**

For the years ended December 31

(in millions of dollars and as a percentage)	2018 <sup>(1)</sup>	2017	2016	2015	2014
Tier 1A capital ratio	<b>15.7%</b>	17.5%	15.9%	N/A <sup>(2)</sup>	N/A <sup>(2)</sup>
Tier 1 capital ratio	<b>15.7</b>	17.5	15.9	N/A <sup>(2)</sup>	N/A <sup>(2)</sup>
Total capital ratio	<b>15.7</b>	17.5	15.9	N/A <sup>(2)</sup>	N/A <sup>(2)</sup>
Leverage ratio	<b>7.4</b>	7.9	7.4	N/A <sup>(2)</sup>	N/A <sup>(2)</sup>
Return on equity <sup>(3)</sup>	<b>8.6</b>	9.4	8.5	8.2%	8.6%
Credit loss provisioning rate <sup>(3)</sup>	<b>0.48</b>	0.50	0.48	0.62	0.62
Gross credit-impaired loans <sup>(4)</sup> / gross loans and acceptances ratio <sup>(3)</sup>	<b>0.56</b>	0.14	0.18	0.17	0.16
Assets under administration	<b>\$ 382,469</b>	\$ 419,981	\$ 428,106	\$ 410,858	\$ 377,836
Assets under management <sup>(5)</sup>	<b>66,359</b>	66,653	59,490	53,561	47,563
Average assets <sup>(3)</sup>	<b>154,106</b>	143,110	134,333	130,051	108,698
Average net loans and acceptances <sup>(3)</sup>	<b>59,973</b>	54,977	51,213	48,831	42,618
Average deposits <sup>(3)</sup>	<b>55,758</b>	52,256	48,376	44,985	37,953

<sup>(1)</sup> The information for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(2)</sup> The Federation has published its capital ratios calculated according to the guideline on the adequacy of capital base standards applicable to financial services cooperatives issued by the AMF since January 1, 2017. The ratios as at December 31, 2016 are as at January 1, 2017.

<sup>(3)</sup> See "Basis of presentation of financial information".

<sup>(4)</sup> Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements.

<sup>(5)</sup> Assets under management may also be administered by the Federation. If applicable, they are included in assets under administration.

# Consolidated Financial Statements of *Fédération des caisses Desjardins du Québec*

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## Annual Report by the Audit and Inspection Commission

The role of the Audit and Inspection Commission (AIC) is to support the Board of Directors of the *Fédération des caisses Desjardins du Québec* (the Federation) in its oversight responsibilities for Desjardins Group. Its mandate consists primarily of:

- Analyzing the financial statements and Management's Discussion and Analysis and their presentation
- Ensuring the quality and integrity of financial reporting and the use of accepted accounting practices
- Overseeing the management of significant financial risks
- Ensuring that an effective internal control system is in place
- Overseeing the work of the internal auditor and independent auditor
- Ensuring that a compliance management framework is applied

The AIC reviews the Federation's interim and annual financial statements and Management's Discussion and Analysis, its prospectuses, and its annual information form. The AIC ensures that management has designed and implemented an effective internal control system with respect to the organization's business processes, financial reporting, safeguarding of assets, fraud detection and regulatory compliance. It also ensures that management has set up systems to manage the principal risks that may influence the financial results of the Federation. The AIC analyzes the information resulting from this financial governance process every quarter.

The independent auditor is under the authority of the AIC. To fulfill its responsibilities in this regard, the AIC ensures and preserves the independent auditor's independence and objectivity by authorizing all of its non-audit services, by recommending its appointment or reappointment to the Federation's Board of Directors, by setting and recommending auditor compensation and by conducting annual auditor evaluations. In addition, the AIC supervises the work of the independent auditor and examines its audit proposal, its mandate, its annual audit plan, its reports, its letter to management and management's comments. Desjardins Group has adopted a policy that governs the awarding of contracts for related services, which addresses the following issues: (a) services that can or cannot be provided by the independent auditor, (b) governance procedures that must be followed before mandates can be awarded, and (c) responsibilities of key stakeholders. Accordingly, the AIC receives a quarterly report on the contracts awarded to the independent auditor by each of the Federation's entities.

The AIC ensures the independence and objectivity of the internal audit function, which is performed by the Desjardins Group Monitoring Office. The AIC analyzes the annual internal audit plan as well as the internal audit team's responsibilities and objectivity. It ensures the plan is carried out, reviews the internal audit results and, if necessary, takes appropriate follow-up action. As part of these duties, the AIC meets with the head of internal audit at Desjardins Group to discuss any major issues submitted to management.

With respect to the Federation's relations with the *Autorité des marchés financiers* (AMF) in Quebec, the AIC reviews and follows up on the inspection reports issued by the AMF and reviews the financial reports that are submitted each quarter to the AMF.

The AIC meets privately with: the independent auditor; the Senior Executive Vice-President and Chief Operating Officer of Desjardins Group; the Executive Vice-President of Finance, Treasury and Administration and Chief Financial Officer of Desjardins Group; and the Chief Monitoring Officer of Desjardins Group. It reports to the Board of Directors on a quarterly basis and, if necessary, makes recommendations. Lastly, in accordance with sound corporate governance practices, once a year the AIC reviews the degree of efficiency and effectiveness with which it has executed the tasks set out in its charter.

The AIC is made up of five independent directors and four observers. These observers are: the chairs of the audit and risk management committees of Desjardins Financial Security Life Assurance Company and Desjardins General Insurance Group Inc., the chair of the Federation's Risk Management Commission, and a caisse general manager who sits on the Federation's Board of Directors. Except for this general manager, none of the AIC members receives direct or indirect compensation from Desjardins Group for services other than those rendered as a member of the Board of Directors of the Federation or other Desjardins Group entities, including their committees and commissions.

In light of the significant changes made to accounting and financial reporting requirements, the AIC members attended a number of training activities during the year. The subjects covered in these activities included changes to the International Financial Reporting Standards and the impact of changes to capital management and corporate governance standards and regulations. All AIC members possess the knowledge required to read and interpret the financial statements of a financial institution, according to the criteria established in the AIC's charter.

The AIC held six meetings and one training session for its members in fiscal 2018. As at December 31, 2018, the five independent directors who are members of the AIC are: Louis Babineau, Michel Doré, Pierre Perras, Mario Simard and Michel Tourangeau. The three observers are: Michel Magnan, FCPA, FCA; Robert St-Aubin, FCPA, FCA; and Jean-François Laporte. During the year, Stéphane Corbeil, Serge Tourangeau, Yves Genest and Neil Hawthorn also participated in the AIC's activities.

**Louis Babineau**  
Chair

Montreal, Quebec  
February 25, 2019

## Management's Responsibility for Financial Reporting

The Consolidated Financial Statements of the *Fédération des caisses Desjardins du Québec* (the Federation) and all information included in its annual Management's Discussion and Analysis are the responsibility of management, which is responsible for ensuring reporting integrity and accuracy.

These Consolidated Financial Statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board, and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec, which do not differ from IFRS. These Consolidated Financial Statements necessarily contain amounts established by management based on estimates which it deems fair and reasonable. These estimates include valuations of insurance contract liabilities performed by the actuaries of the relevant segments. All financial information in the annual Management's Discussion and Analysis is consistent with these audited Consolidated Financial Statements.

Management is responsible for the accuracy of the Federation's Consolidated Financial Statements and related information, as well as the accounting systems from which they are derived, for which purpose it maintains controls over transactions and related accounting practices. Such controls include an organizational structure that ensures effective segregation of duties, a code of professional conduct, hiring and training standards, policies and procedure manuals, and regularly updated control methods, designed to ensure adequate supervision of operations. The internal control system is supported by a compliance team, which helps management ensure that all regulatory requirements are met, and a team from the Desjardins Group Monitoring Office, which has full and unrestricted access to the Audit and Inspection Commission. Management has also implemented a financial governance structure based on market best practices to ensure the controls and disclosure procedures for financial information presented in the annual and interim filings of the Federation are adequately designed and effective. As at December 31, 2018, in our capacities as Chief Executive Officer and Chief Financial Officer of the Federation, we concluded that internal control over financial reporting is effective.

The AMF examines the affairs of the Federation on a regular basis.

For the purposes of approving the financial information contained in the annual report, the Board of Directors of the Federation relies on the recommendation of the Audit and Inspection Commission. The Audit and Inspection Commission is mandated by the Board of Directors to review the Federation's Consolidated Financial Statements and its Management's Discussion and Analysis. In addition, the Audit and Inspection Commission, comprising independent directors and four observers who are neither management nor staff of the Federation, exercises an oversight role to ensure that management has developed and implemented adequate control procedures and systems to deliver quality financial reporting that includes all the required disclosures within the required timeframes.

The Consolidated Financial Statements were audited by PricewaterhouseCoopers LLP, the independent auditor appointed by the Federation's General Meeting, whose report follows. The independent auditor may meet with the members of the Audit and Inspection Commission at any time to discuss its audit and any related issues, including the integrity of the financial information provided and the quality of internal control systems.

**Guy Cormier**  
President and Chief Executive Officer  
Desjardins Group

**Réal Bellemare**  
Executive Vice-President Finance, Treasury, Administration and  
Chief Financial Officer  
Desjardins Group

Lévis, Quebec  
February 27, 2019

# Independent auditor's report

## TO THE MEMBERS OF THE *FÉDÉRATION DES CAISSES DESJARDINS DU QUÉBEC*

### *Our opinion*

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the *Fédération des caisses Desjardins du Québec* and its subsidiaries (together, the Federation) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (IFRS).

### **What we have audited**

The Federation's consolidated financial statements comprise:

- the consolidated balance sheets as at December 31, 2018 and 2017;
- the consolidated statements of income for the years then ended;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of changes in equity for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Certain required disclosures have been presented elsewhere in the Management's Discussion and Analysis, rather than in the notes to the consolidated financial statements. These disclosures are cross-referenced from the consolidated financial statements and are identified as audited.

### *Basis for opinion*

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Independence**

We are independent of the Federation in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

### *Other information*

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis, which we obtained prior to the date of this auditor's report and the information, other than the consolidated financial statements and our auditor's report thereon, included in the annual report, which is expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express an opinion or any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard. When we read the information, other than the consolidated financial statements and our auditor's report thereon, included in the annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

### *Responsibilities of management and those charged with governance for the consolidated financial statements*

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Federation's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Federation or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Federation's financial reporting process.

*Auditor's responsibilities for the audit of the consolidated financial statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Federation's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Federation's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Federation to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Federation to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Michel Larouche.

**PricewaterhouseCoopers LLP<sup>(1)</sup>**

<sup>(1)</sup>CPA auditor, CA, public accountancy permit No. A111799

Montreal, Quebec  
February 27, 2019

## Consolidated Balance Sheets

(in millions of Canadian dollars)	Notes	As at December 31, 2018 <sup>(1)</sup>	As at December 31, 2017
<b>ASSETS</b>			
<b>Cash and deposits with financial institutions</b>		<b>\$ 2,738</b>	<b>\$ 1,731</b>
<b>Securities</b>	6		
Securities at fair value through profit or loss		36,914	31,654
Available-for-sale securities		N/A	15,250
Securities at fair value through other comprehensive income		11,131	N/A
Securities at amortized cost		1,621	N/A
		49,666	46,904
<b>Securities borrowed or purchased under reverse repurchase agreements</b>		<b>14,086</b>	<b>9,377</b>
<b>Loans</b>	7 and 8		
Residential mortgages		4,626	4,323
Consumer, credit card and other personal loans		19,710	17,547
Business and government		37,992	37,012
		62,328	58,882
Allowance for credit losses	7	(491)	(198)
		61,837	58,684
<b>Segregated fund net assets</b>	9	<b>13,234</b>	<b>13,379</b>
<b>Other assets</b>			
Clients' liability under acceptances		160	31
Premiums receivable		2,378	2,098
Derivative financial instruments	19	4,376	3,772
Amounts receivable from clients, brokers and financial institutions		1,487	1,563
Reinsurance assets	15	1,958	2,202
Investment property	10	943	817
Property, plant and equipment	10	811	780
Goodwill	11	121	121
Intangible assets	11	389	466
Deferred tax assets	26	896	746
Other	12	2,480	2,188
Assets of the disposal group held to be transferred		-	881
		15,999	15,665
<b>TOTAL ASSETS</b>		<b>\$ 157,560</b>	<b>\$ 145,740</b>
<b>LIABILITIES AND EQUITY</b>			
<b>LIABILITIES</b>			
<b>Deposits</b>	14		
Individuals		\$ 4,105	\$ 4,353
Business and government		45,998	40,963
Deposit-taking institutions		7,954	6,833
		58,057	52,149
<b>Other liabilities</b>			
Acceptances		160	31
Commitments related to securities sold short		10,829	9,112
Commitments related to securities lent or sold under repurchase agreements		16,233	10,062
Derivative financial instruments	19	3,332	3,677
Amounts payable to clients, brokers and financial institutions		4,105	4,247
Insurance contract liabilities	15	28,764	28,300
Segregated fund net liabilities	9	13,212	13,354
Net defined benefit plan liabilities	16	1,578	1,741
Deferred tax liabilities	26	254	204
Other	17	5,105	4,794
Liabilities of the disposal group held to be transferred		-	662
		83,572	76,184
<b>Subordinated notes</b>		<b>1,378</b>	<b>1,388</b>
<b>TOTAL LIABILITIES</b>		<b>143,007</b>	<b>129,721</b>
<b>EQUITY</b>			
Capital stock	21	8,779	8,537
Undistributed surplus earnings		4,764	5,674
Accumulated other comprehensive income	22	(9)	458
Reserves		271	540
<b>Equity – Group's share</b>		<b>13,805</b>	<b>15,209</b>
<b>Non-controlling interests</b>	13 and 15	<b>748</b>	<b>810</b>
<b>TOTAL EQUITY</b>		<b>14,553</b>	<b>16,019</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>\$ 157,560</b>	<b>\$ 145,740</b>

<sup>(1)</sup> The information presented as at December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated.  
For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Consolidated Financial Statements.

On behalf of the Board of Directors of the *Fédération des caisses Desjardins du Québec*,

**Guy Cormier**  
Chair of the Board

**Serge Rousseau**  
Vice-Chair of the Board

**Consolidated Statements of Income**

For the years ended December 31

(in millions of Canadian dollars)	Notes	2018 <sup>(1)</sup>	2017
<b>INTEREST INCOME</b>			
Loans		\$ 2,597	\$ 2,070
Securities		230	195
		<b>2,827</b>	2,265
<b>INTEREST EXPENSE</b>			
Deposits		1,159	783
Subordinated notes and other		167	78
		<b>1,326</b>	861
<b>NET INTEREST INCOME</b>	24	<b>1,501</b>	1,404
<b>NET PREMIUMS</b>	15	<b>8,923</b>	8,146
<b>OTHER INCOME</b>			
Assessments		392	377
Service agreements		742	727
Lending fees and credit card service revenues		699	660
Brokerage and investment fund services		905	1,030
Management and custodial service fees		579	514
Net investment income	24	170	1,767
Overlay approach adjustment for insurance operations financial assets		523	N/A
Foreign exchange income		92	77
Other		296	362
		<b>4,398</b>	5,514
<b>TOTAL INCOME</b>		<b>14,822</b>	15,064
<b>PROVISION FOR CREDIT LOSSES</b>	7	<b>288</b>	278
<b>CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE</b>			
<b>CONTRACT LIABILITIES</b>	15	<b>6,584</b>	6,795
<b>NON-INTEREST EXPENSE</b>			
Remuneration and other payments		563	536
Salaries and fringe benefits		2,239	2,255
Premises, equipment and furniture, including depreciation		496	514
Service agreements and outsourcing		341	322
Communications		219	244
Other	25	2,534	2,368
		<b>6,392</b>	6,239
<b>OPERATING SURPLUS EARNINGS</b>		<b>1,558</b>	1,752
Income taxes on surplus earnings	26	208	336
<b>SURPLUS EARNINGS BEFORE DIVIDENDS TO MEMBER CAISSES<sup>(2)</sup></b>		<b>1,350</b>	1,416
Dividends to member caisses		70	60
Tax recovery on dividends to member caisses	26	(19)	(16)
<b>NET SURPLUS EARNINGS FOR THE YEAR AFTER DIVIDENDS TO MEMBER CAISSES</b>		<b>\$ 1,299</b>	\$ 1,372
<b>of which:</b>			
Group's share		\$ 1,258	\$ 1,329
Non-controlling interests' share	13	41	43

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

<sup>(2)</sup> The Group's share of "Surplus earnings before dividends to member caisses" is presented in Note 31, "Segmented Information".

The accompanying notes are an integral part of the Consolidated Financial Statements.

## Consolidated Statements of Comprehensive Income

For the years ended December 31

(in millions of Canadian dollars)	2018 <sup>(1)</sup>	2017
<b>Net surplus earnings for the year after dividends to member caisses</b>	<b>\$ 1,299</b>	<b>\$ 1,372</b>
<b>Other comprehensive income, net of income taxes</b>		
<b>Items that will not be reclassified subsequently to the Consolidated Statements of Income</b>		
Remeasurement of net defined benefit plan liabilities	81	(193)
Share of associates and joint ventures accounted for using the equity method	-	(2)
	81	(195)
<b>Items that will be reclassified subsequently to the Consolidated Statements of Income</b>		
Net change in unrealized gains and losses on available-for-sale securities		
Net unrealized gains	N/A	246
Reclassification of net gains to the Consolidated Statements of Income	N/A	(169)
	N/A	77
Net change in unrealized gains and losses on debt securities classified as at fair value through other comprehensive income		
Net unrealized losses	(38)	N/A
Reclassification of net losses to the Consolidated Statements of Income	14	N/A
	(24)	N/A
Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets		
Net unrealized losses	(288)	N/A
Reclassification of net gains to the Consolidated Statements of Income	(129)	N/A
	(417)	N/A
Net change in cash flow hedges		
Net gains (losses) on derivative financial instruments designated as cash flow hedges	(11)	1
Reclassification to the Consolidated Statements of Income of net gains on derivative financial instruments designated as cash flow hedges	(3)	(6)
	(14)	(5)
	(455)	72
<b>Total other comprehensive income, net of income taxes</b>	<b>(374)</b>	<b>(123)</b>
<b>COMPREHENSIVE INCOME FOR THE YEAR</b>	<b>\$ 925</b>	<b>\$ 1,249</b>
<b>of which:</b>		
Group's share	\$ 906	\$ 1,202
Non-controlling interests' share	19	47

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Consolidated Financial Statements.

### Income taxes on other comprehensive income

The tax expense (recovery) related to each component of other comprehensive income for the year is presented in the following table.

For the years ended December 31

(in millions of Canadian dollars)	2018 <sup>(1)</sup>	2017
<b>Item that will not be reclassified subsequently to the Consolidated Statements of income</b>		
Remeasurement of net defined benefit plan liabilities	\$ 29	\$ (69)
	29	(69)
<b>Items that will be reclassified subsequently to the Consolidated Statements of Income</b>		
Net change in unrealized gains and losses on available-for-sale securities		
Net unrealized gains	N/A	51
Reclassification of net gains to the Consolidated Statements of Income	N/A	(35)
	N/A	16
Net change in unrealized gains and losses on debt securities classified as at fair value through other comprehensive income		
Net unrealized losses	(13)	N/A
Reclassification of net losses to the Consolidated Statements of Income	6	N/A
	(7)	N/A
Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets		
Net unrealized losses	(88)	N/A
Reclassification of net gains to the Consolidated Statements of Income	(18)	N/A
	(106)	N/A
Net change in cash flow hedges		
Net gains (losses) on derivative financial instruments designated as cash flow hedges	(7)	1
Reclassification to the Consolidated Statements of Income of net gains on derivative financial instruments designated as cash flow hedges	(1)	(2)
	(8)	(1)
	(121)	15
<b>Total income tax recovery</b>	<b>\$ (92)</b>	<b>\$ (54)</b>

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

## Consolidated Statements of Changes in Equity

For the years ended December 31

		Capital stock (Note 21)	Undistributed surplus earnings	Accumulated other comprehensive income (Note 22)	Reserves			Equity - Group's share	Non-controlling interests (Notes 13 and 15)	Total equity
	Note				Stabilization reserve	General and other reserves	Total reserves			
(in millions of Canadian dollars)										
<b>BALANCE AS AT DECEMBER 31, 2016</b>		\$ 8,066	\$ 4,781	\$ 393	\$ 436	\$ 88	\$ 524	\$ 13,764	\$ 916	\$ 14,680
Net surplus earnings for the year after dividends to member caisses		-	1,329	-	-	-	-	1,329	43	1,372
Other comprehensive income for the year		-	(192)	65	-	-	-	(127)	4	(123)
Comprehensive income for the year		-	1,137	65	-	-	-	1,202	47	1,249
Issuance of F capital shares		375	-	-	-	-	-	375	-	375
F capital share issuance costs		(1)	-	-	-	-	-	(1)	-	(1)
Other net change in capital stock		97	-	-	-	-	-	97	(97)	-
Payments to member caisses		-	(68)	-	-	-	-	(68)	-	(68)
Remuneration of F capital shares		-	(167)	-	-	-	-	(167)	-	(167)
Redemption of share capital		-	-	-	-	-	-	-	(8)	(8)
Dividends		-	-	-	-	-	-	-	(42)	(42)
Transfer between surplus earnings to be distributed and reserves		-	(16)	-	31	(15)	16	-	-	-
Transactions related to put options		-	5	-	-	-	-	5	(3)	2
Other		-	2	-	-	-	-	2	(3)	(1)
<b>BALANCE AS AT DECEMBER 31, 2017</b>		\$ 8,537	\$ 5,674	\$ 458	\$ 467	\$ 73	\$ 540	\$ 15,209	\$ 810	\$ 16,019
Impact of changes in accounting policies	2	-	34	(35)	-	(213)	(213)	(214)	-	(214)
<b>OPENING BALANCE AS AT JANUARY 1, 2018<sup>(1)</sup></b>		\$ 8,537	\$ 5,708	\$ 423	\$ 467	\$ (140)	\$ 327	\$ 14,995	\$ 810	\$ 15,805
Net surplus earnings for the year after dividends to member caisses		-	1,258	-	-	-	-	1,258	41	1,299
Other comprehensive income for the year		-	80	(432)	-	-	-	(352)	(22)	(374)
Comprehensive income for the year		-	1,338	(432)	-	-	-	906	19	925
Issuance of F capital shares		267	-	-	-	-	-	267	-	267
F capital share issuance costs		(1)	-	-	-	-	-	(1)	-	(1)
Other net change in capital stock		(24)	3	-	-	-	-	(21)	-	(21)
Payments to member caisses		-	(1,854)	-	-	-	-	(1,854)	-	(1,854)
Remuneration on capital shares		-	(361)	-	(147)	-	(147)	(508)	-	(508)
Redemption of share capital		-	-	-	-	-	-	-	(11)	(11)
Dividends		-	-	-	-	-	-	-	(36)	(36)
Transfer between surplus earnings to be distributed and reserves		-	(91)	-	97	(6)	91	-	-	-
Transactions related to buy-out options		-	30	-	-	-	-	30	(19)	11
Buy-out of non-controlling interests		-	(13)	-	-	-	-	(13)	(15)	(28)
Other		-	4	-	-	-	-	4	-	4
<b>BALANCE AS AT DECEMBER 31, 2018<sup>(1)</sup></b>		\$ 8,779	\$ 4,764	\$ (9)	\$ 417	\$ (146)	\$ 271	\$ 13,805	\$ 748	\$ 14,553

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Consolidated Financial Statements.

**Consolidated Statements of Cash Flows**

For the years ended December 31

(in millions of Canadian dollars)	2018 <sup>(1)</sup>	2017
<b>CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES</b>		
Operating surplus earnings	\$ 1,558	\$ 1,752
Non-cash adjustments:		
Depreciation of property, plant and equipment and investment property, and amortization of intangible assets	218	224
Net change in insurance contract liabilities	464	974
Provision for credit losses	288	278
Net realized losses on securities classified as at fair value through other comprehensive income	19	N/A
Net realized gains on available-for-sale securities	N/A	(208)
Overlay approach adjustment for insurance operations financial assets	(523)	N/A
Impairment on available-for-sale securities recognized in profit or loss	N/A	6
Other	(2)	(100)
Change in operating assets and liabilities:		
Securities at fair value through profit or loss	(1,883)	(852)
Securities borrowed or purchased under reverse repurchase agreements	(4,710)	(1,664)
Loans	(3,736)	(6,532)
Derivative financial instruments, net amount	(973)	1,079
Net amounts receivable from and payable to clients, brokers and financial institutions	(121)	606
Deposits	5,907	5,247
Commitments related to securities sold short	1,717	916
Commitments related to securities lent or sold under repurchase agreements	6,171	192
Other	548	(10)
Payment of the contingent consideration	(250)	(243)
Income taxes paid on surplus earnings	(237)	(289)
	<b>4,455</b>	<b>1,376</b>
<b>CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES</b>		
Sale (purchase) of debt securities and subordinated notes to (from) third parties on the market	(11)	10
Issuance of F capital shares	125	250
F capital share issuance costs	(1)	(1)
Payment of dividends to member caisses	(1,914)	(68)
Other net change in capital stock	(20)	-
Remuneration on capital stock	(366)	(42)
Redemption of share capital	(11)	(8)
Dividends paid	(36)	(42)
Buy-out of non-controlling interests	(28)	-
Exercise of put options written on non-controlling interests	(63)	(15)
	<b>(2,325)</b>	<b>84</b>
<b>CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES</b>		
Purchase of available-for-sale securities	N/A	(51,240)
Proceeds from disposals of available-for-sale securities	N/A	15,873
Proceeds from maturities of available-for-sale securities	N/A	34,113
Purchase of securities at fair value through other comprehensive income and at amortized cost	(62,858)	N/A
Proceeds from disposals of securities at fair value through other comprehensive income and at amortized cost	9,724	N/A
Proceeds from maturities of securities at fair value through other comprehensive income and at amortized cost	52,343	N/A
Subsidiary disposal, net of cash and cash equivalents sold	-	684
Payment of the contingent consideration recognized at acquisition date	(27)	(23)
Acquisitions of property, plant and equipment, intangible assets and investment property	(409)	(332)
Proceeds from disposals of property, plant and equipment, intangible assets and investment property	78	10
	<b>(1,149)</b>	<b>(915)</b>
<b>Net increase in cash and cash equivalents</b>	<b>981</b>	<b>545</b>
Cash and cash equivalents at beginning of year	1,757	1,212
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>2,738</b>	<b>1,757</b>
Less:		
Cash and cash equivalents of the disposal group held to be transferred	-	26
<b>CASH AND CASH EQUIVALENTS RELATED TO CONTINUING OPERATIONS AT END OF YEAR</b>	<b>\$ 2,738</b>	<b>\$ 1,731</b>
<b>Supplemental information on cash flows from (used in) operating activities</b>		
Interest paid	\$ 1,039	\$ 1,109
Interest and dividends received	4,028	3,288

<sup>(1)</sup> The information presented for the year ended December 31, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Consolidated Financial Statements.

# Notes to the Consolidated Financial Statements

## NOTE 1 – INFORMATION ON THE *FÉDÉRATION DES CAISSES DESJARDINS DU QUÉBEC*

### Nature of operations

The *Fédération des caisses Desjardins du Québec* (the Federation) is the cooperative entity which is responsible for assuming orientation, framework, coordination and development activities for Desjardins Group. It provides its member caisses with a variety of services, including certain technical, financial and administrative services. The member caisses exercise a collective power over the Federation, and each of them has a significant influence over the Federation.

In addition, the Federation is the parent company of several financial services subsidiaries. The various business segments in which the Federation operates are described in Note 31, "Segmented information". The address of its head office is 100 Des Commandeurs Street, Lévis, Quebec, Canada.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

### BASIS OF PRESENTATION

#### Statement of compliance

Pursuant to the *Act Respecting Financial Services Cooperatives* (the Act), these Consolidated Financial Statements have been prepared by the Federation's management in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec, which do not differ from IFRS. Certain comparative figures have been reclassified to conform with the presentation of the Consolidated Financial Statements for the current year. These reclassifications had no impact on the Federation's profit or loss or total assets and liabilities.

The Consolidated Financial Statements for the year ended December 31, 2018 were approved by the Board of Directors of the Federation on February 27, 2019.

The significant measurement and presentation rules applied to prepare these Consolidated Financial Statements are described below.

#### Significant judgments, estimates and assumptions

The preparation of consolidated financial statements in accordance with IFRS requires management to make judgments and estimates and rely on assumptions which have an impact on the reported amount of certain assets, liabilities, income and expenses as well as related disclosures. The significant accounting policies that required management to make difficult, subjective or complex judgments, often about matters that are inherently uncertain, are related to consolidation of structured entities, determination of the fair value of financial instruments, derecognition of financial assets, impairment of financial instruments, impairment of non-financial assets, insurance contract liabilities, provisions, income taxes on surplus earnings, dividends to member caisses, employee benefits as well as goodwill and intangible assets. Consequently, actual results could differ from those estimates and assumptions.

#### Principles of consolidation

The Consolidated Financial Statements of the Federation include the assets, liabilities, operating results and cash flows of the Federation and its subsidiaries. The financial statements of all subsidiaries have been prepared using similar accounting policies. All intercompany transactions and balances have been eliminated.

The Federation administers various funds in accordance with the provisions of the Internal By-laws adopted at the General Meeting. For the purposes of the Consolidated Financial Statements of the Federation, these funds have been grouped together and are designated as a Group.

Management must use its judgment to determine whether the facts and circumstances resulting from a relationship with another entity give the Federation control, joint control or significant influence over such entity. In particular, significant judgments must be made with respect to structured entities.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Subsidiaries

An entity is considered as a subsidiary when it is controlled by the Federation. The Federation controls an investee if and only if it has all the following:

- Power over the investee;
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect the amount of its returns.

### Structured entities

A structured entity is an entity that has been designed so that voting rights or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: restricted activities, a narrow and well-defined objective, insufficient equity to permit it to finance its activities without subordinated financial support, or financing in the form of multiple contractually linked instruments to investors.

### Non-controlling interests

Non-controlling interests represent the share in profit or loss as well as net assets not held by the Group. They are presented separately in the Consolidated Statements of Income, the Consolidated Statements of Comprehensive Income and in equity, in the Consolidated Balance Sheets.

### Associates

An associate is an entity over which the Federation exercises significant influence over financial and operational decisions, without however having control or joint control of such entity. The Federation investments in associates are presented under "Other assets – Other" in the Consolidated Balance Sheets and are accounted for using the equity method. Under this method, investments are initially recognized at cost and adjusted thereafter to reflect the post-acquisition changes in the Federation's share in the relevant entities' equity.

### Joint arrangements

A joint arrangement is an arrangement of which the Federation has joint control, which is the contractually agreed sharing of control of such arrangement with one or more other parties. Joint control exists only when decisions about the relevant activities of the arrangement require the unanimous consent of the parties sharing control.

Joint arrangements are classified under two types based on the rights and obligations of the parties to the arrangement:

- A joint operation is a joint arrangement whereby the parties have rights to the assets, and obligations for the liabilities, relating to the arrangement. Each party must recognize its assets, liabilities, revenue and expenses, including its share of the assets held jointly and of the liabilities incurred jointly as well as its share of the revenue generated and expenses incurred in connection with the joint operation.
- A joint venture is a joint arrangement whereby the parties have rights to the net assets of the arrangement. This type of joint arrangement is accounted for using the equity method. The Federation's investments in joint ventures are presented under "Other assets – Other" in the Consolidated Balance Sheets.

### **Presentation and functional currency**

These Consolidated Financial Statements are expressed in Canadian dollars, which is also the functional currency of the Federation. Dollar amounts presented in the tables of the Notes to the Consolidated Financial Statements are in millions of dollars, unless otherwise stated.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### CHANGES IN ACCOUNTING POLICIES

On January 1, 2018, the Federation adopted IFRS 9, “Financial Instruments”, IFRS 15, “Revenue from Contracts with Customers”, and the amendments to IFRS 4, “Insurance Contracts”, on a retrospective basis without restatement of comparative periods. IFRS 7, “Financial Instruments: Disclosures”, was also amended to reflect the differences between IFRS 9 and IAS 39. Consequently, the information presented for fiscal 2018 is in accordance with these standards, while the information presented for the comparative year is in accordance with the standards that were effective before January 1, 2018.

IFRS 9 replaces IAS 39, “Financial Instruments: Recognition and Measurement”, and gives rise to new requirements for the classification and measurement of financial assets and liabilities and the impairment of financial instruments, as well as requirements for hedge accounting. As permitted by IFRS 9, the Federation decided to continue applying the hedge accounting requirements of IAS 39 instead of adopting the provisions of IFRS 9.

The amendments to IFRS 4 are designed to address the concerns of insurers and their representative bodies about the different effective dates of IFRS 9 and IFRS 17, “Insurance Contracts”. These amendments permit, but do not require, an entity that issues insurance contracts to elect to use one of two options in connection with adopting IFRS 9: deferring the initial application date of IFRS 9 to January 1, 2021 or applying the overlay approach. The Federation elected to apply the overlay approach, which is the only option proposed by these amendments that it could apply, to financial assets that are eligible and designated in accordance with certain specific criteria.

IFRS 15 introduces a single, comprehensive revenue recognition model for all contracts with customers other than those that are within the scope of other standards, such as financial instruments, insurance contracts and leases. The core principle of this standard is that revenue recognition should depict the transfer of control over a good or a service in an amount that reflects the consideration received or expected to be received in exchange for such good or service.

The retrospective impact of applying IFRS 9, IFRS 15 and the amendments to IFRS 4 has been recognized in the opening balances of the Consolidated Balance Sheet as at January 1, 2018 and is presented in the “Impact of changes in accounting policies” section of this note.

### SIGNIFICANT ACCOUNTING POLICIES

#### a) Financial assets and liabilities

Financial assets and liabilities are recognized on the date the Federation becomes a party to their contractual provisions, namely the date of acquisition or issuance of the financial instrument. Regular-way purchases and sales of financial assets are recognized on a trade-date basis.

#### Classification and measurement

##### *Accounting policies applicable since January 1, 2018*

Under IFRS 9, financial assets are classified based on their contractual cash flow characteristics and the business model under which they are held.

##### Contractual cash flow characteristics

In order to meet the cash flow characteristics criterion for purposes of classifying a financial asset, the cash flows from this asset must be solely payments of principal and interest on the principal amount outstanding. Principal is generally the fair value of the financial asset at initial recognition. Interest consists mainly of consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time, but it may also include consideration for other basic lending risks and costs, such as liquidity risk and administrative costs, as well as a certain profit margin.

##### Business models

The Federation’s business models are determined in a manner that reflects how groups of financial assets are managed to achieve a particular business objective. The business models refer to how the Federation manages its financial assets in order to generate cash flows. They therefore reflect whether cash flows will result from collecting contractual cash flows, selling financial assets or both. Determining business models requires the use of judgment and is based on all relevant evidence that is available to the Federation at the date of the assessment.

The Federation’s business models are defined as follows:

- Held to collect contractual cash flows: The objective of holding financial assets is achieved by collecting contractual cash flows.
- Held to collect contractual cash flows and sell: The objective is achieved by both collecting contractual cash flows and selling financial assets.
- Other business models: The objective is not consistent with any of the above-mentioned business models.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The classification and measurement of financial assets under IFRS 9 can be summarized as follows:

Classes		Categories	Recognition	
			Initial	Subsequent
Financial assets	At fair value through profit or loss (i)	Classified as at fair value through profit or loss (ii)	Fair value	Fair value
		Designated as at fair value through profit or loss (iii)	Fair value	Fair value
	At fair value through other comprehensive income (iv)	Classified as at fair value through other comprehensive income (v)	Fair value	Fair value
		Designated as at fair value through other comprehensive income (vi)	Fair value	Fair value
	Amortized cost (vii)		Fair value	Amortized cost

(i) Financial assets included in the “At fair value through profit or loss” class comprise financial assets “Classified as at fair value through profit or loss” and “Designated as at fair value through profit or loss”. Therefore:

- Changes in fair value of financial assets included in this class are recorded under “Net investment income” in the Consolidated Statements of Income.
- Interest income calculated using the effective interest method and dividend income from securities included in the “At fair value through profit or loss” class of the Personal and Business Services segment and the Other category are recognized under “Interest income – Securities” and, for the other segments, such income is mainly recognized under “Net investment income”. Interest income from derivative financial instruments is recognized under “Net investment income”.

(ii) Financial assets “Classified as at fair value through profit or loss” include the following:

- Debt instruments that are managed for trading purposes or on a fair value basis or do not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.
- Equity instruments.
- Derivative financial instruments.

Section m), “Derivative financial instruments and hedging activities”, specifies the nature of the recognition of derivative financial instruments designated as part of hedging relationships.

Certain financial assets “Classified as at fair value through profit or loss” under IFRS 9 are designated for the overlay approach. For more information, see the “Application of the overlay approach to insurance operations financial assets” section of this note.

(iii) Financial assets “Designated as at fair value through profit or loss” are debt securities designated as such by management upon initial recognition, on an instrument-by-instrument basis. Management may make this irrevocable designation if doing so eliminates or significantly reduces a measurement or recognition inconsistency for the financial asset.

The Federation’s financial assets included in this measurement category comprise mainly securities (debt instruments) that back the life and health insurance actuarial liabilities and the property and casualty insurance provisions for claims.

(iv) Financial assets included in the “At fair value through other comprehensive income” class comprise financial assets “Classified as at fair value through other comprehensive income” and “Designated as at fair value through other comprehensive income”. Therefore:

- Changes in fair value of financial assets included in this class, except for changes related to the loss allowance for expected credit losses and exchange gains and losses on financial assets “Classified as at fair value through other comprehensive income”, are recorded in the Consolidated Statements of Comprehensive Income as net unrealized gains and losses. For financial assets “Classified as at fair value through other comprehensive income”, gains and losses are reclassified to the Consolidated Statements of Income when the asset is derecognized, while for financial assets “Designated as at fair value through other comprehensive income”, gains and losses are never reclassified subsequently to the Consolidated Statements of Income and are reclassified immediately to undistributed surplus earnings.
- Premiums and discounts on the purchase of financial assets “At fair value through other comprehensive income” are amortized over the life of the securities using the effective interest method and recognized under “Interest income – Securities” for the Personal and Business Services segment and the Other category. For the other segments, they are mainly recognized under “Net investment income”.

(v) Financial assets “Classified as at fair value through other comprehensive income” include debt instruments that are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.

(vi) Financial assets “Designated as at fair value through other comprehensive income” include equity securities for which an irrevocable election was made, on an instrument-by-instrument basis. Financial assets included in this measurement category comprise investments in private companies that are held on a long-term-basis.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

- (vii) Securities included in the “Amortized cost” class are financial assets that are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.

Securities included in this class are initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they are measured at amortized cost using the effective interest method. Income recognized on securities included in the “Amortized cost” class is presented under “Interest income – Loans” in the Consolidated Statements of Income when it is recognized by the Personal and Business Services segment and the Other category. For the other segments, it is recognized mainly under “Net investment income”.

Financial assets are not reclassified following their initial recognition, except when the business model for managing those financial assets is changed.

### Application of the overlay approach to insurance operations financial assets

The Federation elected to designate certain eligible financial assets for the overlay approach to reduce the volatility in profit or loss arising from the different effective dates of IFRS 9, “Financial Instruments”, and IFRS 17, “Insurance Contracts”. To be eligible, a financial asset must meet the following criteria:

- It is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety applying IAS 39, “Financial Instruments: Recognition and Measurement”.
- It is held in respect of an activity connected with contracts within the scope of IFRS 4.

The overlay approach involves reclassifying between net surplus earnings and other comprehensive income, for designated financial assets, the difference between the amount reported in the Consolidated Statements of Income under IFRS 9 and the amount that would have been reported if the Federation had continued to apply IAS 39. As a result, net surplus earnings related to designated financial instruments reported in the Consolidated Statements of Income correspond to the amount that would have been reported if the Federation had continued to apply IAS 39. In determining the amount that would have been reported in the Consolidated Statements of Income if IAS 39 had been applied, The Federation considers gains (losses) on sales of securities, foreign currency fair value hedge accounting for equity instruments as well as impairment losses on equity instruments using accounting policies required by IAS 39.

Reclassifications are presented under “Overlay approach adjustment for insurance operations financial assets” in the Consolidated Statements of Income and under “Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets” in the Consolidated Statements of Comprehensive Income. The overlay approach may be used for the years beginning before January 1, 2021 or until the adoption of IFRS 17, if earlier.

Financial liabilities are classified based on their characteristics and the intention of management upon their issuance.

The classification and measurement of financial liabilities under IFRS 9 can be summarized as follows:

Classes		Categories	Recognition	
			Initial	Subsequent
Financial liabilities	At fair value through profit or loss (i)	Classified as at fair value through profit or loss (ii)	Fair value	Fair value
		Designated as at fair value through profit or loss (iii)	Fair value	Fair value
	Amortized cost (iv)		Fair value	Amortized cost

- (i) Financial liabilities included in the “At fair value through profit or loss” class comprise financial liabilities “Classified as at fair value through profit or loss” and “Designated as at fair value through profit or loss”. Therefore:

- Changes in fair value of financial liabilities included in this class are recorded under “Net investment income” in the Consolidated Statements of Income. However, for financial liabilities designated as at fair value, the change in fair value that is attributable to the Federation’s own credit risk is recognized in other comprehensive income that will not be reclassified subsequently to the Consolidated Statements of Income and is reclassified immediately to undistributed surplus earnings.
- Interest expense related to financial liabilities included in the “At fair value through profit or loss” class is presented under “Net investment income”.

- (ii) Financial liabilities “Classified as at fair value through profit or loss” are securities held for trading and include debt securities issued with the intention to repurchase them in the near term and securities that are part of a portfolio of securities that are managed together and for which there is evidence of an actual pattern of short-term profit-taking, such as “Commitments related to securities sold short”. Derivative financial instruments are also classified as held for trading.

Section m), “Derivative financial instruments and hedging activities”, of this note specifies the nature of the recognition of derivative financial instruments designated as part of hedging relationships.

- (iii) Financial liabilities “Designated as at fair value through profit or loss” are designated as such by management upon initial recognition, on an instrument-by-instrument basis, and are essentially debt securities. Management may make this irrevocable designation if doing so eliminates or significantly reduces a measurement or recognition inconsistency for the financial liability, if a group of financial liabilities is managed and its performance is evaluated on a fair value basis, or if the liabilities are hybrid financial liabilities containing at least one embedded derivative that would otherwise be separated from the host contract and recognized separately.

Financial liabilities included in this measurement category comprise deposits containing at least one embedded derivative that would otherwise be separated from the host contract and recognized separately.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

(iv) Financial liabilities that are not in the “At fair value through profit or loss” class are included in the “Amortized cost” class.

Financial liabilities included in this class are initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they are measured at amortized cost using the effective interest method. Interest expense on securities included in the “Amortized cost” class is recognized under “Interest expense” in the Consolidated Statements of Income for the Personal and Business Services segment and the Other category. Interest expense for the other segments is recognized mainly under “Net investment income” in the Consolidated Statements of Income.

### *Accounting policies applicable before January 1, 2018*

Under IAS 39, financial assets and liabilities were classified based on their characteristics and the intention of management upon their acquisition or issuance.

The classification and measurement of financial assets under IAS 39 can be summarized as follows:

Classes		Categories	Recognition	
			Initial	Subsequent
Financial assets	At fair value through profit or loss (i)	Held for trading (ii)	Fair value	Fair value
		Designated as at fair value through profit or loss (iii)	Fair value	Fair value
	Loans and receivables (iv)		Fair value	Amortized cost
	Available for sale (v)		Fair value	Fair value
	Held to maturity (vi)		Fair value	Amortized cost

(i) Financial assets in the “At fair value through profit or loss” class included financial assets “Held for trading” and “Designated as at fair value through profit or loss”. Therefore:

- Changes in fair value of securities included in this class were recorded under “Net investment income” in the Consolidated Statements of Income.
- Interest and dividend income from securities included in the “At fair value through profit or loss” class of the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category were recognized under “Interest income – Securities” and, for the other segments, there were mainly recognized under “Net investment income” using the effective interest method.

(ii) Financial assets classified as “Held for trading” included the following:

- Securities acquired for resale purposes in the near term and securities that were part of a portfolio of securities that were managed together and for which there was evidence of an actual pattern of short-term profit-taking; and
- Derivative financial instruments.

Section m), “Derivative financial instruments and hedging activities”, specifies the nature of the recognition of derivative financial instruments designated as part of hedging relationships.

(iii) Financial assets classified as “Designated as at fair value through profit or loss” were essentially securities designated as such by management upon initial recognition, on an instrument-by-instrument basis. Management could designate a financial instrument as at fair value through profit or loss upon initial recognition when one of the following conditions was met:

- The designation eliminated or significantly reduced a measurement or recognition inconsistency.
- The assets were part of a group of financial assets or financial assets and liabilities that were managed and whose performance was evaluated on a fair value basis.
- The assets were hybrid financial instruments containing at least one embedded derivative that would otherwise have been separated from the host contract and recognized separately.

The Federation’s financial assets included in this class mainly comprised certain investments made in connection with derivative instruments that were not designated as part of a hedging relationship and certain securities that backed the life and health insurance actuarial liabilities and the property and casualty insurance provisions for claims. This designation eliminated or significantly reduced a measurement or recognition inconsistency for these financial assets.

(iv) Securities included in the “Loans and receivables” class were non-derivative financial assets with fixed or determinable income that were not quoted in an active market and that were not held for sale upon their acquisition or their granting.

These outstanding securities were initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they were measured at amortized cost using the effective interest method. Income recognized on these securities was presented under “Interest income – Loans” in the Consolidated Statements of Income when it was recognized by the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category. Income for the other segments was recognized under “Other income – Other” in the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

- (v) Securities included in the “Available for sale” class were non-derivative financial assets initially designated as available for sale or not included in the “At fair value through profit or loss”, “Held to maturity” or “Loans and receivables” classes. Available-for-sale securities could be sold further to or in view of fluctuations in interest rates, exchange rates or prices of equity instruments or changes in financing sources or terms, or to meet the liquidity needs of the Federation.

Gains and losses resulting from changes in fair value, except for impairment losses and foreign exchange gains and losses, were recognized under “Net unrealized gains” on available-for-sale securities in the Consolidated Statements of Comprehensive Income until the financial asset was derecognized. Premiums and discounts on the purchase of available-for-sale securities were amortized over the life of the securities using the effective interest method and recognized under “Interest income – Securities” for the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category. For the other segments, they were mainly recognized under “Net investment income”.

- (vi) Securities included in the “Held to maturity” class were non-derivative financial assets with fixed or determinable payments and fixed maturity that management had the intention and ability to hold to maturity. These securities were recognized at amortized cost using the effective interest method. The Federation held no instruments in this class as at December 31, 2017.

The classification and measurement of financial liabilities under IAS 39 can be summarized as follows:

Classes		Categories	Recognition	
			Initial	Subsequent
Financial liabilities	At fair value through profit or loss (i)	Held for trading (ii)	Fair value	Fair value
		Designated as at fair value through profit or loss (iii)	Fair value	Fair value
	At amortized cost (iv)		Fair value	Amortized cost

- (i) Financial liabilities included in the “At fair value through profit or loss” class included financial liabilities “Held for trading” and “Designated as at fair value through profit or loss”. Therefore:

- Changes in fair value of securities included in this class were recorded under “Net investment income” in the Consolidated Statements of Income.
- Interest expense related to financial liabilities included in the “At fair value through profit or loss” class was recognized under “Net investment income”.

- (ii) Financial liabilities classified as “Held for trading” were debt securities issued with the intention to repurchase them in the near term and securities that were part of a portfolio of securities that were managed together and for which there was evidence of an actual pattern of short-term profit-taking, such as “Commitments related to securities sold short”. Derivative financial instruments were also classified as “Held for trading”.

Section m), “Derivative financial instruments and hedging activities”, specifies the nature of the recognition of derivative financial instruments designated as part of hedging relationships.

- (iii) Financial liabilities classified as “Designated as at fair value through profit or loss” had been designated as such by management upon initial recognition, on an instrument-by-instrument basis. Management could designate a financial instrument as at fair value through profit or loss upon initial recognition when one of the following conditions was met:

- The designation eliminated or significantly reduced a measurement or recognition inconsistency.
- The liabilities were part of a group of financial liabilities or financial assets and liabilities that were managed and whose performance was evaluated on a fair value basis.
- The liabilities were hybrid financial instruments containing at least one embedded derivative that would otherwise have been separated from the host contract and recognized separately.

The Federation held no instruments in this class as at December 31, 2017.

- (iv) Financial liabilities that were not included in the “At fair value through profit or loss” class were included in the “At amortized cost” class.

These financial liabilities were initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they were measured at amortized cost using the effective interest method. Interest expense on these securities was recognized under “Interest expense” in the Consolidated Statements of Income for the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category. Income for the other segments was mainly recognized under “Net investment income” in the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Determination of the fair value of financial instruments

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

There is little subjectivity in the determination of the fair value of financial instruments, especially securities and commitments related to securities sold short, obtained from quoted prices on active markets. This fair value is based on the quoted price within the bid-ask spread that is most representative of fair value in the circumstances.

If there are no quoted prices on active markets, fair value is determined using models that maximize the use of observable inputs and minimize the use of unobservable inputs. In such cases, fair value estimates are established using valuation techniques such as cash flow discounting, comparisons with similar financial instruments, option pricing models and other valuation techniques commonly used by market participants, if these techniques have been demonstrated to provide reliable estimates. Valuation techniques rely on assumptions concerning the amount and timing of estimated future cash flows and discount rates that are mainly based on observable data, such as interest rate yield curves, exchange rates, credit curves and volatility factors. When one or several material inputs are not observable on the market, fair value is determined mainly based on internal inputs and estimates that take into account the characteristics specific to the financial instrument and any factor relevant to the measurement. For complex financial instruments, significant judgment is made in determining the valuation technique to be used and in selecting inputs and adjustments associated with this technique. Due to the need to use estimates and make judgments when applying many valuation techniques, fair value estimates for identical or similar assets may differ between entities. Fair value reflects market conditions on a given date and may not be representative of future fair values. It should not be considered as being realizable in the event of immediate settlement of these instruments.

#### Loans

The fair value of performing loans is determined by discounting expected contractual cash flows using market interest rates charged for similar new loans at the reporting date and reflects estimated prepayments, adjusted to take into account credit losses on the loan portfolio. Changes in interest rates and in the creditworthiness of borrowers are the main causes of changes in the fair value of loans held by the Federation, which result in a favourable or unfavourable difference compared to their carrying amount.

#### Deposits

The fair value of fixed-rate deposits is determined by discounting expected cash flows using market interest rates currently being offered for deposits with substantially the same term and reflects estimated prepayments. The fair value of deposits with floating-rate features or with no stated maturity is assumed to be equal to their carrying amount.

#### Subordinated notes

The fair value of subordinated notes is based on brokers' quotes.

#### Derivative financial instruments

The fair value of derivative financial instruments is determined using pricing models that incorporate the current market prices and the contractual prices of the underlying instruments, the time value of money, interest rate yield curves, credit curves and volatility factors. This fair value is presented without taking into account the impact of legally enforceable master netting agreements. However, the Federation adjusts the measurement of these instruments based on credit risk, and such adjustments reflect the financial ability of the counterparties to the contracts and the creditworthiness of the Federation, as well as credit risk mitigation measures such as legally enforceable master netting agreements. Note 19, "Derivative financial instruments and hedging activities", specifies the nature of derivative financial instruments held by the Federation.

#### Financial instruments whose fair value equals their carrying amount

The carrying amount of certain financial instruments that mature in the next 12 months is a reasonable approximation of their fair value. These financial instruments include the following items: "Cash and deposits with financial institutions", "Securities borrowed or purchased under reverse repurchase agreements"; "Clients' liability under acceptances"; "Premiums receivable"; "Amounts receivable from clients, brokers and financial institutions"; some items included in "Other assets – Other", "Acceptances"; "Commitments related to securities lent or sold under repurchase agreements"; "Amounts payable to clients, brokers and financial institutions" and some items included in "Other liabilities – Other".

### Transaction costs

Transaction costs for financial instruments are capitalized and then amortized over the life of the instrument using the effective interest method. However, for financial instruments classified or designated as "At fair value through profit or loss", these costs are expensed as incurred.

### Offsetting of financial assets and liabilities

Financial assets and liabilities are presented on a net basis when there is a legally enforceable and unconditional right to set off the recognized amounts and the Federation intends to settle on a net basis or to realize the asset and settle the liability simultaneously.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Derecognition of financial assets and liabilities

A financial asset is derecognized from the Consolidated Balance Sheets when the contractual rights to the cash flows from the asset expire, when the contractual rights to receive these cash flows are retained but the Federation has the obligation to pay them to a third party under certain conditions, or when the Federation transfers the contractual rights to receive the cash flows and substantially all the risks and rewards of ownership of the asset have been transferred.

When substantially all the risks and rewards of ownership of the transferred financial asset are retained by the Federation, such asset is not derecognized from the Consolidated Balance Sheets and a financial liability is recognized, when appropriate.

When substantially all the risks and rewards related to a financial asset are neither transferred nor retained, the Federation derecognizes the financial asset over which it does not retain control and recognizes an asset or a liability representing the rights and obligations created or retained in the asset transfer. If control of the financial asset is retained, the Federation continues to recognize the asset in the Consolidated Balance Sheets to the extent of its continuing involvement in that asset.

When a financial asset is derecognized in its entirety, a gain or a loss is recognized in the Consolidated Statements of Income for an amount equal to the difference between the carrying amount of the asset and the value of the consideration received.

Management must use its judgment to determine whether the contractual rights to the cash flows have expired, have been transferred or have been retained with an obligation to pay them to a third party. With respect to the transfer of substantially all the risks and rewards of ownership of the assets, management evaluates the Federation's exposure before and after the transfer as well as the changes in the amount and timing of the net cash flows of the transferred asset. Lastly, management must make judgments to determine whether it controls the financial asset and to measure retained rights.

A financial liability is derecognized when the related obligation is discharged, cancelled or expires. The difference between the carrying amount of the transferred financial liability and the consideration paid is recognized in the Consolidated Statements of Income.

### b) Cash and deposits with financial institutions

"Cash and deposits with financial institutions" includes cash and cash equivalents. Cash equivalents consist of deposits with the Bank of Canada, deposits with financial institutions—including net amounts receivable related to cheques and other items in the clearing process—as well as certain fixed-income securities. These financial instruments mature in the short term, are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

### c) Securities

The classification and measurement of securities are determined using the criteria stated in section a), "Financial assets and liabilities", above.

#### Securities purchased under reverse repurchase agreements and securities borrowed

Securities purchased under reverse repurchase agreements and securities borrowed are not recognized in the Consolidated Balance Sheets, as substantially all the risks and rewards of ownership of these securities have not been obtained.

Reverse repurchase agreements are treated as collateralized lending transactions. An asset corresponding to the consideration paid for the securities acquired, including accrued interest, is recognized under "Securities borrowed or purchased under reverse repurchase agreements" in the Consolidated Balance Sheets.

As part of securities borrowings, the Federation pledges cash or securities as collateral. When cash is pledged as collateral, an asset corresponding to the amount that will be received upon the delivery of the borrowed securities is recognized under "Securities borrowed or purchased under reverse repurchase agreements" in the Consolidated Balance Sheets. When securities are pledged as collateral, such securities are not derecognized, as substantially all the risks and rewards of ownership of these securities are retained.

#### Securities sold under repurchase agreements and securities lent

Securities sold under repurchase agreements and securities lent are not derecognized from the Consolidated Balance Sheets, as substantially all the risks and rewards of ownership of these securities are retained.

Repurchase agreements are treated as collateralized borrowing transactions. A liability corresponding to the consideration received for the securities sold, including accrued interest, is recognized under "Commitments related to securities lent or sold under repurchase agreements" in the Consolidated Balance Sheets.

As part of securities loans, the Federation receives cash or securities as collateral. When cash is received as collateral, a liability corresponding to the obligation to deliver cash is recognized under "Commitments related to securities lent or sold under repurchase agreements" in the Consolidated Balance Sheets. When securities are received as collateral, such securities are not recognized, as substantially all the risks and rewards of ownership of these securities have not been obtained.

#### Securities sold short

Securities sold short as part of trading activities, which represent the Federation's obligation to deliver securities that it did not possess at the time of sale, are recognized as liabilities at their fair value. Realized and unrealized gains and losses on these securities are recognized under "Net investment income" in the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### d) Loans

Loans are recorded at amortized cost, net of the allowance for credit losses, using the effective interest method.

Fees collected and direct costs related to the origination, restructuring and renegotiation of loans are treated as being integral to the yield of the loans. They are deferred and amortized using the effective interest method, and the amortization is recognized as interest income over the life of the loan. Collateral is obtained if deemed necessary, based on an assessment of the borrower's creditworthiness. Such collateral normally takes the form of assets such as capital assets, receivables, inventory, equipment, securities (government securities, shares, etc.) or cash.

Restructured loans are loans for which the Federation renegotiated the initial terms by granting concessions to the borrower in the context of financial difficulties or to prevent a failure by the borrower to meet its initial obligations. Once the terms of the loan have been renegotiated and accepted by the borrower, the loan is considered as restructured.

When the modification of the terms of a loan has no significant impact on contractual cash flows, the renegotiated loan is not derecognized. At the date of restructuring, the loan is reduced to the amount of the estimated net cash flows receivable under the modified terms, discounted at the effective interest rate prior to the restructuring, which may result in a gain or loss on modification.

When the modification of the terms of a loan has a significant impact on contractual cash flows, the initial loan should be derecognized, which may result in a gain or loss on derecognition. In addition, a new loan should be recognized based on the new contractual terms.

#### *Accounting policy applicable since January 1, 2018*

When the modification of the terms of a loan does not result in the derecognition of such loan, the date of initial recognition of the loan remains unchanged for purposes of applying the impairment model. The default risk based on the modified contractual terms is then compared to the default risk based on the initial terms to determine whether there has been a significant increase in credit risk since initial recognition.

When the modification of the terms of a loan results in the derecognition of such loan and the recognition of a new loan, the date of the modification should become the date of initial recognition of the new loan for purposes of applying the impairment model. A new loan is usually considered as being in Stage 1 of the impairment model, but it may have to be considered as credit-impaired upon origination.

#### *Accounting policy applicable before January 1, 2018*

Restructured loans remained classified as performing loans when they did not meet the criteria requiring their classification as credit-impaired loans. In addition, management assessed whether such restructured loans were impaired in accordance with its impairment policies.

### e) Impairment of financial instruments

#### *Accounting policies applicable since January 1, 2018*

Under IFRS 9, at each reporting date, the Federation recognizes a loss allowance for expected credit losses for debt instruments classified as at amortized cost or as at fair value through other comprehensive income, as well as certain off-balance sheet items, namely loan commitments and financial guarantees, which are not measured at fair value through profit or loss. This allowance is estimated based on an impairment model that comprises three stages:

- Stage 1: For financial instruments that have not had a significant increase in credit risk since initial recognition and are not considered as credit-impaired financial assets, a loss allowance amounting to 12-month expected credit losses is recognized.
- Stage 2: For financial instruments that have had a significant increase in credit risk since initial recognition but are not considered as credit-impaired financial assets, a loss allowance amounting to the lifetime expected credit losses is recognized.
- Stage 3: For financial instruments considered as credit impaired, a loss allowance amounting to the lifetime expected credit losses continues to be recognized.

Financial instruments may, over their life, move from one impairment model stage to another based on the improvement or deterioration in their credit risk and the level of expected credit losses. Instruments are always classified in the various stages of the impairment model based on the change in credit risk between the reporting date and the initial recognition date of the financial instrument and an analysis of evidence of impairment.

#### **Determination of significant increases in credit risk**

To determine whether, at the reporting date, credit risk has significantly increased since initial recognition, the Federation bases its assessment on the change in default risk over the expected life of the financial instrument, which requires significant judgment.

To this end, the Federation compares the probability of default (PD) of the financial instrument at the reporting date with its PD at the date of initial recognition. In addition, it considers reasonable and supportable information indicating a significant increase in credit risk since initial recognition, including qualitative information and information about future economic conditions to the extent that it affects the assessment of the instrument's PD. The criteria used to determine a significant increase in credit risk vary depending on the type of clients and are mainly based on a relative change combined with an absolute change in the PD. They also include absolute PD thresholds and certain other criteria. All instruments that are more than 30 days past due are transferred to Stage 2 of the impairment model.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

For securities at “Amortized cost” or “Classified as at fair value through other comprehensive income”, the Federation elected to use the low credit risk exemption. Consequently, when credit risk is equivalent to the credit risk of the “investment grade” category at the reporting date, the credit risk on the securities is deemed to not have significantly increased since initial recognition.

### Definition of default and credit-impaired financial asset

The definition of default used in the impairment model corresponds to the definition used for internal credit risk management purposes and for regulatory purposes. It considers relevant quantitative and qualitative factors. In particular, a loan is in default when contractual payments are over 90 days past due. A financial asset is considered credit-impaired when it is in default, unless the detrimental impact on the estimated future cash flows is considered insignificant.

### Measurement of the loss allowance for expected credit losses

The loss allowance for expected credit losses reflects an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, and takes into account reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Generally, the loss allowance for expected credit losses represents the present value of the difference between cash flows that are due, or the amount of the commitment that may be used under the terms and conditions of the contract, and total cash flows that the Federation expects to receive. For credit-impaired financial assets, expected credit losses are calculated based on the difference between the gross carrying amount of the asset and estimated cash flows.

The measurement of the loss allowance for expected credit losses is estimated for each exposure at the reporting date and is based on the result of multiplying the three credit risk parameters, namely PD, loss given default (LGD) and exposure at default (EAD). The result of this multiplication is then discounted using the effective interest rate. The parameters are estimated using an appropriate segmentation that considers common credit risk characteristics. The LGD of certain loans and off-balance sheet items is estimated at 0% due to the nature of the credit enhancement obtained. For financial instruments in Stage 1 of the impairment model, credit risk parameters are projected over a maximum horizon of 12 months, while for those in Stage 2 or Stage 3, they are projected over the remaining life of the instrument.

To determine the credit risk parameters, financial instruments are aggregated based on their common credit risk characteristics. The following table presents the main aggregation variables for the applicable parameters.

PD	LGD	EAD
<i>Loans, loan commitments and financial guarantees:</i> <ul style="list-style-type: none"> <li>Type of clients</li> <li>Risk level</li> <li>Type of instrument</li> <li>Industry</li> </ul>	<i>Loans, loan commitments and financial guarantees:</i> <ul style="list-style-type: none"> <li>f) Type of clients</li> <li>g) Type of collateral</li> <li>h) Type of guarantor</li> <li>i) Risk level</li> <li>j) Type of instrument</li> <li>k) Industry</li> </ul>	<i>Loans :</i> <ul style="list-style-type: none"> <li>No aggregation<sup>(1)</sup></li> </ul> <i>Loan commitments and financial guarantees<sup>(2)</sup>:</i> <ul style="list-style-type: none"> <li>Type of clients</li> <li>Risk level</li> <li>Utilization rate</li> <li>Authorized amount</li> <li>Type of product</li> <li>Industry</li> </ul>

<sup>(1)</sup> No aggregation variable is required to determine the EAD for loans, as it represents the anticipated balance of each loan.

<sup>(2)</sup> To determine the EAD for loan commitments and financial guarantees, a credit conversion factor is applied.

The loss allowance for expected credit losses also considers information about future economic conditions. To incorporate forward-looking information relevant to the determination of significant increases in credit risk and the measurement of the loss allowance for expected credit losses, the Federation uses the econometric models for credit risk projection. These models estimate the impact of macroeconomic variables on the various credit risk parameters. The Federation uses three scenarios (base, upside and downside) to determine the loss allowance for expected credit losses and assigns to each scenario a probability of occurrence. The Federation may also make adjustments to take into account the relevant information that affects the measurement of the loss allowance and that has not been incorporated into the credit risk parameters. Incorporating forward-looking information is based on a set of assumptions and methodologies specific to credit risk and economic projections and therefore requires a high degree of judgment.

For credit-impaired financial assets that are individually material, measuring the loss allowance for expected credit losses does not require using credit risk parameters. It is instead based on an extensive review of the borrower's situation and the realization of collateral held. The measurement represents a probability-weighted present value, calculated using the effective interest rate, of cash flow shortfalls that takes into consideration the impact of various scenarios that may materialize and information about future economic conditions. In some cases, the Federation may not recognize any loss allowance when the probability of the collateral realization scenario is 100% and the estimated realizable value of the collateral exceeds the gross carrying amount of the loan.

### Expected life

The expected life of most financial instruments is equal to the maximum contractual term during which the Federation is exposed to credit risk, including extension options that may be exercised solely by the borrower. The exception to this rule concerns revolving credit facilities, which consist of personal and business lines of credit and credit card loans. Their life is estimated as being the period over which there is exposure to credit risk but for which expected credit losses would not be mitigated by normal credit risk management actions.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Recognition of the loss allowance for expected credit losses

The loss allowance for expected credit losses on loans is recorded under “Allowance for credit losses” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income.

The loss allowance for expected credit losses on loan commitments and financial guarantees is recorded under “Other liabilities – Other” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income.

The loss allowance for expected credit losses on securities at “Amortized cost” is recorded against “Securities – Securities at amortized cost” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income. The loss allowance for expected credit losses on securities “Classified as at fair value through other comprehensive income” is recognized under “Net unrealized losses on debt securities classified as at fair value through other comprehensive income” in the Consolidated Statements of Comprehensive Income and under “Provision for credit losses” in the Consolidated Statements of Income.

### Foreclosed assets

Assets foreclosed to settle credit-impaired loans are recognized on the date of the foreclosure at their fair value less costs to sell. Any difference between the carrying amount of the loan and the fair value recorded for the foreclosed assets is recognized under “Provision for credit losses”.

### Loan write-off

A loan is written off, in whole or in part, when recovery is no longer reasonably expected, which is when all attempts at restructuring or collection have been made and, based on an assessment of the file in its entirety, there are no other means to recover the loan. For secured loans, balances are generally written off once the collateral has been realized. Loans for which a consumer proposal or bankruptcy proceedings are ongoing but for which the Federation has no reasonable expectation of recovery are written off, but they may continue to be subject to recovery measures by an insolvency trustee. Credit card balances are written off completely when no payment has been received at the end of a period of 180 days. These balances could however still be subject to enforcement activity during a certain period after they have been written off. When a loan is written off completely, any subsequent payments are recorded under “Provision for credit losses” in the Consolidated Statements of Income.

### *Accounting policies applicable before January 1, 2018*

#### Credit-impaired loans

Under IAS 39, at the reporting date, the Federation assessed whether there was any objective evidence that a financial asset or a group of financial assets was impaired. A loan was considered credit-impaired when there was such evidence, and more specifically when one of the following conditions was met:

- There was reason to believe that a portion of the principal or interest could not be collected;
- The interest or principal repayment was contractually 90 days past due, unless the loan was fully secured and in the process of collection;
- The interest or principal was more than 180 days past due.

A loan was not classified as credit-impaired when it was fully guaranteed or insured by a Canadian government (federal or provincial) or an agency of a Canadian government.

A loan was considered past due when the borrower had failed to make a payment by the contractual due date.

A loan ceased to be considered credit-impaired when principal and interest payments were up to date and there was no doubt as to its collection or when it was restructured and was treated as a new loan and there was no doubt as to the collection of principal and interest.

Assets foreclosed to settle credit-impaired loans were recognized on the date of the foreclosure at their fair value less costs to sell. Any difference between the carrying amount and the fair value recorded for the acquired assets was recognized under “Provision for credit losses”.

A loan classified as “Loans and receivables” was written off when all attempts at restructuring or collection had been made and the likelihood of future recovery was remote. When a loan was written off completely, any subsequent payments were recorded under “Provision for credit losses” in the Consolidated Statements of Income. Credit card balances were written off completely when no payment had been received at the end of a period of 180 days.

#### Allowance for credit losses on loans

Under IAS 39, objective evidence of impairment resulted from a loss event that had occurred after the loan was granted but before the reporting date and that had an impact on the estimated future cash flows of loans.

The impairment of a loan or a group of loans was determined by estimating the recoverable amount of these financial assets. The allowance was equal to the difference between this amount and the carrying amount. This allowance was presented in deduction of assets under “Allowance for credit losses”. To determine the estimated recoverable amount of a loan, the Federation discounted the estimated future cash flows at the effective interest rate inherent to the loan. When the amounts and timing of future cash flows could not be estimated with reasonable reliability, the estimated recoverable amount was determined using the fair value of the collateral underlying the loan, net of expected costs of realization, or the observable market price for the loan. The collateral could vary depending on the type of loan.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The allowance for credit losses on loans represented management's best estimate for loan impairment at the reporting date. As part of its evaluation, management had to make judgments to determine the data, assumptions and estimates to be used, including determining when a loan was considered credit-impaired and the amount that could have been recovered. Changing these estimates and assumptions would have had an impact on the allowance for credit losses and the provision for credit losses for the year.

The allowance for credit losses related to credit-impaired loans was measured either individually or collectively for loans that were not individually material, while the allowance for credit losses was measured collectively for non-credit impaired loans.

### Individual allowances

The Federation first reviewed its loan portfolios on a loan-by-loan basis to assess credit risk and determined whether there was any objective evidence of impairment for which a loss should have been recognized in the Consolidated Statements of Income. Loan portfolios for which there was no objective evidence of impairment were included in groups of financial assets having similar credit characteristics and were subject to a collective allowance.

### Collective allowance on credit-impaired loans

Certain consumer, credit card and other personal loan portfolios comprised a large number of homogeneous balances that were not individually material. A collective allowance was established on such loans based on the portfolio's historical net loss rate.

### Collective allowance

The method used by the Federation to determine the collective allowance took into account the risk parameters of the various loan portfolios, in particular through the integration of sophisticated credit risk models. These collective allowance models took into account certain factors such as PD (loss frequency), LGD (extent of losses) and EAD (gross exposures at default). These parameters were based on historical losses and determined according to the category and risk rating of each loan. The measurement of the collective allowance relied heavily on management's judgments and depended on management's assessment of current credit quality trends with respect to business sectors, the impact of changes in its credit policies, and economic conditions.

The allowance for credit losses related to off-balance sheet items, namely loan commitments and financial guarantees, was recognized under "Other liabilities – Other" in the Consolidated Balance Sheets and under "Provision for credit losses" in the Consolidated Statements of Income.

### **Available-for-sale securities**

Under IAS 39, securities classified in the "Available for sale" category were examined at the reporting date to determine whether there was any objective evidence that they were impaired. In measuring an impairment loss, the Federation took into account many facts specific to each investment and all the factors that could have indicated that there had been impairment. Factors considered included, but were not limited to, a significant or prolonged decline in fair value, significant financial difficulties of the issuer, a breach of contract, the increasing probability that the issuer would enter bankruptcy or a restructuring, and the disappearance of an active market for the asset. Management also used its judgment to determine when to recognize an impairment loss.

The Federation individually assessed debt securities included in the "Available for sale" class, including preferred shares with characteristics and behaviour similar to those of debt securities, to determine whether there was any objective evidence of impairment. The impairment loss represented the cumulative loss, which was the difference between amortized cost and current fair value, less any impairment loss previously recognized. Future interest income was calculated on the reduced carrying amount using the interest rate used to discount future cash flows in order to measure the impairment loss. When, during a subsequent period, the fair value of a debt security increased and that increase could be objectively related to a credit event occurring after the impairment loss had been recognized in the Consolidated Statements of Income, the impairment loss was reversed through the Consolidated Statements of Income.

For equity securities included in the "Available for sale" class, when evidence of impairment existed, the cumulative loss which corresponded to the difference between acquisition cost and current fair value, less any impairment loss previously recognized was transferred out of other comprehensive income, in the Consolidated Statements of Comprehensive Income, and recognized in the Consolidated Statements of Income. Impairment losses on equity securities were not reversed to the Consolidated Statements of Income. Increases in fair value occurring subsequent to the recognition of an impairment loss were instead recorded directly in other comprehensive income, in the Consolidated Statements of Comprehensive Income. Any impairment loss on securities previously impaired was directly recognized in the Consolidated Statements of Income.

## **f) Property, plant and equipment and investment property**

### **Property, plant and equipment**

Property, plant and equipment consists of land, buildings, computer hardware, furniture, fixtures and other items as well as leasehold improvements. They are recognized at cost less any accumulated depreciation and any accumulated impairment losses, and are depreciated over their expected useful life using the straight-line method.

The depreciable amount of an item of property, plant and equipment is determined after deducting its residual value less costs to sell. The useful life of property, plant and equipment is generally equal to its expected useful life.

The depreciation expense for property, plant and equipment is recognized under "Non-interest expense – Premises, equipment and furniture, including depreciation" in the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Investment property

Investment properties are buildings or land held to earn rentals or for capital appreciation.

Investment properties are recognized at cost less accumulated depreciation and are depreciated over their useful life using the straight-line method. Transfers to or from the “Investment property” category are made only when there is a change in use. Upon a transfer of property, plant and equipment from the “Investment property” category to the “Buildings” category, the cost remains the same and continues to be the carrying amount. If a building held and occupied by the Federation becomes an investment property, it is recorded using the accounting policies applicable to investment properties.

The depreciation expense for investment properties is recognized under “Net investment income” in the Consolidated Statements of Income.

### Depreciation

Property, plant and equipment and investment property are depreciated using the following depreciation periods:

	Depreciation periods
Land	Non-depreciable
Buildings and investment property	5 to 80 years
Computer equipment	1 to 10 years
Furniture, fixtures and other	3 to 10 years
Leasehold improvements	Expected term of the lease

When an item of property, plant and equipment is made up of several significant parts having different useful lives or providing economic benefits according to different patterns, each part is recognized separately and is depreciated over its own depreciation period.

### Derecognition

Property, plant and equipment and investment property are derecognized upon disposal or when they are permanently withdrawn from use and no future economic benefits are expected. Gains and losses on the disposal or sale of buildings are recognized in the Consolidated Statement of Income for the year in which they are realized under “Premises, equipment and furniture, including depreciation” for property, plant and equipment and under “Net investment income” for investment property.

## g) Goodwill and intangible assets

### Goodwill

Goodwill represents the excess of the purchase price over the fair value of the identifiable assets acquired and liabilities assumed in a business combination accounted for using the acquisition method.

At the acquisition date, each item of goodwill is allocated to one or more cash-generating units (CGU or group of CGUs) that are expected to benefit from the combination. A group of CGUs must not be larger than a business segment. A CGU is the smallest identifiable group of assets that generates cash inflows that are independent from the cash inflows from other groups of assets. Subsequent to initial measurement, goodwill is measured at cost less any impairment loss.

### Intangible assets

Intangible assets include acquired and internally generated intangible assets and are initially recognized at cost. The cost of an intangible asset acquired as part of a business combination corresponds to its fair value at the date of acquisition. Subsequent to initial recognition, intangible assets are measured at cost less any accumulated amortization and any impairment losses. Expenditures related to internally generated intangible assets, except for development costs, are recognized in profit or loss as incurred.

The Federation assesses whether the useful life of an intangible asset is finite or indefinite. Intangible assets with finite useful lives include mainly software and client relationships and are amortized using the straight-line method over their estimated useful lives, which do not exceed 40 years. Intangible assets with indefinite useful lives include mainly trademarks and licenses.

Gains or losses resulting from the derecognition of an intangible asset correspond to the difference between the net proceeds of disposal and the net carrying amount of the asset. They are recognized under “Non-interest expense – Other” in the Consolidated Statements of Income upon derecognition of the asset.

## h) Impairment of non-financial assets

The Federation assesses at the reporting date whether there is evidence that an asset may be impaired. An impairment loss is recognized when the carrying amount of an asset exceeds its recoverable amount.

The recoverable amount represents the higher of the fair value less costs of disposal and the value in use. Fair value represents the best estimate of the amount that could be obtained from the sale of the asset in an arm's-length transaction between knowledgeable and willing parties. The value in use is calculated using the most appropriate method, generally by discounting recoverable future cash flows.

Any impairment loss recognized in the Consolidated Statements of Income represents the excess of the carrying amount of the asset over the recoverable amount. Impairment losses on an asset may be subsequently reversed and are recognized in the Consolidated Statements of Income in the year in which they occur.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

Estimating the recoverable amount of a non-financial asset to determine whether it is impaired also requires management to make estimates and assumptions. Any change in these estimates and assumptions could impact the determination of the recoverable amount of non-financial assets and, therefore, the outcome of the impairment test. The main estimates and assumptions used in calculating the recoverable amount are future cash flows estimated based on internal financial forecasts, expected future earnings, the growth rate and the discount rate.

### **Goodwill and intangible assets with indefinite useful lives**

Goodwill and intangible assets with indefinite useful lives are tested for impairment once a year and when there is possible evidence of impairment.

The impairment test for goodwill and intangible assets with indefinite useful lives is performed based on the recoverable amount of the asset or each CGU (or each group of CGUs) to which goodwill or the intangible asset with an indefinite useful life is allocated. Significant judgments must be made to estimate the data taken into account in the model used to determine the recoverable amount of each intangible asset with an indefinite useful life or each CGU.

When the recoverable amount of the asset or the CGU is less than the carrying amount, an impairment loss is recognized in the Consolidated Statement of Income for the year and is first recorded as a reduction of the intangible asset with an indefinite useful life or, in the case of a CGU, as a reduction of the goodwill allocated to the CGU (or group of CGUs) and then as a reduction of the other identifiable assets of the CGU (or group of CGUs) pro rata on the basis of their carrying amount in the unit. The allocation of the impairment loss to the assets of the CGU or group of CGUs must however not result in their carrying amount being lower than the highest of the following amounts: the fair value of the assets less costs to sell, their value in use and zero.

Goodwill impairment losses cannot be reversed.

### **i) Acceptances and clients' liability under acceptances**

Acceptances represent a form of negotiable short-term debt that is issued by our clients and that we guarantee for a fee. The potential liability of the Federation under acceptances is recognized under "Acceptances", in "Other liabilities". The Federation has equivalent offsetting claims against its clients in the event of a call on these commitments, which are recognized under "Clients' liability under acceptances", in "Other assets". Fees are recognized under "Other income – Other".

### **j) Insurance contract liabilities**

Insurance contracts are contracts under which a significant insurance risk is transferred to the insurer upon their issuance. An insurance risk is transferred when the insurance subsidiaries agree to compensate the policyholder if an uncertain future event specified in the contract adversely affects the policyholder. Contracts that transfer a significant insurance risk issued by these subsidiaries are classified as insurance contracts, in accordance with IFRS 4, "Insurance Contracts".

Once a contract is classified as an insurance contract, it continues to be an insurance contract even if the insurance risk it carries decreases significantly during its life.

Insurance contract liabilities include the contract liabilities of the life and health insurance and the property and casualty insurance subsidiaries. They are derecognized when the obligation specified in the contract is discharged or cancelled or expires.

#### **Life and health insurance contract liabilities**

Life and health insurance contract liabilities consist of actuarial liabilities, benefits payable, provisions for claims not reported, provision for dividends and experience refunds, and contract holder deposits.

Actuarial liabilities represent the amounts which, together with estimated future premiums and net investment income, will provide for all the life and health insurance subsidiaries' commitments regarding estimated future benefits, contract holder dividends and related expenses. The appointed actuary of each of these subsidiaries is required to determine the actuarial liabilities needed to meet its future commitments. These actuarial liabilities are determined using the Canadian Asset Liability Method (CALM) in accordance with Canadian accepted actuarial practices, and they are equal to the value in the Consolidated Balance Sheets of the assets that back them.

Under CALM, actuarial liabilities of the life and health insurance subsidiaries are determined based on an explicit projection of cash flows using current best estimate assumptions for each cash flow component and each significant contingency. Each non-economic assumption is adjusted by a margin for adverse deviation. With respect to investment returns, the provision for adverse deviation is established by using yield scenarios that consider the uncertainty associated with the projection of interest rates on the reinvestment of future cash flows in relation to the mismatch of cash flows. These scenarios are established using a deterministic model that includes testing prescribed by Canadian actuarial standards. With respect to minimum guarantees on segregated fund products, the provision for adverse deviation is determined using stochastic modelling.

#### **Property and casualty insurance contract liabilities**

Property and casualty insurance contract liabilities consist of unearned premiums and provisions for claims and adjustment expenses.

Unearned premiums represent the portion of premiums remaining to be earned at the reporting date.

The provisions for claims and adjustment expenses related to the insurance policies of the property and casualty insurance subsidiaries are estimated using actuarial techniques that consider best estimate assumptions, taking into account currently known data, which are regularly reviewed and updated. Any resulting adjustment is recognized in the Consolidated Statement of Income for the year in which the revision occurs. The provisions for claims and adjustment expenses are reported on a discounted basis using the rate of return of the underlying assets, with a margin for adverse deviations.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Discretionary participation features

Certain insurance contracts of the life and health insurance subsidiaries contain a discretionary participation feature that allows the contract holder to participate in the profitability related to their contract. These contracts give the contract holder the contractual right to receive additional benefits as supplement to guaranteed benefits. The life and health insurance subsidiaries elected not to recognize the participating portion of these contracts separately.

### Reinsurance

In order to limit their losses, the insurance subsidiaries enter into reinsurance treaties that vary based on the nature of the activities. In addition, they purchase additional reinsurance protection with respect to large-scale catastrophic events.

Premium income from insurance contracts and expenses related to claims, benefits and changes in insurance contract liabilities associated with contracts under reinsurance treaties are presented net of amounts ceded to reinsurers in the Consolidated Statements of Income.

The share of reinsurers in the insurance contract liabilities is presented under "Reinsurance assets" in the Consolidated Balance Sheets at the same time and using a basis consistent with those used to establish the corresponding liability. These assets comprise the reinsurers' share in actuarial liabilities and provisions for benefits, policyholder dividends and experience refunds for the life and health insurance operations, and the reinsurers' share in unearned premiums and provisions for claims and adjustment expenses for the property and casualty insurance operations.

### k) Segregated funds

Certain insurance contracts allow contract holders to invest in segregated funds held by one of the life and health insurance subsidiaries for their benefit. All risks and rewards of ownership of these investments accrue to the contract holders, even though these investments are held by this subsidiary. Accordingly, the net assets and liabilities of segregated funds are presented on a separate line in the Consolidated Balance Sheets. Segregated fund investments are measured and recognized at fair value at the reporting date, which is determined using the methods described in section a), "Financial assets and liabilities". In addition, if a segregated fund controls a mutual fund in which it has invested, such mutual fund is consolidated in the segregated fund net assets. A liability corresponding to contract holders' rights to the segregated fund net assets is also recognized separately.

### l) Provisions

Provisions are liabilities of uncertain timing or amount. A provision is recognized when the Federation has an obligation (legal or constructive) as a result of a past event, the settlement of which should result in an outflow of resources embodying economic benefits, and when a reliable estimate can be made of the amount of the obligation. The amount of the obligation is discounted where the effect of the time value of money is material.

Provisions are based on management's best estimate of the amounts required to settle the obligations on the reporting date, taking into account the relevant uncertainties and risks. As these estimates are forward-looking in nature, management must use its judgment to forecast the timing and amount of future cash flows. Actual results may differ materially from these forecasts.

Charges to and reversals of provisions are recognized in profit or loss under the items corresponding to the nature of the expenditures covered.

### m) Derivative financial instruments and hedging activities

#### Derivative financial instruments

Derivative financial instruments are financial contracts whose value depends on assets, interest rates, foreign exchange rates or financial indexes. The vast majority of the Federation's derivative financial instruments are negotiated by mutual agreement with the counterparty and include forward exchange contracts, currency swaps, interest rate swaps, credit default swaps, total return swaps, forward rate agreements, as well as currency, interest rate and stock index options. Other transactions are carried out as part of regulated trades and consist mainly of futures. The types of contracts used are defined in Note 19, "Derivative financial instruments and hedging activities".

Derivative financial instruments, including embedded derivatives which are required to be accounted for separately, are recognized at fair value on the Consolidated Balance Sheets. Changes in fair value of embedded derivatives required to be accounted for separately are recognized under "Net investment income" in the Consolidated Statements of Income.

#### Hybrid financial instruments

##### *Accounting policy applicable since January 1, 2018*

When a hybrid contract contains a host that is an asset within the scope of IFRS 9, the entire hybrid contract is classified and recognized based on the characteristics of the hybrid contract.

An embedded derivative is separated from the host and accounted for separately as a derivative when the host is not an asset within the scope of IFRS 9 and the following conditions are met: (a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the hybrid contract is not measured at fair value with changes in fair value recognized in the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### *Accounting policy applicable before January 1, 2018*

Under IAS 39, embedded derivative financial instruments were separated from their host contract and accounted for as derivatives if: (a) the economic characteristics and risks of the embedded derivatives were not closely related to the economic characteristics and risks of the host contract; (b) the embedded derivative had the same terms as a separate instrument; (c) the hybrid instrument or contract was not measured at fair value with changes in fair value recognized in consolidated profit or loss.

### Objectives of holding derivatives

The Federation uses derivative financial instruments for trading or asset-liability management purposes.

Derivative financial instruments held for trading purposes are used to meet the needs of member caisses and clients, and to allow the Federation to generate income on its own trading activities. These instruments are recognized at fair value in the Consolidated Balance Sheets, and changes in their fair value are recognized under "Net investment income" in the Consolidated Statements of Income.

Derivative financial instruments held for asset-liability management purposes are used to manage current and expected risks related to market risk. They enable the Federation to transfer, modify or reduce the interest rate and foreign currency exposures of assets and liabilities recorded in the Consolidated Balance Sheets, as well as firm commitments and forecasted transactions.

### **Hedging activities**

The Federation elected to continue applying the requirements of IAS 39 for hedge accounting instead of adopting the provisions of IFRS 9.

The Federation mainly designates its derivative financial instruments as part of a fair value or cash flow hedging relationship.

When derivative financial instruments are used to manage assets and liabilities, the Federation must determine, for each derivative, whether or not hedge accounting is appropriate. To qualify for hedge accounting, a hedging relationship must be designated and documented at its inception. Such documentation must address the specific strategy for managing risk, the asset, liability or cash flows that are being hedged as well as the measure of hedge effectiveness. Consequently, the effectiveness of each hedging relationship must be assessed, regularly and on an individual basis, to determine with reasonable assurance whether the relationship is effective and will continue to be effective. The derivative financial instrument must prove highly effective to offset changes in the fair value or the cash flows of the hedged item attributable to the risk being hedged.

The Federation may also use derivative financial instruments as an economic hedge for certain transactions in situations where the hedging relationship does not qualify for hedge accounting or where it elects not to apply hedge accounting.

The designation of a derivative financial instrument as hedging instrument is discontinued in the following cases: the hedged item is sold or matures, the derivative financial instrument is repurchased or matures, the hedge is no longer effective, or the Federation terminates the designation of the hedge or no longer expects that the forecasted transaction will occur.

Hedging instruments that meet the strict hedge accounting conditions are recognized as follows:

### Fair value hedges

In a fair value hedge transaction, changes in fair value of the hedging derivative financial instrument are recognized under "Net investment income" in the Consolidated Statements of Income, as are changes in fair value of the hedged asset or liability attributable to the hedged risk. The gain or loss attributable to the hedged risk is applied to the carrying amount of the hedged item. When the changes in fair value of the hedging derivative financial instrument and the hedged item do not entirely offset each other, the resulting amount, which represents the ineffective portion of the relationship, is recognized under "Net investment income" in the Consolidated Statements of Income.

When a fair value hedging relationship is discontinued, hedge accounting is discontinued prospectively. The hedged item is no longer adjusted to reflect the fair value impact of the designated risk. Previously recorded adjustments to the hedged item are amortized using the effective interest method and are recognized in net interest income, in the Consolidated Statements of Income, following the underlying instrument, over the remaining life of the hedged item. However, if the hedged item ceased to exist, the adjustments for the impact of the designated risk are immediately recognized under "Net investment income" in the Consolidated Statements of Income.

### Cash flow hedges

In a cash flow hedge transaction, gains and losses resulting from changes in the fair value of the effective portion of the derivative financial instrument are recognized under "Net gains (losses) on derivative financial instruments designated as cash flow hedges", in other comprehensive income, until the hedged item is recognized in the Consolidated Statements of Income, at which time such changes are recognized in net interest income in the Consolidated Statements of Income, following the underlying instrument. The ineffective portion of cash flow hedge transactions is immediately recognized under "Net investment income" in the Consolidated Statement of Income.

When a cash flow hedging relationship no longer qualifies for hedge accounting, the Federation discontinues hedge accounting prospectively. Gains or losses recognized in other comprehensive income are amortized to net interest income, in the Consolidated Statements of Income, following the underlying instrument, over the expected remaining life of the hedging relationship that was discontinued. If a designated hedged item is sold or matures before the related derivative financial instrument ceases to exist, all gains or losses are immediately recognized in profit or loss under "Net investment income".

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### n) Financial guarantees

A financial guarantee is a contract that could contingently require the Federation to make specified payments to the guaranteed party to repay a loss that such party incurred as a result of a default by a specified third party to make a payment upon maturity in accordance with the original or modified terms and conditions of a debt security.

Financial guarantees are initially recognized as liabilities in the Consolidated Financial Statements for an amount corresponding to the fair value of the commitment resulting from the issuance of the guarantee. After initial recognition, except in cases where it must be measured at fair value through profit or loss, the guarantee is measured at the higher of the following amounts:

- i) The amount initially recorded less, when appropriate, accumulated amortization recognized in the Consolidated Statements of Income;
- ii) Under IFRS 9, the amount of the allowance for credit losses (accounting policy applicable since January 1, 2018) and, under IAS 39, the best estimate of cash outflows required to settle any financial obligation resulting from the guarantee (accounting policy applicable before January 1, 2018).

If a financial guarantee meets the definition of a derivative, it is measured at fair value through profit or loss at each reporting date and presented as a derivative financial instrument. Guarantees presented as derivative financial instruments are a type of over-the-counter credit derivative under which one party transfers to another party the credit risk of an underlying financial instrument.

The carrying amount of guarantees does not reflect the maximum potential amount of future payments under guarantees. The Federation considers the difference between these two amounts as off-balance sheet credit instruments.

### o) Reserves

The Federation's stabilization reserve consists of amounts appropriated from the annual surplus earnings. As at December 31, 2018, amounts appropriated to the Federation's stabilization reserve are essentially used to pay interest on F capital shares it issued, while as at December 31, 2017, these amounts were essentially used to pay interest on permanent shares issued by a caisse when the amounts appropriated to such caisse's stabilization reserve were not sufficient, and to pay interest on F capital shares issued by the Federation when the annual surplus earnings of the Federation were not sufficient.

The general reserve is essentially made up of amounts appropriated by the Federation. As at December 31, 2018, this reserve can only be used to eliminate a deficit and, when surplus earnings and the stabilization reserve are not sufficient, to pay interest on F capital shares. As at December 31, 2017, this reserve could only be used to eliminate a deficit. It cannot be divided amongst member caisses nor used to pay a member dividend.

Other reserves are mainly made up of amounts that can only be taken into account in the calculation of the distribution plan when the amounts previously appropriated to these reserves are realized.

### p) Revenue recognition

In addition to the items mentioned in section a), "Financial assets and liabilities", the specific recognition criteria that follow must also be met before revenue can be recognized.

#### Recognition criteria

##### *Accounting policy applicable since January 1, 2018*

Under IFRS 15, revenue is recognized when the Federation has transferred control of a good or service (the performance obligation is satisfied). Management must use its judgment to determine when performance obligations are satisfied and establish the transaction price and the amounts allocated to such obligations.

##### *Accounting policy applicable before January 1, 2018*

Under IAS 18, revenue was recognized to the extent that it was probable that the economic benefits would flow to the Federation and that it could be measured reliably.

#### Net interest income

##### *Accounting policy applicable since January 1, 2018*

Interest income and expense are mainly earned or incurred by the Personal and Business Services segment and the Other category. They are recognized using the effective interest method for all financial instruments measured at "Amortized cost", for interest-bearing financial assets "Classified as at fair value through other comprehensive income" and for financial instruments included in the "At fair value through profit or loss" class.

The effective interest method is used in the calculation of the amortized cost of a financial asset or liability and in the allocation of interest income or interest expense over the relevant period. Under IFRS 9, the effective interest rate is the rate that discounts future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of a financial asset or to the amortized cost of a financial liability.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

When calculating the effective interest rate, the Federation estimates cash flows considering all contractual terms of the financial instruments, but it does not consider future credit losses. The calculation includes transaction costs and income between parties to the contract as well as premiums or discounts. Transaction costs and income that form an integral part of the effective rate of the contract, such as file setup fees and finders' fees, are assimilated to supplemental interest.

For financial assets that are not considered credit-impaired (Stages 1 and 2), interest income is calculated on the gross carrying amount of the financial instrument. For credit-impaired financial assets (Stage 3), interest income is calculated by applying the effective interest rate to the amortized cost of the asset, which corresponds to the gross carrying amount less the loss allowance for expected credit losses.

### *Accounting policy applicable before January 1, 2018*

Interest income and expense were mainly earned or incurred by the Personal and Business Services segment and the Treasury and Other Support to Desjardins Group Entities category. They were recognized using the effective interest method for all financial instruments measured at amortized cost, for interest-bearing financial assets included in the "Available for sale" class and for financial instruments included in the "At fair value through profit or loss" class.

The effective interest method is a method of calculating the amortized cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period. Under IAS 39, the effective interest rate was the rate that exactly discounted future payments or receipts through the expected life of the financial instrument or, when appropriate, over a shorter period, to obtain the net carrying amount of the financial instrument.

When calculating the effective interest rate, the Federation estimated cash flows considering all contractual terms of the financial instruments but did not consider future credit losses. The calculation included transaction costs and income between parties to the contract as well as premiums or discounts. Transaction costs and income that formed an integral part of the effective rate of the contract, such as file setup fees and finders' fees, were assimilated to supplemental interest.

### **Premiums**

Gross premiums on insurance contracts of the life and health insurance subsidiaries are recognized as revenue when they become due. As soon as they are recognized, an actuarial provision is established and recognized under "Insurance contract liabilities". Premiums are presented, net of premiums ceded under reinsurance treaties, under "Net premiums" in the Consolidated Statements of Income.

Gross premiums on insurance contracts of the property and casualty insurance subsidiaries are recognized as revenue proportionately over the life of the contracts. They are presented, net of premiums ceded under reinsurance treaties, under "Net premiums" in the Consolidated Statements of Income. The portion of the premiums remaining to be earned at the reporting date is presented under "Insurance contract liabilities" in the Consolidated Balance Sheets.

### **Service charges, commissions, brokerage fees and other**

The Federation earns revenue from service charges, commissions and brokerage fees related to the broad range of services and products it provides its member caisses and clients.

Service charges, commissions, brokerage fees and investment fund fees are recognized once the service has been provided or the product has been delivered. This income is recognized under "Brokerage and investment fund services" in the Consolidated Statements of Income.

Loan syndication fees are recognized as revenue when the syndication agreement is signed unless the yield on the loan retained by the Federation is less than the yield of other comparable lending institutions that participate in the financing. In such instances, an appropriate portion of the fees is deferred using the effective interest method. This income is recognized under "Lending fees and credit card service revenues" in the Consolidated Statements of Income.

Commissions and costs arising from the negotiation, or the participation thereto, of a transaction on behalf of a third party-such as the arrangement of share or other securities acquisitions or business purchases or sales-are recognized at the outcome of the underlying transactions. Income from such commissions is recognized under "Brokerage and investment fund services" in the Consolidated Statements of Income. Income from lending fees and credit card service revenue is recorded under "Lending fees and credit card service revenues" in the Consolidated Statements of Income.

Portfolio management fees and fees for other services are recognized based on the applicable service contracts, pro rata over the period during which the service is provided. Portfolio management income is recorded under "Management and custodial service fees" in the Consolidated Statements of Income.

Asset management fees related to investment funds are recognized pro rata over the period during which the service is provided. The same principles are applied to wealth management, financial planning and custodial services that are provided on an ongoing basis over a long period of time. Asset management income is recognized under "Management and custodial service fees" in the Consolidated Statements of Income.

Fees for service agreements related to technical, financial and administrative support are recognized once the service has been provided or the product has been delivered. This income is recognized under "Service agreements" in the Consolidated Statements of Income.

Dividend income is recognized when the Federation's right to receive payment of the dividend is established.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### q) Assets under management and assets under administration

Assets under management and assets under administration are held by and for the benefit of clients. These assets are therefore excluded from the Consolidated Balance Sheets of the Federation. Income from these management services is recognized under "Management and custodial service fees" in the Consolidated Statements of Income when the service is provided.

### r) Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rate prevailing at the reporting date. Non-monetary assets and liabilities measured at historical cost are translated at the exchange rate prevailing at the transaction date, while those that are measured at fair value are translated at the exchange rate prevailing at the date fair value was determined. Income and expenses are translated at the average exchange rate for the year. Realized and unrealized gains and losses resulting from the translation are recognized under "Foreign exchange income" in the Consolidated Statements of Income. However, the following items are presented in other comprehensive income in the Consolidated Statements of Comprehensive Income.

- Translation gains and losses on financial assets "Designated as at fair value through other comprehensive income" (accounting policy applicable since January 1, 2018).
- Unrealized gains and losses on non-monetary financial instruments classified as "Available for sale" (accounting policy applicable before January 1, 2018).
- Gains and losses on derivatives designated as cash flow hedging instruments.

### s) Leases

#### Operating leases

Leases that do not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases.

When the Federation is the lessor, lease income from operating leases is recognized on a straight-line basis over the lease term under "Net other investment income" and the leased asset remains recognized in the Consolidated Balance Sheets. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as the lease income. Contingent rent is recognized in profit or loss in the year during which it is earned.

When the Federation is the lessee, the asset is not recognized as an asset. Lease payments made under operating leases are recognized as an expense on a straight-line basis until the end of the lease under "Premises, equipment and furniture, including depreciation", in the Consolidated Statements of Income.

#### Finance leases

Leases that transfer substantially all the risks and rewards incidental to ownership of an asset and under which the Federation is the lessor are recognized at the commencement of the lease term as a net investment in a finance lease for the present value of minimum lease payments and any unguaranteed residual value accruing to the lessor under "Other assets – Other", in the Consolidated Balance Sheets. Finance income is recognized in profit or loss on a basis that generates a periodic return on the net investment in the finance lease under "Other income – Other".

### t) Income taxes on surplus earnings

The income tax expense on surplus earnings recognized in the Consolidated Statements of Income comprises the current and deferred tax expense on operating surplus earnings as well as the income tax consequences of remuneration on capital stock and dividends when certain conditions are met. The total income tax expense includes the income tax expense on surplus earnings recognized in the Consolidated Statements of Income as well as current and deferred taxes on items recognized outside profit or loss directly in the Consolidated Statements of Comprehensive Income or the Consolidated Statements of Changes in Equity.

The total income tax expense is based on the expected tax treatment of the transactions. To determine the current and deferred portions of income taxes on surplus earnings, management must make judgments to establish the assumptions concerning the dates on which deferred income tax assets and liabilities will be reversed. Significant judgment must be used to interpret the relevant tax legislation in order to determine the income tax expense. If the Federation's interpretation differs from that of taxation authorities or if the reversal dates do not correspond with the forecasted dates, the provision for income taxes on surplus earnings may increase or decrease in subsequent years.

#### Current income taxes

Current income tax assets and liabilities for the current year and prior years are measured based on the amount that the Federation expects to recover from or pay to the taxation authorities. Tax laws and tax rates applied to determine these amounts are those that have been enacted or substantively enacted at the reporting dates.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

### Deferred income taxes

Deferred taxes are recognized, using the balance sheet liability method, for all temporary differences existing at the reporting date between the tax basis of assets and liabilities and their carrying amount in the Consolidated Balance Sheets.

Deferred tax liabilities are recognized for all taxable temporary differences, except in the following cases:

- i) When the deferred tax liability arises from the initial recognition of goodwill or the initial recognition of an asset or liability in a transaction which is not a business combination and which, at the time of the transaction, affects neither accounting profit nor taxable profit (or tax loss).
- ii) For taxable temporary differences associated with investments in subsidiaries, when the date at which the difference reverses can be controlled and it is probable that it will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences as well as all tax loss carryforwards and unused tax credits, to the extent that it is probable that a taxable profit will be available against which these differences, tax loss carryforwards and tax credits can be utilized, except in the following cases:

- i) When the deferred tax asset associated with the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction which is not a business combination and which, at the time of the transaction, affects neither accounting profit nor taxable profit (or tax loss).
- ii) For deductible temporary differences associated with investments in subsidiaries, associates and joint ventures. Deferred tax assets are recognized only to the extent that it is probable that the difference will reverse in the foreseeable future and that a taxable profit will be available against which such difference can be utilized.

The carrying amount of a deferred tax asset is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of a deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it becomes probable that a future taxable profit will be available to recover them.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply during the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to set off current tax assets against current tax liabilities, and if these deferred taxes relate to the same taxable entity and the same taxation authority.

### u) Dividends to member caisses

Dividends to member caisses recognized in the Consolidated Statements of Income reflect management's best estimate. They are based on a resolution of the Board of Directors to recommend to the general meeting that payment of these dividends be approved. The annual dividends are determined on the basis of the distribution of the surplus earnings that the Annual General Meeting of the Federation members has approved. Transfers to the reserves are recognized when approved by the member caisses.

### v) Employee benefits

#### Short-term benefits

Short-term benefits include salaries and commissions, social security contributions and certain bonuses payable within 12 months after the reporting date. An expense is recorded for these benefits in the period during which the services giving right to them were rendered.

#### Post-employment benefits

##### Pension and post-retirement benefit plans

The Federation offers to a majority of its employees a defined benefit pension plan and a defined benefit supplemental pension plan. It also offers a post-retirement benefit plan that provides medical, dental and life insurance to retiring employees and their dependents.

The cost of these plans is recognized in the Consolidated Statements of Income and includes current service cost, past service cost and net interest on net defined benefit plan liabilities. Past service cost resulting from a plan amendment or curtailment is immediately recognized in the Consolidated Statements of Income.

Remeasurements of net defined benefit plan liabilities are recognized in items of other comprehensive income that will not be reclassified subsequently to the Consolidated Statements of Income and are immediately reclassified to undistributed surplus earnings. These remeasurements include actuarial gains and losses and the difference between the actual return on plan assets and the interest income generated by such assets, which is recognized in the Consolidated Statements of Income. Actuarial gains and losses result from changes in actuarial assumptions used to determine the defined benefit plan obligation and experience gains and losses on such obligation.

Net defined benefit plan assets or liabilities are equal to the present value of the plans' obligation, calculated using the projected unit credit method, less the fair value of plan assets. The value of any defined benefit plan asset is, when appropriate, limited to the present value of any economic benefits available in the form of refunds from the plans or reductions in future contributions to the pension plans.

**NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)**

The Federation participates in defined benefit group plans whose risks are shared by entities under common control. The Federation's share in the cost recognized and the liability for the defined benefit group pension plans of Desjardins Group is mainly determined based on funding rules, as described in the plan's by-laws. The main Desjardins Group pension plan is funded by both employee and employer contributions, which are based on the financial position and the funding policy of the plan. Employers' contributions are determined using a percentage of the assessable payroll for their employees participating in the plan.

The Federation's share in the cost of the group other post-retirement benefit plan of Desjardins Group is determined based on the number of active insureds of the Federation as a percentage of the total number of active insureds for Desjardins Group as a whole. The method used to determine such share was revised during the year and is now based on eligible insureds.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

### IMPACT OF CHANGES IN ACCOUNTING POLICIES

The retrospective impact of applying IFRS 9, IFRS 15 and amendments to IFRS 4 has been recognized in the opening balances of the Consolidated Balance Sheet as at January 1, 2018.

The following table presents the impact of adopting these standards and amendments on the Federation's Consolidated Balance Sheet as at January 1, 2018.

	Balance as at December 31, 2017	IFRS 9	IFRS 15	IFRS 4	Opening balance as at January 1, 2018
<b>ASSETS</b>					
Cash and deposits with financial institutions	\$ 1,731	\$ -	\$ -	\$ -	\$ 1,731
Securities	46,904	-	-	-	46,904
Securities borrowed or purchased under reverse repurchase agreements	9,377	-	-	-	9,377
Loans	58,882	-	-	-	58,882
Allowance for credit losses	(198)	(295)	-	-	(493)
Segregated fund net assets	13,379	-	-	-	13,379
Other assets	15,665	77	46	-	15,788
<b>TOTAL ASSETS</b>	<b>\$ 145,740</b>	<b>\$ (218)</b>	<b>\$ 46</b>	<b>\$ -</b>	<b>\$ 145,568</b>
<b>LIABILITIES AND EQUITY</b>					
<b>LIABILITIES</b>					
Deposits	\$ 52,149	\$ -	\$ -	\$ -	\$ 52,149
Other liabilities	76,184	(6)	48	-	76,226
Subordinated notes	1,388	-	-	-	1,388
<b>TOTAL LIABILITIES</b>	<b>129,721</b>	<b>(6)</b>	<b>48</b>	<b>-</b>	<b>129,763</b>
<b>EQUITY</b>					
Capital stock	8,537	-	-	-	8,537
Undistributed surplus earnings	5,674	410	-	(376)	5,708
Accumulated other comprehensive income	458	(411)	-	376	423
Reserves	540	(211)	(2)	-	327
<b>Equity - Group's share</b>	<b>15,209</b>	<b>(212)</b>	<b>(2)</b>	<b>-</b>	<b>14,995</b>
<b>Non-controlling interests</b>	<b>810</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>810</b>
<b>TOTAL EQUITY</b>	<b>16,019</b>	<b>(212)</b>	<b>(2)</b>	<b>-</b>	<b>15,805</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 145,740</b>	<b>\$ (218)</b>	<b>\$ 46</b>	<b>\$ -</b>	<b>\$ 145,568</b>

The following table presents additional information on the impact of adopting these standards and amendments on the Federation's "Equity – Group's share" as at January 1, 2018.

	Group's share
<b>Undistributed surplus earnings</b>	
Balance as at December 31, 2017	\$ 5,674
Adoption of the IFRS 9 measurement categories	412
Net unrealized gains related to the overlay approach adjustment for insurance operations financial assets	(376)
Recognition of expected credit losses on financial instruments	(2)
<b>Opening balance as at January 1, 2018</b>	<b>\$ 5,708</b>
<b>Accumulated other comprehensive income</b>	
Balance as at December 31, 2017	\$ 458
Adoption of the IFRS 9 measurement categories	(412)
Recognition of expected credit losses on debt securities at fair value through other comprehensive income	1
Net unrealized gains related to the overlay approach adjustment for insurance operations financial assets	376
<b>Opening balance as at January 1, 2018</b>	<b>\$ 423</b>
<b>Reserves</b>	
Balance as at December 31, 2017	\$ 540
Recognition of expected credit losses on financial instruments	(211)
Impact of the adoption of IFRS 15	(2)
<b>Opening balance as at January 1, 2018</b>	<b>\$ 327</b>

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

The following table presents the impact of adopting IFRS 9 on the classification and measurement of financial instruments as at January 1, 2018.

	Notes	Measurement category under IAS 39	Measurement category under IFRS 9	Carrying amount under IAS 39 as at December 31, 2017	Carrying amount under IFRS 9 as at January 1, 2018
<b>Financial assets</b>					
<b>Cash and deposits with financial institutions</b>					
	(1)	At fair value through profit or loss – held for trading	Amortized cost	\$ 23	\$ 23
		At fair value through profit or loss – designated as at fair value through profit or loss	Designated as at fair value through profit or loss	298	298
		Available for sale	Classified as at fair value through other comprehensive income	639	639
		Loans and receivables	Amortized cost	771	771
<b>Securities</b>					
<b>Debt instruments</b>					
		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	13,271	13,271
		At fair value through profit or loss – designated as at fair value through profit or loss	Designated as at fair value through profit or loss	16,665	16,665
	(2)	At fair value through profit or loss – designated as at fair value through profit or loss	Classified as at fair value through profit or loss	6	6
	(3)	Available for sale	Classified as at fair value through profit or loss	23	23
		Available for sale	Classified as at fair value through other comprehensive income	10,860	10,860
	(4)	Available for sale	Amortized cost	1,090	1,090
<b>Equity instruments</b>					
	(5)	At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	41	41
		At fair value through profit or loss – designated as at fair value through profit or loss	Classified as at fair value through profit or loss	1,671	1,671
	(6)	Available for sale	Classified as at fair value through profit or loss	3,275	3,275
	(7)	Available for sale	Designated as at fair value through other comprehensive income	2	2
<b>Securities borrowed or purchased under reverse repurchase agreements</b>					
		Loans and receivables	Amortized cost	\$ 9,377	\$ 9,377

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES *(continued)*

The following table presents the impact of adopting IFRS 9 on the classification and measurement of financial instruments as at January 1, 2018 *(continued)*.

	Notes	Measurement category under IAS 39	Measurement category under IFRS 9	Carrying amount under IAS 39 as at December 31, 2017	Carrying amount under IFRS 9 as at January 1, 2018
<b>Financial assets <i>(continued)</i></b>					
<b>Loans</b>		Loans and receivables	Amortized cost	\$ 58,684	\$ 58,389
<b>Other financial assets</b>					
Clients' liability under acceptances		Loans and receivables	Amortized cost	31	31
Premiums receivable		Loans and receivables	Amortized cost	2,098	2,098
Derivative financial instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	3,772	3,772
Amounts receivable from clients, brokers and financial institutions		Loans and receivables	Amortized cost	1,563	1,563
Other		Loans and receivables	Amortized cost	1,013	1,013
<b>Total financial assets</b>				<b>\$ 125,173</b>	<b>\$ 124,878</b>
<b>Financial liabilities</b>					
<b>Deposits</b>		Financial liabilities at amortized cost	Amortized cost	\$ 52,149	\$ 52,149
<b>Other financial liabilities</b>					
Acceptances		Financial liabilities at amortized cost	Amortized cost	31	31
Commitments related to securities sold short		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	9,112	9,112
Commitments related to securities lent or sold under repurchase agreements		Financial liabilities at amortized cost	Amortized cost	10,062	10,062
Derivative financial instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	3,677	3,677
Amounts payable to clients, brokers and financial institutions		Financial liabilities at amortized cost	Amortized cost	4,247	4,247
Other		Financial liabilities at amortized cost	Amortized cost	2,019	2,019
		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	452	452
<b>Subordinated notes</b>		Financial liabilities at amortized cost	Amortized cost	<b>1,388</b>	<b>1,388</b>
<b>Total financial liabilities</b>				<b>\$ 83,137</b>	<b>\$ 83,137</b>

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES *(continued)*

- (1) Certain items in cash and deposits with financial institutions were classified as “Held for trading” under IAS 39 as at December 31, 2017. As at January 1, 2018, the Federation classified these debt instruments as at “Amortized cost” under IFRS 9 as they are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest. All these securities matured or were sold during fiscal 2018. The effective interest rate on these debt instruments ranged from 0.59% and 1.73% as at January 1, 2018, and interest income recognized on these securities following the adoption of IFRS 9 was insignificant.
- (2) These debt instruments were classified as “Designated as at fair value through profit or loss” under IAS 39 as at December 31, 2017. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as the contractual terms of these financial assets give rise to cash flows that are not solely payments of principal and interest on the principal amount outstanding.
- (3) These debt instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, these debt instruments were “Classified as at fair value through profit or loss” under IFRS 9 because they are held within a business model whose objective is achieved by selling financial assets or because they do not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest.
- (4) These debt instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, the Federation classified them as at “Amortized cost” under IFRS 9 as they are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest. The fair value of the securities still held as at December 31, 2018 was \$30 million. If these securities had not be reclassified to be measured at “Amortized cost” under IFRS 9 as at January 1, 2018, an immaterial loss would have been recognized in the Consolidated Statement of Comprehensive Income for the year ended December 31, 2018.
- (5) These equity instruments were classified as “Designated as at fair value through profit or loss” under IAS 39 as at December 31, 2017. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as, under IFRS 9, all investments in equity instruments other than those designated as at fair value through other comprehensive income have to be included in this measurement category.
- (6) These equity instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as, under IFRS 9, all investments in equity instruments other than those designated as at fair value through other comprehensive income have to be included in this measurement category.
- (7) These equity instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, these instruments, which consist of an investment in a private company that will be held on a long-term basis, were irrevocably “Designated as at fair value through other comprehensive income”. Gains and losses on these instruments will therefore never be reclassified subsequently to the Consolidated Statements of Income.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

The following table reconciles the carrying amounts of financial assets recognized under IAS 39 as at December 31, 2017 to the carrying amounts under IFRS 9 as at January 1, 2018.

	Carrying amount under IAS 39 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
<b>Financial assets</b>				
<b>Classified as at fair value through profit or loss<sup>(1)</sup></b>				
Cash and deposits with financial institutions	\$ 23	\$ -	\$ -	\$ 23
To securities at amortized cost	-	(23)	-	(23)
	23	(23)	-	-
<b>Securities</b>				
Debt instruments	13,271	-	-	13,271
From securities designated as at fair value through profit or loss	-	6	-	6
From available-for-sale securities	-	23	-	23
Equity instruments	41	-	-	41
From securities designated as at fair value through profit or loss	-	1,671	-	1,671
From available-for-sale securities	-	3,275	-	3,275
	13,312	4,975	-	18,287
Derivative financial instruments	3,772	-	-	3,772
<b>Total financial assets classified as at fair value through profit or loss</b>	<b>17,107</b>	<b>4,952</b>	<b>-</b>	<b>22,059</b>
<b>Designated as at fair value through profit or loss<sup>(2)</sup></b>				
Cash and deposits with financial institutions	298	-	-	298
<b>Securities</b>				
Debt instruments	16,671	-	-	16,671
To securities classified as at fair value through profit or loss	-	(6)	-	(6)
Equity instruments	1,671	-	-	1,671
To securities classified as at fair value through profit or loss	-	(1,671)	-	(1,671)
	18,342	(1,677)	-	16,665
<b>Total financial assets designated as at fair value through profit or loss</b>	<b>18,640</b>	<b>(1,677)</b>	<b>-</b>	<b>16,963</b>
<b>Available for sale</b>				
Cash and deposits with financial institutions	639	-	-	639
To securities classified as at fair value through other comprehensive income	-	(639)	-	(639)
	639	(639)	-	-
<b>Securities</b>				
Debt instruments	11,973	-	-	11,973
To securities classified as at fair value through profit or loss	-	(23)	-	(23)
To securities classified as at fair value through other comprehensive income	-	(10,860)	-	(10,860)
To securities at amortized cost	-	(1,090)	-	(1,090)
Equity instruments	3,277	-	-	3,277
To securities classified as at fair value through profit or loss	-	(3,275)	-	(3,275)
To securities designated as at fair value through other comprehensive income	-	(2)	-	(2)
	15,250	(15,250)	-	-
<b>Total available-for-sale financial assets</b>	<b>\$ 15,889</b>	<b>\$ (15,889)</b>	<b>\$ -</b>	<b>\$ -</b>

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

The following table reconciles the carrying amounts of financial assets recognized under IAS 39 as at December 31, 2017 to the carrying amounts under IFRS 9 as at January 1, 2018 (continued).

	Carrying amount under IAS 39 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
<b>Financial assets (continued)</b>				
<b>Classified as at fair value through other comprehensive income</b>				
Cash and deposits with financial institutions	\$ -	\$ -	\$ -	\$ -
From available-for-sale securities	-	639	-	639
	-	639	-	639
Securities				
Debt instruments	-	-	-	-
From available-for-sale securities	-	10,860	-	10,860
	-	10,860	-	10,860
<b>Total financial assets classified as at fair value through other comprehensive income</b>	-	11,499	-	11,499
<b>Designated as at fair value through other comprehensive income</b>				
Securities				
Equity instruments	-	-	-	-
From available-for-sale securities	-	2	-	2
<b>Total financial assets designated as at fair value through other comprehensive income</b>	-	2	-	2
<b>Amortized cost<sup>(3)</sup></b>				
Cash and deposits with financial institutions	771	-	-	771
From securities held for trading	-	23	-	23
	771	23	-	794
Securities				
Debt instruments	-	-	-	-
From available-for-sale securities	-	1,090	-	1,090
	-	1,090	-	1,090
Securities borrowed or purchased under reverse repurchase agreements	9,377	-	-	9,377
Loans	58,684	-	(295)	58,389
Other financial assets	4,705	-	-	4,705
<b>Total financial assets at amortized cost</b>	<b>\$ 73,537</b>	<b>\$ 1,113</b>	<b>\$ (295)</b>	<b>\$ 74,355</b>

<sup>(1)</sup> For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the "At fair value through profit or loss – held for trading" category.

<sup>(2)</sup> For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the "At fair value through profit or loss – designated as at fair value through profit or loss" category.

<sup>(3)</sup> For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the "Loans and receivables" category.

The adoption of IFRS 9 had no impact on the measurement of financial liabilities as at January 1, 2018.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

The following table reconciles allowances determined under IAS 39 and IAS 37, “Provisions, Contingent Liabilities and Contingent Assets”, as at December 31, 2017 to the allowance determined using the IFRS 9 expected credit losses model as at January 1, 2018.

	Carrying amount under IAS 39 and IAS 37 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
<b>Allowance on financial assets at amortized cost</b>				
Loans and receivables reclassified as at amortized cost	\$ 198	\$ -	\$ 295	\$ 493
	198	-	295	493
<b>Allowance on securities at fair value through other comprehensive income</b>				
Available-for-sale securities reclassified as at fair value through other comprehensive income	-	-	1	1
	-	-	1	1
<b>Allowance on off-balance sheet items</b>	40	-	(6)	34
<b>Total allowances</b>	<b>\$ 238</b>	<b>\$ -</b>	<b>\$ 290</b>	<b>\$ 528</b>

## FUTURE ACCOUNTING CHANGES

Accounting standards and amendments issued by the IASB but not yet effective as at December 31, 2018 are presented below. Regulatory authorities have stated that early adoption of these standards and amendments will not be permitted, unless they indicate otherwise.

### IFRS 16, “Leases”

In January 2016, the IASB issued IFRS 16, “Leases”, which will replace the current standard, IAS 17, “Leases”, and related interpretations. IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. Under IFRS 16, a lease is a contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

IFRS 16 introduces a single recognition model for the lessee, thereby eliminating the current distinction between operating and finance leases. The lessee must recognize on the Consolidated Balance Sheets a lease liability corresponding to the present value of the remaining lease payments as well as a right-of-use asset measured at the amount of the lease liability, plus or minus certain adjustments, if any. An interest expense and a depreciation charge relating to the lease liability and the right-of-use asset, respectively, must be recognized and presented separately in the Consolidated Statements of Income. Leases with terms of 12 months or less and low-value leases will continue to be recognized as a lease expense based on the terms of the lease. In addition, the Federation will apply the practical expedient which allows not to separate non-lease components from lease components for a contract.

For the lessor, the standard does not provide for any significant changes except for enhanced disclosures.

The Federation will have to adopt IFRS 16 as at January 1, 2019 on a retrospective basis. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 16 will be recognized in the opening Consolidated Balance Sheet. The Federation decided not to restate comparative periods upon adopting the provisions of IFRS 16. Consequently, the retrospective impact of applying IFRS 16 will be recognized in the Consolidated Balance Sheet as at January 1, 2019, which is the effective date of the new standard. In addition, the Federation elected to apply the following transitional expedients proposed in the standard as at the date of transition:

- The right-of-use asset will be equal to the amount of the lease liability adjusted by the amount of prepaid lease payments.
- Existing contracts at the date of transition will not be reassessed to determine whether they are, or contain, a lease under IFRS 16.

The Federation estimates that adopting IFRS 16 will result on January 1, 2019, in the recognition of a right-of-use asset of approximately \$330 million and the recognition of a corresponding lease liability. These changes will result in a decrease of approximately 8 basis points in regulatory capital ratios.

## NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES *(continued)*

### IFRS 17, “Insurance Contracts”

In May 2017, the IASB issued IFRS 17, “Insurance Contracts”, which will replace the current standard, IFRS 4, “Insurance Contracts”. IFRS 17 sets out the recognition, measurement, presentation and disclosure requirements applicable to all insurance contracts.

IFRS 17 requires that insurance contract liabilities be measured using a general model based on current value. This model uses assumptions as at the reporting date to estimate the amount, timing and uncertainty of future cash flows and takes into account market interest rates and the impact of insurance contract holder options and guarantees.

In addition, under IFRS 17, profits on the sale of insurance policies will no longer be recognized upon initial recognition, but will instead be deferred as separate liabilities and recognized in profit or loss over the contract term as services are provided.

The Federation is currently assessing the impact of adopting IFRS 17, which will be effective for annual periods beginning on or after January 1, 2021. In November 2018, the IASB tentatively decided to defer the effective date of IFRS 17 to the annual periods beginning on or after January 1, 2022.

### Conceptual Framework for Financial Reporting

In March 2018, the IASB issued the “Conceptual Framework for Financial Reporting”, which replaces the current version of the conceptual framework. The “Conceptual Framework for Financial Reporting” includes new concepts, updates the definitions and recognition criteria for assets and liabilities and clarifies some key concepts. The Federation is currently assessing the impact of adopting this new framework, which will be effective for annual periods beginning on or after January 1, 2020.

## NOTE 3 – CARRYING AMOUNT OF FINANCIAL INSTRUMENTS

### CLASSIFICATION AND CARRYING AMOUNT OF FINANCIAL INSTRUMENTS

The following tables present the carrying amount of financial assets and liabilities according to their classification in the classes defined in the financial instrument standards.

	At fair value through profit or loss		At fair value through other comprehensive income		Amortized cost <sup>(2)</sup>	Total
	Classified as at fair value through profit or loss <sup>(1)</sup>	Designated as at fair value through profit or loss	Classified as at fair value through other comprehensive income <sup>(2)</sup>	Designated as at fair value through other comprehensive income		
<b>As at December 31, 2018</b>						
<b>Financial assets</b>						
Cash and deposits with financial institutions	\$ -	\$ 291	\$ 1,068	\$ -	\$ 1,379	\$ 2,738
Securities	20,606	16,308	11,088	43	1,621	49,666
Securities borrowed or purchased under reverse repurchase agreements	-	-	-	-	14,086	14,086
Loans <sup>(3)</sup>	-	-	-	-	61,837	61,837
Other financial assets						
Clients' liability under acceptances	-	-	-	-	160	160
Premiums receivable	-	-	-	-	2,378	2,378
Derivative financial instruments <sup>(4)</sup>	4,376	-	-	-	-	4,376
Amounts receivable from clients, brokers and financial institutions	-	-	-	-	1,487	1,487
Other	13	-	-	-	794	807
<b>Total financial assets</b>	<b>\$ 24,995</b>	<b>\$ 16,599</b>	<b>\$ 12,156</b>	<b>\$ 43</b>	<b>\$ 83,742</b>	<b>\$ 137,535</b>
<b>Financial liabilities</b>						
Deposits	\$ -	\$ -	\$ -	\$ -	\$ 58,057	\$ 58,057
Other financial liabilities						
Acceptances	-	-	-	-	160	160
Commitments related to securities sold short	10,829	-	-	-	-	10,829
Commitments related to securities lent or sold under repurchase agreements	-	-	-	-	16,233	16,233
Derivative financial instruments <sup>(4)</sup>	3,332	-	-	-	-	3,332
Amounts payable to clients, brokers and financial institutions	-	-	-	-	4,105	4,105
Other	319	-	-	-	2,448	2,767
Subordinated notes	-	-	-	-	1,378	1,378
<b>Total financial liabilities</b>	<b>\$ 14,480</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 82,381</b>	<b>\$ 96,861</b>

<sup>(1)</sup> An amount of \$2,758 million corresponds to financial assets designated for the overlay approach.

<sup>(2)</sup> As at December 31, 2018, the allowance for credit losses on securities at "Amortized cost" totalled \$1 million, and the allowance for credit losses on securities "Classified as at fair value through other comprehensive income" totalled \$2 million. Detailed information on the allowance for credit losses on loans is presented in Note 7, "Loans and allowance for credit losses".

<sup>(3)</sup> For more information, see Note 7, "Loans and allowance for credit losses".

<sup>(4)</sup> Include derivative financial instruments designated as hedging instruments amounting to \$783 million in assets and \$202 million in liabilities. Detailed information on derivatives designated as hedging instruments is presented in Note 19 "Derivative financial instruments and hedging activities".

During the year ended December 31, 2018, no financial instruments have been reclassified.

## NOTE 3 – CARRYING AMOUNT OF FINANCIAL INSTRUMENTS *(continued)*

### CLASSIFICATION AND CARRYING AMOUNT OF FINANCIAL INSTRUMENTS *(continued)*

As at December 31, 2017	At fair value through profit or loss		Available for sale <sup>(1)</sup>	Loans and receivables, and financial liabilities at amortized cost	Total
	Held for trading	Designated as at fair value through profit or loss			
<b>Financial assets</b>					
Cash and deposits with financial institutions	\$ 23	\$ 298	\$ 639	\$ 771	\$ 1,731
Securities	13,312	18,342	15,250	-	46,904
Securities borrowed or purchased under reverse repurchase agreements	-	-	-	9,377	9,377
Loans <sup>(2)</sup>	-	-	-	58,684	58,684
Other financial assets					
Clients' liability under acceptances	-	-	-	31	31
Premiums receivable	-	-	-	2,098	2,098
Derivative financial instruments <sup>(3)</sup>	3,772	-	-	-	3,772
Amounts receivable from clients, brokers and financial institutions	-	-	-	1,563	1,563
Other	-	-	-	1,013	1,013
<b>Total financial assets</b>	<b>\$ 17,107</b>	<b>\$ 18,640</b>	<b>\$ 15,889</b>	<b>\$ 73,537</b>	<b>\$ 125,173</b>
<b>Financial liabilities</b>					
Deposits	\$ -	\$ -	\$ -	\$ 52,149	\$ 52,149
Other financial liabilities					
Acceptances	-	-	-	31	31
Commitments related to securities sold short	9,112	-	-	-	9,112
Commitments related to securities lent or sold under repurchase agreements	-	-	-	10,062	10,062
Derivative financial instruments <sup>(3)</sup>	3,677	-	-	-	3,677
Amounts payable to clients, brokers and financial institutions	-	-	-	4,247	4,247
Other	452	-	-	2,019	2,471
Subordinated notes	-	-	-	1,388	1,388
<b>Total financial liabilities</b>	<b>\$ 13,241</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 69,896</b>	<b>\$ 83,137</b>

<sup>(1)</sup> During the year ended December 31, 2017, the Federation concluded that there was no objective evidence of material impairment.

<sup>(2)</sup> For more information, see Note 7, "Loans and allowance for credit losses".

<sup>(3)</sup> Include derivative financial instruments designated as hedging instruments amounting to \$275 million in assets and \$351 million in liabilities.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS

### FAIR VALUE HIERARCHY

The fair value measurement of financial instruments is determined using the following three-level fair value hierarchy:

- Level 1 – Measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Valuation techniques based primarily on observable market data;
- Level 3 – Valuation techniques not based primarily on observable market data.

### TRANSFERS BETWEEN LEVELS

Transfers between hierarchy levels for instruments measured at fair value are made at the reporting date.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

### HIERARCHY OF FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE

The following tables present the hierarchy for financial instruments measured at fair value in the Consolidated Balance Sheets.

As at December 31, 2018	Level 1	Level 2	Level 3	Total
<b>Financial assets</b>				
<b>Financial assets at fair value through profit or loss</b>				
Cash and deposits with financial institutions	\$ 27	\$ 264	\$ -	\$ 291
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	10,632	994	-	11,626
Provincial governmental entities and municipal corporations in Canada	15,063	1,108	-	16,171
School or public corporations in Canada	14	85	-	99
Foreign public administrations	191	-	-	191
Other securities				
Financial institutions	32	800	56	888
Other issuers	3	2,763	742	3,508
Equity securities	3,106	627	698	4,431
	29,068	6,641	1,496	37,205
Derivative financial instruments				
Interest rate contracts	-	1,707	-	1,707
Foreign exchange contracts	-	1,300	-	1,300
Other contracts	-	1,369	-	1,369
	-	4,376	-	4,376
Other assets	-	-	13	13
<b>Total financial assets at fair value through profit or loss</b>	29,068	11,017	1,509	41,594
<b>Financial assets at fair value through other comprehensive income</b>				
Cash and deposits with financial institutions	135	933	-	1,068
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	1,950	595	-	2,545
Provincial governmental entities and municipal corporations in Canada	4,402	641	-	5,043
Other securities				
Financial institutions	-	2,810	-	2,810
Other issuers	-	593	97	690
Equity securities	-	43	-	43
<b>Total financial assets at fair value through other comprehensive income</b>	6,487	5,615	97	12,199
Financial instruments of segregated funds	5,556	7,610	72	13,238
<b>Total financial assets</b>	\$ 41,111	\$ 24,242	\$ 1,678	\$ 67,031
<b>Financial liabilities</b>				
<b>Financial liabilities at fair value through profit or loss</b>				
Other liabilities				
Commitments related to securities sold short	\$ 10,535	\$ 294	\$ -	\$ 10,829
Other	-	-	319	319
	10,535	294	319	11,148
Derivative financial instruments				
Interest rate contracts	-	1,726	-	1,726
Foreign exchange contracts	-	278	-	278
Other contracts	-	1,328	-	1,328
	-	3,332	-	3,332
<b>Total financial liabilities</b>	\$ 10,535	\$ 3,626	\$ 319	\$ 14,480

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

### HIERARCHY OF FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE (continued)

As at December 31, 2017	Level 1	Level 2	Level 3	Total
<b>Financial assets</b>				
<b>Financial assets at fair value through profit or loss</b>				
Cash and deposits with financial institutions	\$ 8	\$ 313	\$ -	\$ 321
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	7,620	1,247	-	8,867
Provincial governmental entities and municipal corporations in Canada	15,232	1,176	-	16,408
School or public corporations in Canada	14	94	-	108
Foreign public administrations	312	-	-	312
Other securities				
Financial institutions	29	800	58	887
Other issuers	-	2,497	867	3,364
Equity securities	1,236	236	236	1,708
	24,451	6,363	1,161	31,975
Derivative financial instruments				
Interest rate contracts	-	1,624	-	1,624
Foreign exchange contracts	-	390	-	390
Other contracts	-	1,758	-	1,758
	-	3,772	-	3,772
<b>Total financial assets at fair value through profit or loss</b>	24,451	10,135	1,161	35,747
<b>Available-for-sale financial assets</b>				
Cash and deposits with financial institutions	36	603	-	639
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	1,821	573	-	2,394
Provincial governmental entities and municipal corporations in Canada	4,610	1,205	-	5,815
Foreign public administrations	7	28	-	35
Other securities				
Financial institutions	-	2,878	-	2,878
Other issuers	5	751	95	851
Equity securities	2,367	631	279	3,277
<b>Total available-for-sale financial assets</b>	8,846	6,669	374	15,889
Financial instruments of segregated funds	5,859	7,456	60	13,375
<b>Total financial assets</b>	\$ 39,156	\$ 24,260	\$ 1,595	\$ 65,011
<b>Financial liabilities</b>				
<b>Financial liabilities held for trading</b>				
Other liabilities				
Commitments related to securities sold short	\$ 8,951	\$ 161	\$ -	\$ 9,112
Other	-	-	452	452
	8,951	161	452	9,564
Derivative financial instruments				
Interest rate contracts	-	1,619	-	1,619
Foreign exchange contracts	-	365	-	365
Other contracts	-	1,693	-	1,693
	-	3,677	-	3,677
<b>Total financial liabilities</b>	\$ 8,951	\$ 3,838	\$ 452	\$ 13,241

During the years ended December 31, 2018 and December 31, 2017, no material transfers attributable to changes in the observability of market data were made between hierarchy levels for instruments measured at fair value.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

### HIERARCHY OF FINANCIAL INSTRUMENTS WHOSE CARRYING AMOUNT DOES NOT EQUAL FAIR VALUE

The carrying amount of certain financial instruments measured at amortized cost does not equal fair value. The following tables present those instruments by hierarchy level.

As at December 31, 2018	Carrying amount	Fair value	Level 1	Level 2	Level 3
<b>Financial assets</b>					
Securities	\$ 1,621	\$ 1,621	\$ -	\$ 1,621	\$ -
Loans	61,837	61,610	-	32,957	28,653
<b>Financial liabilities</b>					
Deposits	58,057	57,842	1,222	56,620	-
Subordinated notes	1,378	1,433	-	1,433	-

As at December 31, 2017	Carrying amount	Fair value	Level 1	Level 2	Level 3
<b>Financial assets</b>					
Loans	\$ 58,684	\$ 58,838	\$ -	\$ 32,337	\$ 26,501
<b>Financial liabilities</b>					
Deposits	52,149	50,182	1,169	49,013	-
Subordinated notes	1,388	1,488	-	1,488	-

### FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3

#### Valuation process for financial instruments categorized within Level 3

The Federation has implemented various key controls and procedures to ensure that financial instruments categorized within Level 3 are appropriately and reliably measured. The financial governance framework provides for independent monitoring and segregation of duties in that respect.

The most significant financial instruments categorized within Level 3 that are held by the Federation are mortgage bonds, equity securities and the financial liability related to a contingent consideration resulting from a price adjustment clause for certain property and casualty insurance contracts acquired.

For mortgage bonds, the Federation developed a list of parameters based on comparable inputs that is reviewed annually and adjusted based on market trends. Tests are performed quarterly to ensure that the rates used by the system are consistent with this list and evolve reasonably.

The Federation measures the majority of equity securities based on brokers' valuations obtained from independent third parties. Data obtained are reviewed and approved by the Federation.

In connection with the acquisition of the Canadian businesses of State Farm Mutual Automobile Insurance Company (State Farm), the Federation recognized a contingent consideration resulting from the price adjustment clause of the agreement. Under such clause, State Farm will compensate the Federation for 95% of the unfavourable development of the provision for claims and adjustment expenses related to the property and casualty insurance contracts transferred as part of the acquisition, while the Federation will give State Farm 90% of the favourable development of such provision.

#### Sensitivity of financial instruments categorized within Level 3

The Federation performs sensitivity analyses to measure the fair value of financial instruments categorized within Level 3. Changing unobservable inputs to one or more reasonably possible alternative assumptions does not significantly change the fair value of financial instruments categorized within Level 3.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

### FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3 (continued)

#### Changes in fair value of financial instruments categorized within Level 3

The following tables present the changes in fair value of financial instruments categorized within Level 3 of the hierarchy, namely financial instruments whose fair value is determined using valuation techniques not based mainly on observable market data.

	Balance as at December 31, 2017	Impact of changes in accounting policies (Note 2)	Balance as at January 1, 2018	Realized gains / losses recognized in profit or loss <sup>(1)</sup>	Unrealized gains / losses recognized in profit or loss <sup>(2)</sup>	Unrealized gains / losses recognized in other comprehensive income <sup>(3)</sup>	Transfers of instruments into (out of) Level 3	Purchases / Issuances / Other	Sales / Settlements / Other	Balance at end of year
<b>For the year ended December 31, 2018</b>										
<b>Financial assets</b>										
<b>Financial assets at fair value through profit or loss</b>										
Securities										
Other securities										
Financial institutions										
Mortgage bonds	\$ 58	\$ -	\$ 58	\$ -	\$ (2)	\$ -	\$ -	\$ -	\$ -	\$ 56
Other issuers										
Hedge funds	4	-	4	-	(3)	-	-	-	-	1
Asset-backed term notes	6	-	6	-	2	-	-	-	(3)	5
Mortgage bonds	857	-	857	-	(26)	-	-	-	(95)	736
Equity securities	236	279	515	-	45	-	-	150	(12)	698
Other assets	-	-	-	-	2	-	-	15	(4)	13
<b>Total financial assets at fair value through profit or loss</b>	<b>1,161</b>	<b>279</b>	<b>1,440</b>	<b>-</b>	<b>18</b>	<b>-</b>	<b>-</b>	<b>165</b>	<b>(114)</b>	<b>1,509</b>
<b>Available-for-sale financial assets</b>										
Securities										
Other securities										
Other issuers										
Mortgage bonds	95	(95)	-	-	-	-	-	-	-	-
Equity securities	279	(279)	-	-	-	-	-	-	-	-
<b>Total available-for-sale financial assets</b>	<b>374</b>	<b>(374)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Financial assets at fair value through other comprehensive income</b>										
Securities										
Other securities										
Other issuers										
Mortgage bonds	-	95	95	-	-	(3)	-	-	(3)	89
Other	-	-	-	-	-	-	-	8	-	8
<b>Total financial assets at fair value through other comprehensive income</b>	<b>-</b>	<b>95</b>	<b>95</b>	<b>-</b>	<b>-</b>	<b>(3)</b>	<b>-</b>	<b>8</b>	<b>(3)</b>	<b>97</b>
Financial instruments of segregated funds	60	-	60	(1)	1	-	-	82	(70)	72
<b>Total financial assets</b>	<b>\$ 1,595</b>	<b>\$ -</b>	<b>\$ 1,595</b>	<b>\$ (1)</b>	<b>\$ 19</b>	<b>\$ (3)</b>	<b>\$ -</b>	<b>\$ 255</b>	<b>\$ (187)</b>	<b>\$ 1,678</b>
<b>Financial liabilities</b>										
<b>Financial liabilities at fair value through profit or loss</b>										
Other liabilities – Other										
Financial liability related to put options	\$ 64	\$ -	\$ 64	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (64)	\$ -
Financial liability related to the contingent consideration	388	-	388	-	208	-	-	-	(277)	319
<b>Total financial liabilities</b>	<b>\$ 452</b>	<b>\$ -</b>	<b>\$ 452</b>	<b>\$ -</b>	<b>\$ 208</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (341)</b>	<b>\$ 319</b>

<sup>(1)</sup> Realized gains or losses on financial assets classified or designated as at fair value through profit or loss are presented under "Net investment income".

<sup>(2)</sup> Unrealized gains or losses on financial assets classified or designated as at fair value through profit or loss are presented under "Net investment income", while unrealized gains or losses on financial liabilities "Classified as at fair value through profit or loss" are recognized under "Net investment income" and "Other income – Other", respectively.

<sup>(3)</sup> Unrealized gains or losses on financial assets "Classified as at fair value through other comprehensive income" are recognized under "Net unrealized losses" on debt securities at fair value through other comprehensive income, while unrealized gains or losses on financial assets "Designated as at fair value through other comprehensive income" are recognized under "Net change in gains and losses on equity securities designated as at fair value through other comprehensive income" in the Consolidated Statements of Comprehensive Income.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

### FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3 (continued)

#### Changes in fair value of financial instruments categorized within Level 3 (continued)

	Balance at beginning of year	Realized gains / losses recognized in profit or loss <sup>(1)</sup>	Unrealized gains / losses recognized in profit or loss <sup>(2)</sup>	Unrealized gains / losses recognized in other comprehensive income <sup>(3)</sup>	Transfers of instruments into (out of) Level 3	Purchases / Issuances / Other	Sales / Settlements / Other	Balance at end of year
For the year ended December 31, 2017								
<b>Financial assets</b>								
<b>Financial assets at fair value through profit or loss</b>								
Securities								
Other securities								
Financial institutions								
Mortgage bonds	\$ 60	\$ -	\$ (2)	\$ -	\$ -	\$ -	\$ -	\$ 58
Other issuers								
Hedge funds	7	-	5	-	-	-	(8)	4
Asset-backed term notes	8	-	1	-	-	-	(3)	6
Mortgage bonds	981	-	(22)	-	-	-	(102)	857
Equity securities	97	(1)	13	-	(7)	172	(38)	236
<b>Total financial assets at fair value through profit or loss</b>	<b>1,153</b>	<b>(1)</b>	<b>(5)</b>	<b>-</b>	<b>(7)</b>	<b>172</b>	<b>(151)</b>	<b>1,161</b>
<b>Available-for-sale financial assets</b>								
Securities								
Other securities								
Other issuers								
Mortgage bonds	101	-	-	(3)	-	-	(3)	95
Equity securities	130	-	3	24	-	130	(8)	279
<b>Total available-for-sale financial assets</b>	<b>231</b>	<b>-</b>	<b>3</b>	<b>21</b>	<b>-</b>	<b>130</b>	<b>(11)</b>	<b>374</b>
Financial instruments of segregated funds	20	-	3	-	(4)	44	(3)	60
<b>Total financial assets</b>	<b>\$ 1,404</b>	<b>\$ (1)</b>	<b>\$ 1</b>	<b>\$ 21</b>	<b>\$ (11)</b>	<b>\$ 346</b>	<b>\$ (165)</b>	<b>\$ 1,595</b>
<b>Financial liabilities</b>								
<b>Financial liabilities held for trading</b>								
Other liabilities - Other								
Financial liability related to put options	\$ 68	\$ -	\$ 7	\$ -	\$ -	\$ -	\$ (11)	\$ 64
Financial liability related to the contingent consideration	364	-	290	-	-	-	(266)	388
<b>Total financial liabilities</b>	<b>\$ 432</b>	<b>\$ -</b>	<b>\$ 297</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (277)</b>	<b>\$ 452</b>

<sup>(1)</sup> Realized gains or losses on financial assets held for trading and designated as at fair value through profit or loss are presented under "Net investment income".

<sup>(2)</sup> Unrealized gains or losses on financial assets held for trading and designated as at fair value through profit or loss are presented under "Net investment income", while unrealized gains or losses on financial liabilities held for trading are recognized under "Net investment income" and "Other income – Other", respectively.

<sup>(3)</sup> Unrealized gains or losses on available-for-sale financial assets are recognized under "Net unrealized gains" on available-for-sale securities in the Consolidated Statements of Comprehensive Income.

## NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

### Valuation techniques and inputs used to measure the fair value of financial instruments categorized within Level 3

The following tables present the main techniques and inputs used to measure the fair value of the significant financial instruments categorized within Level 3.

As at December 31, 2018	Fair value	Main valuation techniques	Unobservable inputs	Input value ranges
<b>Financial assets</b>				
Securities				
Mortgage bonds	\$ 881	Discounted cash flows	Credit spread <sup>(B,C)</sup> Comparable inputs <sup>(B,C)</sup>	0 bp to 300 bp 37 bp to 251 bp
Equity securities	79	Brokers' valuations	Brokers' inputs	- - <sup>(1)</sup>
Other financial assets <sup>(2)</sup>	619	Adjusted net asset value	Adjusted net asset value <sup>(A,C)</sup>	- - <sup>(1)</sup>
<b>Total financial assets</b>	<b>\$ 1,678</b>			
<b>Financial liabilities</b>				
Other liabilities - Other				
Financial liability related to the contingent consideration	319	Actuarial techniques <sup>(3)</sup>	Provision for claims and adjustment expenses <sup>(B)</sup>	- - <sup>(1)</sup>
<b>Total financial liabilities</b>	<b>\$ 319</b>			

As at December 31, 2017	Fair value	Main valuation techniques	Unobservable inputs	Input value ranges
<b>Financial assets</b>				
Securities				
Mortgage bonds	\$ 1,010	Discounted cash flows	Credit spread <sup>(B,C)</sup> Comparable inputs <sup>(B,C)</sup>	0 bp to 300 bp 0 bp to 410 bp
Equity securities	54	Brokers' valuations	Brokers' inputs	- - <sup>(1)</sup>
Other financial assets <sup>(2)</sup>	461	Adjusted net asset value	Adjusted net asset value <sup>(A,C)</sup>	- - <sup>(1)</sup>
<b>Total financial assets</b>	<b>\$ 1,595</b>			
<b>Financial liabilities</b>				
Other liabilities - Other				
Financial liability related to put options	\$ 64	Discounted cash flows	Enterprise value <sup>(A,C)</sup> Discount rate <sup>(B,C)</sup> Put option exercise date <sup>(B,C)</sup>	- 7.5% 6 months to 2 years
Financial liability related to the contingent consideration	388	Actuarial techniques <sup>(3)</sup>	Provision for claims and adjustment expenses <sup>(B)</sup>	- - <sup>(1)</sup>
<b>Total financial liabilities</b>	<b>\$ 452</b>			

<sup>(1)</sup> Due to the nature of these financial instruments, no input value range is presented.

<sup>(2)</sup> Include other financial assets such as financial instruments of segregated funds.

<sup>(3)</sup> The actuarial techniques used to prospectively measure the provision for claims and adjustment expenses are in accordance with Canadian accepted actuarial practices. For more details about such practices, refer to the "Actuarial assumptions" section of Note 15, "Insurance contract liabilities".

<sup>(4)</sup> Due to the wide-ranging operations of the underlying business lines associated with the enterprise value, no input value range is presented.

### Fair value sensitivity to changes in unobservable inputs

<sup>(A)</sup> An increase (decrease) in this unobservable input, taken individually, generally results in an increase (decrease) in fair value.

<sup>(B)</sup> An increase (decrease) in this unobservable input, taken individually, generally results in a decrease (increase) in fair value.

<sup>(C)</sup> There is no predictable relationship between this input and other material unobservable inputs.

## NOTE 5 – OFFSETTING FINANCIAL ASSETS AND LIABILITIES

A financial asset and a financial liability must be offset in the Consolidated Balance Sheets when, and only when, the Federation has a legally enforceable and unconditional right to set off the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously. The Federation has a legally enforceable and unconditional right to set off a financial asset and a financial liability when such right is enforceable in the normal course of business and in the event of default, insolvency or bankruptcy.

Securities borrowed or purchased under reverse repurchase agreements and commitments related to securities lent or sold under repurchase agreements are subject to master netting agreements or similar agreements that do not meet the criteria for offsetting in the Consolidated Balance Sheets as they give a right to set off that is enforceable only in the event of default, insolvency or bankruptcy. However, when such transactions are carried out with clearing houses, the criteria for offsetting in the Consolidated Balance Sheets are met.

In addition, over-the-counter derivatives subject to International Swaps and Derivatives Association's master netting agreements do not meet the criteria for offsetting in the Consolidated Balance Sheets as they also give a right to set off that is enforceable only in the event of default, insolvency or bankruptcy. As part of these transactions, the Federation pledges and receives assets as collateral to manage credit risk in accordance with the terms and conditions of the credit support annex.

Exchange-traded derivatives are also subject to master netting agreements entered into directly with stock exchanges or clearing houses and indirectly through brokers. Master netting agreements entered into directly with stock exchanges and clearing houses meet the criteria for offsetting in the Consolidated Balance Sheets, unlike those entered into indirectly through brokers, as they give a right to set off that is enforceable only in the normal course of business.

Certain amounts receivable from clients, brokers and financial institutions as well as certain amounts payable to clients, brokers and financial institutions are subject to master netting agreements that meet the criteria for offsetting in the Consolidated Balance Sheets.

The following tables present information about financial assets and liabilities that are set off and not set off in the Consolidated Balance Sheets and are subject to a master netting agreement or a similar agreement.

				Associated amounts not set off in the Consolidated Balance Sheets <sup>(1)</sup>		
	Gross recognized amounts	Set off amounts	Net amounts presented in the Consolidated Balance Sheets <sup>(2)</sup>	Financial instruments <sup>(3)</sup>	Financial collateral held / pledged	Residual amounts not set off
As at December 31, 2018						
Financial assets						
Securities borrowed or purchased under reverse repurchase agreements	\$ 14,780	\$ 694	\$ 14,086	\$ 5,485	\$ 8,600	\$ 1
Derivative financial instruments	4,304	-	4,304	1,903	2,203	198
Amounts receivable from clients, brokers and financial institutions and other	48	27	21	2	-	19
Total financial assets	\$ 19,132	\$ 721	\$ 18,411	\$ 7,390	\$ 10,803	\$ 218
Financial liabilities						
Commitments related to securities lent or sold under repurchase agreements	\$ 16,927	\$ 694	\$ 16,233	\$ 5,485	\$ 10,745	\$ 3
Derivative financial instruments	2,028	-	2,028	1,903	69	56
Amounts payable to clients, brokers and financial institutions	56	27	29	2	-	27
Total financial liabilities	\$ 19,011	\$ 721	\$ 18,290	\$ 7,390	\$ 10,814	\$ 86

<sup>(1)</sup> Any over-collateralization is excluded from the table.

<sup>(2)</sup> The difference between the net amounts presented in this table and balances appearing in the Consolidated Balance Sheets represents financial assets and liabilities that are not subject to master netting agreements or similar agreements.

<sup>(3)</sup> Carrying amount of financial assets and liabilities that are subject to a master netting agreement or similar agreement but that do not meet offsetting criteria.

**NOTE 5 – OFFSETTING FINANCIAL ASSETS AND LIABILITIES (continued)**

As at December 31, 2017	Gross recognized amounts	Set off amounts	Net amounts presented in the Consolidated Balance Sheets <sup>(2)</sup>	Associated amounts not set off in the Consolidated Balance Sheets <sup>(1)</sup>		
				Financial instruments <sup>(3)</sup>	Financial collateral held / pledged	Residual amounts not set off
<b>Financial assets</b>						
Securities borrowed or purchased under reverse repurchase agreements	\$ 11,308	\$ 1,931	\$ 9,377	\$ 4,538	\$ 4,839	\$ -
Derivative financial instruments	3,760	-	3,760	1,883	1,848	29
Amounts receivable from clients, brokers and financial institutions and other	33	24	9	5	-	4
<b>Total financial assets</b>	<b>\$ 15,101</b>	<b>\$ 1,955</b>	<b>\$ 13,146</b>	<b>\$ 6,426</b>	<b>\$ 6,687</b>	<b>\$ 33</b>
<b>Financial liabilities</b>						
Commitments related to securities lent or sold under repurchase agreements	\$ 11,993	\$ 1,931	\$ 10,062	\$ 4,538	\$ 5,520	\$ 4
Derivative financial instruments	2,058	-	2,058	1,883	111	64
Amounts payable to clients, brokers and financial institutions	90	24	66	5	-	61
<b>Total financial liabilities</b>	<b>\$ 14,141</b>	<b>\$ 1,955</b>	<b>\$ 12,186</b>	<b>\$ 6,426</b>	<b>\$ 5,631</b>	<b>\$ 129</b>

<sup>(1)</sup> Any over-collateralization is excluded from the table.

<sup>(2)</sup> The difference between the net amounts presented in this table and balances appearing in the Consolidated Balance Sheets represents financial assets and liabilities that are not subject to master netting agreements or similar agreements.

<sup>(3)</sup> Carrying amount of financial assets and liabilities that are subject to a master netting agreement or similar agreement but that do not meet offsetting criteria.

## NOTE 6 – SECURITIES

### MATURITIES OF SECURITIES

The following tables present an analysis of the maturities of the Federation's securities.

	Terms to maturity						Total
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 to 10 years	Over 10 years	No specific maturity	
<b>As at December 31, 2018</b>							
<b>Financial assets</b>							
<b>Financial assets at fair value through profit or loss</b>							
Securities							
Debt securities issued or guaranteed by							
Canadian governmental entities	\$ 2,246	\$ 2,252	\$ 4,590	\$ 1,419	\$ 1,119	\$ -	\$ 11,626
Provincial governmental entities and municipal corporations in Canada	1,970	2,137	1,342	2,500	8,222	-	16,171
School or public corporations in Canada	-	-	1	16	82	-	99
Foreign public administrations	55	-	-	82	54	-	191
Other securities							
Financial institutions	281	294	65	146	102	-	888
Other issuers	189	286	451	411	2,171	-	3,508
Equity securities	-	-	-	2	6	4,423	4,431
<b>Total financial assets at fair value through profit or loss</b>	<b>4,741</b>	<b>4,969</b>	<b>6,449</b>	<b>4,576</b>	<b>11,756</b>	<b>4,423</b>	<b>36,914</b>
<b>Financial assets at fair value through other comprehensive income</b>							
Securities							
Debt securities issued or guaranteed by							
Canadian governmental entities	575	740	1,195	25	10	-	2,545
Provincial governmental entities and municipal corporations in Canada	755	1,427	695	1,370	796	-	5,043
Other securities							
Financial institutions	2,174	342	188	103	3	-	2,810
Other issuers	160	74	206	230	20	-	690
Equity securities	-	-	-	-	-	43	43
<b>Total financial assets at fair value through other comprehensive income</b>	<b>3,664</b>	<b>2,583</b>	<b>2,284</b>	<b>1,728</b>	<b>829</b>	<b>43</b>	<b>11,131</b>
<b>Financial assets at amortized cost</b>							
Securities							
Debt securities issued or guaranteed by							
Provincial governmental entities and municipal corporations in Canada	174	2	3	6	-	-	185
Foreign public administrations	-	-	1	8	18	-	27
Other securities							
Financial institutions	1,281	-	-	-	-	(1)	1,280
Other issuers	129	-	-	-	-	-	129
<b>Total financial assets at amortized cost</b>	<b>1,584</b>	<b>2</b>	<b>4</b>	<b>14</b>	<b>18</b>	<b>(1)</b>	<b>1,621</b>
<b>Total securities</b>	<b>\$ 9,989</b>	<b>\$ 7,554</b>	<b>\$ 8,737</b>	<b>\$ 6,318</b>	<b>\$ 12,603</b>	<b>\$ 4,465</b>	<b>\$ 49,666</b>

## NOTE 6 – SECURITIES (continued)

### MATURITIES OF SECURITIES (continued)

As at December 31, 2017	Terms to maturity						Total
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 to 10 years	Over 10 years	No specific maturity	
<b>Financial assets</b>							
<b>Financial assets at fair value profit or loss</b>							
Securities							
Debt securities issued or guaranteed by							
Canadian governmental entities	\$ 2,403	\$ 1,471	\$ 3,035	\$ 375	\$ 1,583	\$ -	\$ 8,867
Provincial governmental entities and municipal corporations in Canada	1,677	2,251	1,546	2,843	8,091	-	16,408
School or public corporations in Canada	-	-	-	22	86	-	108
Foreign public administrations	81	-	178	27	26	-	312
Other securities							
Financial institutions	293	313	55	113	113	-	887
Other issuers	231	178	349	489	2,113	4	3,364
Equity securities	-	-	-	-	-	1,708	1,708
<b>Total financial assets at fair value through profit or loss</b>	<b>4,685</b>	<b>4,213</b>	<b>5,163</b>	<b>3,869</b>	<b>12,012</b>	<b>1,712</b>	<b>31,654</b>
<b>Available-for-sale financial assets</b>							
Securities							
Debt securities issued or guaranteed by							
Canadian governmental entities	227	822	1,273	72	-	-	2,394
Provincial governmental entities and municipal corporations in Canada	1,402	1,265	1,060	1,294	794	-	5,815
Foreign public administrations	9	-	1	10	15	-	35
Other securities							
Financial institutions	2,347	205	222	92	12	-	2,878
Other issuers	269	70	138	361	13	-	851
Equity securities	-	-	-	-	6	3,271	3,277
<b>Total available-for-sale financial assets</b>	<b>4,254</b>	<b>2,362</b>	<b>2,694</b>	<b>1,829</b>	<b>840</b>	<b>3,271</b>	<b>15,250</b>
<b>Total securities</b>	<b>\$ 8,939</b>	<b>\$ 6,575</b>	<b>\$ 7,857</b>	<b>\$ 5,698</b>	<b>\$ 12,852</b>	<b>\$ 4,983</b>	<b>\$ 46,904</b>

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES

The information presented in the following tables has been prepared in accordance with IFRS 9 as at December 31, 2018 and in accordance with IAS 39 as at December 31, 2017. For more information, see Note 2, "Basis of presentation and significant accounting policies".

### EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS

At each reporting date, loans and off-balance sheet items are classified based on their credit quality using their 12-month PD adjusted to take into consideration relevant forward-looking information over their lifetime. This is the PD used to determine whether credit risk has significantly increased since initial recognition or identify financial instruments in regulatory default.

The following tables present PD tranches in relation with risk levels for loans and off-balance sheet items.

#### Residential mortgages, consumer, credit card and other personal loans

Risk levels	PD tranches
Excellent	0.00% to 0.08%
Very low	0.09% to 0.33%
Low	0.34% to 2.09%
Moderate	2.10% to 7.32%
High	7.33% to 99.99%
Default	100.00%

#### Business and government

Risk levels	PD tranches
Investment grade	0.00% to 0.36%
Non-investment grade	0.37% to 4.50%
Under watch	4.51% to 99.99%
Default	100.00%

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

### EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS *(continued)*

The following tables present the gross carrying amount of loans and the exposure amount for off-balance sheet items for which the Federation estimates a loss allowance for expected credit losses, according to credit quality and the impairment model stage in which they are classified.

#### Loans

As at December 31, 2018	Non-credit impaired		Credit-impaired <sup>(1)</sup>	Total
	Stage 1	Stage 2	Stage 3	
<b>Residential mortgages</b>				
Excellent	\$ 626	\$ -	\$ -	\$ 626
Very low	2,120	-	-	2,120
Low	1,663	9	-	1,672
Moderate	82	73	-	155
High	8	32	-	40
Default	-	3	10	13
<b>Total gross residential mortgages</b>	<b>\$ 4,499</b>	<b>\$ 117</b>	<b>\$ 10</b>	<b>\$ 4,626</b>
Allowance for credit losses	(4)	(1)	(5)	(10)
<b>Total net residential mortgages</b>	<b>\$ 4,495</b>	<b>\$ 116</b>	<b>\$ 5</b>	<b>\$ 4,616</b>
<b>Consumer, credit card and other personal loans</b>				
Excellent	\$ 1,529	\$ -	\$ -	\$ 1,529
Very low	3,352	-	-	3,352
Low	8,139	92	-	8,231
Moderate	3,522	1,320	-	4,842
High	33	1,523	-	1,556
Default	-	-	200	200
<b>Total gross consumer, credit card and other personal loans</b>	<b>\$ 16,575</b>	<b>\$ 2,935</b>	<b>\$ 200</b>	<b>\$ 19,710</b>
Allowance for credit losses	(102)	(249)	(110)	(461)
<b>Total net consumer, credit card and other personal loans</b>	<b>\$ 16,473</b>	<b>\$ 2,686</b>	<b>\$ 90</b>	<b>\$ 19,249</b>
<b>Business and government loans<sup>(2)</sup></b>				
Investment grade	\$ 33,588	\$ -	\$ -	\$ 33,588
Non-investment grade	3,753	353	-	4,106
Under watch	65	255	-	320
Default	-	-	138	138
<b>Total gross business and government loans</b>	<b>\$ 37,406</b>	<b>\$ 608</b>	<b>\$ 138</b>	<b>\$ 38,152</b>
Allowance for credit losses	(9)	(5)	(6)	(20)
<b>Total net business and government loans</b>	<b>\$ 37,397</b>	<b>\$ 603</b>	<b>\$ 132</b>	<b>\$ 38,132</b>

<sup>(1)</sup> As at December 31, 2018, 43.6% of credit-impaired loans were fully or partially secured, generally by immovable, movable or other security. Additional information on collateral held as security and other credit enhancements is presented in the "Credit Risk Mitigation" section of the Management's Discussion and Analysis.

<sup>(2)</sup> Including clients' liability under acceptances.

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

### EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS *(continued)*

#### Off-balance sheet items<sup>(1)</sup>

As at December 31, 2018	Non-credit impaired		Credit-impaired	Total
	Stage 1	Stage 2	Stage 3	
<b>Residential mortgages, consumer, credit card and other personal loans</b>				
Excellent	\$ 12,121	\$ 5	\$ -	\$ 12,126
Very low	18,338	1	-	18,339
Low	7,221	121	-	7,342
Moderate	3,318	1,362	-	4,680
High	16	662	-	678
Default	-	-	23	23
<b>Total gross off-balance sheet items</b>	<b>\$ 41,014</b>	<b>\$ 2,151</b>	<b>\$ 23</b>	<b>\$ 43,188</b>
Allowance for credit losses	(25)	(8)	-	(33)
<b>Total net off-balance sheet items</b>	<b>\$ 40,989</b>	<b>\$ 2,143</b>	<b>\$ 23</b>	<b>\$ 43,155</b>
<b>Business and government</b>				
Investment grade	\$ 61,224	\$ -	\$ -	\$ 61,224
Non-investment grade	3,387	384	-	3,771
Under watch	18	54	-	72
Default	-	-	8	8
<b>Total gross off-balance sheet items</b>	<b>\$ 64,629</b>	<b>\$ 438</b>	<b>\$ 8</b>	<b>\$ 65,075</b>
Allowance for credit losses	(2)	(2)	-	(4)
<b>Total net off-balance sheet items</b>	<b>\$ 64,627</b>	<b>\$ 436</b>	<b>\$ 8</b>	<b>\$ 65,071</b>

<sup>(1)</sup> Loan commitments for which the Federation estimates a loss allowance for expected credit losses comprise credit commitments and documentary letters of credit, while financial guarantees for which it estimates a loss allowance for expected credit losses comprise guarantees and standby letters of credit.

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

### ALLOWANCE FOR CREDIT LOSSES

The following table presents the changes in the balance of the loss allowance for expected credit losses on loans.

	Non-credit impaired		Credit-impaired	Allowance for credit losses
	Stage 1	Stage 2	Stage 3	
<b>For the year ended December 31, 2018</b>				
<b>Residential mortgages</b>				
<b>Balance as at January 1, 2018</b>	\$ 4	\$ 1	\$ 4	\$ 9
Provision for credit losses	-	-	-	-
Transfers to <sup>(1)</sup> :				
Stage 1	-	-	-	-
Stage 2	-	-	-	-
Stage 3	-	-	-	-
Net remeasurement due to transfers <sup>(2)</sup>	-	-	-	-
Changes in model inputs <sup>(3)</sup>	-	-	-	-
New originations or acquisitions <sup>(4)</sup>	-	-	-	-
Derecognition and maturities <sup>(5)</sup>	-	-	-	-
Net drawdowns (repayments) <sup>(6)</sup>	-	-	-	-
Write-offs and recoveries	-	-	-	-
<b>Balance as at December 31, 2018</b>	\$ 4	\$ 1	\$ 5	\$ 10
<b>Consumer, credit card and other personal loans<sup>(7)</sup></b>				
<b>Balance as at January 1, 2018</b>	\$ 96	\$ 304	\$ 94	\$ 494
Provision for credit losses	-	-	-	-
Transfers to <sup>(1)</sup> :				
Stage 1	284	(271)	(13)	-
Stage 2	(43)	75	(32)	-
Stage 3	(1)	(31)	32	-
Net remeasurement due to transfers <sup>(2)</sup>	(139)	68	115	44
Changes in model inputs <sup>(3)</sup>	(96)	149	287	340
New originations or acquisitions <sup>(4)</sup>	86	185	-	271
Derecognition and maturities <sup>(5)</sup>	(40)	(207)	(175)	(422)
Net drawdowns (repayments) <sup>(6)</sup>	(19)	(13)	88	56
Other	1	-	-	1
Write-offs and recoveries	33	(45)	302	290
<b>Balance as at December 31, 2018</b>	\$ 129	\$ 259	\$ 110	\$ 498
<b>Business and government</b>				
<b>Balance as at January 1, 2018</b>	\$ 7	\$ 9	\$ 8	\$ 24
Provision for credit losses	-	-	-	-
Transfers to <sup>(1)</sup> :				
Stage 1	7	(7)	-	-
Stage 2	(1)	2	(1)	-
Stage 3	-	-	-	-
Net remeasurement due to transfers <sup>(2)</sup>	(4)	1	2	(1)
Changes in model inputs <sup>(3)</sup>	(3)	4	1	2
New originations or acquisitions <sup>(4)</sup>	4	-	-	4
Derecognition and maturities <sup>(5)</sup>	(2)	(1)	(3)	(6)
Net drawdowns (repayments) <sup>(6)</sup>	1	-	(1)	-
Other	-	(3)	1	(2)
Write-offs and recoveries	2	(4)	(1)	(3)
<b>Balance as at December 31, 2018</b>	\$ 9	\$ 5	\$ 6	\$ 20
<b>Total balances as at December 31, 2018</b>	\$ 142	\$ 265	\$ 121	\$ 528
<b>Composed of:</b>				
Loans	\$ 115	\$ 255	\$ 121	\$ 491
Off-balance sheet items <sup>(8)</sup>	27	10	-	37

<sup>(1)</sup> Represent transfers between stages before the remeasurement of expected credit losses.

<sup>(2)</sup> Represent the remeasurement of the loss allowance for expected credit losses resulting from transfers between stages.

<sup>(3)</sup> Represent the change in the allowance resulting from changes in credit risk parameters and other model inputs.

<sup>(4)</sup> Represent the increase in the allowance for new originations or acquisitions during the year, including loans that were derecognized and for which a new asset was recognized following a modification of terms.

<sup>(5)</sup> Represent mainly the decrease in the allowance for fully repaid loans, including loans that were derecognized and for which a new asset was recognized following a modification of terms.

<sup>(6)</sup> Represent changes in the allowance attributable to drawdowns and repayments on outstanding loans.

<sup>(7)</sup> For purposes of this table, the entire allowance for credit losses on off-balance sheet items is presented in the "Consumer, credit card and other personal loans" section the allowance amounts and changes therein attributable to other off-balance sheet item categories are not material.

<sup>(8)</sup> The allowance for credit losses on off-balance sheet items is presented under "Other liabilities – Other" in the Consolidated Balance Sheets.

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES (*continued*)

### KEY DATA AND ASSUMPTIONS

Determining the loss allowance for expected credit losses under IFRS 9 is based on a set of assumptions and methodologies specific to credit risk and changes in economic conditions. Significant judgment must therefore be exercised to determine the loss allowance for expected credit losses. The main items requiring significant judgment that affected its measurement as at December 31, 2018 are the following:

- Changes in the borrowers' credit risk rating (or PD)
- Incorporation of forward-looking information
- Estimated life of revolving credit facilities

#### Changes in the borrowers' credit risk rating or probability of default

The borrowers' credit risk rating is the foundation of the credit risk assessment model. The rating of a borrower is directly related to its estimated PD. Many variables are taken into consideration in credit risk assessment models. For more information about these models, see section 4.2, "Risk Management", of the Management's Discussion and Analysis. Changes in the borrowers' credit risk rating have an impact on determining significant increases in credit risk, as this is mainly based on the change in the borrower's PD, and measuring the loss allowance for expected credit losses.

Changes in the borrowers' credit risk rating may increase or decrease the loss allowance for expected credit losses. Generally, a deterioration in a borrower's credit risk rating gives rise to an increase in the allowance, while an improvement results in a decrease in the allowance.

#### Incorporation of forward-looking information

The Federation uses three different scenarios to determine the loss allowance for expected credit losses, namely a base scenario, an upside scenario and a downside scenario. Projections for each scenario are provided for a four-year horizon. The macroeconomic variables projected under each scenario and the related probability of occurrence have a significant impact on determining significant increases in credit risk and measuring the loss allowance for expected credit losses. The models vary depending on the portfolios and include one or several of the main variables presented in the table below. The macroeconomic variable projection and the determination of the probabilities of occurrence are reviewed quarterly.

The incorporation of forward-looking information may increase or decrease the loss allowance for expected credit losses. Generally, an improvement in the outlook will give rise to a decrease in the allowance, while a deterioration will result in an increase in the allowance.

As at December 31, 2018, the macroeconomic scenarios selected for calculating the loss allowance for expected credit losses include the following value ranges over the projection horizon for the most significant variables for credit risk parameters:

	2018					
	Base scenario		Upside scenario		Downside scenario	
	Next 12 months	Remaining forecast period	Next 12 months	Remaining forecast period	Next 12 months	Remaining forecast period
<b>Macroeconomic variables<sup>(1)</sup></b>						
Gross domestic product (annualized change)	2.1%	1.0%	2.9%	1.7%	0.1%	0.9%
Unemployment rate (average)	5.1%	4.8%	4.9%	3.9%	6.3%	7.1%
Consumer Price Index (annualized change)	2.2%	1.0%	2.9%	2.6%	1.2%	0.7%
Housing prices (annualized change)	0.8%	1.2%	4.0%	2.9%	(2.7)%	0.1%
Corporate credit spread <sup>(2)</sup> (average)	109 bp	128 bp	98 bp	81 bp	141 bp	166 bp
S&P/TSX stock index <sup>(2)</sup> (annualized change)	9.1%	2.1%	10.9%	8.7%	(11.5)%	4.8%

<sup>(1)</sup> All macroeconomic variables relate to the Quebec economy, unless otherwise noted.

<sup>(2)</sup> Macroeconomic variables related to the Canadian economy.

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES (*continued*)

### Estimated life of revolving credit facilities

To determine the life of revolving credit facilities, the Federation determines the period over which there is exposure to credit risk but for which expected credit losses would not be mitigated by normal credit risk management actions, and considers the following:

- the period over which it was exposed to credit risk on similar financial instruments;
- the length of time for defaults to occur on similar financial instruments following a significant increase in credit risk;
- the credit risk management actions that it expects to take once the credit risk on the financial instruments has increased.

The determination of the estimated life of revolving credit facilities has a significant impact on estimating the loss allowance for expected credit losses, mainly for revolving credit facilities in Stage 2 of the impairment model. Generally, an increase in the estimated life of revolving credit facilities gives rise to an increase in expected credit losses.

### SENSITIVITY ANALYSIS OF THE ALLOWANCE FOR CREDIT LOSSES ON NON-CREDIT IMPAIRED LOANS

#### Scenarios

The amount of the loss allowance for expected credit losses depends on the probability of occurrence associated with each scenario. The following table compares the allowance for credit losses on non-credit impaired loans and off-balance sheet items as at December 31, 2018, which takes into account the probability weighting for the three scenarios, with the allowance for credit losses that would have been obtained if a weighting of 100% had been assigned to each scenario individually.

	Allowance for credit losses on non-credit impaired loans and off-balance sheet items
Under IFRS 9	\$ 407
<b>Weighting of 100% assigned to the scenario</b>	
Base	\$ 394
Upside	374
Downside	448

#### Transfers between stages

The following table compares the allowance for credit losses on non-credit impaired loans and off-balance sheet items as at December 31, 2018 with the allowance for credit losses that would have been obtained if all non-credit impaired loans had been included in Stage 1 of the impairment model.

	Allowance for credit losses on non-credit impaired loans and off-balance sheet items
Under IFRS 9	\$ 407
If all non-credit impaired loans and off-balance sheet items had been included in Stage 1	\$ 318

## NOTE 7 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

The comparative information presented in the following tables has been prepared in accordance with IAS 39.

### LOANS, CREDIT-IMPAIRED LOANS<sup>(1)</sup> AND ALLOWANCE FOR CREDIT LOSSES

The following table presents the credit quality of loans.

As at December 31, 2017 <sup>(1)</sup>	Gross loans neither past due nor credit-impaired	Gross loans past due but not credit-impaired	Gross credit-impaired loans	Individual allowances	Collective allowance <sup>(2)</sup>	Net loans
Residential mortgages	\$ 4,260	\$ 55	\$ 8	\$ 5	\$ 2	\$ 4,316
Consumer, credit card and other personal loans	16,764	711	72	-	136	17,411
Business and government	36,986	22	4	4	51	36,957
	\$ 58,010	\$ 788	\$ 84	\$ 9	\$ 189	\$ 58,684

<sup>(1)</sup> Following the adoption of IFRS 9 as at January 1, 2018, all loans included in Stage 3 of the impairment model are considered credit-impaired. Under IAS 39, the criteria applied to determine whether a loan is credit-impaired were different.

<sup>(2)</sup> Includes the collective allowance on credit-impaired loans of \$23 million.

### GROSS LOANS PAST DUE BUT NOT CREDIT-IMPAIRED

The following table presents the aging of gross loans that are past due but not credit-impaired.

As at December 31, 2017	1 to 29 days	30 to 59 days	60 to 89 days	90 days or more	Total
Residential mortgages	\$ 43	\$ 4	\$ -	\$ 8	\$ 55
Consumer, credit card and other personal loans	559	104	48	-	711
Business and government	21	1	-	-	22
	\$ 623	\$ 109	\$ 48	\$ 8	\$ 788

### ALLOWANCE FOR CREDIT LOSSES

The following table presents the changes in the allowance for credit losses for the year ended December 31, 2017.

	Residential mortgages	Consumer, credit card and other personal loans	Business and government	Total
<b>Balance at beginning of year</b>	\$ 3	\$ 148	\$ 87	\$ 238
Provision for credit losses	4	281	(7)	278
Write-offs and recoveries	-	(278)	-	(278)
<b>Balance at end of year</b>	\$ 7	\$ 151	\$ 80	\$ 238
<b>Composed of:</b>				
Loans	\$ 7	\$ 137	\$ 54	\$ 198
Off-balance sheet items <sup>(1)</sup>	-	14	26	40

<sup>(1)</sup> The allowance for credit losses on off-balance sheet items is presented under "Other liabilities – Other" in the Consolidated Balance Sheets.

## NOTE 8 – DERECOGNITION OF FINANCIAL ASSETS

### FINANCIAL ASSETS TRANSFERRED BUT NOT DERECOGNIZED

#### Loan securitization

As part of Desjardins Group's liquidity and capital management strategy, the Federation participates in the National Housing Act (NHA) Mortgage-Backed Securities Program. Under this program, the Federation acquires interests in securitized mortgage loans from Desjardins Group member caisses. The residential mortgage loans guaranteed by Canada Mortgage and Housing Corporation (CMHC) are bundled by the Federation into mortgage-backed securities (NHA MBSs) and they are then either transferred to the Canada Housing Trust (CHT) or legally held by the Federation. The acquired interests in securitized mortgage loans do not meet the recognition criteria as member caisses retain substantially all the risks, including prepayment, interest rate and credit risks, and the rewards related to these securities, namely the cash flows associated with the assets. Furthermore, the Federation treats any transfers as collateralized financing transactions and recognizes a liability in that respect. Where applicable, this liability, which is equal to the consideration received for the sale of NHA MBSs that do not meet the derecognition criteria, is presented under "Deposits – Business and government" in the Consolidated Balance Sheets. The CHT funds these purchases by issuing Canada Mortgage Bonds (CMBs) to investors. The legal guarantee of third parties holding CMBs is limited to the transferred assets.

The terms and conditions of the program giving rise to the transfer of NHA MBSs to the CHT require that interest rate swaps be entered into by the CHT and the Federation to allow the monthly receipt of all cash flows related to the mortgage loans underlying the NHA MBSs. The Federation pays the CHT an amount corresponding to the interest payable to the holders of CMBs, the difference between these amounts being considered as excess interest margin. As part of these swaps, the Federation must also create a separate account for reinvestment purposes (principal reinvestment account) for any principal payment received on mortgage loans in order to meet the obligations related to the repayment of CMBs at maturity.

Under this same program, the Federation bundles some of its residential mortgage loans guaranteed by CMHC into NHA MBSs and transfers them to a related party. As part of these transactions, the Federation retains substantially all the risks, including prepayment, interest rate and credit risks, and the rewards related to these securities, namely the cash flows associated with the assets. As a result, these loans continue to be recognized in the Consolidated Balance Sheets. Furthermore, the Federation treats the transfers as collateralized financing transactions and recognizes a liability in that respect. This liability, which is equal to the consideration received for the sale of NHA MBSs that do not meet the derecognition criteria, is presented under "Deposits – Business and government" in the Consolidated Balance Sheets.

No material loss is expected on the mortgage loans as they are guaranteed by CMHC. Income related to securitization transactions is recognized under "Interest income – Securities" and "Interest income – Loans".

#### Securities lent or sold under repurchase agreements

As part of transactions involving securities lent or sold under repurchase agreements, the Federation transfers financial assets under terms and conditions providing for their future repurchase. These financial assets remain recognized in the Consolidated Balance Sheets as the Federation retains substantially all the risks and rewards related to these assets.

The following table presents the carrying amount and the fair value of financial assets transferred by the Federation but not derecognized as well as the related liabilities recognized in the Consolidated Balance Sheets.

	As at December 31, 2018		As at December 31, 2017	
	Carrying amount	Fair value	Carrying amount	Fair value
<b>Financial assets transferred but not derecognized</b>				
Financial assets transferred through securitization transactions	\$ 42	\$ 42	\$ 34	\$ 34
Securities sold under repurchase agreements	9,656	9,656	6,537	6,537
Securities lent	4	4	2	2
	<b>\$ 9,702</b>	<b>\$ 9,702</b>	<b>\$ 6,573</b>	<b>\$ 6,573</b>
<b>Related liabilities</b>	<b>\$ 9,706</b>	<b>\$ 9,706</b>	<b>\$ 6,473</b>	<b>\$ 6,473</b>

## NOTE 9 – SEGREGATED FUNDS

### Segregated fund net assets

The following table presents the carrying amount of segregated fund net assets.

	As at December 31, 2018	As at December 31, 2017
Investments		
Bonds	\$ 584	\$ 541
Shares and mutual fund units	12,616	12,789
Money market securities	38	45
Securities borrowed or purchased under reverse repurchase agreements	31	30
Other assets	65	74
Commitments related to securities lent or sold under repurchase agreements	(9)	(6)
Liabilities	(60)	(63)
<b>Net assets held for segregated fund contract holders</b>	<b>\$ 13,265</b>	<b>\$ 13,410</b>
Assets held for the insurer	(31)	(31)
<b>Total segregated fund net assets<sup>(1)</sup></b>	<b>\$ 13,234</b>	<b>\$ 13,379</b>

<sup>(1)</sup> The difference between the segregated fund net assets and net liabilities represents the elimination of balances between the segregated funds and the various companies included in the Federation's scope of consolidation. These eliminations amounted to \$22 million as at December 31, 2018 (\$25 million as at December 31, 2017).

### Fair value of financial instruments

Segregated fund net assets include financial instruments recognized at fair value. The Federation classifies these instruments using a three-level hierarchy that reflects the significance of the inputs used to measure them. A description of the three hierarchy levels and guidance on inputs used in fair value measurements are presented in Note 4, "Fair value of financial instruments".

The carrying amount of certain financial instruments that mature in the next 12 months is a reasonable approximation of their fair value. These financial instruments include the following items: "Securities borrowed or purchased under reverse repurchase agreements", "Other assets", "Commitments related to securities lent or sold under repurchase agreements" and "Liabilities".

The following tables present the financial instruments included in segregated fund net assets and recognized at fair value.

As at December 31, 2018	Level 1	Level 2	Level 3	Total
Investments				
Bonds	\$ 304	\$ 280	\$ -	\$ 584
Shares and mutual fund units	5,221	7,323	72	12,616
Money market securities	31	7	-	38
<b>Total financial instruments recognized at fair value</b>	<b>\$ 5,556</b>	<b>\$ 7,610</b>	<b>\$ 72</b>	<b>\$ 13,238</b>

As at December 31, 2017	Level 1	Level 2	Level 3	Total
Investments				
Bonds	\$ 305	\$ 236	\$ -	\$ 541
Shares and mutual fund units	5,518	7,211	60	12,789
Money market securities	36	9	-	45
<b>Total financial instruments recognized at fair value</b>	<b>\$ 5,859</b>	<b>\$ 7,456</b>	<b>\$ 60</b>	<b>\$ 13,375</b>

During the years ended December 31, 2018 and 2017, no transfers attributable to changes in the observability of market data were made between hierarchy levels for instruments recognized at fair value.

## NOTE 9 – SEGREGATED FUNDS *(continued)*

### Derecognition of financial assets

As part of transactions involving securities lent or sold under repurchase agreements, the segregated funds transfer financial assets under terms and conditions providing for their future repurchase. These assets remain recognized in the Consolidated Balance Sheets as the segregated funds retain substantially all the risks and rewards related to these assets.

As at December 31, 2018 and 2017, the carrying amount and the fair value of such transferred financial assets and related liabilities recognized in the Consolidated Balance Sheets were \$9 million and \$6 million, respectively.

### Financial assets pledged and held as collateral

The carrying amount of financial assets pledged as collateral for liabilities or contingent liabilities in the normal course of the segregated funds' operations amounted to \$9 million as at December 31, 2018 (\$6 million as at December 31, 2017). The fair value of the financial assets held as collateral that the segregated funds are permitted to sell or repledge in the absence of default totalled \$1 million (\$5 million as at December 31, 2017). No financial assets held as collateral had been sold or repledged in 2018 and 2017. These financial assets were received as collateral in transactions involving securities borrowed or purchased under reverse repurchase agreements.

### Financial instrument risks

The Federation is not exposed to the risks related to financial instruments included in the assets held for segregated fund contract holders since such holders assume the risks and obtain the benefits arising from these financial instruments.

### Segregated fund net liabilities

The following table presents the changes in segregated fund net liabilities.

	As at December 31, 2018	As at December 31, 2017
<b>Balance at beginning of year – Net liabilities to segregated fund contract holders</b>	<b>\$ 13,386</b>	<b>\$ 11,987</b>
<b>Additions</b>		
Amounts received from contract holders	2,025	1,840
Net investment income (loss)	(276)	1,183
	<b>1,749</b>	<b>3,023</b>
<b>Deductions</b>		
Withdrawals and redemptions	1,747	1,479
Management fees	145	146
	<b>1,892</b>	<b>1,625</b>
<b>Balance at end of year – Net liabilities to segregated fund contract holders</b>	<b>\$ 13,243</b>	<b>\$ 13,385</b>
Liabilities to the insurer	(31)	(31)
<b>Total segregated fund net liabilities<sup>(1)</sup></b>	<b>\$ 13,212</b>	<b>\$ 13,354</b>

<sup>(1)</sup> The difference between the segregated fund net assets and net liabilities represents the elimination of balances between the segregated funds and the various companies included in the Federation's scope of consolidation. These eliminations amounted to \$22 million as at December 31, 2018 (\$25 million as at December 31, 2017).

## NOTE 10 – PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY

The following tables present the changes in property, plant and equipment and investment property.

	PROPERTY, PLANT AND EQUIPMENT						INVESTMENT PROPERTY		
	Land	Buildings	Computer equipment	Furniture, fixtures and other	Leasehold improvements	Total	Land	Buildings	Total
<b>Cost</b>									
As at December 31, 2016	\$ 33	\$ 586	\$ 330	\$ 184	\$ 267	\$ 1,400	\$ 186	\$ 842	\$ 1,028
Additions	-	17	54	22	57	150	-	36	36
Disposals	(1)	(3)	(72)	(48)	(43)	(167)	(6)	-	(6)
Other	-	-	-	-	(2)	(2)	1	4	5
As at December 31, 2017	\$ 32	\$ 600	\$ 312	\$ 158	\$ 279	\$ 1,381	\$ 181	\$ 882	\$ 1,063
Additions	-	18	51	28	42	139	45	128	173
Disposals	-	-	(22)	(36)	(21)	(79)	(11)	(2)	(13)
Other	-	(4)	-	2	(1)	(3)	-	(2)	(2)
<b>As at December 31, 2018</b>	<b>\$ 32</b>	<b>\$ 614</b>	<b>\$ 341</b>	<b>\$ 152</b>	<b>\$ 299</b>	<b>\$ 1,438</b>	<b>\$ 215</b>	<b>\$ 1,006</b>	<b>\$ 1,221</b>

	PROPERTY, PLANT AND EQUIPMENT						INVESTMENT PROPERTY		
	Land	Buildings	Computer equipment	Furniture, fixtures and other	Leasehold improvements	Total	Land	Buildings	Total
<b>Accumulated depreciation</b>									
As at December 31, 2016	\$ -	\$ 159	\$ 236	\$ 102	\$ 134	\$ 631	\$ 4	\$ 218	\$ 222
Depreciation	-	20	49	14	18	101	-	29	29
Disposals	-	(2)	(65)	(38)	(30)	(135)	(4)	-	(4)
Other	-	1	1	3	(1)	4	-	(1)	(1)
As at December 31, 2017	\$ -	\$ 178	\$ 221	\$ 81	\$ 121	\$ 601	\$ -	\$ 246	\$ 246
Depreciation	-	19	44	14	18	95	-	34	34
Disposals	-	-	(21)	(31)	(20)	(72)	-	-	-
Other	-	-	-	2	1	3	-	(2)	(2)
<b>As at December 31, 2018</b>	<b>\$ -</b>	<b>\$ 197</b>	<b>\$ 244</b>	<b>\$ 66</b>	<b>\$ 120</b>	<b>\$ 627</b>	<b>\$ -</b>	<b>\$ 278</b>	<b>\$ 278</b>

	PROPERTY, PLANT AND EQUIPMENT						INVESTMENT PROPERTY		
	Land	Buildings	Computer equipment	Furniture, fixtures and other	Leasehold improvements	Total	Land	Buildings	Total
<b>Net carrying amount</b>									
<b>As at December 31, 2018</b>	<b>\$ 32</b>	<b>\$ 417</b>	<b>\$ 97</b>	<b>\$ 86</b>	<b>\$ 179</b>	<b>\$ 811</b>	<b>\$ 215</b>	<b>\$ 728</b>	<b>\$ 943</b>
As at December 31, 2017	\$ 32	\$ 422	\$ 91	\$ 77	\$ 158	\$ 780	\$ 181	\$ 636	\$ 817

For the years ended December 31, 2018 and 2017, the Federation had no amounts representing costs related to buildings under construction. In addition, as at December 31, 2018 and 2017, the Federation had no commitments related to the acquisition of these buildings.

As at December 31, 2018, the fair value of investment property was \$1,754 million (\$1,502 million as at December 31, 2017). Investment property is categorized within Level 3 of the fair value hierarchy as defined in Note 4, "Fair value of financial instruments", as it is measured using techniques that are not primarily based on observable market inputs. The fair value of investment property is determined annually by management, mainly by using the work of independent real estate appraisers with recognized and relevant professional qualifications and any other significant information that may be deemed relevant. These appraisers use a range of valuation methods, including normalized net income direct discounting and cash flow discounting. These techniques, which are based on observable and unobservable inputs, involve estimating capitalization rates and adjusted net operating income, in the case of the normalized net income direct discounting method, and estimating discount and capitalization rates and applicable future cash flows, in the case of the cash flow discounting method.

For the year ended December 31, 2018, rental income from investment property amounted to \$155 million (\$157 million in 2017). Amounts recognized in profit or loss for operating expenses related to investment property that generated rental income during the year totalled \$113 million (\$103 million in 2017), while no amount has been recognized for those that did not generate rental income. These amounts are presented under "Net investment income" in the Consolidated Statements of Income.

## NOTE 11 – GOODWILL AND INTANGIBLE ASSETS

### GOODWILL

The following table presents goodwill allocated to CGUs and groups of CGUs.

	Property and Casualty Insurance segment	Wealth Management and Life and Health Insurance segment	Total
<b>Cost</b>			
As at December 31, 2016	\$ 415	\$ 56	\$ 471
Disposals <sup>(1)</sup> / Retirements <sup>(2)</sup>	(315)	(35)	(350)
As at December 31, 2017	\$ 100	\$ 21	\$ 121
<b>As at December 31, 2018</b>	<b>\$ 100</b>	<b>\$ 21</b>	<b>\$ 121</b>

<sup>(1)</sup> For more information, see Note 20, "Significant transactions".

<sup>(2)</sup> As at December 31, 2017, goodwill attributable to Qtrade Canada Inc., which was previously presented in the Wealth Management and Life and Health Insurance segment, was presented under "Assets of the disposal group held to be transferred". On April 1, 2018, this subsidiary was part of the transaction that resulted in the creation of Aviso Wealth, as mentioned in Note 20, "Significant transactions".

The Property and Casualty Insurance segment includes Desjardins General Insurance Group Inc. The Wealth Management and Life and Health Insurance segment includes notably Desjardins Financial Security Life Assurance Company, Desjardins Securities Inc. and, Desjardins Financial Corporation Inc.

Test results show that the recoverable amount of CGUs and groups of CGUs represented by each of these segments exceeds its carrying amount and, consequently, no goodwill impairment losses have been recognized for the year ended December 31, 2018 and prior years. The recoverable amount of CGUs and groups of CGUs has been determined based on a calculation of value in use, using cash flow projections based on the budget and financial plan approved by the Board of Directors and covering a four-year period. The key assumptions used in the budget and financial plan are based on past performance and management's expectations of the evolution of the market.

### INTANGIBLE ASSETS

The following tables show changes in intangible assets.

	Software	Client relationships	Other <sup>(1)</sup>	Total
<b>Cost</b>				
As at December 31, 2016	\$ 846	\$ 197	\$ 229	\$ 1,272
Acquisitions / Additions	142	-	4	146
Disposals <sup>(2)</sup> / Retirements <sup>(3)</sup>	(158)	(178)	(108)	(444)
Other	(2)	-	(1)	(3)
As at December 31, 2017	\$ 828	\$ 19	\$ 124	\$ 971
Acquisitions / Additions	96	-	1	97
Disposals / Retirements	(108)	-	(1)	(109)
Other	(6)	-	-	(6)
<b>As at December 31, 2018</b>	<b>\$ 810</b>	<b>\$ 19</b>	<b>\$ 124</b>	<b>\$ 953</b>

	Software	Client relationships	Other <sup>(1)</sup>	Total
<b>Accumulated amortization</b>				
As at December 31, 2016	\$ 476	\$ 61	\$ 45	\$ 582
Amortization	82	5	7	94
Disposals <sup>(2)</sup> / Retirements <sup>(3)</sup>	(107)	(59)	(12)	(178)
Other	7	-	-	7
As at December 31, 2017	\$ 458	\$ 7	\$ 40	\$ 505
Amortization	82	2	5	89
Disposals / Retirements	(35)	-	(1)	(36)
Other	6	-	-	6
<b>As at December 31, 2018</b>	<b>\$ 511</b>	<b>\$ 9</b>	<b>\$ 44</b>	<b>\$ 564</b>

	Software	Client relationships	Other <sup>(1)</sup>	Total
<b>Net carrying amount</b>				
<b>As at December 31, 2018</b>	<b>\$ 299</b>	<b>\$ 10</b>	<b>\$ 80</b>	<b>\$ 389</b>
As at December 31, 2017	\$ 370	\$ 12	\$ 84	\$ 466

<sup>(1)</sup> The "Other" category mainly includes the amount related to the acquisition of insurance contract portfolios and a distribution network.

<sup>(2)</sup> For more information, see Note 20, "Significant transactions".

<sup>(3)</sup> As at December 31, 2017, certain intangible assets were presented under "Assets of the disposal group held to be transferred". These intangible assets were during the year ended December 31, 2018 as part of the creation of Aviso Health, as mentioned in Note 20, "Significant transactions".

## NOTE 12 – OTHER ASSETS – OTHER

The following table presents the breakdown of “Other assets – Other”.

	As at December 31, 2018	As at December 31, 2017
Investments in companies accounted for using the equity method (Note 13)	\$ 907	\$ 515
Accounts receivable	508	597
Interest receivable	273	295
Prepaid expenses	184	159
Taxes receivable	166	48
Other	442	574
	<b>\$ 2,480</b>	<b>\$ 2,188</b>

## NOTE 13 – INTERESTS IN OTHER ENTITIES

### SUBSIDIARIES

The main subsidiaries of the Federation have been incorporated in Canada and their principal place of business is in this country.

The following table presents the nature of the operations of these subsidiaries and the proportion of ownership interests held by the Federation in each of them.

	Nature of operations	As at December 31, 2018 <sup>(1)</sup>	As at December 31, 2017 <sup>(1)</sup>
Desjardins Capital Inc.	Issuance of securities on the markets and financing of the Desjardins caisses	100 %	100 %
Desjardins Financial Holding Inc.	Holding company	100	100
Zag Bank <sup>(2)</sup>	Financial institution	100	100
Desjardins Financial Corporation Inc.	Holding company	100	100
Desjardins Global Asset Management Inc.	Asset management	100	100
Desjardins General Insurance Group Inc.	Property and casualty insurance	100	100
Property and casualty insurance subsidiaries <sup>(3)</sup>	Property and casualty insurance	90	90
Desjardins Financial Security Life Assurance Company	Life and health insurance and financial services	100	100
Desjardins Investments Inc.	Design, administration and distribution of insurance and savings products	100	100
Desjardins Trust Inc.	Asset custody and trust services	100	100
Desjardins Technology Group Inc.	Development and maintenance of Desjardins Group's technology	100	100
Qtrade Canada Inc. <sup>(4)</sup>	Online brokerage and wealth management services	-	80.8
Desjardins Securities Inc.	Securities brokerage	100	100

<sup>(1)</sup> Represents also the proportion of voting rights held by the Federation in these subsidiaries, except for Qtrade Canada Inc., in which the Federation held 100% of the voting rights as at December 31, 2017.

<sup>(2)</sup> The Federation plans to wind up this subsidiary in the coming year.

<sup>(3)</sup> Represents a group of six property and casualty insurance subsidiaries.

<sup>(4)</sup> On April 1, 2018, this subsidiary was part of the transaction that resulted in the creation of Aviso Health. For more information, see Note 20, “Significant transactions”.

## NOTE 13 – INTERESTS IN OTHER ENTITIES (continued)

### Subsidiaries that have material non-controlling interests

As at December 31, 2018 and 2017, the subsidiaries that have material non-controlling interests comprise the six property and casualty insurance subsidiaries aggregated under “Property and casualty insurance subsidiaries”.

The following tables present summarized financial information about the subsidiaries that have material non-controlling interests. This information is presented before eliminating intragroup accounts and transactions and has been adjusted to reflect the fair value adjustments made at the time of acquisition.

	As at December 31, 2018	As at December 31, 2017
Assets <sup>(1)</sup>	\$ 14,685	\$ 14,672
Liabilities	12,134	11,861
Equity <sup>(1)</sup>	\$ 2,551	\$ 2,811
<b>Non-controlling interests</b>	<b>\$ 750</b>	<b>\$ 776</b>

<sup>(1)</sup> Include goodwill of \$100 million as at December 31, 2018 (\$100 million as at December 31, 2017).

For the years ended December 31	2018	2017
Total income	\$ 4,710	\$ 3,945
Net surplus earnings for the year after member caisses dividends	176	162
Comprehensive income for the year	\$ (46)	\$ 199
<b>Share of net surplus earnings for the year after member caisses dividends attributable to holders of non-controlling interests</b>	<b>\$ 42</b>	<b>\$ 41</b>
Dividends / distributions paid to holders of non-controlling interests	\$ 36	\$ 42

### CONSOLIDATED STRUCTURED ENTITY

#### Covered bonds

Under its covered bond program, the Federation issues debt securities guaranteed by a pool of mortgage loans. CCDQ Covered Bond (Legislative) Guarantor Limited Partnership, a structured entity is in place to guarantee principal and interest payments owing to the holders of the covered bonds issued by the Federation. The operations of this entity are included in the Consolidated Financial Statements of the Federation as this entity is controlled by the Federation. The Federation granted financing to this entity to facilitate the acquisition of the assets for purposes of guaranteeing the covered bonds issued. The financing granted by the Federation may reach a maximum amount equal to the outstanding loans held by this entity. Under the terms and conditions of each of the issuance agreements, the Federation has limited access to the assets that are legally owned by this structured entity. These assets do not meet the recognition criteria neither for the structured entity nor for the Federation, and are therefore not recognized in their respective balance sheets. The covered bonds, amounting to \$5,859 million as at December 31, 2018 (\$4,517 million as at December 31, 2017), are presented under “Deposits – Business and government” in the Consolidated Balance Sheets.

## NOTE 13 – INTERESTS IN OTHER ENTITIES (continued)

### JOINT VENTURES

#### Information about material joint ventures

The Federation holds interests in the RPADS LP, 101 St-Clair and Aviso Wealth joint ventures. RPADS LP is an entity that acquires and develops real estate portfolios, 101 St-Clair is a real estate management and investment company, and Aviso Wealth, is a wealth management company. These joint ventures have been incorporated in Canada and their principal place of business is in this country.

The following tables present summarized financial information about these joint ventures, namely the amounts included in their IFRS financial statements.

	As at December 31, 2018			As at December 31, 2017	
	RPADS LP	101 St-Clair	Aviso Wealth <sup>(1)</sup>	RPADS LP	101 St-Clair
<b>Proportion of ownership interest held</b>	<b>55.10 %</b>	<b>60.00 %</b>	<b>50.00 %</b>	50.10 %	60.00 %
Assets	\$ 552	\$ 138	\$ 1,972	\$ 474	\$ 116
Liabilities <sup>(2)</sup>	50	1	1,758	37	5
Equity	\$ 502	\$ 137	\$ 214	\$ 437	\$ 111
<b>Interests in joint ventures<sup>(3)</sup></b>	<b>\$ 272</b>	<b>\$ 82</b>	<b>\$ 335</b>	<b>\$ 219</b>	<b>\$ 66</b>

<sup>(1)</sup> The Aviso Wealth joint venture was created in 2018, as mentioned in Note 20, "Significant transactions". The interest in the joint venture reflects adjustments of \$228 million made when using the equity method.

<sup>(2)</sup> Consisting primarily of financial liabilities other than accounts payable and provisions.

<sup>(3)</sup> Represents the carrying amount of the interests in joint ventures recognized in the Consolidated Balance Sheets.

For the years ended December 31	2018			2017	
	RPADS LP	101 St-Clair	Aviso Wealth <sup>(1)</sup>	RPADS LP	101 St-Clair
Total income	\$ 102	\$ 2	\$ 374	\$ 95	\$ -
<b>Net income and comprehensive income for the year</b>	<b>\$ 24</b>	<b>\$ (2)</b>	<b>\$ 9</b>	<b>\$ 23</b>	<b>\$ -</b>

<sup>(1)</sup> Total income, net income and comprehensive income of Aviso Wealth are based on data for the nine-month period ended December 31, 2018.

### JOINT OPERATIONS

The Federation holds an 80% ownership interest in a joint arrangement with Fonds Immobilier Cogir 1 and a 50% ownership interest in a joint arrangement with First Capital Realty Inc. to invest in undivided co-ownership in commercial buildings in Quebec. It also holds a 50.5% ownership interest in a second joint arrangement with First Capital Realty Inc. formed during fiscal 2018 to invest in undivided co-ownership in commercial buildings in Ontario.

The Federation also participates in a joint arrangement with 9509593 Canada Inc. formed to invest in undivided co-ownership in multi-residential buildings in Quebec. The Federation holds a 50% ownership interest in this joint arrangement.

These joint arrangements are joint operations giving the joint operators rights to the assets and obligations for the liabilities based on their ownership interests. All decisions about the relevant activities require the unanimous consent of the joint operators. These joint operations have been incorporated in Canada and their principal place of business is in this country.

### ASSOCIATES

#### Information about material associates

The Federation holds an interest in Fiera Holdings Inc. an associate, which operates in the investment management industry. It has been incorporated in Canada and its principal place of business is in this country. The interest previously held in Northwest & Ethical Investments L.P. (Northwest & Ethical), an associate, was part of the transaction that resulted in the creation of Aviso Wealth, on April 1, 2018, as mentioned in Note 20, "Significant transactions".

## NOTE 13 – INTERESTS IN OTHER ENTITIES (continued)

The following tables present summarized financial information about Fiera Holdings Inc., namely the amounts included in its IFRS financial statements adjusted to reflect adjustments made by the Federation when using the equity method, such as fair value adjustments made at the time of acquisition and adjustments for differences in accounting policies.

	As at December 31, 2018	As at December 31, 2017	
	Fiera Holdings Inc.	Fiera Holdings Inc.	Northwest & Ethical <sup>(1)</sup>
<b>Proportion of ownership interest held<sup>(2,3)</sup></b>	<b>37.20 %</b>	37.18 %	50.00 %
Assets <sup>(4,5)</sup>	\$ 1,418	\$ 1,113	\$ 204
Liabilities <sup>(5)</sup>	773	566	54
Equity <sup>(4,5)</sup>	\$ 645	\$ 547	\$ 150
<b>Interests in associates<sup>(6)</sup></b>	<b>\$ 50</b>	\$ 52	\$ 85

<sup>(1)</sup> On April 1, 2018, Northwest & Ethical was part of a transaction that resulted in the creation of Aviso Wealth. For more information, see Note 20, "Significant transactions".

<sup>(2)</sup> Represents also the proportion of voting rights held by the Federation in the associates.

<sup>(3)</sup> As at December 31, 2018, the Federation indirectly held an 7.41% ownership interest (8.09% as at December 31, 2017) in Fiera Capital Corporation through its in Fiera Holdings Inc.

<sup>(4)</sup> Include goodwill of \$10 million (\$10 million as at December 31, 2017) related to Fiera Holdings Inc.

<sup>(5)</sup> The assets, liabilities and equity of Fiera Holdings Inc. for 2018 and 2017 are based on data as at September 30. The assets, liabilities and equity of Northwest & Ethical for 2017 were also based on data as at September 30.

<sup>(6)</sup> Represents the carrying amount of the interests in associates recognized in the Consolidated Balance Sheets.

For the years ended December 31	2018	2017	
	Fiera Holdings Inc.	Fiera Holdings Inc.	Northwest & Ethical
Total income <sup>(1)</sup>	\$ 528	\$ 427	\$ 111
<b>Net income and comprehensive income for the year<sup>(1)</sup></b>	<b>\$ 2</b>	\$ 15	\$ 11

<sup>(1)</sup> Total income, net income and comprehensive income of Fiera Holdings Inc. for 2018 and 2017 are based on data for the twelve-month periods ended September 30. Total income, net income and comprehensive income of Northwest & Ethical were also based on data for the twelve-month periods ended September 30, 2017.

## UNCONSOLIDATED STRUCTURED ENTITIES

### Mutual funds

The Federation holds interests in mutual fund units. Even though it holds, in certain cases, a significant exposure to or has the right to a significant share of variable returns as a result of the units it holds in these funds, these units do not give the Federation power over the relevant activities of these funds. Accordingly, the Federation does not control these funds, which are considered as unconsolidated structured entities.

The investments of these funds are made pursuant to a diversified investment policy, and the nature of the operations of these funds and their characteristics are comparable to those that are found under normal market terms for these types of funds. The Federation's maximum exposure to loss from its interests in these mutual funds is limited to the value of the investments in such funds.

## NOTE 14 – DEPOSITS

Deposits consist of demand deposits (payable on demand), notice deposits (payable upon notice) and term deposits (payable on a fixed date). Demand deposits are interest-bearing or non-interest-bearing deposits, primarily accounts with chequing privileges, for which the Federation does not have the right to require notice prior to withdrawal. Notice deposits are interest-bearing deposits, primarily savings accounts, for which the Federation has the legal right to require notice prior to withdrawal. Term deposits are interest-bearing deposits, primarily fixed-term deposit accounts, guaranteed investment certificates or other similar instruments, with a term that generally varies from one day to 10 years and mature on a predetermined date.

The following tables present the breakdown of deposits.

	As at December 31, 2018				As at December 31, 2017			
	Payable on demand	Payable upon notice	Payable on a fixed date	Total	Payable on demand	Payable upon notice	Payable on a fixed date	Total
Individuals	\$ 2,961	\$ 41	\$ 1,103	\$ 4,105	\$ 3,154	\$ 50	\$ 1,149	\$ 4,353
Business and government	3,274	-	42,724	45,998	3,452	-	37,511	40,963
Deposit-taking institutions	4,448	-	3,506	7,954	2,757	-	4,076	6,833
	<b>\$ 10,683</b>	<b>\$ 41</b>	<b>\$ 47,333</b>	<b>\$ 58,057</b>	<b>\$ 9,363</b>	<b>\$ 50</b>	<b>\$ 42,736</b>	<b>\$ 52,149</b>

## NOTE 15– INSURANCE CONTRACT LIABILITIES

### PREMIUMS

	2018			2017		
	Life and health insurance	Property and casualty insurance	Total	Life and health insurance	Property and casualty insurance	Total
Gross premiums	\$ 4,708	\$ 4,640	\$ 9,348	\$ 4,516	\$ 4,295	\$ 8,811
Premiums ceded under reinsurance treaties	(180)	(245)	(425)	(198)	(467)	(665)
<b>Net premiums</b>	<b>\$ 4,528</b>	<b>\$ 4,395</b>	<b>\$ 8,923</b>	<b>\$ 4,318</b>	<b>\$ 3,828</b>	<b>\$ 8,146</b>

### COMPOSITION OF INSURANCE CONTRACT LIABILITIES

	As at December 31, 2018	As at December 31, 2017
<b>Insurance contract liabilities</b>		
Actuarial liabilities – Life and health insurance	\$ 18,553	\$ 18,428
Provisions for claims and adjustment expenses – Property and casualty insurance	6,489	6,457
Unearned premiums	2,547	2,274
Policyholder deposits	670	646
Provisions for benefits, policyholder dividends and experience refunds	470	480
Other	35	15
	<b>\$ 28,764</b>	<b>\$ 28,300</b>

### ACTUARIAL LIABILITIES – LIFE AND HEALTH INSURANCE

#### Composition

Actuarial liabilities and assets backing actuarial liabilities comprise the following amounts.

	As at December 31, 2018	As at December 31, 2017
<b>Gross actuarial liabilities</b>		
Non-participating policies	\$ 14,565	\$ 14,326
Participating policies	3,988	4,102
	<b>18,553</b>	<b>18,428</b>
Amounts ceded to reinsurers	(915)	(915)
<b>Net actuarial liabilities</b>	<b>\$ 17,638</b>	<b>\$ 17,513</b>

	As at December 31, 2018	As at December 31, 2017
<b>Composition of assets backing net actuarial liabilities</b>		
Bonds	\$ 11,138	\$ 10,884
Mortgage and business loans	2,434	2,536
Investment property	1,116	1,040
Equities	1,430	1,531
Other	1,520	1,522
	<b>\$ 17,638</b>	<b>\$ 17,513</b>

The fair value of assets backing net actuarial liabilities was \$18,383 million as at December 31, 2018 (\$18,117 million as at December 31, 2017).

#### Actuarial assumptions

The computation of actuarial liabilities is based on estimates and assumptions. The nature of the main assumptions used in the computation of actuarial liabilities and the method used to establish these assumptions are described in the following paragraphs.

The basic assumptions used in computing actuarial liabilities are those that prove to be the best estimates for various contingencies. The appointed actuary must, for each of these assumptions, establish a margin for adverse deviation in order to mitigate the random event, allow for the risk of deteriorating underwriting experience and ensure that provisions are adequate to meet future commitments. The extent of the margins for adverse deviation is prescribed by Canadian accepted actuarial practices. These margins vary for each assumption and type of product. The margins for adverse deviation increase actuarial liabilities and reduce the profit or loss that would otherwise be recognized at inception of the contracts. With time and as estimation risks decline, these margins are reversed and recognized in the Consolidated Statements of Income.

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

The risks associated with the accuracy of the actuarial assumptions used to compute actuarial liabilities arise from the non-materialization of expected assumptions. The actuary periodically carries out studies on the underwriting experience related to each assumption and modifies the assumptions, if appropriate, to take into account the current and future expected situation. Any impact resulting from these modifications is immediately recognized in the Consolidated Statements of Income.

### Mortality

The life and health insurance subsidiaries determine their mortality assumptions based on the annual studies of their recent underwriting experience and, when the results cannot serve as the sole source of reference due to their insufficient credibility, they also take into account industry studies. Mortality assumptions vary based on gender, risk category and type of contract. A future mortality improvement assumption is taken into account in accordance with Canadian accepted actuarial practices.

### Morbidity

For morbidity assumptions regarding the occurrence of accidents and illness, the life and health insurance subsidiaries use industry-developed morbidity tables modified based on current data provided by their studies of their underwriting experience and those of the industry.

### Contract cancellation rates

The life and health insurance subsidiaries carry out an annual study of their underwriting experience with respect to individual insurance contract cancellation, as holders can cancel their policy before the expiry of their contractual coverage period by discontinuing premium payment without using the non-forfeiture options, if any. The contract cancellation rate assumptions are based on these subsidiaries' recent underwriting experience. These assumptions are adjusted on the basis of the industry's underwriting experience when the assumptions of the subsidiaries are not sufficiently credible.

### Investment return

Investment return is based on projected investment income using the current portfolios of assets backing the actuarial liabilities and projected reinvestment strategies. The life and health insurance subsidiaries manage the investments backing their actuarial liabilities by taking into account the characteristics of the commitments of each of their business segments, using clearly defined mechanisms set out in their matching policy. By closely matching the cash flows related to the assets with those related to the actuarial liabilities, they mitigate their sensitivity to future changes in interest rate levels. According to CALM, changes in the fair value of assets backing the actuarial liabilities are essentially offset by corresponding changes in the value of actuarial liabilities.

Under CALM, cash flows from these assets are matched with cash flows that will arise from future asset acquisitions or sales to determine the expected rates of return on these assets for the coming years. The projected reinvestment strategies are determined based on the characteristics of the commitments of each segment, and reinvestment returns are based on current and expected market rates for fixed-rate investments and on expected rates for floating-rate investments. In addition, the asset cash flow projections include assumptions for investment management fees and credit risk.

Investment return assumptions take into account expected future credit losses on fixed-income investments. In that regard, in addition to the loss allowance for expected credit losses recognized through a write-down of the carrying amount of the assets, a provision amounting to \$336 million as at December 31, 2018 (\$345 million as at December 31, 2017) has been included in actuarial liabilities as a protection against the risk of insufficient return on assets.

### Operating expenses and taxes

The operating expense assumptions reflect the projected costs for managing and processing contracts in force, including indirect overhead expenses. The life and health insurance subsidiaries carry out an annual study of operating expenses by major product line, and these expenses are projected using the expected rate of inflation and the expected development of blocks of business, when relevant.

Taxes reflect the assumptions relating to future premium taxes and taxes other than income taxes. For income taxes, actuarial liabilities are adjusted only when there are temporary differences or to take into account the impact of non-deductible or non-taxable items on cash flows from the liabilities and the assets related to insurance contracts.

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

### Sensitivity of actuarial liabilities to changes in assumptions

The following table shows the impact on “Net surplus earnings for the year after dividends to member caisses” of the sensitivity of actuarial liabilities to changes in underlying non-economic best estimate assumptions for the years ended December 31.

	2018	2017
2% negative change in future mortality rates		
Products for which a rate increase increases actuarial liabilities	\$ (53)	\$ (49)
Products for which a rate decrease increases actuarial liabilities	(23)	(23)
5% increase in future morbidity rates	(80)	(75)
10% negative change in future contract cancellation rates	(153)	(138)
5% increase in future operating expenses	(45)	(44)

### Changes in actuarial liabilities

The change in net actuarial liabilities during the years ended December 31 was due to business activities and to changes in actuarial estimates, as follows:

	2018			2017		
	Gross amount	Amount ceded to reinsurers	Net amount	Gross amount	Amount ceded to reinsurers	Net amount
<b>Balance at beginning of year</b>	\$ 18,428	\$ (915)	\$ 17,513	\$ 17,574	\$ (935)	\$ 16,639
Change due to						
Passage of time	(512)	4	(508)	556	(29)	527
New business	674	(18)	656	538	(24)	514
Changes in actuarial assumptions	(24)	(13)	(37)	(84)	34	(50)
Disposals <sup>(1)</sup>	-	-	-	(162)	53	(109)
	138	(27)	111	848	34	882
Other changes	(13)	27	14	6	(14)	(8)
<b>Balance at end of year</b>	\$ 18,553	\$ (915)	\$ 17,638	\$ 18,428	\$ (915)	\$ 17,513

<sup>(1)</sup> For more information, see Note 20, “Significant transactions”.

### Changes in actuarial assumptions

The economic and non-economic assumptions taken into account in the computation of actuarial liabilities are periodically updated to reflect the actual or projected underwriting experience associated with each of them. The following table presents the impact of changes made to assumptions on “Net surplus earnings for the year after dividends to member caisses” for the years ended December 31.

	2018	2017
<b>Changed assumptions</b>		
Mortality	\$ 22	\$ 119
Morbidity	9	1
Contract cancellation rates	(79)	(166)
Investment return	17	59
Operating expenses	47	17
Methods and other	11	6
	\$ 27	\$ 36

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

### PROVISIONS FOR CLAIMS AND ADJUSTMENT EXPENSES – PROPERTY AND CASUALTY INSURANCE

#### Methodology and assumptions

The provisions for claims and adjustment expenses include provisions on file for each claim reported as well as provisions for adjustment expenses, changes in reported claims and claims incurred but not reported by the insured parties.

The provisions for claims and adjustment expenses are estimated using appropriate actuarial methods for loss prospective valuation in accordance with Canadian accepted actuarial practices. These methods are used to estimate the ultimate claims by projecting claims amounts by business lines and accident year.

The main assumption underlying these methods is that past claims development can be used to project what future claims development will be (or that future claims development will be similar to past claims development). An additional qualitative judgment is made to assess the extent by which past trends may not apply in the future and make the necessary adjustments to ensure that the provisions for claims and adjustment expenses are adequate and represent the best estimates of future payments on outstanding claims, including claims incurred but not reported that can be expected, based on data and information currently known. The assumptions used to develop this estimate are selected by risk category and geographic area. In addition, the estimates take into consideration various factors, including the average settlement cost per claim, the average number of claims and claims severity and frequency trends.

The initial estimate of the provisions for claims and adjustment expenses is a non-discounted amount. This estimate is then discounted to take into account the time value of money. The discount rate used is based on the rate of return for the assets backing the provisions for claims and adjustment expenses.

Since determining claims estimates is subject to uncertainties and such estimates may change significantly in the short term, the property and casualty insurance subsidiaries include margins for adverse deviation in the assumptions with respect to claims development, expected reinsurance recoveries and future investment income from the asset portfolio backing the provisions for claims and adjustment expenses. These margins for adverse deviation are determined in accordance with Canadian accepted actuarial practices to ensure that the amount of the provisions for claims and adjustment expenses is sufficient to settle future benefits.

#### Change in provisions for claims and adjustment expenses

The following table shows the change in the provisions for claims and adjustment expenses for the years ended December 31.

	2018			2017		
	Gross amount	Amount ceded to reinsurers	Net amount	Gross amount	Amount ceded to reinsurers	Net amount
Balance at beginning of year	\$ 6,457	\$ (1,056)	\$ 5,401	\$ 6,679	\$ (1,080)	\$ 5,599
Claims incurred during the year	3,926	(223)	3,703	3,538	(364)	3,174
Development of claims incurred in prior years	(532)	74	(458)	(620)	35	(585)
Changes in discount rates	(43)	6	(37)	(64)	10	(54)
Claims paid during the year	(3,319)	264	(3,055)	(3,073)	343	(2,730)
Disposals	-	-	-	(3)	-	(3)
Balance at end of year	\$ 6,489	\$ (935)	\$ 5,554	\$ 6,457	\$ (1,056)	\$ 5,401

Changes in assumptions had no material impact on the Consolidated Financial Statements as at December 31, 2018 and 2017.

#### Assumption sensitivity analysis

The following table shows the impact on the Consolidated Statements of Income of the sensitivity of the provisions for claims and adjustment expenses to changes in certain key assumptions for the years ended December 31. The impact of a change in the discount rate is presented in the "Interest rate risk management" section of this note.

	Changes in actuarial assumptions	Impact on "Net surplus earnings for the year after dividends to member caisses"	
		2018	2017
Average claims settlement cost	+ 5%	\$ (239)	\$ (227)

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

### Claims and adjustment expenses development

The following table shows the development of claims and adjustment expenses on a net basis. It presents the estimated ultimate claims amount, including claims reported and claims incurred but not reported at the reporting date for each accident year, with cumulative payments made to date.

	2008 and before	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total
<b>Estimated ultimate claims amount</b>												
At the end of the accident year		\$ 1,076	\$ 1,101	\$ 1,272	\$ 1,375	\$ 1,471	\$ 1,536	\$ 2,186	\$ 2,417	\$ 3,158	<b>\$ 3,691</b>	
1 year later		1,063	1,103	1,272	1,322	1,447	2,453	2,168	2,387	3,121		
2 years later		1,077	1,091	1,238	1,328	2,186	2,349	2,165	2,365			
3 years later		1,072	1,071	1,221	1,967	2,086	2,272	2,117				
4 years later		1,062	1,055	1,781	1,839	1,977	2,184					
5 years later		1,049	1,577	1,657	1,769	1,910						
6 years later		1,466	1,515	1,567	1,717							
7 years later		1,379	1,434	1,547								
8 years later		1,330	1,386									
9 years later		1,295										
<b>Cumulative payments to date</b>		1,156	1,223	1,373	1,478	1,582	1,706	1,683	1,772	2,111	<b>1,977</b>	
Net provisions for claims and adjustment expenses	\$ 282	\$ 139	\$ 163	\$ 174	\$ 239	\$ 328	\$ 478	\$ 434	\$ 593	\$ 1,010	<b>\$ 1,714</b>	\$ 5,554
Reinsurers' share in provisions for claims and adjustment expenses	4	-	-	-	-	-	-	288	361	161	<b>121</b>	935
<b>Gross provisions for claims and adjustment expenses</b>	<b>\$ 286</b>	<b>\$ 139</b>	<b>\$ 163</b>	<b>\$ 174</b>	<b>\$ 239</b>	<b>\$ 328</b>	<b>\$ 478</b>	<b>\$ 722</b>	<b>\$ 954</b>	<b>\$ 1,171</b>	<b>\$ 1,835</b>	<b>\$ 6,489</b>

### Insurance risk management

Insurance risk refers to the risk that events may turn out differently from the assumptions used when designing, pricing or measuring actuarial reserves for insurance products, and that profitability of these products may be affected.

The life and health insurance subsidiaries are exposed to insurance risk through the products they sell. Depending on the insurance product, these subsidiaries may be exposed to mortality risk, morbidity risk and forfeiture risk. All products sold expose these subsidiaries to expenditure risk.

The property and casualty insurance subsidiaries underwrite automobile, home and commercial property insurance contracts to individuals and businesses. In the normal course of their operations, these subsidiaries are exposed to insurance risk, which includes several components: underwriting risk, catastrophe risk and reserve risk.

To manage insurance risk, the insurance subsidiaries apply stringent policies and criteria with respect to product and service development and pricing, and regularly carry out analyses to compare forecasts with actual results and revise pricing assumptions if needed.

In addition, for the life and health insurance subsidiaries, certain products allow for price adjustments depending on whether assumptions materialize or not.

Furthermore, for property and casualty insurance subsidiaries, insurance risk is also managed through various aspects, including by actively and rigorously managing risk segmentation (through underwriting and pricing) and claims. With respect to catastrophes, the property and casualty insurance subsidiaries have established a governance structure to monitor the various risks caused by such events and use sophisticated tools to simulate the related financial losses and operational impact. Given the unpredictable nature of large-scale catastrophic events, the property and casualty insurance subsidiaries have a catastrophe reinsurance treaty, which is reviewed at least annually.

The insurance subsidiaries also set up actuarial liabilities and provisions for claims and adjustment expenses in accordance with Canadian accepted actuarial practices and constantly monitor the development of loss experience.

#### Use of reinsurance

In order to limit their losses, the life and health and property and casualty insurance subsidiaries enter into reinsurance treaties for contracts with coverage in excess of certain maximum amounts that vary based on the nature of the activities. This reinsurance structure takes into account their respective risk profile and appetite. In addition, these subsidiaries purchase additional reinsurance protection with respect to large-scale catastrophic events. The retention and limit amounts selected for the property and casualty insurance subsidiaries' catastrophe treaty are subject to a detailed annual review based on these subsidiaries' various catastrophe models and the positioning of their competitors in the industry.

In connection with the acquisition of the Canadian businesses of State Farm, the property and casualty insurance subsidiaries signed a share reinsurance treaty under which, over a five-year period, all premiums and claims from new business and renewals related to the acquired businesses occurring after the acquisition date are ceded using percentages decreasing from 90% for the 2015 accident year to 10% for the 2019 accident year. Pursuant to the terms and conditions of the reinsurance treaty, amounts payable and receivable under the treaty will be settled on a net basis.

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

In order to reduce reinsurance risk, the life and health and property and casualty insurance subsidiaries do business with many reinsurers that meet financial strength criteria, most of which are governed by the same regulatory authorities as the subsidiaries. In addition, the solvency of the companies to which they cede a portion of their risks is periodically examined. These reinsurance treaties do not release these subsidiaries from their obligations toward their policyholders, but they mitigate the risks to which they are exposed. Under the share reinsurance treaty signed with State Farm on the acquisition, State Farm must hold investments in trust so that it can fulfill its reinsurance obligations.

For the years ended December 31, the impact of reinsurance reduced the Consolidated Statements of Income items presented in the table below by the following amounts:

	2018			2017		
	Life and health insurance	Property and casualty insurance	Total	Life and health insurance	Property and casualty insurance	Total
Premiums	\$ 180	\$ 245	\$ 425	\$ 198	\$ 467	\$ 665
Claims, benefits, annuities and changes in insurance contract liabilities	146	142	288	153	319	472

### Segregated fund risk management

Investments held for segregated fund contract holders are exposed to various financial risks. Pursuant to the contracts' clauses, the risks and rewards associated with the return of these investments accrue to the holders, even though these investments are held by the life and health insurance subsidiary that sells segregated fund contracts. This life and health insurance subsidiary offers minimum guarantees for death benefits, maturity value and withdrawals in payout situations to protect the unitholders of certain funds. The actuarial liabilities of this subsidiary include amounts sufficient to pay these minimum guarantees.

To reduce the potential negative impact that may arise from the segregated fund contract guarantee risk, the life and health insurance subsidiary selling segregated fund contracts uses a hedging program aimed at offsetting the impact of unfavourable stock market movements on the future cost of guarantees as well as a hedging program aimed at offsetting the impact of unfavourable changes in interest rates on these future costs. These programs cover all the segregated fund contracts that include a guarantee offered to clients by this subsidiary.

### Interest rate risk management

The insurance subsidiaries are exposed to interest rate risk, which represents the potential impact of interest rate fluctuations on the Consolidated Statements of Income and equity. Sound and prudent management is applied to minimize the negative impact of interest rate movements.

The asset-liability matching policy of the life and health insurance subsidiaries describes the techniques used to measure interest rate risk, the tolerated limits and the monitoring procedures to use in managing this risk. The policy sets out, in particular, the limits of the gap between the duration of liabilities and the duration of the related assets. These subsidiaries' management is responsible for applying the policy and ensures that there are practices in place to administer and monitor interest rate risk. In addition, if needed, it may apply rebalancing techniques to correct or improve the backing status.

The non-matching of cash flows would have no impact on the Consolidated Statements of Income in the event that interest rates fluctuate within the limits considered to establish actuarial liabilities; however, interest rate fluctuations outside these limits would have an impact on the Consolidated Statements of Income of the life and health insurance subsidiaries. In addition, for the guarantees offered under segregated fund contracts, the actuarial liabilities are calculated using the current rates curve, and a change in these rates would have a direct impact on the value of these liabilities and, consequently, on the Consolidated Statements of Income. However, the subsidiary that sells these contracts has implemented a hedging program for these segregated fund products in order to minimize the impact of interest rate fluctuations on the Consolidated Statements of Income.

The following table shows, for the years ended December 31, the estimated impact on "Net surplus earnings for the year after dividends to member caisses" of a change in interest rates on the life and health insurance subsidiaries' actuarial liabilities and the assets backing these actuarial liabilities.

	2018	2017
1% increase in interest rates	\$ 53	\$ 43
1% decrease in interest rates	(78)	(60)

The interest rate risk management policy of the property and casualty insurance subsidiaries describes the techniques used to measure interest rate risk, the tolerated limits and the monitoring procedures to use in managing this risk. The policy sets out, in particular, the limit of the gap compared to the target duration of the consolidated fixed-income portfolio and as well as the limit of the gap between the duration of assets and liabilities to be backed. The property and casualty insurance subsidiaries' management is responsible for applying the policy and ensures that there are practices in place to administer and monitor interest rate risk. In addition, if needed, it may implement an action plan apply rebalancing techniques to correct or improve the backing status.

## NOTE 15 – INSURANCE CONTRACT LIABILITIES *(continued)*

The following table shows, for the years ended December 31, the estimated impact on “Net surplus earnings for the year after dividends to member caisses” arising from the impact of a change in interest rates on the property and casualty insurance subsidiaries’ provisions for claims and adjustment expenses and the assets backing these provisions.

	2018	2017
1% increase in interest rates	\$ 7	\$ 5
1% decrease in interest rates	(8)	(6)

### Liquidity risk management

The life and health insurance subsidiaries manage liquidity risk in order to ensure that they have timely and cost-effective access to the funds needed to meet their financial obligations as they become due, in both routine and crisis situations.

For these subsidiaries, managing this risk involves maintaining a sufficient level of liquid securities, monitoring indicators and adopting a contingency plan to implement in the event of a liquidity crisis.

For the property and casualty insurance subsidiaries, managing this risk involves maintaining a sufficient level of liquid securities and spreading the collection of insurance premiums throughout the year, which generally supports a large portion of the cash outflows associated with claims and other expenses.

The following table presents the contractual maturity terms for actuarial liabilities and provisions for claims and adjustment expenses. The projections in this table are greater than the balances for actuarial liabilities and provisions for claims and adjustment expenses presented in the Consolidated Balance Sheets since they represent expected outflows that exclude, among others, the impact of discounting. The cash flows related to actuarial liabilities included in this table are presented net of expected periodic premium flows from insured parties. In addition, the amounts are presented net of reinsurance and represent estimated cash flows that may differ from actual cash flows.

	As at December 31, 2018	As at December 31, 2017
Less than 1 year	\$ 2,746	\$ 2,626
1 to 5 years	5,801	5,438
Over 5 years	36,278	34,580
<b>Total</b>	<b>\$ 44,825</b>	<b>\$ 42,644</b>

## NOTE 16 – NET DEFINED BENEFIT PLAN LIABILITIES

This note should be read in conjunction with Note 16, “Net defined benefit plan liabilities”, to the audited Combined Financial Statements of Desjardins Group for the year ended December 31, 2018 approved on February 27, 2019, which presents the defined benefit group plans, the risks related to pension plans and information on non-group plans.

### GROUP PLANS

#### Pension plans

The Federation participates in a pension plan and a supplemental pension plan through Desjardins Group’s defined benefit group plans. Consequently, the Federation recognizes its share in the liabilities of these plans in its Consolidated Balance Sheets.

#### Post-retirement benefit plan

The Federation also offers a post-retirement benefit plan, including medical, dental and life insurance, to retiring employees and their dependents through the defined benefit group plan of Desjardins Group. Consequently, the Federation recognizes its share in the liability of this plan in its Consolidated Balance Sheets.

## NOTE 16 – NET DEFINED BENEFIT PLAN LIABILITIES (continued)

### NON-GROUP PLANS

The Federation also offers certain active and retired executives other defined benefit supplemental pension plans for which a liability representing future obligations with respect to these plans was recognized in the Consolidated Balance Sheets.

In addition, the employees of certain subsidiaries are offered specific defined benefit pensions plans and defined benefit post-retirement benefit plan that are not part of Desjardins Group's defined benefit group plans.

The following tables present the recognized defined benefit plan liabilities, cost and remeasurement of net liabilities for all the plans as well as the Federation's share in defined benefit group plans.

	As at December 31, 2018		As at December 31, 2017	
<b>Net defined benefit plan liabilities</b>				
Group plans				
Pension plans	\$	1,002	65%	\$ 926 64%
Post-retirement benefit plan		257	38	482 57
		1,259		1,408
Non-group plans		319		333
<b>Total net defined benefit plan liabilities</b>	\$	1,578		\$ 1,741

	As at December 31, 2018		As at December 31, 2017	
<b>Defined benefit plan cost recognized</b>				
Group plans				
Pension plans	\$	243	\$	208
Post-retirement benefit plan <sup>(1)</sup>		(48)		24
		195		232
Non-group plans		34		40
<b>Total defined benefit plan cost recognized</b>	\$	229	\$	272

<sup>(1)</sup> The defined benefit plan cost recognized reflects the impact of the amendment to the post-retirement benefit plan made during the year ended December 31, 2018.

	As at December 31, 2018		As at December 31, 2017	
<b>Remeasurement of net defined benefit plan liabilities</b>				
Group plans				
Pension plans	\$	65	\$	198
Post-retirement benefit plan		(165)		35
		(100)		233
Non-group plans		(10)		29
<b>Total remeasurement of net defined benefit plan liabilities</b>	\$	(110)	\$	262

## NOTE 17 – OTHER LIABILITIES – OTHER

The following table presents the breakdown of "Other liabilities – Other".

	As at December 31, 2018		As at December 31, 2017	
Accounts payable and other accrued liabilities	\$	2,698	\$	2,344
Client contract liabilities		565		309
Interest payable		439		151
Provisions for risks and expenses		84		226
Taxes payable		62		56
Borrowings from financial institutions		28		30
Other		1,229		1,678
	\$	5,105	\$	4,794

## NOTE 18 – SUBORDINATED NOTES

The subordinated notes presented in the Federation's Consolidated Balance Sheets are senior notes issued by Desjardins Capital Inc. whose gross proceeds are invested in notes issued by the Desjardins caisses in Quebec that are subordinated to the claims of depositors and certain other creditors. These senior notes rank prior, in right of payment, to the subordinated debt securities of Desjardins Capital Inc. and are secured by a hypothec on the subordinated notes issued by the Desjardins caisses in Quebec.

Repayments and cancellations of the notes are subject to the consent and approval of the various regulatory authorities. These notes comprise the following items:

	As at December 31, 2018	As at December 31, 2017
Senior Series G notes (par value of \$900 million), issued on May 5, 2010, maturing in May 2020, bearing interest at an annual rate of 5.187%, redeemable at the option of the issuer.	\$ 879	\$ 898
Senior Series J notes (par value of \$500 million), issued on December 15, 2011, maturing in December 2026, bearing interest at an annual rate of 4.954% for the first 10 years, and for the following 5 years, at an annual rate equal to the 90-day bankers' acceptance rate plus 2.67%, redeemable at the option of the issuer starting in 2021.	499	490
	\$ 1,378	\$ 1,388

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

The hedge accounting disclosures for 2018 presented in this note are in accordance with the disclosure requirements of IFRS 7, "Financial Instruments: Disclosures", which have been effective since January 1, 2018. As permitted by transitional requirements, the comparative information has not been restated and is therefore presented in accordance with the disclosure requirements of IFRS 7 that were effective before January 1, 2018. For more information, see Note 2, "Basis of presentation and significant accounting policies".

### DERIVATIVE FINANCIAL INSTRUMENTS

The Federation's derivative financial instruments include the following types of contracts:

#### Interest rate contracts

Interest rate contracts include swaps, forward rate agreements and futures. Interest rate swaps are transactions in which two parties exchange interest flows on a specified notional amount for a predetermined period based on agreed-upon fixed and floating rates. Principal amounts are not exchanged. Forward rate agreements are forward transactions on interest rates, based on a notional amount, which call for cash settlement at a future date for the difference between the contractual interest rate and the market rate. Futures represent a future commitment to purchase or deliver financial instruments on a later specified date at a specified price. Futures are traded in predetermined amounts on organized exchanges and are subject to daily cash margining. The Federation uses interest rate contracts primarily for asset and liability management purposes.

#### Foreign exchange contracts

Foreign exchange contracts include forward contracts, spot transactions and currency swaps. Forward exchange contracts are commitments to exchange, at a future date, two currencies based on a rate agreed by both parties at the inception of the contract. Spot transactions are similar to forward exchange contracts, except that delivery must be made within two business days following the contract date. Currency swaps and cross-currency interest rate swaps are transactions in which the parties exchange interest payments on notional amounts in different currencies. Principal notional amounts are exchanged upon entering into the transaction and upon maturity. The Federation uses currency swaps and cross-currency interest rate swaps to manage its foreign-currency denominated asset and liability exposures.

#### Other financial derivative contracts

Other derivative financial contracts used by the Federation include total return swaps and stock index options, which are related to financial index transactions, as well as credit default swaps, which are used to manage the credit risk associated with assets and liabilities. Total return swaps are transactions in which one party agrees to pay to or receive from the other party the rate of return on an underlying asset, group of assets or index in exchange for a remuneration specified in the contract. Credit default swaps are transactions in which one of the parties agrees to pay interest to the other party who, in turn, undertakes to make a payment if a predetermined credit incident occurs.

#### Options

Options are contractual agreements under which the seller grants the purchaser the right but not the obligation to buy (call option) or sell (put option) a specified amount of a financial instrument at a predetermined price, on or before a specified date. The seller receives a premium from the purchaser in exchange for this right. The Federation enters into various options, such as interest rate, currency, stock index and commodity options, primarily to meet the needs of its members and clients and to manage its own asset-liability exposures.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES *(continued)*

### MATURITIES AND FAIR VALUE OF DERIVATIVE FINANCIAL INSTRUMENTS

The following table presents the maturities of the notional amounts and the fair value of derivative financial instruments recognized in the Consolidated Balance Sheets.

As at December 31, 2018	Terms to maturity				Notional amount	Carrying amount of derivative financial instruments	
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years		Assets	Liabilities
<b>Designated as hedging instruments<sup>(1)</sup></b>							
<b>Fair value hedges</b>							
<b>Interest rate contracts / Interest rate risk</b>							
Over-the-counter interest rate swaps	\$ 2,029	\$ 4,414	\$ 6,263	\$ 2,182	\$ 14,888	\$ 73	\$ 176
<i>Average rate</i>	2.1%	1.4%	2.2%	2.3%			
	2,029	4,414	6,263	2,182	14,888	73	176
<b>Foreign exchange contracts / Currency risk</b>							
Over-the-counter currency swaps	5,893	6,368	1,173	-	13,434	689	-
<i>CAD-US average rate</i>	1.3347	1.2963	-	-			
<i>CAD-EUR average rate</i>	1.5346	1.5268	1.5202	-			
	5,893	6,368	1,173	-	13,434	689	-
<b>Total – Fair value hedges</b>	<b>7,922</b>	<b>10,782</b>	<b>7,436</b>	<b>2,182</b>	<b>28,322</b>	<b>762</b>	<b>176</b>
<b>Cash flow hedges</b>							
<b>Interest rate contracts / Interest rate risk</b>							
Over-the-counter interest rate swaps	790	1,856	1,971	12	4,629	20	25
<i>Average rate</i>	2.1%	2.0%	2.3%	1.9%			
	790	1,856	1,971	12	4,629	20	25
<b>Total – Cash flow hedges</b>	<b>790</b>	<b>1,856</b>	<b>1,971</b>	<b>12</b>	<b>4,629</b>	<b>20</b>	<b>25</b>
<b>Total – Designated as hedging instruments</b>	<b>\$ 8,712</b>	<b>\$ 12,638</b>	<b>\$ 9,407</b>	<b>\$ 2,194</b>	<b>\$ 32,951</b>	<b>\$ 782</b>	<b>\$ 201</b>

<sup>(1)</sup> Hedging instruments are presented under "Derivative financial instruments" in the Consolidated Balance Sheets.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

The following table presents the maturities of the notional amounts and the fair value of derivative financial instruments recognized in the Consolidated Balance Sheets (continued).

	Terms to maturity				Notional amount	Carrying amount of derivative financial instruments	
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years		Assets	Liabilities
<b>As at December 31, 2018</b>							
<b>Trading purposes<sup>(1)</sup></b>							
<b>Interest rate contracts</b>							
<b>Over-the-counter contracts</b>							
Interest rate swaps	\$ 72,967	\$ 102,114	\$ 54,985	\$ 13,793	\$ 243,859	\$ 1,476	\$ 1,373
Forward rate agreements	3,492	-	-	-	3,492	24	23
<b>Contracts traded through a clearing house</b>							
Interest rate swaps	13,864	14,830	3,868	2,751	35,313	111	118
<b>Exchange-traded contracts</b>							
Futures	8,284	4,816	-	-	13,100	-	-
Options purchased	49,794	-	-	-	49,794	4	-
Options written	36,686	-	30	30	36,746	-	12
	185,087	121,760	58,883	16,574	382,304	1,615	1,526
<b>Foreign exchange contracts</b>							
<b>Over-the-counter contracts</b>							
Forward contracts	28,150	956	49	-	29,155	465	233
Currency swaps	2,350	10	100	450	2,910	111	26
Options purchased	729	147	24	-	900	34	-
Options written	1,050	179	20	-	1,249	-	18
	32,279	1,292	193	450	34,214	610	277
<b>Other contracts<sup>(2)</sup></b>							
<b>Over-the-counter contracts</b>							
Swaps	144	89	117	-	350	6	2
Options purchased	3,461	11,592	10,422	-	25,475	1,363	-
Options written	3,290	10,390	8,937	-	22,617	-	1,326
<b>Contracts traded through a clearing house</b>							
Swaps	-	-	539	-	539	-	-
<b>Exchange-traded contracts</b>							
Futures	941	-	-	-	941	-	-
	7,836	22,071	20,015	-	49,922	1,369	1,328
<b>Total – Trading purposes</b>	225,202	145,123	79,091	17,024	466,440	3,594	3,131
<b>Total derivative financial instruments before impact of master netting agreements</b>	\$ 233,914	\$ 157,761	\$ 88,498	\$ 19,218	\$ 499,391	\$ 4,376	\$ 3,332
Less :							
Impact of master netting agreements <sup>(3)</sup>	-	-	-	-	-	1,903	1,903
<b>Total derivative financial instruments after impact of master netting agreements</b>	\$ 233,914	\$ 157,761	\$ 88,498	\$ 19,218	\$ 499,391	\$ 2,473	\$ 1,429

<sup>(1)</sup> As at December 31, 2018, include derivatives with notional amounts totalling \$516 million that would have been designated as hedging instruments if the Federation had continued to apply IAS 39 to insurance operations financial assets designated for the overlay approach. The impact that the designation of these derivatives as hedging instruments would have had is taken into account in the calculation of the overlay approach adjustment. For more information on the application of the overlay approach, see Note 2, "Basis of presentation and significant accounting policies".

<sup>(2)</sup> Include contracts related to indexed term savings products.

<sup>(3)</sup> Impact of offsetting credit exposure when the Federation holds master netting agreements without the intention of settling on a net basis or simultaneously.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

The following table presents comparative information on the maturities of the notional amounts of derivative financial instruments.

As at December 31, 2017	Terms to maturity				Notional amount
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years	
<b>Interest rate contracts</b>					
<b>Over-the-counter contracts</b>					
Interest rate swaps	\$ 68,509	\$ 95,416	\$ 53,811	\$ 7,016	\$ 224,752
Forward rate agreements	2,258	-	-	-	2,258
Options purchased	1,708	754	-	-	2,462
Options written	400	-	-	-	400
<b>Contracts traded through a clearing house</b>					
Interest rate swaps	2,453	5,796	2,078	224	10,551
<b>Exchange-traded contracts</b>					
Futures	6,512	425	-	-	6,937
Options purchased	8,238	-	-	-	8,238
Options written	7,755	-	-	-	7,755
	97,833	102,391	55,889	7,240	263,353
<b>Foreign exchange contracts</b>					
<b>Over-the-counter contracts</b>					
Forward contracts	22,911	887	37	-	23,835
Currency swaps	6,001	8,575	-	300	14,876
Options purchased	804	98	6	-	908
Options written	770	111	6	-	887
<b>Exchange-traded contracts</b>					
Futures	1	-	-	-	1
	30,487	9,671	49	300	40,507
<b>Other contracts<sup>(1)</sup></b>					
<b>Over-the-counter contracts</b>					
Swaps	-	125	47	-	172
Options purchased	2,910	8,014	9,336	50	20,310
Options written	2,772	7,620	8,053	-	18,445
<b>Contracts traded through a clearing house</b>					
Swaps	-	-	616	-	616
<b>Exchange-traded contracts</b>					
Futures	1,037	-	-	-	1,037
	6,719	15,759	18,052	50	40,580
<b>Total derivative financial instruments</b>	<b>\$ 135,039</b>	<b>\$ 127,821</b>	<b>\$ 73,990</b>	<b>\$ 7,590</b>	<b>\$ 344,440</b>

<sup>(1)</sup> Include contracts related to indexed term savings products.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

The following table presents comparative information on the fair value of derivative financial instruments recognized in the Consolidated Balance Sheets.

As at December 31, 2017	Notional amount	Assets	Liabilities
<b>Designated as hedging instruments</b>			
<b>Fair value hedges</b>			
Interest rate contracts			
Swaps – Other	\$ 14,658	\$ 36	\$ 229
	14,658	36	229
Foreign exchange contracts			
Forward contracts	255	2	-
Currency swaps	10,347	219	101
	10,602	221	101
<b>Total – Fair value hedges</b>	25,260	257	330
<b>Cash flow hedges</b>			
Interest rate contracts			
Swaps	3,644	18	21
<b>Total – Cash flow hedges</b>	3,644	18	21
<b>Total – Designated as hedging instruments</b>	28,904	275	351
<b>Trading purposes</b>			
Interest rate contracts			
Swaps traded through a clearing house	10,550	18	33
Swaps – Other	206,451	1,530	1,327
Forward rate agreements	2,258	19	7
Futures	6,937	-	-
Options purchased	10,700	3	-
Options written	8,155	-	2
	245,051	1,570	1,369
Foreign exchange contracts			
Forward contracts	23,581	154	214
Currency swaps	4,529	6	29
Options purchased	908	9	-
Options written	887	-	21
	29,905	169	264
Other contracts			
Swaps traded through a clearing house	616	13	2
Swaps – Other	172	1	1
Futures	1,037	-	-
Options purchased	20,310	1,744	-
Options written	18,445	-	1,690
	40,580	1,758	1,693
<b>Total – Trading purposes</b>	315,536	3,497	3,326
<b>Total derivative financial instruments before impact of master netting agreements</b>	\$ 344,440	\$ 3,772	\$ 3,677
Less :			
Impact of master netting agreements <sup>(1)</sup>	-	1,883	1,883
<b>Total derivative financial instruments after impact of master netting agreements</b>	\$ 344,440	\$ 1,889	\$ 1,794

<sup>(1)</sup> Impact of offsetting credit exposure when the Federation holds master netting agreements without the intention of settling on a net basis or simultaneously.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

### HEDGING ACTIVITIES

The manner in which the Federation assesses market risks as well as the objectives, policies and methods it uses to manage them are presented in Section 4.0, "Risk Management", of the Management's Discussion and Analysis.

#### Fair value hedges

Fair value hedge transactions involve mostly the use of interest rate swaps to hedge the changes in fair value of a fixed-rate financial instrument caused by a change in interest rates on the market. In addition, when a financial instrument is denominated in a foreign currency, The Federation may enter into fair value hedges by using currency swaps or cross-currency interest rate swaps. The change in fair value of hedging derivative financial instruments offsets the change in fair value of hedged items. The Federation uses fair value hedge strategies for its loan, deposit and securities portfolios.

#### Cash flow hedges

Cash flow hedge transactions involve mostly the use of interest rate swaps to hedge the changes in future cash flows from a floating-rate financial instrument. Hedging derivative financial instruments reduce the variability of future cash flows from the hedged item. The Federation uses cash flow hedge strategies for its loan, deposit and securities portfolios.

#### Effectiveness assessment and sources of hedging relationship ineffectiveness

The Federation assesses the effectiveness of a hedging relationship by comparing the change in fair value or cash flows of the hedging instrument with that of the hedged item attributable to the hedged risk to demonstrate the existence of a highly effective correlation between the two instruments. When derivative financial instruments are designated as hedging instruments for a currency risk, only the change in currency risk is taken into account to assess hedge effectiveness.

There is ineffectiveness when the change in fair value of the hedged item attributable to the hedged risk differs from the change in fair value of the hedging instrument. The main sources of ineffectiveness are a difference between the actual and expected repricing dates, a difference between the discounting factors used and a difference between the payment dates for the hedging instrument and the hedged item.

The following tables present information on the ineffectiveness of fair value and cash flow hedges for the year ended December 31, 2018.

	Gains (losses) on hedging instruments used as the basis for calculating hedge ineffectiveness	Hedge ineffectiveness recognized in profit or loss <sup>(1)</sup>
<b>2018</b>		
<b>Fair value hedges</b>		
Interest rate contracts / Interest rate risk	\$ 68	\$ -
Over-the-counter interest rate swaps		
Foreign exchange contracts / Currency risk		
Over-the-counter currency swaps	570	(10)
<b>Total – Fair value hedges</b>	<b>\$ 638</b>	<b>\$ (10)</b>

<sup>(1)</sup> The hedge ineffectiveness and reclassification adjustment are recognized under "Net investment income".

	Gains (losses) on hedging instruments used as the basis for calculating hedge ineffectiveness	Hedge ineffectiveness recognized in profit or loss <sup>(1)</sup>	Hedging gains (losses) recognized in other comprehensive income	Gains (losses) reclassified from the cash flow hedge reserve into profit or loss	
				Active hedges <sup>(2)</sup>	Terminated hedges <sup>(1)</sup>
<b>2018</b>					
<b>Cash flow hedges</b>					
Interest rate contracts / Interest rate risk					
Over-the-counter interest rate swaps	\$ (1)	\$ -	\$ (15)	\$ (7)	\$ 3
<b>Total – Cash flow hedges</b>	<b>\$ (1)</b>	<b>\$ -</b>	<b>\$ (15)</b>	<b>\$ (7)</b>	<b>\$ 3</b>

<sup>(1)</sup> The hedge ineffectiveness and reclassification adjustment are recognized under "Net investment income".

<sup>(2)</sup> The reclassification adjustment is included under "Interest income – Loans" and "Interest expense – Deposits".

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

The following table presents the impact of hedge accounting on balances recognized in the Consolidated Balance Sheets and in accumulated other comprehensive income as at December 31, 2018.

	Cash flow hedges			Fair value hedges			
	Balance of the cash flow hedge reserve	Balance of the reserve for discontinued hedges	Gains (losses) on hedged items used as the basis for calculating hedge ineffectiveness for the year	Carrying amount of the hedged item	Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item	Accumulated amount of fair value hedge adjustments for any hedged items that have ceased to be adjusted	Gains (losses) on hedged items used as the basis for calculating hedge ineffectiveness for the year
<b>Interest rate risk</b>							
<b>Assets</b>							
Securities	\$ 1	\$ (2)	\$ (2)	\$ 177	\$ -	\$ -	\$ 1
Loans	(5)	1	(4)	1,452	(12)	-	7
<b>Liabilities</b>							
Deposits	(2)	-	7	12,942	137	2	(76)
<b>Currency risk</b>							
<b>Liabilities</b>							
Deposits	\$ -	\$ -	\$ -	\$ 13,428	\$ 16	\$ -	\$ (579)

The comparative information presented in the following tables has been prepared in accordance with the disclosure requirements of IFRS 7 that were effective before January 1, 2018.

The following table presents comparative information on the ineffectiveness of fair value and cash flow hedges, namely the gross amounts related to the ineffectiveness of fair value hedges and the amounts related to the ineffectiveness of cash flow hedges that were recognized under "Net investment income" in the Consolidated Statement of Income for the year ended December 31, 2017.

	2017
Gains on hedged items	\$ 728
Losses on derivative instruments	(740)
<b>Fair value hedge ineffectiveness</b>	\$ (12)
<b>Cash flow hedge ineffectiveness</b>	\$ (1)

The following tables present the comparative information as at December 31, 2017 on the expected date of occurrence of hedged cash flows.

2017	Terms to maturity				
	Under 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years	Total
Cash inflows (assets)	\$ 32	\$ 50	\$ 21	\$ 1	\$ 104
Cash outflows (liabilities)	27	58	18	-	103
<b>Net cash flows</b>	\$ 5	\$ (8)	\$ 3	\$ 1	\$ 1

The net impact on excess cash flows related to interest is recognized using the effective interest method over the life of the underlying instrument. During the year ended December 31, 2017, the main hedging transactions occurred as expected.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (continued)

### DERIVATIVE FINANCIAL INSTRUMENTS – CREDIT RISK

The credit risk associated with derivative financial instruments refers to the risk that a counterparty will fail to honour its contractual obligations toward the Federation at a time when the fair value of the instrument is positive for the Federation. The manner in which the Federation assesses this risk as well as the objectives, policies and methods it uses to manage it are presented in Section 4.0, "Risk Management", of the Management's Discussion and Analysis. The shaded areas containing text and tables presented in that section are an integral part of these Consolidated Financial Statements.

<b>Notional amount</b>	Contract amount to which a rate or price is applied in order to calculate the exchange of cash flows.
<b>Replacement cost</b>	The cost of replacing, at current market rates, all contracts with a positive fair value, without taking into consideration the impact of netting agreements or any collateral which may be obtained.
<b>Credit risk equivalent</b>	The total of the replacement cost and future credit exposure, which is represented by the change in value determined using a formula prescribed by the Bank for International Settlements (BIS), excluding items prescribed by the BIS, such as the replacement cost of forward exchange contracts with an original maturity of less than 14 days and exchange-traded derivatives subject to daily cash margining.
<b>Risk-weighted balance</b>	The balance weighted by the risk related to the creditworthiness of the counterparty calculated at the rates prescribed by the BIS.

The following table gives an overview of the Federation's derivative financial instruments portfolio and related credit risk, before and after the impact of master netting agreements.

	As at December 31, 2018				As at December 31, 2017			
	Notional amount	Replacement cost	Credit risk equivalent	Risk-weighted balance	Notional amount	Replacement cost	Credit risk equivalent	Risk-weighted balance
<b>Interest rate contracts</b>								
Interest rate swaps	\$ 298,689	\$ 1,681	\$ 2,858	\$ 981	\$ 235,303	\$ 1,602	\$ 2,481	\$ 887
Forward rate agreements	3,492	24	38	38	2,258	19	41	41
Futures	13,100	-	-	-	6,937	-	-	-
Options purchased	49,794	2	5	2	10,700	3	5	2
Options written	36,746	-	-	-	8,155	-	-	-
	401,821	1,707	2,901	1,021	263,353	1,624	2,527	930
<b>Foreign exchange contracts</b>								
Forward contracts	29,155	466	612	225	23,836	156	429	228
Currency swaps	16,344	800	1,265	361	14,876	225	736	234
Options purchased	900	34	8	6	908	9	22	14
Options written	1,249	-	-	-	887	-	-	-
	47,648	1,300	1,885	592	40,507	390	1,187	476
<b>Other contracts</b>								
Swaps	890	6	4	1	788	14	22	3
Futures	941	-	-	-	1,037	-	-	-
Options purchased	25,474	1,363	3,342	1,290	20,310	1,744	3,324	1,109
Options written	22,617	-	-	-	18,445	-	-	-
	49,922	1,369	3,346	1,291	40,580	1,758	3,346	1,112
<b>Total derivative financial instruments before impact of master netting agreements</b>	<b>\$ 499,391</b>	<b>\$ 4,376</b>	<b>\$ 8,132</b>	<b>\$ 2,904</b>	<b>\$ 344,440</b>	<b>\$ 3,772</b>	<b>\$ 7,060</b>	<b>\$ 2,518</b>
Less:								
Impact of master netting agreements <sup>(1)</sup>	-	1,903	-	820	-	1,883	-	858
<b>Total derivative financial instruments after impact of master netting agreements</b>	<b>\$ 499,391</b>	<b>\$ 2,473</b>	<b>\$ 8,132</b>	<b>\$ 2,084</b>	<b>\$ 344,440</b>	<b>\$ 1,889</b>	<b>\$ 7,060</b>	<b>\$ 1,660</b>

<sup>(1)</sup> Impact of offsetting credit exposure when the Federation holds master netting agreements without the intention of settling on a net basis or simultaneously.

## NOTE 19 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES *(continued)*

The following table presents derivative financial instruments by credit risk rating and type of counterparty.

	As at December 31, 2018		As at December 31, 2017	
	Replacement cost	Risk-weighted balance	Replacement cost	Risk-weighted balance
Credit risk rating <sup>(1)</sup>				
AAA, AA+, AA, AA-	\$ 2,975	\$ 1,755	\$ 2,524	\$ 1,409
A+, A, A-	955	989	1,128	824
BBB, B, BB-, BBB-	70	32	47	112
Not rated	376	128	73	173
<b>Total</b>	<b>4,376</b>	<b>2,904</b>	<b>3,772</b>	<b>2,518</b>
Less:				
Impact of master netting agreements <sup>(2)</sup>	1,903	820	1,883	858
<b>Total after impact of master netting agreements</b>	<b>\$ 2,473</b>	<b>\$ 2,084</b>	<b>\$ 1,889</b>	<b>\$ 1,660</b>
Type of counterparty				
Financial institutions	\$ 3,390	\$ 2,247	\$ 3,041	\$ 1,748
Other	986	657	731	770
<b>Total</b>	<b>4,376</b>	<b>2,904</b>	<b>3,772</b>	<b>2,518</b>
Less:				
Impact of master netting agreements <sup>(2)</sup>	1,903	820	1,883	858
<b>Total after impact of master netting agreements</b>	<b>\$ 2,473</b>	<b>\$ 2,084</b>	<b>\$ 1,889</b>	<b>\$ 1,660</b>

<sup>(1)</sup> Credit risk ratings are established by recognized credit agencies. Non-rated counterparties are mainly member caisses or clients of the Federation.

<sup>(2)</sup> Impact of offsetting credit exposure when the Federation holds master netting agreements without the intention of settling on a net basis or simultaneously.

## NOTE 20 – SIGNIFICANT TRANSACTIONS

### Year ended December 31, 2018

On April 1, 2018, the Federation and a partnership comprised of five provincial credit union centrals (the Centrals) and The CUMIS Group completed an agreement to merge their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments LP. This transaction resulted in the creation of Aviso Wealth, a wealth management company, in which the Federation and the partnership formed by the Centrals and The CUMIS Group each hold a 50% interest.

The Federation's interest in Aviso Wealth, amounting to \$332 million as at April 1, 2018, is an interest in a joint venture and is accounted for using the equity method in the Wealth Management and Life and Health Insurance segment.

The assets and liabilities transferred by the Federation at the time Aviso Wealth was created were as follows:

	As at April 1, 2018
<b>Assets disposed of</b>	
Cash and deposits with financial institutions	\$ 14
Securities at fair value through profit or loss	82
Amounts receivable from clients, brokers and financial institutions	630
Property, plant and equipment	2
Goodwill	32
Intangible assets	61
Deferred tax assets	1
Other assets	96
<b>Total assets disposed of</b>	<b>\$ 918</b>
<b>Liabilities disposed of</b>	
Deferred tax liabilities	\$ 14
Amounts payable to clients, brokers and financial institutions	682
Other liabilities	22
<b>Total liabilities disposed of</b>	<b>\$ 718</b>

A gain of \$132 million on this transaction was recognized under "Other income – Other" in the Consolidated Statement of Income for the year ended December 31, 2018.

The operations of the Qtrade Canada Inc. subsidiary and the interest in the Northwest & Ethical Investments LP associate were presented in the Wealth Management and Life and Health Insurance segment.

### Year ended December 31, 2017

On July 1, 2017, the Federation completed the sale of two of its subsidiaries, Western Financial Group Inc., a financial services company and Western Life Assurance Company, a life and health insurance company, to Trimont Financial Ltd., a subsidiary of the Wawanesa Mutual Insurance Company.

The assets and liabilities of the two subsidiaries disposed of were as follows as at the date of disposal.

	As at July 1, 2017
<b>Net assets disposed of</b>	
Cash and deposits with financial institutions	\$ 82
Securities at fair value through profit or loss	123
Available-for-sale securities	59
Amounts receivable from clients, brokers and financial institutions	17
Reinsurance assets	55
Property, plant and equipment	17
Goodwill	293
Intangible assets	155
Deferred tax assets	3
Other assets	110
Insurance contract liabilities	(161)
Deferred tax liabilities	(40)
Other liabilities	(288)
	<b>\$ 425</b>
<b>Proceeds from disposal</b>	
Cash	\$ 722
Less: Costs directly attributable to the disposal	19
<b>Net proceeds from disposal</b>	<b>\$ 703</b>

A gain of \$278 million on the disposal of these subsidiaries was recognized under "Other income – Other" in the Consolidated Statement of Income for the year ended December 31, 2017.

The operations of these two subsidiaries were presented in the Property and Casualty Insurance segment.

## NOTE 21 – CAPITAL STOCK

### AUTHORIZED

The capital stock of the Federation comprises the following qualifying shares and capital shares:

There is an unlimited number of qualifying shares with a par value of \$5. These shares may be issued only to members of the Federation and are redeemable only at the Board of Directors' option under certain conditions stipulated in the by-law.

There is an unlimited number of A and G capital shares with a par value of \$5 and an unlimited number of F capital shares and contingent Z-capital shares (Z capital shares) with a par value of \$10. The A and G shares may be issued only to members of the Federation, while F capital shares may be issued only to members of Desjardins caisses in Quebec, including their auxiliary members. Z capital shares may be issued to any person in accordance with the Act, but only for converting non-viability contingent capital instruments of the Federation or at the discretion of the Federation after such conversion. The Federation has the right, by resolution of the Board of Directors and with the authorization of the AMF, to redeem unilaterally, in whole or in part, A, G, F and Z capital shares, if any, at any time. The Federation may also purchase, in whole or in part, A, G, F and Z capital shares, if any, by private agreement, at any time, with the authorization of the AMF. Furthermore, the A and G capital shares may be converted, at any time, by a resolution of the Board of Directors, in whole or in part, into another category of shares issued for this purpose. As of the year ended December 31, 2018, the interest rate on A, G, F and Z capital shares, if any, is determined by the Federation's Board of Directors which approves annually the surplus earnings that may be allocated to the payment of interest on these capital shares. Previously, it was determined by the Federation's Board of Directors and the general meeting approved the surplus earnings that may allocated to the payment of interest. The repayment of principal and payment of interest on the A, G, F and Z capital shares, if any, are subject to compliance with certain conditions.

There is an unlimited number of FIN-5A, INV, and SER capital shares related to an investment fund. These shares may be issued only to members of the Federation; they have no par value and do not bear interest. Subject to provisions of the Federation's own by-law, the holders of these shares divide up the net income of the funds. These shares are redeemable, with the authorization of the AMF, at the option of the Board of Directors or by private agreement. Furthermore, they may be converted, by a resolution of the Board of Directors, in whole or in part, into another category of shares issued for this purpose.

The qualifying share and the capital shares of the Federation do not entitle their holders to be called, participate or vote at the Federation members meetings.

### SHARES ISSUED AND PAID

(in thousands of dollars)	As at December 31, 2018		As at December 31, 2017	
	Number of shares	Amount	Number of shares	Amount
Qualifying shares	32,600	\$ 163	32,810	\$ 164
A capital shares	13,789,467	68,947	13,789,467	68,947
F capital shares	478,768,270	4,766,943	452,125,823	4,501,237
G capital shares	600,532,931	3,002,665	600,532,931	3,002,665
INV capital shares	47,856,914	-	47,856,914	18,946
SER capital shares	2,865,680	23,395	2,865,680	23,395
FED-7 capital shares	-	-	1,084,566	4,676
FIN-5A capital shares	694,258,599	916,974	694,258,599	916,974
		<b>\$ 8,779,087</b>		<b>\$ 8,537,004</b>

### ISSUANCE OF SHARES

During the year ended December 31, 2018, the Federation issued 12,433,692 F capital shares for a cash consideration of \$124 million, which represents the gross proceeds of this issuance of \$125 million less issue costs of \$1 million. In addition, the Federation issued 14, 208, 755 F capital shares having a value of \$142 million as interest payments when the holders elected to receive their remuneration in F capital shares.

In 2017, the Federation had issued 24,967,040 F capital shares for a cash consideration of \$249 million, which represents the gross proceeds of this issuance of \$250 million less issue costs of \$1 million. In addition, the Federation had issued 12, 535, 746 F capital shares having a value of \$125 million as interest payments when the holders elected to receive their remuneration in F capital shares. It had also issued 4,925,420 A capital shares for a cash consideration of \$25 million and 14,459,580 G capital shares for a cash consideration of \$72 million.

### CONVERSION OF SHARES

In 2017, the Federation had converted all CCD capital shares into 586,073,351 G capital shares. This conversion had no impact on the value of capital stock.

### REDEMPTION OF SHARES

During the year ended December 31, 2018, the Federation redeemed for cancellation all FED-7 capital shares for a cash consideration of \$2 million. It also redeemed 210 qualifying shares for an immaterial cash consideration.

In 2017, the Federation had redeemed 190 qualifying shares for an immaterial cash consideration.

## NOTE 22 – ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table presents the main components of “Accumulated other comprehensive income” (net of taxes).

	As at December 31, 2018		As at December 31, 2017	
	Group's share	Non-controlling interests' share	Group's share	Non-controlling interests' share
<b>Items that will be reclassified subsequently to the Consolidated Statements of Income</b>				
Net unrealized gains on available-for-sale securities	N/A	N/A	\$ 446	\$ 21
Net unrealized gains (losses) on debt securities classified as at fair value through other comprehensive income <sup>(1)</sup>	\$ 14	\$ (1)	N/A	N/A
Net unrealized losses related to the overlay approach adjustment for insurance operations financial assets	(17)	(2)	N/A	N/A
Net gains (losses) on derivative financial instruments designated as cash flow hedges	(7)	-	11	-
Net unrealized exchange gains on the translation of a net investment in a foreign operation, net of hedging transactions	1	-	1	-
<b>Accumulated other comprehensive income</b>	<b>\$ (9)</b>	<b>\$ (3)</b>	<b>\$ 458</b>	<b>\$ 21</b>

<sup>(1)</sup> Including an allowance for credit losses of \$2 million on securities classified as at fair value through other comprehensive income.

## NOTE 23 – CAPITAL MANAGEMENT

Capital management is a crucial element of financial management covering all Desjardins Group operations, including those of the Federation. Accordingly, the description of the Federation's capital management and the manner in which it meets its capital management objectives is derived from the orientation followed for all Desjardins Group operations. The goal of capital management at Desjardins Group is to ensure that a sufficient level of high-quality capital is maintained for the following reasons: to have flexibility for its development, to maintain favourable credit ratings and to maintain the confidence of depositors and financial markets. Capital is managed in accordance with the Desjardins Group capital management policy approved by the Federation's Board of Directors.

### DESJARDINS GROUP'S INTEGRATED CAPITAL MANAGEMENT FRAMEWORK

The regulatory capital adequacy and composition of the Federation are evaluated using the guideline on adequacy of capital base standards applicable to financial services cooperatives (the guideline) issued by the AMF, which is derived from the normative framework developed by the Basel Committee on Banking Supervision. The holding company Desjardins Financial Corporation Inc. is subject to the guideline on capital adequacy requirements for life and health insurers issued by the AMF. Consequently, for purposes of calculating capital, the holding company Desjardins Financial Corporation Inc., which mainly holds the insurance companies, is deconsolidated and partly deducted from capital, in accordance with the significant investments rules set out in the guideline.

Some of the Federation's subsidiaries are subject to regulatory requirements issued by the AMF or other regulatory authorities. Most of these subsidiaries must comply with minimum capital requirements. Desjardins Group monitors and manages these entities' capital requirements to ensure capital is effectively used and regulations are complied with on an ongoing basis.

### BASEL III

The Federation's capital ratios are calculated according to the guideline and are expressed as regulatory capital as a percentage of risk-weighted assets. The Federation must maintain a minimum Tier 1A capital ratio of 8.0%. Its Tier 1 capital ratio and total capital ratio must be above 9.5% and 11.5%, respectively.

## NOTE 23 – CAPITAL MANAGEMENT *(continued)*

The regulatory capital of the Federation differs from the equity disclosed in the Consolidated Balance Sheets. It comprises the following components:

- i) Tier 1 capital, which is designed to ensure going concern. It comprises two categories: Tier 1A (core capital) and Tier 1B (additional capital). Tier 1A capital consists, among other items, of eligible capital shares, reserves, undistributed surplus earnings and accumulated other comprehensive income. Tier 1B capital consists of non-controlling interests. Non-controlling interests are determined, in particular, based on the nature of the operations and the capitalization of the investee.
- ii) Tier 2 capital, which is designed to absorb losses in the event of a liquidation. It consists of subordinated notes, eligible qualifying shares and the eligible portion of the collective allowance.

The Federation is required by the AMF to meet a minimum leverage ratio of 3%. This ratio is determined by dividing Tier 1 capital by the exposure measure. The exposure measure is independent from risk and includes: 1) on-balance sheet exposures; 2) securities financing transaction exposures; 3) derivative exposures; and 4) off-balance sheet exposures.

The following table presents the Federation's regulatory capital, risk-weighted assets and capital ratios.

(in millions of dollars and as a percentage)	As at December 31, 2018	As at December 31, 2017
<b>Capital</b>		
Tier 1A capital	\$ 9,897	\$ 9,162
Tier 1 capital	9,897	9,162
Total capital	9,897	9,162
<b>Risk-weighted assets for capital calculation purposes</b>		
For Tier 1A capital	63,106	52,364
For Tier 1 capital	63,150	52,409
For total capital	63,193	52,445
<b>Risk-weighted assets for total capital calculation purposes</b>		
Credit risk <sup>(1)</sup>	49,216	42,336
Market risk	5,396	1,965
Operational risk	8,581	8,143
<b>Total risk-weighted assets</b>	<b>\$ 63,193</b>	<b>\$ 52,444</b>
<b>Ratios and leverage ratio exposure</b>		
Tier 1A capital	15.7%	17.5%
Tier 1 capital	15.7	17.5
Total capital	15.7	17.5
Leverage	7.4	7.9
Leverage ratio exposure	<b>\$ 134,198</b>	<b>\$ 115,915</b>

<sup>(1)</sup> The scaling factors used to take into account the requirements for the CVA charge have been phased in since January 1, 2014 to calculate the Tier 1A, Tier 1 and total capital ratios. They were respectively 80%, 83% and 86% in 2018 (72%, 77% and 81% in 2017) and will reach 100% for each capital tier by 2019.

### COMPLIANCE WITH REQUIREMENTS

The Federation and its subsidiaries that are subject to regulatory requirements with respect to minimum capital were in compliance with said requirements as at December 31, 2018, as they were in the previous year.

## NOTE 24 – NET INTEREST INCOME AND NET INVESTMENT INCOME

The information presented in the following tables has been prepared in accordance with IFRS 9 for the year ended December 31, 2018 and in accordance with IAS 39 for the year ended December 31, 2017. For more information, see Note 2, "Basis of presentation and significant accounting policies".

### NET INTEREST INCOME

The following table presents the breakdown of net interest income according to the classification of financial assets and liabilities.

For the year ended December 31	2018
<b>Interest income on financial assets</b>	
At amortized cost	\$ 2,624
At fair value through other comprehensive income	166
At fair value through profit or loss	37
	<b>2,827</b>
<b>Interest expense on financial liabilities</b>	
At amortized cost	1,326
	<b>\$ 1,501</b>

### NET INVESTMENT INCOME

The following table presents the breakdown of investment income and loss according to the classification of financial assets and liabilities.

For the year ended December 31	2018		
	Interest income and expense	Fair value gains (losses) and other	Total
<b>Net investment income on financial assets and liabilities</b>			
Classified as at fair value through profit or loss	\$ 371	\$ (625)	\$ (254)
Designated as at fair value through profit or loss	505	(446)	59
Classified as at fair value through other comprehensive income	136	(14)	122
At amortized cost and other	144	99	243
	<b>\$ 1,156</b>	<b>\$ (986)</b>	<b>\$ 170</b>

The comparative information presented in the following tables has been prepared in accordance with IAS 39.

### FINANCIAL INSTRUMENTS HELD FOR TRADING

The following table presents the impact of income from financial instruments held for trading on the Consolidated Statements of Income.

For the year ended December 31	2017
<b>Income</b>	
Net interest income	\$ 40
Net investment income	44
	<b>\$ 84</b>

### FINANCIAL INSTRUMENTS DESIGNATED AS AT FAIR VALUE THROUGH PROFIT OR LOSS

The following table presents the impact of income from financial instruments designated as at fair value through profit or loss on the Consolidated Statements of Income.

For the year ended December 31	2017
<b>Income</b>	
Net interest income	\$ 10
Net investment income	1,114
	<b>\$ 1,124</b>

For the year ended December 31, 2017, net income on available-for-sale securities of \$405 million was included in profit or loss under "Net investment income" in the Consolidated Statement of Income.

## NOTE 25 – NON-INTEREST EXPENSE – OTHER

For the years ended December 31, “Non-interest expense – Other” presented in the Consolidated Statements of Income consisted of the following:

	2018	2017
Commissions	\$ 774	\$ 794
Recovery of expenses related to reinsurance	(73)	(133)
Professional fees	567	528
Business and capital taxes	322	312
Other employee expenses	108	106
Amortization of intangible assets	89	94
Sponsorships and donations	44	30
Other	703	637
	\$ 2,534	\$ 2,368

## NOTE 26 – INCOME TAXES ON SURPLUS EARNINGS

### INCOME TAXES ON SURPLUS EARNINGS FOR THE YEAR

The income tax expense (recovery) recognized in the Consolidated Financial Statements for the years ended December 31 is detailed as follows:

	2018	2017
<b>Consolidated Statements of Income</b>		
Current income taxes		
Current income tax expense on surplus earnings	\$ 412	\$ 286
Adjustments for current tax of prior years	(11)	(3)
Current tax recovery on remuneration on capital stock	(136)	-
Tax recovery on dividends to member caisses	(19)	(16)
	246	267
Deferred income taxes		
Origination and reversal of temporary differences	(58)	55
Changes in tax rates	1	(2)
	(57)	53
	\$ 189	\$ 320
<b>Consolidated Statements of Comprehensive Income</b>		
Current income taxes	\$ (127)	\$ 13
Deferred income taxes	35	(67)
	(92)	(54)
<b>Total income tax expense</b>	\$ 97	\$ 266

Income taxes on surplus earnings presented in the Consolidated Statements of Income for the years ended December 31 are detailed as follows:

	2018	2017
Income taxes on surplus earnings	\$ 208	\$ 336
Tax recovery on dividends to member caisses	(19)	(16)
<b>Income taxes on surplus earnings</b>	\$ 189	\$ 320

### TAX RATE RECONCILIATION

The income tax expense (recovery) on surplus earnings recognized in the Consolidated Statements of Income for the years ended December 31 differs from the income tax expense (recovery) determined using the Canadian statutory rate for the following reasons:

	2018	2017
Income taxes at the combined Canadian federal and provincial statutory rate of 26.83% (26.79% in 2017)	\$ 399	\$ 453
Non-taxable investment income and other items	(93)	(73)
Changes in tax rates	1	(2)
Non-deductible expenses	4	7
Adjustment for current tax of prior years	(11)	(3)
Tax recovery on remuneration on capital stock	(136)	(44)
Tax rate differential applicable to the gain on disposal of subsidiaries	2	(47)
Other	23	29
	\$ 189	\$ 320

## NOTE 26 – INCOME TAXES ON SURPLUS EARNINGS (continued)

### DEFERRED INCOME TAXES

The deferred income tax sources are as follows:

	Consolidated Balance Sheets		Consolidated Statements of Income	
	As at December 31, 2018	As at December 31, 2017	2018	2017
<b>Deferred tax assets</b>				
Insurance contract liabilities	\$ -	\$ 9	\$ 9	\$ 5
Allowance for credit losses	133	30	(26)	2
Net defined benefit plan liabilities	419	462	7	(1)
Tax losses	168	96	(84)	32
Other	175	171	9	(6)
	<b>895</b>	<b>768</b>	<b>(85)</b>	<b>32</b>
<b>Deferred tax liabilities</b>				
Property, plant and equipment and investment property	164	154	10	(4)
Securities and other financial instruments	64	72	(7)	25
Insurance contract liabilities	25	-	25	-
	<b>253</b>	<b>226</b>	<b>28</b>	<b>21</b>
<b>Net deferred income tax assets</b>	<b>\$ 642</b>	<b>\$ 542</b>	<b>\$ (57)</b>	<b>\$ 53</b>

For the purposes of presenting the Consolidated Balance Sheets, deferred tax assets and liabilities are measured by legal entities and presented as follows:

	As at December 31, 2018	As at December 31, 2017
Deferred tax assets <sup>(1)</sup>	\$ 896	\$ 746
Deferred tax liabilities <sup>(1)</sup>	254	204
	<b>\$ 642</b>	<b>\$ 542</b>

<sup>(1)</sup> Deferred income taxes will reverse mainly in the long term.

There were no deductible temporary differences, tax losses and tax credits for which no deferred tax assets have been recognized in the Consolidated Balance Sheets as at December 31, 2018 and 2017.

## NOTE 27 – COMMITMENTS, GUARANTEES AND CONTINGENT LIABILITIES

### COMMITMENTS AND FINANCIAL GUARANTEES

In the normal course of operations, the Federation uses credit instruments and off-balance sheet guarantees to meet the financing needs of its member caisses and clients. The following table shows the contractual amount of commitments as well as the maximum potential amount of future payments under the guarantees that the Federation granted to third parties. The maximum credit risk associated with commitments corresponds to the full amount of additional credit that the Federation could be required to grant if commitments were entirely used. The maximum credit risk associated with guarantees corresponds to the maximum cash outflows that the Federation could be required to make in the event of a complete default by the parties to the guarantees, without taking into account the amounts it could possibly recover through collateral held, insurance policies or other credit risk mitigation methods. These commitments and guarantees do not necessarily represent future cash requirements since many of these instruments will expire or terminate without being funded. In both cases, the maximum risk of loss is substantially greater than the amount recognized in the Consolidated Balance Sheets.

The amounts shown in the following table represent the maximum exposure to credit risk for financial instruments whose maximum risk differs from the value recognized. Other financial instruments presented in the Consolidated Balance Sheets expose the Federation to a credit risk. For such instruments, the maximum exposure to credit risk is equal to their carrying amount.

	As at December 31, 2018	As at December 31, 2017
Commitments		
Credit commitments	\$ 107,415	\$ 95,285
Indemnification commitments related to securities lending	2,474	2,024
Documentary letters of credit	1	1
Financial guarantees		
Guarantees and standby letters of credit	847	667
Credit default swaps	537	540

#### Credit commitments

Credit commitments represent unused portions of authorizations to extend credit in the form of loans, guarantees or letters of credit. The primary purpose of these instruments is to ensure that member caisses and clients have funds available, when necessary, for variable maturity terms and under specific conditions.

#### Indemnification commitments related to securities lending

As part of its asset custody operations, the Federation enters into securities lending agreements with clients. The Federation makes indemnification commitments to certain clients who lend securities to ensure that the fair value of the securities lent will be reimbursed in the event that the borrower does not return the borrowed securities and the fair value of assets held as collateral is insufficient to cover the fair value of the securities lent. These commitments usually mature before being used.

The borrower must secure the loan at all times with marketable securities generally issued by the federal or provincial governments and representing 102% of the contractual amount. There is a risk of loss if the borrower defaults on its commitments and the value of the collateral is not adequate to cover the amount of the loan. To limit this risk, the value of the collateral pledged by the borrower is adjusted on a daily basis, which ensures a sufficient coverage.

#### Documentary letters of credit

Documentary letters of credit are instruments issued for a client and represent the Federation's agreement to honour drafts presented by a third party upon completion of certain activities, up to a set maximum amount. The Federation is exposed to the risk that the client does not ultimately pay the amount of the drafts. However, the amounts used are secured by the related goods.

#### Guarantees and standby letters of credit

Guarantees and standby letters of credit represent irrevocable commitments by the Federation to make payments in the event that a client cannot meet financial obligations to third parties. The Federation's policy with respect to collateral received for these instruments is generally the same as for loans.

#### Credit default swaps

In the normal course of its investment operations, the Federation entered into credit default swaps and undertook to assume the credit risk for the bonds that constitute the underlying assets for these swaps. The guarantee given is to provide partial or total payment for one security or a group of securities in the event of a payment default by the issuer.

The maximum amount of the guarantee is equal to the notional amount of the swap. The amounts that could be required to be paid depend on the nature of the default and the recovery rates of the securities in collection.

## NOTE 27 – COMMITMENTS, GUARANTEES AND CONTINGENT LIABILITIES (*continued*)

### Other indemnification agreements

In the normal course of its operations, the Federation enters into agreements containing indemnification provisions. These indemnifications are normally related to acquisition, disposal, service and lease contracts, clearing agreements and contracts entered into with directors or officers. Under these agreements, the Federation may be liable for indemnifying a counterparty if certain events occur, such as amendments to statutes and regulations (including tax rules) as well as to disclosed financial positions, the existence of undisclosed liabilities, and losses resulting from third-party activities or as a result of third-party litigation. The indemnification provisions vary from one contract to the next. In several cases, no predetermined amount or limit is stated in the contract, and future events that would trigger a payment are difficult to foresee. Therefore, the maximum amount that the Federation could be required to pay counterparties cannot be estimated. In the past, payments made under these indemnification agreements have been immaterial.

### ASSETS PLEDGED AND HELD AS COLLATERAL

In the normal course of its operations, the Federation enters into asset pledge agreements and receives from its clients assets as collateral that it is permitted to sell or repledge in the absence of default in accordance with the standardized terms and conditions for these types of transactions. Following are examples of terms and conditions for assets pledged as collateral:

- The risks and rewards of the assets pledged as collateral accrue to the borrower;
- Additional collateral is required when the market value of the transaction exceeds the threshold agreed upon with the borrower;
- The creditor's right to sell the assets or repledge them depends on the agreement under which the assets have been pledged as collateral;
- The assets pledged as collateral are returned to the borrower when mandatory terms and conditions are met. When the creditor is permitted to sell or repledge an asset held as collateral, a comparable asset is returned to the borrower.

The following table shows the carrying amount of the Federation's financial assets pledged as collateral for liabilities or contingent liabilities as well as the fair value of assets from third parties held as collateral or repledged.

	As at December 31, 2018	As at December 31, 2017
<b>Financial assets of the Federation pledged as collateral:</b>		
Cash and deposits with financial institutions	\$ 63	\$ 42
Securities	19,340	14,641
Loans	4,149	3,534
Other	1	1
	<b>23,553</b>	<b>18,218</b>
<b>Assets from third parties:</b>		
Assets held as collateral that may be sold or repledged	14,658	11,563
Less: Assets not sold or not repledged	4,123	1,861
	<b>10,535</b>	<b>9,702</b>
	<b>\$ 34,088</b>	<b>\$ 27,920</b>
<b>Use of assets</b>		
Transactions involving commitments related to securities sold under repurchase agreements and securities lent and borrowed	\$ 16,617	\$ 11,781
Transactions involving commitments related to securities sold short	10,193	9,237
Securitization transactions	42	34
Transactions on derivative financial instruments	197	137
Clearing systems, payment systems and depositories <sup>(1)</sup>	4,916	4,067
Transactions involving provisions for claims and adjustment expenses <sup>(2)</sup>	1,918	2,501
Caisse network money supply from the Bank of Canada	205	163
	<b>\$ 34,088</b>	<b>\$ 27,920</b>

<sup>(1)</sup> In the normal course of its operations, the Federation must pledge intraday collateral to the Bank of Canada for the use of the Large Value Transfer System. Such collateral is excluded as it is released back at the end of the daily settlement cycle.

<sup>(2)</sup> Represent securities pledged as collateral in connection with the reinsurance treaty that transferred, at the date of acquisition, the property and casualty insurance contract liabilities of the Canadian businesses of State Farm to the Federation.

### LITIGATION

In the normal course of its business, the Federation is involved in various litigation matters and legal proceedings. It is not currently possible to predict the outcome of certain of these litigation matters and legal proceedings, the timing of such outcomes, or the potential impact on the financial position of the Federation. In management's opinion, the fair value of the contingent liabilities resulting from such litigation matters and legal proceedings, to the extent that it can be measured, could have an impact on the profit or loss of the Federation for a specific period, but would not have a significant adverse impact on its financial position.

## NOTE 28 – LEASES

### LEASES – AS LESSEE

#### Operating leases

The minimum future commitments under leases for premises and equipment for the years ended December 31 are presented in the following table.

	2018	2017
Under 1 year	\$ 42	\$ 45
1 to 5 years	132	142
Over 5 years	168	212
<b>Total minimum future commitments</b>	<b>\$ 342</b>	<b>\$ 399</b>

Lease payments recognized as expenses for the year ended December 31, 2018 totalled \$46 million (\$53 million in 2017).

### LEASES – AS LESSOR

#### Operating leases

For the years ended December 31, future minimum lease payments to be received under non-cancellable leases for premises and equipment are as follows:

	2018	2017
Under 1 year	\$ 82	\$ 63
1 to 5 years	240	188
Over 5 years	390	366
<b>Total future minimum payments</b>	<b>\$ 712</b>	<b>\$ 617</b>

No contingent rents were recognized as income for the years ended December 31, 2018 and 2017.

## NOTE 29 – FINANCIAL INSTRUMENT RISK MANAGEMENT

The Federation and its subsidiaries are exposed to different types of financial instrument risks in the normal course of operations, such as credit risk, market risk and liquidity risk. The manner in which the Federation assesses these risks as well as the objectives, policies and methods it uses to manage them are presented in Section 4.0, "Risk Management", of the Management's Discussion and Analysis. The shaded areas and tables marked with an asterisk (\*) presented in that section are an integral part of these Consolidated Financial Statements. . In addition, as a result of adopting IFRS 9 on January 1, 2018, information on credit risk related to the recognition and measurement of expected credit losses are presented in these Consolidated Financial Statements, mainly in Note 2, "Basis of presentation and significant accounting policies", and in Note 7, "Loans and allowance for credit losses".

## NOTE 30 – INTEREST RATE SENSITIVITY AND MATURITY MATCHING

The following table presents the exposure to interest rate risk. Financial instruments are presented based on their maturity date or repricing date, whichever is earlier. Certain maturity or contractual repricing dates may be adjusted based on behavioural assumptions with respect to early repayment or redemption. In addition, certain financial instruments are presented in the "Non-interest-sensitive and provisions" column while they are actually managed using a different risk profile. Behavioural assumptions and models are internally developed using historical analyses, among others.

	Floating rate	Under 3 months	3 to 6 months	Over 6 to 12 months	Over 1 to 5 years	Over 5 years	Non-interest-sensitive and provisions	As at December 31, 2018
<b>Assets</b>								
Cash and deposits with financial institutions	\$ 972	\$ 1,486	\$ -	\$ -	\$ -	\$ -	\$ 280	\$ 2,738
<i>Effective interest rate</i>		2.04 %						
Securities	411	5,948	1,544	1,471	14,923	18,822	6,547	49,666
<i>Effective interest rate</i>		2.23 %	1.90 %	2.24 %	2.22 %	3.61 %		
Securities borrowed or purchased under reverse repurchase agreements	-	14,086	-	-	-	-	-	14,086
<i>Effective interest rate</i>		1.76 %						
Loans	10,903	28,262	2,191	3,216	14,118	3,241	(94)	61,837
<i>Effective interest rate</i>		3.56 %	5.57 %	5.82 %	6.07 %	4.54 %		
Segregated fund assets and other assets <sup>(1)</sup>	-	-	-	-	-	-	29,233	29,233
	\$ 12,286	\$ 49,782	\$ 3,735	\$ 4,687	\$ 29,041	\$ 22,063	\$ 35,966	\$ 157,560
<b>Liabilities and equity</b>								
Deposits	\$ 9,284	\$ 23,007	\$ 1,166	\$ 5,069	\$ 16,135	\$ 1,965	\$ 1,431	\$ 58,057
<i>Effective interest rate</i>		1.79 %	2.31 %	1.93 %	1.65 %	2.39 %		
Commitments related to securities sold short	209	101	-	39	4,968	4,968	544	10,829
<i>Effective interest rate</i>		0.52 %		1.83 %	2.07 %	3.27 %		
Commitments related to securities lent or sold under repurchase agreements	-	16,233	-	-	-	-	-	16,233
<i>Effective interest rate</i>		1.80 %						
Insurance contract liabilities	-	-	-	-	-	-	28,764	28,764
Other liabilities <sup>(1)</sup>	5	10	-	-	-	13	28,466	28,494
Subordinated notes	-	-	-	-	879	499	-	1,378
<i>Effective interest rate</i>					5.19 %	4.95 %		
Equity	-	-	-	-	-	-	13,805	13,805
	\$ 9,498	\$ 39,351	\$ 1,166	\$ 5,108	\$ 21,982	\$ 7,445	\$ 73,010	\$ 157,560
Gap – Consolidated Balance Sheet items	\$ 2,788	\$ 10,431	\$ 2,569	\$ (421)	\$ 7,059	\$ 14,618	\$ (37,044)	\$ -
Gap – Derivative financial instruments, based on notional amounts	-	(20,179)	1,207	5,196	9,453	4,323	-	-
<b>Total gap</b>	\$ 2,788	\$ (9,748)	\$ 3,776	\$ 4,775	\$ 16,512	\$ 18,941	\$ (37,044)	\$ -

<sup>(1)</sup> Segregated fund assets and liabilities have no impact on the Federation interest rate risk exposure. For more information, see the "Segregated fund risk management" section of Note 15, "Insurance contract liabilities".

## NOTE 31 – SEGMENTED INFORMATION

The Federation is made up of the three following segments: Personal and Business Services; Wealth Management and Life and Health Insurance; and Property and Casualty Insurance. These segments have been structured according to the needs of the members of the Desjardins caisse network and clients and the markets in which the Federation operates, and they reflect the Federation's internal management method. Financial information related to activities that are not specific to a business segment is presented under the Treasury and Other Support to Desjardins Group Entities category.

The Personal and Business Services segment is responsible for upgrading and marketing a comprehensive, integrated offer designed to meet the needs of individuals, businesses, institutions, non-profit organizations and cooperatives, through the Desjardins caisse network, the Desjardins Business centres as well as specialized teams. The line of products and services includes day-to-day, convenience transactions, savings, payment, financing, specialized services, access to capital markets, development capital, business ownership transfers and advice. The Personal and Business Services segment supports the caisses and their service centres in distributing products and services by optimizing the performance and profitability of physical and virtual networks through the introduction and management of complementary access networks, by phone, online and via, applications for mobile devices, as well as ATMs.

The Wealth Management and Life and Health Insurance segment provides various categories of service offerings aimed at increasing the wealth of members and clients of Desjardins Group and helping them protect their financial security. These offerings are intended for individuals and businesses, while group insurance or savings plans meet the needs of employees through their businesses or those of individuals who are part of any other group. This segment designs several lines of life and health insurance protection and savings and investment products. In addition to its own products and services, it distributes external savings and investment products as well as securities and private management products. This segment also includes asset management for institutional clients. Its products and services are distributed through employees of the caisse network and Desjardins Business centres, financial security advisors, investment advisors, private managers, exclusive agents, independent partners, actuarial consulting firms and group plan representatives. Certain product lines are also distributed online, via applications for mobile devices and through client care centres. This segment includes the operations of Qtrade and the interest in Northwest & Ethical up to April 1, 2018, as well as the operations of the interest in Aviso Wealth since that same date.

The Property and Casualty Insurance segment offers insurance products allowing members and clients of Desjardins Group to protect themselves against the impact of a disaster. It includes the activities of Desjardins General Insurance Group Inc., and Western Financial Group Inc. until its disposal by the Federation on July 1, 2017. Its products are distributed through property and casualty insurance agents in the Desjardins caisse network and in several client contact centres and Desjardins Business centres, through a network of exclusive agents in the field in Quebec and outside Quebec, online and via applications for mobile devices.

The Treasury and Other Support to Desjardins Group Entities category includes financial information that is not specific to any particular business segment. It primarily includes treasury activities and activities related to financial intermediation between surplus liquidity and the liquidity needs of the caisses, as well as orientation and organizational activities for Desjardins Group. This category also includes the operations of Desjardins Capital Inc. It also includes Desjardins Technology Group Inc., which encompasses all of Desjardins Group's IT operations. In addition to the various adjustments that are necessary to prepare the consolidated financial statements, the intersegment balance eliminations are classified in this category.

Intersegment transactions are recognized at the exchange amount, which represents the amount agreed to by the various legal entities and business units. The terms and conditions of these transactions are comparable to those offered on financial markets. The results of the main segments reflect data collected by internal financial reporting systems and are consistent with the policies applicable to the preparation of the Consolidated Financial Statements of the Federation.

## NOTE 31 – SEGMENTED INFORMATION (continued)

### RESULTS BY BUSINESS SEGMENT

The following table provides a summary of the Federation's financial results by business segment for the years ended December 31.

	Personal and Business Services		Wealth Management and Life and Health Insurance		Property and Casualty Insurance		Treasury and Other Support to Desjardins Group Entities		Consolidated	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Net interest income	\$ 1,144	\$ 1,089	\$ 4	\$ 1	\$ -	\$ 1	\$ 353	\$ 313	\$ 1,501	\$ 1,404
Net premiums	-	-	4,676	4,406	4,402	3,896	(155)	(156)	8,923	8,146
Other income	1,684	1,596	2,103	2,920	148	292	463	706	4,398	5,514
<b>Total income</b>	<b>2,828</b>	<b>2,685</b>	<b>6,783</b>	<b>7,327</b>	<b>4,550</b>	<b>4,189</b>	<b>661</b>	<b>863</b>	<b>14,822</b>	<b>15,064</b>
Provision for credit losses	288	274	(1)	4	-	-	1	-	288	278
Claims, benefits, annuities and changes in insurance contract liabilities	-	-	3,369	4,233	3,209	2,555	6	7	6,584	6,795
Non-interest expense	2,137	1,972	2,296	2,329	1,127	1,099	832	839	6,392	6,239
<b>Operating surplus earnings</b>	<b>403</b>	<b>439</b>	<b>1,119</b>	<b>761</b>	<b>214</b>	<b>535</b>	<b>(178)</b>	<b>17</b>	<b>1,558</b>	<b>1,752</b>
Income taxes on surplus earnings	102	122	225	149	41	89	(160)	(24)	208	336
<b>Surplus earnings before dividends to member caisses<sup>(1)</sup></b>	<b>301</b>	<b>317</b>	<b>894</b>	<b>612</b>	<b>173</b>	<b>446</b>	<b>(18)</b>	<b>41</b>	<b>1,350</b>	<b>1,416</b>
Dividends to member caisses, net of income tax recovery	-	-	-	-	-	-	51	44	51	44
<b>Net surplus earnings for the year after dividends to member caisses</b>	<b>\$ 301</b>	<b>\$ 317</b>	<b>\$ 894</b>	<b>\$ 612</b>	<b>\$ 173</b>	<b>\$ 446</b>	<b>\$ (69)</b>	<b>\$ (3)</b>	<b>\$ 1,299</b>	<b>\$ 1,372</b>
<b>of which:</b>										
Group's share	\$ 301	\$ 317	\$ 894	\$ 610	\$ 132	\$ 405	\$ (69)	\$ (3)	\$ 1,258	\$ 1,329
Non-controlling interests' share	-	-	-	2	41	41	-	-	41	43

<sup>(1)</sup> For the year ended December 31, 2018, the Group's share of "Surplus earnings before dividends to member caisses" was \$301 million (\$317 million in 2017) for the Personal and Business Services segment, \$894 million (\$610 million in 2017) for the Wealth Management and Life and Health Insurance segment, \$132 million (\$405 million in 2017) for the Property and Casualty Insurance segment and \$(18) million (\$41 million in 2017) for the Treasury and Other Support to Desjardins Group entities category.

### SEGMENT ASSETS

	Personal and Business Services	Wealth Management and Life and Health Insurance	Property and Casualty Insurance	Treasury and Other Support to Desjardins Group Entities	Consolidated
<b>As at December 31, 2018</b>	<b>\$ 60,982</b>	<b>\$ 41,916</b>	<b>\$ 13,007</b>	<b>\$ 41,655</b>	<b>\$ 157,560</b>
As at December 31, 2017	\$ 51,696	\$ 42,005	\$ 13,138	\$ 38,901	\$ 145,740

## NOTE 32 – RELATED PARTY DISCLOSURES

The Federation's related parties include entities included in the group scope of Desjardins Group and primarily member caisses. They also include associates, joint ventures and employee benefit plans, as well as certain entities for which the substance of the relationship indicates that they are related to the Federation, including the Desjardins Funds. In addition, they include key management personnel and close members of their family, as well as entities over which these persons exercise, directly or indirectly, control, joint control or significant influence.

### TRANSACTIONS WITH THE FEDERATION'S RELATED PARTIES

Transactions with the Federation's related parties were entered into under normal market terms and conditions and were initially recognized at fair value.

The Federation and its subsidiaries carry out transactions with related parties, and primarily member caisses. Services rendered to member caisses include various technical, administrative and financial services for which income, such as assessments and fees, are earned. On the other hand, member caisses earn remuneration income from the Federation on products and services such as credit cards, payroll services, as well as fund and investment services and financial engineering. The Federation also plays a treasurer role, which allows the caisses to borrow or lend liquidities. Swaps are also entered into between member caisses and the Federation.

Through Desjardins Investments Inc., the Federation earns management fees as manager of the Desjardins Funds for the following services: accounting, record-keeping, securities custody, portfolio management and transfer agent services. Through Desjardins Trust Inc., the Federation also earns fees as fund custodian. Finally, the Federation also earns management income from pension plans and pays interest expense to the Desjardins Group Pension Plan.

These transactions and balances as at the reporting dates are as follows:

	2018				2017			
	Member caisses	Associates / Joint ventures	Other related parties	Total	Member caisses	Associates / Joint ventures	Other related parties	Total
<b>Consolidated Statements of Income</b>								
Interest income	\$ 667	\$ 3	\$ -	\$ 670	\$ 489	\$ 4	\$ -	\$ 493
Interest expense	(169)	(1)	(2)	(172)	(153)	-	(1)	(154)
Net premiums	100	-	1	101	97	-	-	97
Assessments	376	-	16	392	376	-	1	377
Service agreements	694	-	14	708	682	-	23	705
Brokerage and investment fund services	-	2	544	546	-	1	503	504
Investment income	(41)	4	55	18	165	-	3	168
Remuneration and other	(563)	-	-	(563)	(536)	-	-	(536)
Other income	184	10	121	315	173	13	16	202
Other expenses	(112)	(5)	4	(113)	(101)	(7)	(1)	(109)
<b>Consolidated Balance Sheets</b>								
Cash and deposits with financial institutions	\$ 168	\$ -	\$ -	\$ 168	\$ 87	\$ -	\$ -	\$ 87
Securities	1	99	178	278	1	103	316	420
Securities borrowed or purchased under reverse repurchase agreements	2,152	-	347	2,499	702	-	676	1,378
Segregated fund net assets	-	-	1,237	1,237	-	-	1,234	1,234
Loans	25,805	75	-	25,880	26,228	65	-	26,293
Other assets	978	23	68	1,069	725	2	23	750
Deposits	6,391	49	154	6,594	5,006	69	295	5,370
Commitments related to securities lent or sold under repurchase agreements	-	-	149	149	-	-	50	50
Derivative financial instruments	1,831	-	15	1,846	2,190	-	(25)	2,165
Other liabilities	663	1	3	667	439	1	10	450
<b>Other</b>								
Credit commitments given	\$ 43,966	\$ -	\$ 242	\$ 44,208	\$ 37,607	\$ -	\$ 213	\$ 37,820
Guarantees given	1	-	149	150	1	-	50	51
Credit commitments received	34	-	-	34	35	-	-	35
Guarantees received	2,172	-	347	2,519	718	-	676	1,394

## NOTE 32 – RELATED PARTY DISCLOSURES *(continued)*

### KEY MANAGEMENT PERSONNEL COMPENSATION

The Federation's key management personnel comprises the members of its Board of Directors and its Management Committee. These individuals have the authority and responsibility for planning, directing and controlling the activities of the Federation. In the normal course of operations, the Federation carries out financial transactions with its management personnel. In addition to the compensation paid to key management personnel, the main financial transactions also include routine financial intermediation transactions as well as wealth management, life and health insurance, and property and casualty insurance transactions with the various entities included in the scope of consolidation of the Federation. These transactions were entered into under terms and conditions equivalent to those of arm's length transactions and were initially recognized at fair value.

For the years ended December 31, the compensation of the Federation's key management personnel was as follows:

	2018	2017
Short-term benefits	\$ 15	\$ 12
Long-term and post-employment benefits	6	5
Termination benefits	-	2
	<b>\$ 21</b>	<b>\$ 19</b>

# SIMPLE, PEOPLE-FOCUSED GOVERNANCE

The values and democratic structure of Desjardins Group (Desjardins) are central to the organization's strategic vision and initiatives. When we shape and define our strategic priorities at the Congress and general meetings, members have a voice—the directors of local and group caisses are there to represent them.

Our governance has undergone considerable change. We've updated how members participate in the democratic process, modernized caisse supervision structures and transformed regional decision-making bodies into collaborative groups committed to building closer relationships with our members and their communities. We've also introduced an enhanced group profile to help the Board of Directors (Board) achieve a balanced representation of members and boast a wide range of expertise and experience that reflect our strategic priorities of always doing what's best for our members and clients, showing our cooperative difference and harnessing the full potential of our cooperative group.

## Governance highlights

In 2018, we focused on implementing the priorities identified at the 23rd Congress of Elected Officers, which took place in 2017. These priorities are all about simplifying and modernizing Desjardins's democratic governance structure. By giving local caisse directors the opportunity to weigh in on the priorities in the early stages, we were able to gain their support. While the proposed changes were being implemented, we rolled out an initiative challenging our directors, managers and employees to question our business and management practices and systems, and explore the profiles and skills we need to become everyone's #1 choice and enrich the lives of people and communities.

These are the main changes:

### A. Federation governance

- We abolished the regional councils and the group caisse council and set up community collaboration groups that bring local caisses together to focus on communities. The groups are made up of one director from each caisse, young directors and general managers.
- At the network level, we abolished the Assembly of Representatives and created the Desjardins Collaboration Forum. This forum of influence, liaison and alignment brings together caisse board chairs and general managers, and young directors. Since forum directors are also members of the community collaboration groups, they know what's happening at the local level and are able to weigh in on broader issues.
- Following a three-year transition period, an enhanced group profile will be in place to ensure the Board is representative and includes members with the right skillsets. Membership will go from 22 to 20, including 15 caisse directors and two general managers who will now all be elected at Desjardins's annual general meetings, plus Desjardins's President and CEO. The Board will ensure its skills target is met by appointing two external members in April.
- Similar changes are being made to Desjardins's Board of Ethics and Professional Conduct (BEPC). It now has five members instead of eight, and membership is now based on an enhanced group profile. Members of the BEPC will also be elected at Desjardins's annual general meetings.
- To reflect Desjardins's status as a cooperative group under the *Act Respecting Financial Services Cooperatives*, the *Bylaws of the Groupe coopératif Desjardins* (group bylaws) have replaced the Federation bylaws. The group bylaws include the standard caisse bylaws which apply to all caisses.

### B. A single Election Committee for electing Desjardins's President, Board directors and BEPC members

The Election Committee oversees the proper conduct of the election process for positions on the Board and the BEPC. It is also responsible for overseeing all processes for electing the President and CEO. The committee provides guidelines for the electoral process and ensures compliance with them, sets up processes that enable the electoral colleges to properly fulfill their role, and assesses the nominations according to the profile adopted by the Board and by the BEPC for the purposes of reporting at the general meeting. The Election Committee is made up of five caisse directors who are neither directors of the Federation nor members of its BEPC.

### C. Election of Desjardins's President

The electoral college is now made up of one director from each caisse. This director is the person who represents the caisse on the community collaboration group and the Desjardins Collaboration Forum.

The new electoral college:

- Fosters a balance between member and caisse representation in choosing the person who will become Desjardins's President and CEO
- Ensures all caisses are involved in the election process
- Is smaller to give electors the support they need, streamline the election process and maintain confidentiality

We've redefined the eligibility criteria to better reflect the duties of the chief representative of Desjardins, and its members and clients. On top of the legal requirements that must be met to run for President of Desjardins, candidates must meet certain criteria, including being a member and client of Desjardins for at least one year and being able to demonstrate that they do regular business with Desjardins.

#### D. Caisse governance

We dissolved the boards of supervision and created two new mandatory committees for the Board (Audit and Professional Conduct Committee and Governance and Ethics Committee).

We updated the areas of responsibility of caisse boards of directors and the Board committees' mandate to take into account the priorities identified at the 23rd Congress. The changes are mainly related to the Board's broader role in ensuring that member needs are being met and the new caisse monitoring approach following the dissolution of the boards of supervision. Responsibility for professional conduct has been transferred to the Audit and Professional Conduct Committee and a Governance and Ethics Committee is now mandatory for Quebec caisses. Caisses can decide whether the Governance and Ethics Committee or a separate committee will be responsible for cooperation.

Enhanced group profile with representation and skills targets

Just like the Federation's Board of Directors, the caisse boards must now adopt an enhanced group profile with representation and skills targets that take into account member circumstances and needs. Since it's impossible for a single person to possess all the required skills, the group of directors as a whole must have the appropriate levels of knowledge, experience and professional expertise to carry out their responsibilities. The enhanced group profiles will be used to identify criteria for electing directors or filling Board vacancies.

Rules for electing caisse directors

From now on, the call for nominations will include the enhanced group profile criteria. Nominations will be assessed by the Nomination Committee. During the general meeting, the Chair of this committee will go over the nominations received and how well they correspond to the criteria. During the election period, the candidates will have the opportunity to explain to members why they want to be a director and demonstrate how they are a good fit for the target profile. Starting in 2019, there's a 12-year limit on caisse board Chair positions.

Mandatory training

All directors agree to take the mandatory training. If they haven't completed this training by the end of their first term, they won't be eligible for re-election.

#### E. Amendments to the *Act Respecting Financial Services Cooperatives*

On June 13, 2018, the National Assembly of Quebec passed Bill 141, an act to improve the regulation of the financial sector. The changes will come into force in stages. Some changes took effect on July 13, 2018, and the Federation adopted the group bylaws on December 7, 2018. We've started taking a closer look at our internal governance documents to ensure they reflect all the changes. The amended *Act Respecting Financial Services Cooperatives* now specifically recognizes the Groupe coopératif Desjardins (the Group) as a cooperative group consisting of the Federation, the Quebec caisses and the Desjardins Security Fund. It also sets out new obligations and powers that, together, formalize the financial solidarity between the entities belonging to the Group. These powers and obligations include:

- The obligation of directors of entities belonging to the Group to act not only in the interest of their own component, but also in the interest of the Group (in case of conflict, the Group's interests will prevail)
- New responsibilities for the Federation, including overseeing the Group's financial security
- New powers for the Federation and the Desjardins Security Fund to intervene in matters regarding caisses and their directors and managers

The financial solidarity established under the act allows us to take a holistic approach to managing the capitalization of entities belonging to the Group. The Federation is now also responsible for overseeing the caisses' financial performance in areas that have an impact on Desjardins's capitalization, such as surplus earnings, growth and the payment of dividends.

The amended *Act Respecting Financial Services Cooperatives* provides a modern legislative framework that meets the highest international standards and that allows Desjardins to quickly and effectively respond to member and client needs, continue to grow and ensure the organization's long-term success.

## Governance structure

The purpose of Desjardins's corporate governance practices is to enable us to carry out our mission, which is to contribute to improving the economic and social well-being of people and communities. The Federation oversees the development and application of the Desjardins-wide governance structure, which takes into account Desjardins's cooperative nature, its social responsibility objectives, the complexity of its activities, and Autorité des marchés financiers (AMF) guidelines. This structure covers the activities of the Federation, the Desjardins Security Fund, the Fédération des caisses populaires de l'Ontario Inc., the Desjardins subsidiaries and the caisses. As certain components are subject to specific laws and regulations, the structure largely complies with rules established by the Canadian Securities Administrators (CSA) and the Office of the Superintendent of Financial Institutions, as well as industry best practices.

## Mandate of the Board of Directors

### 1. Administration of the Federation

Pursuant to the *Act Respecting Financial Services Cooperatives*, the Board is responsible for managing the affairs of the Federation, with support from its commissions and committees. It ensures that the necessary mechanisms and structures are in place for it to play its role as the organization that guides, plans, coordinates, monitors and controls all Desjardins operations. As part of its fiduciary role, it makes the necessary decisions and coordinates the components' actions to ensure Desjardins's long-term viability. The organizational structure, which is built around the business sectors and support functions, serves to optimize overall performance, streamline the organization and improve financial and risk management. The Board's responsibilities include the following:

#### a. Corporate culture

The Board is responsible for promoting the corporate culture based on Desjardins's values: money at the service of human development, democratic action, personal commitment, integrity and rigour in the cooperative enterprise, and solidarity with the community and intercooperation, with a view to earning the trust of the public and ensuring members and clients have confidence in their financial services cooperative. The Board is also responsible for enforcing Desjardins's rules of professional conduct.

At the heart of this ever-evolving culture is the strategic framework defined by the Board, which is based on Desjardins's purpose: *At Desjardins, we enrich the lives of people and communities through our members and clients*. All our decision-making and actions are guided by our goal of becoming everyone's #1 choice by doing what's best for our members and clients.

The Federation has a Board of Ethics and Professional Conduct (BEPC) whose members are all independent from management and from the Board of Directors (Board). For Desjardins caisses in Quebec, responsibility for ethics and professional conduct is assumed by an Audit and Professional Conduct Committee and a Governance and Ethics Committee made up of caisse directors. For caisses in Ontario, this responsibility is assumed by an Audit Committee made up of caisse directors. Desjardins also has a policy for reporting regulatory violations and violations of Desjardins's Code of Professional Conduct. This policy is combined with a confidential reporting mechanism that protects the anonymity of those who use it.

Desjardins's Code of Professional Conduct, which is available to the public on Desjardins.com, is applicable to all Desjardins components. It includes a section on ethics and Desjardins's mission and values, and a section that describes all the rules of professional conduct. All Desjardins employees and directors and members of the BEPC must sign an annual acknowledgement that they have read and agree to uphold the Code.

#### b. Strategic and financial planning process

The Board has an ongoing strategic and financial planning process for Desjardins that includes a financial plan, crisis scenarios, a funding plan and a capitalization plan. This process is the basis for all other plans (for the caisse network, business sectors and support functions) and focuses on maintaining continuity, setting priorities and fostering commitment. The Board adopts a rolling strategic plan that is updated periodically, with input from the caisses, Desjardins's democratic bodies and business sectors, as well as the decision-making bodies of its subsidiaries.

The respective boards of directors of Desjardins Financial Security Life Assurance Company, Desjardins General Insurance Group Inc., Desjardins Securities Inc., Desjardins Capital Inc. and Desjardins Trust Inc. adopt their own strategic and financial plan that is in line with Desjardins's strategic and financial plan, but specific to their own sector.

Desjardins is unique in that the strategic planning process occasionally calls on the Congress, which is an assembly of more than 1,000 caisse delegates. Mechanisms are in place to ensure that all components are aligned with key strategic directions.

The Board plays a supervisory and monitoring role in this process, with support from the Desjardins Group Management Committee (DGMC). The DGMC produces regular reports via the performance review so the Board can monitor the progress made on Desjardins's strategic plan and the business plans, and make changes as needed.

### c. Identification and management of main risks

The Board is responsible for identifying the main risks facing Desjardins, setting risk appetite limits and ensuring that management sets up the required systems to manage these risks in a sound and prudent manner. The Board is supported in these tasks by the Risk Management Executive Division. Backed by the Risk Management Commission (RMC), the Board works with the Audit and Inspection Commission (AIC), which is responsible for risks related to the financial disclosure process. The DGMC also supports the Board in carrying out its financial disclosure responsibilities. All RMC sessions include closed-door meetings with the Risk Management Executive Division, as well as closed-door meetings which are not attended by management.

A detailed presentation of the risk management principles applied at Desjardins Group can be found in the Risk Management section of the Management's Discussion and Analysis on page 54.

The complete mandate and composition of the commissions and committees that support the Federation's Board of Directors in the performance of its duties are available on Desjardins's website at [www.desjardins.com/ca/about-us/desjardins/governance-democracy/board-directors/commissions-committees/index.jsp](http://www.desjardins.com/ca/about-us/desjardins/governance-democracy/board-directors/commissions-committees/index.jsp). Additional information specifically about the RMC and its governance practices can also be found there.

### d. Succession planning

The Board oversees the senior management succession and development program and is supported in this task by the Human Resources Commission (HRC) and the Human Resources and Communications Executive Division. The HRC runs the program and reports to the Board, making recommendations as needed. This program is an important tool for the DGMC, as it promotes personal development, supports succession planning, and helps protect the organization against human resources-related risks.

Talent development, succession planning and hiring processes promote professional qualification and diversity among Desjardins staff.

#### President and CEO

In keeping with Desjardins's cooperative nature, the President and CEO of Desjardins is chosen by an electoral college made up of representatives from all Quebec and Ontario caisses. Although the Board does not have the power to appoint the President and CEO, it does have a role to play in succession planning, mainly through the senior management succession program and skills development for directors at local caisses, subsidiaries or the Federation.

The electoral process is governed by the group bylaws and Desjardins's *Code of Professional Conduct* and is overseen by an Election Committee made up of directors who are independent from the Board and the BEPC, whose responsibility is to establish the rules of the electoral process and the rules of conduct applicable to the electoral college, candidates, employees and directors from local caisses. There is a two-term limit for the position of President and CEO of Desjardins. In addition to these parameters, the Board also establishes the profile for the position of President and CEO, and develops a candidate evaluation guide based on this profile to be used by the members of the electoral college.

#### Senior Executive Vice-President and COO

To bolster independence, stability and succession planning, the Board approves the appointment of the Senior Executive Vice-President and COO who assumes, for the purposes of the law and the group bylaws, the role of general manager of the Federation. The Senior Executive Vice-President and COO also recommends a working organizational structure for Federation and Desjardins senior executives to the President and CEO.

### e. Integrity of internal control and management reporting systems

The Board, backed by its Audit and Inspection Commission (AIC), ensures the implementation of effective control systems and obtains the required reporting information from management. The Board is supported in this responsibility by Desjardins's Chief Monitoring Officer, whose annual work plan is approved by the AIC. A rigorous financial governance process is applied throughout Desjardins to properly support the Executive Vice-President of Finance, Treasury and Administration and CFO who, together with Desjardins's President and CEO, is responsible for certifying Desjardins's Combined Financial Statements.

The Federation discloses financial information in compliance with CSA *National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings*. Desjardins Group is not, on a combined basis, a reporting issuer according to the Regulation. However, it has elected to comply with the Regulation to show its willingness to observe best practices in financial governance. Under Federation's financial governance system, its signing officers certify, at the end of the fiscal year, the design and operating effectiveness of disclosure controls and procedures, as well as the internal controls over financial reporting.

The caisse network has an effective and efficient internal control system in place that is tailored to its particular needs. This system is designed to provide boards of directors with reasonable assurance that the network is achieving its business objectives in compliance with regulatory requirements.

The Board ensures that the DGMC provides the Board and its commissions and committees with information that is accurate, timely and adapted to the specific needs of its directors so they can take advantage of business opportunities and measure the risks involved. Board members are invited to assess the quality of documents used in the decision-making process.

The Board benefits from the information used by each business sector to effectively monitor key performance indicators, as it allows its members to quickly obtain strategic information pertinent to the decision-making process.

Board members receive financial and operating reports at least quarterly so they can assess Desjardins's situation and the status of the Federation's projects. The Board ensures that appropriate policies and procedures are in place to facilitate the production and presentation of this information.

To effectively carry out its duties, the Board holds regular meetings on a predetermined schedule. Board members receive the meeting agenda in advance, along with any relevant documentation, to ensure productive discussions and to facilitate the decision-making process. The Board constantly seeks to increase its efficiency and focus its efforts on strategic issues by optimizing meeting agendas and by delegating certain operational responsibilities to the DGMC.

Directors have access to technological tools so they can easily and securely access all meeting-related documentation and management guidelines for Desjardins's operations. They are required to comply with Desjardins's information security policy.

#### **f. Strategic communications**

The Board adopts a communications policy and strategic communications priorities for Desjardins, in line with the Desjardins Group strategic plan, including actions to be taken and targets. The Federation also draws up internal and external communications plans or strategies in order to better manage its relations with the caisses and their members; the business sectors and their clients; its employees; socio-economic, community and non-governmental organizations; opinion makers; the public; the media; rating agencies; and the government. It ensures consistent, quality communications across Desjardins, helps promote Desjardins's cooperative difference, contributes to the promotion, development and growth of the Desjardins brand; and listens to internal and external audiences.

The Federation oversees the financial reporting process and the disclosure of any major changes that may affect the financial position of Desjardins Group. It uses different teams and various channels to communicate effectively with its many stakeholders.

These teams and channels include: the Office of the Ombudsman, the Desjardins ethics and professional conduct support team and the caisse complaint-handling procedure (*Your Satisfaction, Our Priority*); as well as, within Desjardins: the annual general meetings, the disclosure of quarterly financial results, publications (including our annual report, which includes social and cooperative responsibility disclosure, set out in a separate document), toll-free telephone numbers, intranet portals (including one designed especially for caisse directors), the website (which includes information on the Co-opme Program on education, cooperation and dialogue with our members and clients, as well as a Member Relations section), the Federation's member services, the procedure for reporting violations of Desjardins's *Code of Professional Conduct* and other regulatory instruments, newsletters, and social media (Facebook, YouTube, LinkedIn, Twitter, etc.).

In addition, the Federation maintains relations with international rating agencies and coordinates Desjardins's relationships with the different levels of government in compliance with applicable lobbying legislation.

## **2. Composition of the board of directors**

The Federation's Board consists of 20 members, the majority of whom are independent directors. There are 15 representatives from the caisse network, two caisse general managers, two external directors and the President and CEO, who is also Chair of the Board. The changes to the Board's membership, which came into effect on December 7, 2018, provide a transition period to allow members of the Board, directors and managing directors in office at the time to finish their terms. The Board's managing director seats are currently filled by the vice-presidents of two regional councils (Outaouais, Abitibi-Témiscamingue and Nord du Québec; and Bas-Saint-Laurent and Gaspésie—Îles-de-la-Madeleine). With the regional councils being dissolved, these two managing directors will remain Board members until their respective terms end. As was the case with their previous positions on the Board, they do not have voting rights.

Additionally, the following members of management support the Board by attending its meetings: the Senior Executive Vice-President and COO; the Executive Vice-President, Finance, Treasury and Administration and CFO; the Secretary General and Vice-President, Governance and Sustainable Development; and the Vice-President, President's Office, Cooperation and Director Support.

### 3. Nomination process

In accordance with Desjardins's democratic structure and the principle of delegation, the 15 members of the Board and the two general managers, who are all from the caisse network, are elected by the delegates of the Federation member caisses during the annual general meeting. The Federation therefore benefits from having directors who have in-depth knowledge of their community and the activities of Desjardins yet remain independent from management. Their knowledge of the organization is one of the considerable advantages of Desjardins's democratic structure. Having two caisse general managers sit on the Board also helps ensure that the priorities adopted and implemented by the Board reflect the caisses' needs and priorities.

The two external directors, who are neither caisse directors nor general managers, are appointed by the Board for a one-year term renewable for up to 12 years.

The final position is reserved for the President and CEO of Desjardins.

Board members have three-year renewable terms, and each year one-third of the Board members are outgoing. Federation directors and members of the BEPC are subject to a limit of four three-year terms, consecutive or not.

Board membership is also based on an enhanced group profile, in accordance with the group bylaws. The Board adopts and updates, as needed, this enhanced group profile, which it strives to achieve, and which takes into account the following criteria: skills related to the individual qualities required to be a member of the Board; representation from diverse communities, members and clients, and the caisse network; skills relevant to the reality of a regulated cooperative financial institution and skills relevant to Desjardins's strategic priorities. The Federation has designed tools to help electors understand what is expected of directors, so they can make an informed choice.

Desjardins has a voluntary gender parity commitment for the boards of directors of its caisses, subsidiaries and the Federation. Parity is taken into account when selecting members of boards and subsidiaries. At the caisse and Federation levels, each board has an enhanced group profile that addresses parity. An Election Committee oversees the electoral process and helps the Federation's Board of Directors in achieving group profiles. However, achieving parity, at both the caisse and Federation levels, is ultimately dependent on the electoral process inherent to Desjardins's democratic structure.

### 4. Application of independent director

A director is considered independent if they do not have any significant relationship with Desjardins that, in the opinion of the Board, may affect the independence of their judgment.

There are three non-independent members of the Board of Directors: Desjardins's President and CEO, plus two caisse general managers. The President and CEO is a non-independent party because they are a member of Federation management, and the caisse general managers are non-independent parties because they are employees of cooperatives belonging to Desjardins (the caisses). The directors do not have any business or personal relationships with members of the DGMC; nor do they have any interests which, in the opinion of the Board, could significantly interfere with their ability to act in the best interests of the Groupe coopératif Desjardins, or any interests of any other nature which, in the opinion of the Board, could reasonably be perceived as harmful. As a result, the members of the Board, both individually and collectively, are able to exercise objective and impartial judgment on Desjardins business free of undue influence from senior management or third parties.

For guidance in these matters, the Board refers to the provisions of Desjardins's *Code of Professional Conduct*, which governs the actions of its directors, and to the declarations of interests filed annually by the directors. None of the directors sits on the board of directors of a public company.

#### Independent directors

In the opinion of the Board, and in accordance with CSA *National Instrument 52-110 – Audit Committees* and the AMF *Governance Guideline*, the following directors are independent:

- |                         |                       |
|-------------------------|-----------------------|
| • Louis Babineau        | • Annie P.Bélanger    |
| • Claude Chapdelaine    | • Carole Chevalier    |
| • Stéphane Corbeil      | • Michel Doré         |
| • André Grenier         | • Nadine Groulx       |
| • Jean-François Laporte | • Jean-Robert Laporte |
| • Camil Maltais         | • Roch Ouellet        |
| • Serge Rousseau        | • Mario Simard        |
| • Michel Tourangeau     | • Stéphane Trottier   |
| • Yvon Vinet            |                       |

Michel Doré's and André Grenier's terms began on March 24, 2018.

Christian Savard's and Serge Tourangeau's terms ended on March 24, 2018.

Michel Allard and Pierre Perras are managing directors. They are independent in the same way directors are independent.

## Non-independent directors

In the opinion of the Board, and in accordance with CSA *National Instrument 52-110 – Audit Committees* and the AMF *Governance Guideline*, the following directors are not independent:

- Guy Cormier
- Benoît Bélanger
- Neil Hawthorn

Sylvain Dessureault's term ended on September 9, 2018, and Yves Genest's term ended on December 31, 2018.

## 5. Performance reviews and director skills

### Performance reviews

The Board and its commissions and committees conduct a review of their performance every two years. A two-year action plan based on these performance reviews is then submitted to the Board by the Corporate Governance Commission (CGC), which oversees the plan.

This exercise is accompanied by individual meetings between each director and the Chair of the Board. These meetings, whether formal or not, are intended to enhance the performance of decision-making bodies and each director's contribution. Directors have regular meetings with the Chair throughout the year.

### Director skills

The Board has adopted an enhanced group profile with criteria to help elect members of the Board at the general meeting. The profile also guides the disclosure of how well the membership of the Federation's board lines up with these criteria.

Moreover, on the recommendation of its CGC and in accordance with the AMF *Guideline Governing Integrity and Competency Criteria*, the Board performs a self-assessment of the skills of its members. Every two years, each member completes a self-assessment grid for this purpose. The results are used to establish the skills development plan.

The matrix below shows that the members of the Federation's Board collectively possess a wide range of experience and complementary skills that enable them to make an active and enlightened contribution to Desjardins's governance. The new enhanced group profile adopted by the Board in 2018 and this matrix were reviewed together and the results show what the Board needs to focus on to gradually achieve this profile. This voluntary disclosure will evolve over time. The weighting for self-assessments is determined by the Chair and Vice-Chair of the Board and presented to the CGC.

Directors	Financial institution skills that meet AMF requirements							Strategic planning skills					Expertise recognized by a professional title and relevant experience					Representation									
	Financial services market	Cooperation	Business and distribution model	Risk management	Entrepreneurship/Economic sectors	Education	Sustainable development	Doing what's best for our members and clients	Member and client experience	Digital innovation and IT management	Insurance market	Canadian market	Accounting and finance	Law	Human resources	Actuarial services	Governance	Sex		Age	Cultural community <sup>1</sup>	Community <sup>2</sup>			Network <sup>3</sup>		
																		Male	Female			Urban	Semi-urban	Rural	Large caisse	Medium caisse	Small caisse
Allard, Michel		✓		✓				✓	✓	✓								✓		63			✓				✓
Babineau, Louis	✓	✓		✓		✓	✓	✓	✓	✓			✓				✓	✓		60		✓			✓		
Bélanger, Annie P.		✓				✓	✓	✓	✓		✓	✓			✓		✓		✓	70				✓			✓
Bélanger, Benoît	✓	✓	✓	✓	✓			✓	✓				✓		✓			✓		48			✓		✓		
Chapdelaine, Claude	✓	✓	✓		✓	✓		✓	✓	✓					✓			✓		65		✓				✓	
Chevalier, Carole		✓				✓	✓	✓	✓						✓		✓		✓	61		✓			✓		
Corbeil, Stéphane		✓		✓	✓			✓	✓			✓	✓					✓		52		✓				✓	
Cormier, Guy	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓		✓		✓	✓		49		✓					
Dessureault, Sylvain <sup>4</sup>	✓	✓	✓	✓	✓	✓		✓	✓				✓		✓			✓		58		✓				✓	
Doré, Michel		✓						✓	✓				✓		✓			✓		55				✓			GC <sup>5</sup>
Genest, Yves <sup>6</sup>	✓	✓	✓	✓	✓	✓	✓	✓	✓				✓		✓			✓		61				✓		✓	
Grenier, André		✓			✓	✓		✓	✓									✓		55				✓		✓	

<sup>1</sup> Director from a cultural community<sup>2</sup> Based on Statistics Canada's classification:

- Urban: Caisse located in a census metropolitan area
- Semi-urban: Caisse located in a census agglomeration
- Rural: Caisse located in an agglomeration with less than 10,000 persons that is not contiguous with an urban or semi-urban centre

<sup>3</sup> Small caisse: 1 to 15,000 members; Medium caisse: 15,001 to 35,000 members; Large caisse: Over 35,000 members; and Group caisse<sup>4</sup> Term ended on September 9, 2018<sup>5</sup> GC = Group caisse<sup>6</sup> Term ended on December 31, 2018

Directors	Financial institution skills that meet AMF requirements							Strategic planning skills					Expertise recognized by a professional title and relevant experience					Representation									
	Financial services market	Cooperation	Business and distribution model	Risk management	Entrepreneurship/Economic sectors	Education	Sustainable development	Doing what's best for our members and clients	Member and client experience	Digital innovation and IT management	Insurance market	Canadian market	Accounting and finance	Law	Human resources	Actuarial services	Governance	Sex		Age	Cultural community <sup>1</sup>	Community <sup>2</sup>			Network <sup>3</sup>		
																		Male	Female			Urban	Semi-urban	Rural	Large caisse	Medium caisse	Small caisse
Groulx, Nadine		✓			✓	✓		✓	✓								✓		✓	47				✓		✓	
Hawthorn, Neil	✓	✓	✓	✓	✓			✓	✓	✓		✓	✓		✓			✓		56		✓			✓		
Laporte, Jean-François		✓		✓				✓	✓		✓	✓	✓		✓			✓		59				✓		✓	
Laporte, Jean-Robert	✓	✓		✓		✓		✓	✓		✓	✓		✓	✓		✓	✓		68			✓		✓		
Maltais, Camil		✓			✓			✓	✓									✓		55				✓			✓
Ouellet, Roch		✓						✓	✓									✓		68				✓		✓	
Perras, Pierre		✓						✓	✓				✓					✓		61		✓				✓	
Rousseau, Serge		✓		✓		✓		✓	✓						✓		✓	✓		52			✓			✓	
Simard, Mario		✓				✓		✓	✓				✓		✓			✓		60		✓				✓	
Tourangeau, Michel		✓						✓	✓		✓			✓			✓	✓		62		✓			✓		
Trottier, Stéphane	✓	✓			✓	✓		✓	✓		✓	✓						✓		53		✓				✓	
Vinet, Yvon	✓	✓				✓		✓	✓		✓	✓		✓	✓		✓	✓		59			✓		✓		
<b>TOTAL / 24 =</b>	10	24	6	11	11	14	5	24	24	5	7	8	11	3	14	0	9	21	3	n/a	0	11	5	8	7	12	4

## 6. Onboarding and training program for new Federation directors and BEPC members

The Federation organizes onboarding and training programs for all its directors and members of the Board of Ethics and Professional Conduct (BEPC). It develops individual and group knowledge acquisition and enhancement activities, so Board and BEPC members can learn more about the various aspects of their roles and responsibilities. All new directors and members of the BEPC attend orientation sessions where they meet with members of management and receive a reference manual containing all the information they need to carry out their duties. Onboarding sessions are held to ensure effective and efficient integration of new members of Board commissions and committees.

The training program for Board and BEPC members is based on needs identified through their skills self-assessments. The CGC reviews these needs and creates a two-year skills development program for both boards. The Board also holds conferences on specific topics related to strategic planning and the associated challenges. These conferences, which are also attended by members of the DGMC, prove to be intensive skills development opportunities for Board members.

## 7. Compensation policy for Federation directors and BEPC members

The Board reviews, whenever it deems it necessary and at least every three years, its policy on the compensation of Federation directors and BEPC members. It receives recommendations from the CGC, which keeps a close eye on industry developments. The policy's compensation rates are consistent with those of comparable cooperative organizations in Quebec, Canada and Europe.

The policy includes guidelines for calculating the compensation for caisse directors, Federation directors, Federation BEPC members and subsidiary directors. The policy was reviewed and came into effect on July 1, 2018.

In accordance with the *Act Respecting Financial Services Cooperatives*, the total budget for the payment of attendance fees to directors and BEPC members is authorized by the Federation's general meeting. The total compensation budget (annual stipends plus attendance fees) is reported to the general meeting. The general meeting receives a report on changes to the compensation budget every year. The total budget for 2018 was \$2,880,500, the same as in 2017.

The policy's compensation rates can be found on page 217 of this section of the Federation annual report.

## 8. Independence of the board of directors from Desjardins Group management

Desjardins Group governing bodies have established a number of structures and procedures to ensure the Board's independence from management:

- There is only one board member who is also a member of Desjardins management: the President and CEO of Desjardins, who is also a director elected by an electoral college made up of representatives from all caisses. Since the President and CEO does not select the members of the Board, its legitimacy and independence are ensured.
- The Vice-Chair of the Board, an independent director, presides over the Board's meetings, playing the role of lead director, when the issues being discussed require the recusal of the President and CEO. The group bylaws specify that the Vice-Chair of the Board replaces the Chair when the latter is unable to act, such as when the Chair is in a real or perceived conflict of interest. Descriptions of the positions of Vice-Chair and Secretary of the Board are attached to the governance policy adopted by the Board.
- The directors hold periodic informal meetings among themselves. The Chair of the Board and CEO of Desjardins provides updates to the members of the DGMC, who are not present at these meetings. Both independent and non-independent directors attend these meetings, given that the discussions pertain to matters that do not bear any risk of conflict of interest for the non-independent directors.
- Closed-door sessions not attended by management (except for the Chair of the Board and CEO) are held at the end of each meeting of the Board and of the Executive Committee. The same is true for Board commissions and committees.
- Once a year, the Board holds a closed-door meeting with the BEPC.
- Closed-door sessions not attended by the President and CEO are held with the individuals in independent oversight functions, namely the Executive Vice-President, Finance, Treasury and Administration and CFO; the Executive Vice-President, Risk Management; the Chief Monitoring Officer of Desjardins; and the Vice-President and Chief Compliance Officer.
- The Corporate Governance Commission (CGC), the Audit and Inspection Commission (AIC) and the Risk Management Commission (RMC) are chaired by independent directors.
- The CGC, chaired by the Vice-Chair of the Board and of which only one member is a non-independent party, assumes responsibility for:
  - Managing relations between the Board and the DGMC
  - Ensuring that the Board fulfills its duties (however, the responsibility of drawing up and overseeing meeting agendas for the Board and its commissions/committees falls to the Chair of the Board and is subject to the process for assessing the performance of governing bodies).
- Only independent directors serve on the CAR.

- The division of responsibilities between the Board and the DGMC is formally documented in the group bylaws, the governance policy and the mandates of these two governing bodies, which define their respective areas of activity.
- The members of the Human Resources Commission (HRC) and the Committee on the Aggregate Remuneration of the President and CEO of Desjardins Group (CAR) are supported, when needed, by an external consultant when dealing with issues involving the aggregate remuneration of senior management.

## Position against separating the functions of Chair of the Board from those of CEO

The responsibilities of Desjardins's President and CEO are set out in the group bylaws. The functions of Desjardins's Chair of the Board and CEO are concurrent. This decision, which was made by the Federation's general meeting and reaffirmed in 2018, has been integrated into its bylaws.

At the 23rd Congress held in the fall of 2017, caisse delegates adopted a priority confirming that the roles of Desjardins's Chair of the Board and CEO should be held by the same person. The priority was integrated into the group bylaws. Considering the fact that risk management for Desjardins's leadership transition process is the responsibility of the Federation's Board, the bylaws also allow for the following: when someone new assumes this role, it happens promptly and there is a structured transition process lasting up to six months, under the Board's supervision.

The main reasons for making the responsibilities concurrent are:

- The CEO is elected by an electoral college made up of a representative from each caisse. This individual's primary responsibility is to ensure the group is always doing what's best for members and clients, the group's interests are protected, democratic bodies are functioning properly and cooperative values are respected.
- The Chair of the Board and CEO has no influence over the choice of directors, who are elected at the annual general meeting. Their observations are used to select the two external directors; however, the Board of Directors has decision-making powers, on the recommendation of the CGC, which is chaired by the lead director (who is an independent director). The Chair of the Board and CEO also has no influence on the selection of BEPC members.
- The Board created the CAR, which is chaired by the lead director (Vice-Chair of the Board) and made up entirely of independent directors, to eliminate any risk of conflict of interest. CAR meetings are closed-door. The committee also holds working sessions with the Board of Directors, which the President and CEO does not attend.
- Owing to the complex nature of Desjardins's management structure and activities, and to the expectations of regulators and the general public, it is essential that the Chair of the Board be thoroughly familiar with the activities, business and projects of both the Federation and Desjardins in order to effectively act as a leader for the democratic and decision-making bodies, the management teams of the Desjardins subsidiaries and employees.
- Desjardins's structure frees its President and CEO from the everyday operational concerns of the Federation and Desjardins. This person can therefore focus on other areas, such as: managing Desjardins; defining, developing and overseeing the implementation of key strategic directions; listening to members and clients; overseeing development, innovation and governance; engaging people; and representing Desjardins as a socio-economic leader.
- With a view to freeing the President and CEO from such responsibilities, the Senior Executive Vice-President and COO oversees all Desjardins business sectors and support functions.

## 9. Senior management reviews

### a. Setting annual management objectives and performance reviews

#### President and CEO

The annual objectives of Desjardins's President and CEO are recommended to the Board by the CAR. The CAR is chaired by the lead director in accordance with the established independence standards. The President and CEO is not present for the committee's deliberations.

The degree to which these objectives are achieved is measured through a year-end review process. The CAR supervises the performance review of Desjardins's President and CEO and sets out how Board members participate in the process.

#### Senior Executive Vice-President and COO

The annual objectives of the Senior Executive Vice-President and COO are set by the Board, on the recommendation of the President and CEO.

#### Executive vice-presidents on the DGMC

The objectives of the executive vice-presidents on the DGMC are set by the President and CEO and the Senior Executive Vice-President and COO, and provided to the Board for information purposes.

**b. Variable compensation evaluation**

President and CEO

The compensation paid to the President and CEO of Desjardins is determined by an evaluation of the annual objectives by the Board of Directors and the results of certain indicators in the general incentive plan.

Senior Executive Vice-President and COO and executive vice-presidents on the DGMC

The Board has established guidelines for setting objectives for the various indicators to ensure sound management of Desjardins's general incentive plan. The results are reviewed by the HRC and approved by the Board.

**10. External consultants**

A director may require the Board to retain the services of an external consultant at the Federation's expense. However, to ensure that such services are relevant, a request must be submitted to the CGC.

# Mandates and membership of the Federation's commissions, committees and BEPC

## As at December 31, 2018

The Board of Directors (Board) creates committees and commissions and defines their mandates in order to support and streamline its guidance, planning, monitoring and control activities. These commissions and committees are made up entirely or almost entirely of independent parties. At the end of each meeting, these commissions and committees hold closed-door sessions which members of management do not attend, except for the Chair of the Board and CEO (unless this individual's recusal is necessary for independence reasons). The composition and mandate of these commissions and committees are reviewed annually. Any work carried out by a commission or committee is documented in a report, which is presented at the next Board meeting.

The detailed mandates of these bodies are available on Desjardins's website at:  
[www.desjardins.com/ca/about-us/desjardins/governance-democracy/board-directors/commissions-committees/index.jsp](http://www.desjardins.com/ca/about-us/desjardins/governance-democracy/board-directors/commissions-committees/index.jsp).

Note: In this section, when the name of a director is followed by an asterisk (\*), it means that the person is an independent director. A double asterisk (\*\*) indicates that the person is also a managing director.

## EXECUTIVE COMMITTEE

This committee has the same functions and powers as the board, with the exception of those which the Board may reserve for itself or assign to another committee or commission. It held 8 meetings, including 5 conference calls, in 2018.

The Executive Committee is composed of seven directors:

- Guy Cormier, Chair of the Board and Chair of the Committee
- Serge Rousseau\*, Vice-Chair of the Board
- Jean-Robert Laporte\*, Secretary of the Board
- Annie P. Bélanger\*
- Carole Chevalier\*
- Neil Hawthorn<sup>(i)</sup>
- Yvon Vinet\*

(i) Term began on March 24, 2018

Yves Genest was a member until March 24, 2018.

## COOPERATION AND NETWORK LIAISON COMMISSION

This commission assists the Board with issues related to Desjardins's cooperative culture and the relationship between the Federation's governing bodies and the caisse network. The commission ensures the effective and efficient implementation of mechanisms for collaboration, participation and connection with the network. In addition, it examines Desjardins's Social and Cooperative Responsibility Report and recommends its adoption to the Board. It also makes recommendations to the Board, if need be. It held 6 meetings, including 1 conference call, in 2018.

The Cooperation and Network Liaison Commission is composed of six directors:

- Nadine Groulx\*, Chair
- Michel Allard\*\*
- Benoît Bélanger
- Claude Chapdelaine\*
- André Grenier<sup>(i)</sup>
- Camil Maltais<sup>(i)</sup>

(i) Terms began on May 15, 2018

Mario Simard\* and Pierre Perras\*\* were members until May 15, 2018.

Sylvain Dessureault was a member until September 9, 2018.

Yves Genest was a member until December 31, 2018.

## AUDIT AND INSPECTION COMMISSION

The Audit and Inspection Commission (AIC), established under the *Act Respecting Financial Services Cooperatives*, acts as the audit committee for the Federation's caisse inspection activities. It is composed entirely of independent directors.

The roles and responsibilities of the AIC have been defined to give its members a clear understanding of their oversight duties. It reviews all financial information, supervises the required reporting activities and plays a lead role in overseeing financial disclosure controls and assessing their accuracy. The AIC has a direct line of communication with the Desjardins Group Monitoring Office (DGM), which oversees the internal audit of the Desjardins subsidiaries and components and the inspections of the Quebec and Ontario caisses. It also has a line of communication with the external auditors, should the need arise to discuss and review any issues.

The DGMO provides independent opinions on the management of the caisses. Through its inspections, it monitors the risks associated with network activities and determines whether these risks are being managed according to sound and prudent practices and in compliance with applicable legislation, regulations, standards and rules of conduct. The AIC ensures the independence of Desjardins's internal audit function and adopts its annual action plan. It held 7 meetings, including 1 conference call, in 2018.

The AIC is composed of five directors:

- Louis Babineau\*, Chair
- Michel Doré<sup>(i)</sup>
- Pierre Perras<sup>\*/\*\*<sup>(i)</sup></sup>
- Mario Simard<sup>(i)</sup>
- Michel Tourangeau\*

(i) Terms began on May 15, 2018

Serge Tourangeau\* was a member until March 24, 2018.

Stéphane Corbeil\* and Jean-François Laporte\* were members until May 15, 2018.

Jean-François Laporte\*, Michel Magnan and Robert Saint-Aubin sit on the AIC as observers.

## RISK MANAGEMENT COMMISSION

The Risk Management Commission (RMC) is main role is to assist the Board with overall strategies and directions for risk management. It ensures the implementation of an integrated risk management framework, standards and policies that establish the rules for accepting, monitoring, managing and reporting the material risks that Desjardins is exposed to. The commission also monitors compliance with Desjardins's risk appetite framework and examines the steps that need to be taken when established limits have been exceeded. It held 8 meetings, including 1 conference call, in 2018.

The RMC is composed of five directors:

- Jean-François Laporte<sup>\*(i)</sup>, Chair
- André Grenier<sup>\*(i)</sup>
- Camil Maltais\*
- Roch Ouellet\*
- Stéphane Trottier\*

(i) Terms began on May 15, 2018

Christian Savard\* and Serge Tourangeau\* were members until March 24, 2018.

Stéphane Corbeil\* was a member until May 15, 2018.

Louis Babineau\*, Benoît Bélanger, Claudia Champagne and Sonia Gauthier sit on the RMC as observers.

## HUMAN RESOURCES COMMISSION

The Human Resources Commission (HRC) supports the Board in the following areas: governance and risk management of issues relating to human resources and overall compensation across Desjardins; creation and maintenance of the integration and skills development program for general managers, managers and employees; the senior management succession plan; creation and maintenance of the profile of general managers, managers and employees; annual salary recommendations, including incentive plans; the group insurance plan; changes to the pension plan; union relations; the management structure, etc. The mandate of the HRC does not include the terms of employment for the President and CEO. It held 7 meetings, including 2 conference calls, in 2018.

The HRC is composed of five directors:

- Guy Cormier, Chair of the Board and Chair of the Commission
- Serge Rousseau<sup>\*(i)</sup>, Vice-Chair of the Board
- Jean-Robert Laporte\*, Secretary of the Board
- Carole Chevalier\*
- Mario Simard\*

(i) Terms began on May 15, 2018

Annie P. Bélanger\* and Yvon Vinet\* were members until May 15, 2018.

## COMMITTEE ON THE AGGREGATE REMUNERATION OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER OF DESJARDINS GROUP

This committee, whose members are all independent directors, is mandated to make recommendations to the Board regarding the President and CEO's remuneration, working conditions, annual objectives and performance review. It held 3 meetings in 2018.

The CAR is composed of four directors:

- Serge Rousseau<sup>\*(i)</sup>, Vice-Chair of the Board and Chair of the Committee
- Jean-Robert Laporte\*, Secretary of the Board<sup>(i)</sup>
- Carole Chevalier<sup>\*(i)</sup>
- Mario Simard\*

(i) Terms began on May 15, 2018

Annie P. Bélanger\* and Yvon Vinet\* were members until May 15, 2018.

## CORPORATE GOVERNANCE COMMISSION

The Corporate Governance Commission (CGC) supports the Board in applying and updating Desjardins's corporate governance framework and policy. The CGC examines guidelines and reports issued by regulatory authorities. It also assists the Board in applying its enhanced group profile. The CGC oversees the selection process for the directors of Desjardins's subsidiaries, the performance review program for members of the Board and its commissions and committees, as well as the integration and skills development program for Federation directors. It also administers various policies, including the policy on the compensation of directors and BEPC members and the policy on Desjardins's commitment to sustainable development. It held 10 meetings, including 5 conference calls, in 2018.

The CGC is composed of five directors:

- Serge Rousseau\*, Vice-Chair of the Board and Chair of the Commission<sup>(i)</sup>
- Annie P. Bélanger<sup>(i)</sup>
- Guy Cormier, Chair of the Board
- Nadine Groulx\*
- Camil Maltais<sup>(i)</sup>

(i) Terms began on May 15, 2018

Christian Savard\* was a member until March 24, 2018.

Carole Chevalier\* and Yvon Vinet\* were members until May 15, 2018.

## DESJARDINS GROUP INVESTMENT COMMISSION

The Investment Commission (IC) role is to monitor the markets and develop an integrated overview to provide a Desjardins-wide framework for portfolio positioning and asset distribution. The IC also follows up on strategies and directions and acts as an advisory body. The commission's activities complement—but do not overlap—the RMC and Desjardins's various other investment committees. It held 4 meetings in 2018.

The IC is composed of five directors:

- Carole Chevalier\*, Chair
- Benoît Bélanger<sup>(i)</sup>
- Stéphane Corbeil<sup>(i)</sup>
- Neil Hawthorn
- Stéphane Trottier\*

(i) Terms began on May 15, 2018

Robert J. Boucher and Normand Provost sit on the IC as observers.

Yves Genest and Camil Maltais\* were members until May 15, 2018.

Sylvain Dessureault was a member until September 9, 2018.

## ELECTION COMMITTEE

This committee oversees the proper conduct of the election process for positions on the Board and BEPC. It's also responsible for overseeing all processes for electing the President and CEO. The committee provides guidelines for the electoral process and ensures compliance with them, sets up processes that enable the electoral college to properly fulfill its role and assesses the nominations received based on the enhanced group profile adopted by the Board. The committee also establishes any other measures or rules necessary for the electoral process to run properly and makes any other decisions regarding the process. The Election Committee was formed when the Federation bylaws were adopted on September 25, 2018, and committee members assumed their roles on December 7, 2018. While the committee is not composed of directors, it is accountable to the Board. The committee met for the first time on December 19, 2018.

The Election Committee is composed of five caisse directors who are neither Federation directors nor BEPC members:

- Lorraine Bédard, Chair
- Marie-Claude Beaudin, Vice-Chair
- Érik Asselin
- Marie Caron
- Marc Lemieux

## DESJARDINS GROUP RETIREMENT COMMITTEE

By virtue of the powers vested in it by the *Supplemental Pension Plans Act* and by the *Desjardins Group Pension Plan Regulation*, the Retirement Committee (DGRC) is in charge of administering the Desjardins Group Pension Plan (DGPP), managing the pension fund and paying members and their survivors the benefits they are entitled to. The committee members, who represent employers, active members, non-active members and beneficiaries, share the role of trustee for the pension fund. It held four meetings in 2018.

The Federation assumes the responsibilities of the DGPP's sponsor. The Federation's Board has decision-making powers in certain areas, including the *Desjardins Group Pension Plan Regulation*, the nature and terms of benefit payments to members and retirees, contribution rates and the use of any surplus. The Federation stands surety for the obligations (payment of benefits) resulting from the participation of all Desjardins employers in the DGPP.

The DGRC is composed of 14 members: six employer representatives (including the Chair), four who represent active members, three who represent non-active members and beneficiaries, and one external member. The employer representatives and the external member are appointed by the Federation's Board, and those who represent active members, non-active members and beneficiaries are elected. The DGRC's governance structure will be changing in 2019 as a result of the new governance structure adopted in late 2018. It held 4 meetings in 2018.

**Employer representatives:**

- Yvon Vinet\*, Chair<sup>(i)</sup>
- Michel Allard\*/\*\*
- Claude Chapdelaine\*
- Stéphane Corbeil<sup>(i)</sup>
- Roch Ouellet\*
- Pierre Perras\*/\*\*

(i) Terms began on May 15, 2018

Christian Savard\* was a member until March 24, 2018.

Serge Rousseau\* was a member until May 15, 2018.

**Active member representatives:**

- Robert Bastien
- Vincent Coulombe<sup>(i)</sup>
- Dominique Laurin
- Julie Tremblay

(i) Term began on March 23, 2018

David Gingras was a member until March 23, 2018.

**External member:**

- Marc Saint-Pierre

**Non-active member and beneficiary representatives:**

- Michel-Pierre Bergeron: member selected by retirees, beneficiaries and members entitled to a deferred pension
- Mario Lévesque: observer selected by active members
- Robert Desbiens: observer selected by retirees, beneficiaries and members entitled to a deferred pension

## DGRC INVESTMENT COMMITTEE

Under the responsibility of the DGRC, which adopts the investment policy, the Investment Committee's mandate is to ensure that the policy is applied, respected and followed. The committee approves investments and ensures they are monitored. It held 12 meetings, including six conference calls and three videoconferences, in 2018. The committee's membership and mandate will be changing in 2019 as a result of the new governance structure adopted in late 2018.

The DGRC Investment Committee is composed of eight members:

- Yvon Vinet<sup>(i)</sup>, Chair
- Michel Allard\*/\*\*
- Robert Bastien
- Claude Chapdelaine\*
- Stéphane Corbeil<sup>(i)</sup>
- Pierre Perras\*/\*\*
- Marc Saint-Pierre, external member
- Nicolas Richard, observer

(i) Terms began on May 15, 2018

Christian Savard\* was a member until March 24, 2018.

Serge Rousseau\* was a member until May 15, 2018.

## DGRC RISK MANAGEMENT ADVISORY COMMITTEE

Under the responsibility of the DGRC, the Risk Management Advisory Committee is responsible for assessing the main risks associated with managing the DGPP's activities. It does this by issuing opinions on the integrated risk profile submitted to the DGRC, on the asset allocation strategy and on investment opportunities, for which the opinion is forwarded to the RCIC. It held nine meetings, including five conference calls and four videoconferences, in 2018. The committee's membership and mandate will be changing in 2019 as a result of the new governance structure adopted in late 2018.

The DGRC Risk Management Advisory Committee is composed of six members:

- Renaud Coulombe, Vice-President, Legal Affairs, Desjardins Group
- Marie-Claude Desroches, Manager, Credit Analysis, Investments, Desjardins Group
- François Hudon, Director, Liability Management, Asset Allocation and Risk, Desjardins Group Pension Plan
- Mario Robitaille, Vice-President, Insurance Risk, Desjardins Group
- Guy Rochette, Director, Corporate Banking, Credit Granting, Counterparty and Issuer Risk, Risk, Credit Granting and Special Loans Division, Desjardins Group
- Marc Saint-Pierre, consultant for the DGRC

## BOARD OF ETHICS AND PROFESSIONAL CONDUCT

Pursuant to the *Act Respecting Financial Services Cooperatives*, the Federation has a Board of Ethics and Professional Conduct (BEPC) that is independent from its Board of Directors (Board). Five members are directors of local caisses. The BEPC is supported by a team that reports to the Office of the Secretariat General and Governance and Sustainable Development Division, which enables it to organize education and training activities and provide advisory services.

One of the main responsibilities of the BEPC is to ensure the independence and objectivity of the Federation's inspection service for the caisses (DGMO) and make recommendations to the Board regarding the appointment of the person responsible for managing this service. In addition to the above-mentioned responsibilities, the BEPC's role includes adopting the rules of conduct applicable to the directors of Desjardins and its subsidiaries and to the employees of the Federation and the caisses; presenting these rules for approval to the Board and ensuring the caisses and the Federation comply with them; supporting the caisses and the Federation in applying the rules of conduct; issuing advice, observations and recommendations on ethical and professional conduct issues (Desjardins's mission and values), particularly in cases of misconduct; notifying the Board of violations of the rules of professional conduct or of violations by the Federation of the *Act Respecting Financial Services Cooperatives* or the regulations governing restricted party transactions and conflicts of interest; and ensuring that complaints about the Federation originating from the caisses or other Federation members (holding companies or subsidiaries) are addressed. Members of the BEPC and directors attend meetings with AMF representatives. In 2018, the BEPC made changes to Desjardins's *Code of Professional Conduct* that were approved by the Federation's Board. The BEPC holds closed-door meetings that are not attended by management.

The BEPC held seven meetings, including three conference calls, in 2018. Its members were also invited to attend the annual conference of the Réseau d'éthique organisationnelle du Québec.

The BEPC is composed of five members:

- Michel Guénette, Chair
- Normand Gingras
- Maryse Lapierre
- Ronald Pichette
- Michel Yelle

Michel C. Bélsile, Lucie Tremblay and Roger Turcotte were members until December 7, 2018.

## DESJARDINS GROUP MANAGEMENT COMMITTEE

This committee supports the President and CEO and the Board in their responsibility of managing Desjardins. The Desjardins Group Management Committee (DGMC) helps the Board incorporate the strategic directions of the cooperative network, business sectors and support functions and implement business development strategies. It also oversees operations in accordance with the rules and requirements set by the Board and other Desjardins governing bodies. The DGMC is responsible for operational files with economic, environmental and social significance that have an impact on Desjardins. It held 21 meetings, including 1 conference call, in 2018.

The DGMC is composed of 11 members of management, including four women (36%):

- **Guy Cormier**  
President and CEO of Desjardins
- **Denis Berthiaume**  
Senior Executive Vice-President and COO
- **Réal Bellemare**  
Executive Vice-President, Finance, Treasury and Administration and CFO
- **Marie-Claude Boisvert**  
Executive Vice-President, Business Services
- **Francine Champoux**  
Executive Vice-President, Risk Management
- **Gregory Chrispin**  
Executive Vice-President, Wealth Management and Life and Health Insurance
- **Marie-Huguette Cormier**  
Executive Vice-President, Human Resources and Communications
- **Denis Dubois**  
Executive Vice-President, Property and Casualty Insurance
- **Chadi Habib**  
Executive Vice-President, Information Technology
- **Éric Lachaine**  
Executive Vice-President, Caisse Network and Member and Client Services
- **Nathalie Larue**  
Executive Vice-President, Strategy, Marketing and Personal Services

The Vice-President, President's Office, Cooperation and Director Support, always attends DGMC meetings.

DGMC members are deemed to be Federation managers within the meaning of section 93 of the *Act Respecting Financial Services Cooperatives*. The following individuals are also considered Federation managers:

- Daniel Dupuis, Chief Monitoring Officer, Desjardins Group
- Sylvain Perreault, Vice-President and Chief Compliance Officer
- Renaud Coulombe, Vice-President and Chief Legal Officer
- Isabelle Garon, Vice-President, President's Office, Cooperation and Director Support
- Pauline D'Amboise, Secretary General and Vice-President Governance and Sustainable Development

The DGMC has Desjardins-wide coordination committees in the following areas:

- Disclosure
- Finance and risk management
- Environmental, social and governance issues
- Development planning and follow-up

## DIRECTOR COMPENSATION

Certain Desjardins components, namely the Federation and Desjardins Capital Inc., are subject to obligations regarding the disclosure of director compensation. As required by CSA *National Instrument 51-102 Respecting Continuous Disclosure Obligations*, the compensation of directors from these components is presented in the Federation's Annual Information Form and the disclosure document filed by Desjardins Capital Inc. and incorporated by reference in this annual report. The Annual Information Form and the disclosure document are available on the SEDAR website ([www.sedar.com](http://www.sedar.com)) under each component's respective company profile.

Compensation rates for the members of the boards of directors of the Federation, Desjardins Technology Group Inc. and Desjardins Trust Inc., and the members of the board of ethics and professional conduct of the Federation

	Federation <sup>(1)</sup>	Subsidiaries
Chair of the Board of Directors <sup>(2)</sup>	\$0 This position is held by the President and CEO of Desjardins	\$11,500
Annual stipend for the Chair of a commission or committee of the Board of Directors <sup>(3)</sup>	\$7,400 (not including the AIC)	\$7,500
Additional annual stipend for the Chair of the AIC	\$14,800	N/A
Annual stipend for the Vice-Chair of the Board of Directors	\$22,800	N/A
Annual stipend for a member of the Board of Directors <sup>(4)</sup>	\$51,500	\$11,500
Annual stipend for a member of a commission or a committee of the Board of Directors <sup>(5)</sup>	\$2,300	\$2,300
Additional annual stipend for a member of the AIC	\$2,300	\$2,300 (Audit and Risk Management Committee)
Attendance fee for a meeting of the Board of Directors	\$1,375 (daily maximum)	\$1,400 (daily maximum)
Attendance fee for a meeting of a commission or committee of the Board of Directors <sup>(6)</sup>	\$1,375 (daily maximum) \$685 (per half-day)	\$1,400 (daily maximum) \$700 (per half-day)
Conference call	\$230	\$230
Attendance fee for a meeting of the Board of Ethics and Professional Conduct or the Professional Conduct Committee <sup>(7)</sup>	\$2,750 (for the Chair) \$1,375 (for members)	\$700 (per half-day)

\*\*\* The compensation rates were updated in 2018 further to the review of the policy on the compensation of directors and BEPC members and changes to the organization's governance structure.

N/A: Not applicable

- (1) The director compensation indicated for the Federation includes, where applicable, the portion paid to members of the Board to also serve as directors for Desjardins Trust Inc. and Desjardins Technology Group Inc.
- (2) The position of Chair of the boards of directors of the following subsidiaries is held by a member of the Federation's Board: Développement international Desjardins, Desjardins General Insurance Group Inc., Desjardins Financial Security Life Assurance Company and Desjardins Financial Corporation Inc.
- (3) The attendance fee is doubled in lieu of the annual stipend for the Chairs of commissions or committees that hold fewer than four meetings per year, except for the Chair of the CAR.
- (4) The stipend paid to the two managing directors is \$35,800.
- (5) A member's annual stipend is paid regardless of the number of commissions or committees they sit on for the Federation, Desjardins Trust Inc. or Desjardins Technology Group Inc. In other words, a single stipend is paid for all positions held for all three entities.
- (6) The maximum daily attendance fee for the Federation, Desjardins Trust Inc. and Desjardins Technology Group Inc. is \$1,375, regardless of the number of board of directors, commission or committee meetings a member attends in a single day. Every effort is made to schedule multiple meetings on the same day to keep costs to a minimum. The Federation's Board may invite any caisse director to sit on any of its committees. The Board determines the compensation to be paid based on the nature of the responsibilities entrusted to the caisse director and the compensation schedule. General managers who sit on the Board or on a commission or committee do not receive an attendance fee.
- (7) This represents the fee for full-day meetings of the Federation's BEPC. The fee for half-day meetings is \$1,375 for the Chair and \$685 for members.

## Director compensation

The compensation paid to each member in 2018 for the duties they assume as directors of the Federation, Desjardins Trust Inc., Desjardins Technology Group Inc., Desjardins Capital Inc. or for other duties listed below is detailed as follows:

Name	Compensation received as a director of the Federation, Desjardins Technology Group Inc., Desjardins Trust Inc. and Desjardins Capital Inc. <sup>(9)</sup>		Other fees <sup>(1)</sup>		2018 TOTAL
	Attendance fees	Annual stipend	Attendance fees	Annual stipend	
Allard, Michel*	\$36,264.99	\$40,125.00	\$9,240.00	\$10,000.00	\$95,629.99
Babineau, Louis	\$46,217.61	\$68,301.00	\$2,232.40	\$24,276.00	\$141,027.01
Bélanger, Annie P. (Chair of the Board, DID) <sup>(2)</sup>	\$40,346.57	\$51,401.00	\$16,178.43	\$50,650.00	\$158,576.00
Bélanger, Benoît	\$1,200.00	\$40,151.00	\$0	\$0	\$41,351.00
Chapdelaine, Claude	\$35,834.99	\$51,401.00	\$0	\$10,000.00	\$97,235.99
Chevalier, Carole	\$43,214.92	\$58,351.00	\$1,750.09	\$10,747.00	\$114,063.01
Corbeil, Stéphane	\$39,355.37	\$51,401.00	\$604.62	\$9,972.21	\$101,333.20
Cormier, Guy (Chair of the Board, DSF) <sup>(2)(4)</sup>	N/A	N/A	N/A	N/A	N/A
Dessureault, Sylvain <sup>(7)</sup>	\$900.00	\$24,462.31	\$0	\$0	\$25,362.31
Doré, Michel <sup>(3)</sup>	\$29,595.94	\$40,980.72	\$1,374.04	\$3,514.89	\$75,465.59
Genest, Yves <sup>(8)</sup>	\$1,200.00	\$41,300.00	\$0	\$3,000.00	\$45,500.00
Grenier, André <sup>(3)</sup>	\$32,989.99	\$39,830.72	\$0	\$0	\$72,820.71
Groulx, Nadine	\$41,324.99	\$55,931.56	\$0	\$0	\$97,256.55
Hawthorn, Neil	\$1,400.00	\$40,151.00	\$0	\$11,050.00	\$52,601.00
Laporte, Jean-François	\$45,410.36	\$61,612.12	\$604.62	\$1,847.22	\$109,474.32
Laporte, Jean-Robert (Chair of the Board, DGAG) <sup>(2)</sup>	\$42,052.76	\$51,401.00	\$20,172.25	\$41,970.00	\$155,596.01
Maltais, Camil	\$45,274.99	\$51,401.00	\$0	\$0	\$96,675.99
Ouellet, Roch	\$38,384.99	\$51,401.00	\$0	\$7,500.00	\$97,285.99
Perras, Pierre*	\$38,315.94	\$41,275.00	\$554.04	\$13,514.89	\$93,659.97
Rousseau, Serge <sup>(6)</sup>	\$39,768.66	\$81,356.82	\$1,456.35	\$21,212.50	\$143,794.33
Savard, Christian <sup>(5)</sup>	\$18,300.00	\$11,148.88	\$200.00	\$2 275.28	\$31,924.16
Simard, Mario (Chair of the Board, FSD) <sup>(2)</sup>	\$43,325.94	\$54,952.39	\$10,774.04	\$7,027.78	\$116,080.15
Tourangeau, Michel	\$40,378.82	\$52,551.00	\$1,036.16	\$5,376.00	\$99,341.98
Tourangeau, Serge <sup>(5)</sup>	\$16,780.00	\$14,106.74	\$720.00	\$1,137.64	\$32,744.38
Trottier, Stéphane	\$43,784.99	\$51,401.00	\$3,800.00	\$12,500.00	\$111,485.99
Vinet, Yvon	\$42,397.92	\$61,602.95	\$1,832.09	\$27,025.00	\$132,857.96
<b>Total</b>	<b>\$804,020.74</b>	<b>\$1,187,997.21</b>	<b>\$72,529.13</b>	<b>\$274,596.41</b>	<b>\$2,327,893.49</b>

N/A: Not applicable

\* Managing director

(1) Amounts received for chairing the board of a subsidiary, sitting on the DGRC or the RCIC, sitting on the board of directors of Desjardins Financial Corporation Inc., Desjardins Capital Inc., Desjardins Security Fund, Desjardins Technology Group Inc., Desjardins Shared Services Group Inc. and contributing to other ad hoc committees.

(2) Développement international Desjardins, Desjardins General Insurance Group Inc., Desjardins Financial Security Life Assurance Company and Desjardins Security Fund.

(3) Term began on March 24, 2018.

(4) Desjardins's President and CEO does not receive any compensation for the position of Chair of the boards of directors of the Federation, Desjardins Trust Inc., Desjardins Technology Group Inc., Desjardins Capital Inc., Desjardins General Insurance Group and Desjardins Financial Security.

(5) Christian Savard's and Serge Tourangeau's terms ended on March 24, 2018.

(6) Serge Rousseau receives compensation for his roles as Vice-Chair of the Board, Chair of the CGC and Chair of the CAR.

(7) Sylvain Dessureault was a member until September 9, 2018.

(8) Yves Genest was a member until December 31, 2018.

(9) These amounts include fees paid for regional council and group caisses council meetings (these councils were abolished on September 25, 2018)

## Compensation of members of the Federation's board of ethics and professional conduct

Name	Attendance fees
Belisle, Michel C., Secretary	\$6,805.00
Guénette, Michel, Chair	\$11,770.00
Gingras, Normand	\$6,345.00
Lapierre, Maryse	\$6,345.00
Pichette, Ronald	\$6,345.00
Tremblay, Lucie	\$5,660.00
Turcotte, Roger	\$6,345.00
Yelle, Michel	\$6,245.00

Michel C. Bélisle, Lucie Tremblay and Roger Turcotte were members until December 7, 2018.

## Record of attendance for Federation directors

Name	BoD	BoD conf. calls	EC	CNLC	AIC	RMC	HRC	CAR	CGC	IC	DGRC	RCIC
Allard, Michel*/**	14/14	4/5		6/6							4/4	12/12
Babineau, Louis*	14/14	5/5			7/7	8/8						
Bélanger, Annie P.*	13/14	3/5	8/8				3/3	2/2	5/6			
Bélanger, Benoît	14/14	5/5		4/4		8/8				3/3		
Chapdelaine, Claude*	14/14	4/5		6/6							4/4	12/12
Chevalier, Carole*	14/14	4/5	8/8				4/4	1/1	4/4	4/4		
Corbeil, Stéphane*	14/14	5/5			3/3	4/4				3/3	3/3	6/7
Cormier, Guy	14/14	5/5	8/8				7/7		10/10			
Dessureault, Sylvain	9/11	3/3		4/4						1/2		
Doré, Michel&	9/9	3/3			3/4							
Genest, Yves	10/14	3/5	1/1	2/4	1/4					1/1		
Grenier, André*	9/9	3/3		4/4		4/4						
Groulx, Nadine*	14/14	5/5		6/6					10/10			
Hawthorn, Neil	14/14	4/5	7/7		3/3					4/4		
Laporte, Jean-François*	14/14	5/5			6/7	4/4						
Laporte, Jean-Robert*	14/14	4/5	8/8				6/7	3/3				
Maltais, Camil*	14/14	5/5		4/4		8/8			6/6	1/1		
Ouellet, Roch*	13/14	4/5				8/8					4/4	
Perras, Pierre*/**	14/14	5/5		2/2	3/4						4/4	11/12
Rousseau, Serge*	14/14	5/5	8/8				4/4	1/1	8/8		1/1	4/4
Savard, Christian*	5/5	2/2				3/3			2/2		1/1	2/3
Simard, Mario*	14/14	5/5		2/2	4/4		7/7	3/3				
Tourangeau, Michel*	14/14	5/5			7/7							
Tourangeau, Serge*	5/5	2/2			2/2	3/3						
Trottier, Stéphane*	14/14	5/5				8/8				4/4		
Vinet, Yvon*	14/14	5/5	8/8				3/3	2/2	4/4		3/3	7/7

BoD = Board of Directors, EC = Executive Committee, CNLC = Cooperation and Network Liaison Commission, AIC = Audit and Inspection Commission, RMC = Risk Management Commission, HRC = Human Resources Commission, CAR = Committee on the Aggregate Remuneration of the President and CEO of Desjardins, CGC = Corporate Governance Commission, IC = Desjardins Group Investment Commission, DGRC = Desjardins Group Retirement Committee and RCIC = Desjardins Group Retirement Committee Investment Committee

Note: In the above table, when the name of a director is followed by an asterisk (\*), it means that the person is an independent director. A double asterisk (\*\*) indicates that the person is also a managing director.

The Board held 14 meetings over 22 days and 5 conference calls, in 2018. The Board may invite any caisse director to sit on any of its committees. The Board determines the compensation to be paid based on the nature of the responsibilities entrusted to them and the compensation schedule. Directors may be absent for professional or personal reasons, but justification is required in all instances.

## Record of attendance for the members of the Federation's Board of Ethics and Professional Conduct

Name	Number of meetings
Bélisle, Michel C., secrétaire	7/7
Guénette, Michel, président	5/7
Gingras, Normand	7/7
Lapierre, Maryse	7/7
Pichette, Ronald	7/7
Tremblay, Lucie	6/7
Turcotte, Roger	7/7
Yelle, Michel	7/7

Michel C. Bélisle, Lucie Tremblay and Roger Turcotte were members until December 7, 2018.

# Main subsidiaries<sup>(1)</sup>

As at December 31, 2018

Subsidiaries	Main activities
<b>FÉDÉRATION DES CAISSES DESJARDINS DU QUÉBEC</b>	Planning, supervision, coordination, treasury and development of Desjardins Group, Desjardins Group's financial agent on the Canadian and international markets and payment solution and credit card issuance
DESJARDINS CAPITAL INC.	Capital issuances on financial markets and financing for the Desjardins caisses
COLLABRIA FINANCIAL SERVICES INC.	Payment solution and credit card issuance
DESJARDINS FINANCIAL SERVICES FIRM INC.	Mutual fund brokerage and financial planning services
DESJARDINS CAPITAL MANAGEMENT INC.	Development and venture capital fund management
DESJARDINS FINANCIAL HOLDING INC.	Holding company
Zag Bank	Financial institution
Desjardins Financial Corporation Inc.	Holding company
Desjardins Global Asset Management Inc.	Asset management
Desjardins General Insurance Group Inc.	Property and casualty insurance
<i>Certas Direct Insurance Company</i>	Property and casualty insurance
<i>Certas Home and Auto Insurance Company</i>	Property and casualty insurance
<i>Desjardins General Insurance Inc.</i>	Property and casualty insurance
<i>Desjardins General Insurance Services Inc.</i>	Property and casualty insurance
<i>The Personal General Insurance Inc.</i>	Property and casualty insurance
<i>The Personal Insurance Company</i>	Property and casualty insurance
Desjardins Financial Security Life Assurance Company	Life and health insurance and financial services
<i>Assistel Inc.</i>	Assistance services
<i>Desjardins Investment Product Operations Inc.</i>	Processing and administration of savings and investment accounts and specialized products for Desjardins Group components
<i>Desjardins Investments Inc.</i>	Design, administration and distribution of insurance and savings products
<i>Desjardins Financial Security Investments Inc.</i>	Mutual fund and insurance brokerage
Desjardins Trust Inc.	Asset custody and trust services
Desjardins Investment Management Inc.	Investment management
Desjardins Technology Group Inc.	Development, maintenance and modernization of Desjardins Group technology
Aviso Wealth	Wealth management company held in equal shares by Desjardins Group and the partnership between five provincial credit union centrals and CUMIS Group
Desjardins Securities Inc.	Securities brokerage

<sup>(1)</sup> Additional information on the *Fédération des caisses Desjardins du Québec*'s activities is presented in Section 2.3 "Analysis of business segment results" in the 2018 Management's Discussion and Analysis.

# Glossary

## Acceptance

Short-term debt security traded on the money market, guaranteed by a financial institution for a borrower in exchange for a stamping fee.

## Allowance for credit losses

The loss allowance for expected credit losses reflects an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, and takes into account reasonable and supportable information about past events, current conditions and forecasts of future economic conditions.

## Amortized cost

For a financial asset or a financial liability, represents the historical cost at initial recognition, decreased or increased by amortization and any differences that made it fluctuate from initial recognition to maturity.

## Annuity premium

Amount invested by a policyholder in order to receive annuity payments, immediately or after an accumulation period.

## Assets under administration

Assets administered by a financial institution that are beneficially owned by its caisse members or clients and are therefore not recognized on its Consolidated Balance Sheet. Services provided in respect of such assets are administrative in nature, such as custodial services, collection of investment income and settlement of buy and sell transactions. Assets resulting from securitization transactions are not considered assets under administration.

## Assets under management

Assets managed by a financial institution that are beneficially owned by its caisse members or clients and are therefore not recognized on its Consolidated Balance Sheet. Services provided in respect of assets under management include selecting investments and offering investment advice. Assets under management may also be administered by the financial institution. Assets resulting from securitization transactions are not considered assets under management.

## Autorité des marchés financiers (AMF)

Organization whose mission is to enforce the laws governing the financial industry in Quebec, particularly in the areas of insurance, securities, deposit-taking institutions and financial product and service distribution.

## Basis point

Unit of measure equal to one one-hundredth of a percent (0.01%).

## Bond

Certificate evidencing a debt under which the issuer promises to pay the holder a specified amount of interest for a specified period of time, and to repay the borrowing at maturity. Generally, assets are pledged as security for the borrowing, except in the case of government or corporate bonds. This term is often used to describe any debt security.

## Capital ratios

Regulatory Tier 1A capital, Tier 1 capital or total regulatory capital divided by risk-weighted assets. These measures are governed by the guidelines issued by the AMF, which are based on the standards developed by the Basel Committee on Banking Supervision.

## Catastrophe and notable event

### - Catastrophe

In property and casualty insurance, group of claims caused by one or multiple close events arising from, among others, natural or other than natural causes, for which the cost is deemed significant since it reaches a minimum threshold, established annually *Fédération des caisses Desjardins du Québec's* (the Federation) management, for the reinsurance program retention.

- Natural catastrophes can take many forms and include, but are not limited to, hurricanes, tornados, windstorms, hailstorms, heavy rainfalls, ice storms, floods, extreme weather conditions and wildfires.
- Catastrophes other than natural catastrophes include, but are not limited to, terrorist acts, riots, explosions, crashes, train wrecks, large-scale cyber attacks.

### - Notable event

In property and casualty insurance, group of claims caused by one or multiple close events arising from, among others, natural or other than natural causes, for which the impact on the loss ratio and claims frequency is deemed significant by the Federation's management.

## Commercial mortgage-backed security

Security created through the securitization of a pool of commercial mortgage loans.

**Commitment**- Direct commitment

Any agreement entered into by a Desjardins Group component with a natural or legal person creating a on- or off-balance sheet exposure, either disbursed or non-disbursed, revocable or irrevocable, with or without condition, that may lead to losses for the component if the debtor is unable to meet its obligations.

- Indirect commitment

Any financial receivable creating a credit exposure that is acquired by a Desjardins Group component in connection with a purchase on the market or the delivery of a financial asset pledged as collateral by a client or a counterparty, whose value may change in particular as a result of the deterioration of the creditworthiness of the counterparty associated to this receivable or changes in market prices.

**Counterparty and issuer risk**

Credit risk related to different types of securities, derivative financial instruments and securities lending transactions.

**Covered bond**

Full recourse on-balance sheet bond issued by a financial institution and secured by assets, comprised mainly of mortgage loans, over which investors enjoy a priority claim in the event of an issuer's insolvency or bankruptcy. These assets are separated from the issuer's assets in the event of the issuer's insolvency or bankruptcy and belong to a bankruptcy remote structured entity that guarantees the bond.

**Credit commitment**

Unused portions of authorizations to extend credit in the form of loans, guarantees or letters of credit, whose primary purpose is to ensure that caisse members and clients have funds available, when necessary, for variable maturity terms and under specific conditions.

**Credit-impaired loan**

A financial asset is credit impaired when one or more events that have a detrimental impact on the estimated cash flows of that financial asset have occurred or when contractual payments are 90 days past due.

**Credit instrument**

Credit facility offered in the form of a loan or other financing vehicle recognized in the Consolidated Balance Sheets or in the form of an off-balance sheet product. Credit instruments include credit commitments, documentary letters of credit as well as guarantees and standby letters of credit.

**Credit risk**

Risk of losses resulting from a borrower's, guarantor's, issuer's or counterparty's failure to honour its contractual obligations, whether or not such obligations appear on the Consolidated Balance Sheets.

**Credit valuation adjustment**

Adjustment representing the market value of a potential loss on over-the-counter derivatives due to counterparty risk.

**Defined benefit pension plan**

Pension plan guaranteeing each participant a defined level of retirement income that is often based on a formula set by the plan in terms of the participant's salary and years of service.

**Derivative financial instrument, or derivative**

Financial contract whose value fluctuates based on an underlying asset, but that does not require holding or delivering the underlying asset itself. Derivatives are used to transfer, modify or reduce current or expected risks, including risks related to interest and exchange rates and financial indexes.

**Desjardins Group component**

Cooperative or subsidiary that is part of Desjardins Group.

**Dividend to member caisses**

The Federation distributes to its member caisses a portion of its surplus earnings for a given year, taking into account its financial capacity. This distribution, called dividend to member caisses, is paid based on the volume of assessments paid during the year by the member caisses to the Federation.

**Documentary letter of credit**

Instrument issued for a caisse member or a client that represents Federation's agreement to honour drafts presented by a third party upon completion of certain activities, up to a set maximum amount. Federation is exposed to the risk that the client does not ultimately pay the amount of the drafts. However, the amounts used are secured by the related goods.

**Economic capital**

Amount of capital that an institution must maintain, in addition to anticipated losses, to ensure its solvency over a certain horizon and at a high confidence level.

**Effective interest rate**

Rate determined by discounting total future cash flows, including those related to commissions paid or received, premiums or discounts and transaction costs.

**Environmental or social risk**

Risk that the impact of an environmental event or a social issue in connection with Desjardins Group's operations or its financing, investing or insurance activities could result in financial losses or damage Desjardins Group's reputation.

**Exposure at default**

Estimate of the amount of a given exposure at time of default. For balance sheet exposures, it corresponds to the balance as at observation time. For off-balance sheet exposures, it includes an estimate of additional draws that may be made between observation time and default.

**Exposures related to residential mortgage loans**

In accordance with the regulatory capital framework, risk category that includes mortgage loans and credit margins secured by real property granted to individuals.

**Fair value**

Price that would be received to sell an asset or paid to transfer a liability in an orderly transaction at the measurement date.

**Fair value measurement**

Measurement to determine the approximate value at which financial instruments could be traded in a current transaction between willing parties.

**Financial asset-backed security**

Security created through the securitization of a pool of financial assets.

**Foreign exchange risk**

Risk that arises when the actual or expected value of assets denominated in a foreign currency is higher or lower than that of liabilities denominated in the same currency.

**Forward contract**

Contractual commitment to sell or purchase a determined quantity of a specified underlying asset on a future specified date and at a predetermined price. These contracts, which are derivatives, are tailored and traded over the counter.

**Forward exchange contract**

Contractual commitment to sell or purchase a fixed amount of foreign currency on a specified future date and at a predetermined exchange rate.

**Futures contract**

Contractual commitment to sell or purchase a determined quantity of a specified underlying asset on a future specified date and at a predetermined price. These contracts, which are derivatives, are standardized and exchange-traded.

**Gross premiums written**

In property and casualty insurance, the premiums stipulated in insurance policies issued during the year.

**Guarantee and standby letter of credit**

Irrevocable commitment by a financial institution to make payments in the event that a caisse member or client cannot meet financial obligations to third parties. Federation's policy with respect to collateral received for these instruments is generally the same as for loans.

**Hedge fund**

Investment fund offered to accredited investors. A hedge fund manager enjoys great latitude with respect to the investment strategies to be used, which may include selling short, leverage, program trading, swaps, arbitrage and derivatives.

**Hedging**

Transaction designed to reduce or offset the Federation's exposure to one or more financial risks that involves taking a position exposed to effects that are equivalent, but of opposite direction, to the effects of market fluctuations on an existing or forecasted position.

**Incremental risk charge (IRC)**

Additional capital charge related to default and migration risks of positions with issuer risk in trading portfolios.

**Indemnification commitment related to securities lending**

Commitment made to caisse members and clients with whom Federation entered into securities lending agreements and intended to ensure that the fair value of the securities lent will be reimbursed if the borrower does not return the borrowed securities or if the fair value of assets held as collateral is insufficient to cover the fair value of the securities lent. These commitments usually mature before being used.

**Insurance and investment contract liabilities**

Provision representing the amount of an insurance company's commitments toward all insureds and beneficiaries, established to guarantee the payment of benefits.

**Insurance premium**

Payment that the insurance policyholder is required to make to maintain the contract in force. This payment represents the cost of insurance and can sometimes include a savings component. The premium is directly proportional to the amount of risk underwritten by the insurer.

**Insurance risk**

Risk that events may turn out differently from the assumptions used when designing, pricing or measuring actuarial reserves for insurance products, and that profitability of these products may be affected.

**Insurance sales**

Metric used to measure growth in Wealth Management and Life and Health Insurance segment operations. It is equal to annualized gross new premiums under group and individual insurance policies.

**Internal Model Method**

Approach used to calculate, with internal models, risk-weighted assets for the four areas of market risk: interest rate risk, equity price risk, foreign exchange risk and commodity risk. The calculation is based on different risk measures, such as Value at Risk, stressed Value at Risk and the incremental risk charge (IRC).

**Internal Ratings-Based Approach**

Approach under which risk weighing is based on the type of counterparty (individuals, small or medium-sized business, large corporation, etc.) and risk-weighting factors determined using internal parameters: the borrower's probability of default, loss given default, effective maturity and exposure at default.

**Large loss**

In property and casualty insurance, single claim having a significant cost.

**Legal and regulatory risk**

Risk associated with the non-compliance by Desjardins Group with obligations arising from the interpretation or application of a legislative or regulatory provision or a contractual commitment, which could have an impact on the conduct of its operations, its reputation, its strategies and its financial objectives.

**Leverage ratio**

Ratio calculated as the capital measure (namely Tier 1 capital) divided by the exposure measure. The exposure measure includes: 1) on-balance sheet exposures; 2) securities financing transaction exposures; 3) derivative exposures; and 4) off-balance sheet items.

**Liquidity coverage ratio**

Basel III metric representing a liquidity standard that measures the sufficiency of high quality liquid assets available to face net short-term financial obligations over a 30 day period in an acute liquidity stress scenario.

**Liquidity risk**

Risk related to Desjardins Group's capacity to raise the necessary funds (by increasing liabilities or converting assets) to meet a financial obligation, whether or not it appears on the Consolidated Balance Sheets.

**Loss given default**

Economic loss that may be incurred should the borrower default, expressed as a percentage of exposure at default.

**Market risk**

Risk of changes in the fair value of financial instruments resulting from fluctuations in the parameters affecting this value, in particular, interest rates, exchange rates, credit spreads and their volatility.

**Master netting agreement**

Standard agreement developed to reduce the credit risk of multiple derivative transactions by creating a legal right to set off the obligations of a counterparty in the event of default.

**Matching**

Process of adjusting asset, liability and off-balance sheet item maturities in order to reduce risks related to interest or exchange rates and financial indexes. Matching is used in asset/liability management.

**Morbidity rate**

Probability that a person of a given age will suffer an illness or disability. The accident/health insurance premium paid by a person belonging to a particular age group is based on this group's morbidity rate.

**Mortality rate**

Rate of death in a particular group of persons. The life insurance premium paid by a person belonging to a particular age group is based on this group's mortality rate.

**Mortgage-backed security**

Security created through the securitization of a pool of residential mortgage loans under the *National Housing Act*.

**Net interest income**

Difference between what a financial institution receives on assets such as loans and securities and what it pays out on liabilities such as deposits and subordinated bonds.

**Net premiums earned**

In property and casualty insurance, premiums earned for a given period, net of reinsurance premiums.

**Net sales of savings products**

Metric used to measure growth in Wealth Management and Life and Health Insurance segment operations. It is equal to sales of group and individual savings products manufactured and distributed by segment entities, and is comprised of on- or off-balance sheet deposits, less redemptions.

**Notional amount**

Reference amount used to calculate payments for instruments such as forward rate agreements and interest rate swaps. This amount is called "notional" because it does not change hands.

**Office of the Superintendent of Financial Institutions (OSFI)**

Organization whose mission is to enforce all laws governing the financial industry in Canada, particularly as concerns banks, insurance companies, trust companies, loan companies, cooperative credit associations, fraternal companies and private pension plans subject to federal oversight.

**Operational risk**

Risk of inadequacy or failure attributable to processes, people, internal systems or external events and resulting in losses, failure to achieve objectives or a negative impact on reputation.

**Option**

Contractual agreement that grants the right, but not the obligation, to sell (put option) or to buy (call option) a specified amount of a financial instrument at a predetermined price (the exercise or strike price) on or before a specified date.

**Other retail client exposures**

In accordance with the regulatory capital framework, risk category that includes all loans granted to individuals except for exposures related to residential mortgage loans and qualifying revolving retail client exposures.

**Pension plan**

Contract under which participants receive retirement benefits under certain terms starting at a given age. A pension plan is funded through contributions made either by the employer alone or by both the employer and the participants.

**Pension plan risk**

Risk of loss resulting from pension plan commitments made by Desjardins Group for the benefit of its employees. This risk basically arises from rate, price, foreign exchange and longevity risks.

**Permanent share or capital share**

Equity security offered to Desjardins caisse members.

**Price risk**

Risk of potential loss resulting from a change in the market value of assets (shares, commodities, real estate properties, index-based assets) but not resulting from a change in interest or foreign exchange rates or in the credit quality of a counterparty.

**Probability of default**

Probability that a borrower defaults on his obligations over a period of one year.

**Qualifying revolving retail client exposures**

In accordance with the regulatory capital framework, risk category that includes credit card loans and unsecured credit margins granted to individuals.

**Regulatory capital**

In accordance with the definition set out in the guideline on adequacy of capital base standards applicable to financial services cooperatives issued by the AMF, the regulatory capital under Basel III comprises Tier 1A capital, Tier 1 capital and Tier 2 capital. The composition of these various tiers is presented in the “Capital management” section of the Management's Discussion and Analysis.

**Regulatory funds**

Funds needed to cover unexpected losses, calculated according to parameters and methods prescribed by regulatory authorities.

**Reinstatement premium**

Premium payable to restore the original reinsurance coverage limit that has been reduced by the occurrence of a catastrophe. Reinstatement premiums are recognized in net premiums.

**Reinsurance treaty**

Agreement whereby one insurer assumes all or part of a risk undertaken by another insurer. Despite the treaty, the original insurer remains fully liable to its policyholders for the insurance obligations.

**Repurchase agreement**

Agreement involving both the sale of securities for cash and the repurchase of these securities for value at a later date. This type of agreement represents a form of short-term financing.

**Reputation risk**

Risk that a negative perception by the stakeholders, whether or not justified, of Desjardins Group's practices, actions or lack of action could have an unfavourable impact income and equity, and the trust that Desjardins Group inspires.

**Reverse repurchase agreement**

Agreement involving both the purchase of securities for cash and the sale of these securities for value at a later date. This type of agreement represents a form of short-term financing.

**Risk-weighted assets**

Assets adjusted based on a risk-weighting factor prescribed by regulations to reflect the level of risk associated with items presented in the Consolidated Balance Sheets. Some assets are not weighted, but rather deducted from capital. The calculation method is defined in the AMF guidelines. For more details, see the “Capital management” section of the Management's Discussion and Analysis.

**Scaling factor**

Adjustment representing 6.0% of assets valued according to the Internal Ratings-Based Approach, applied to credit exposures in compliance with section 1.3 of the AMF guideline on the capital adequacy standards applicable to financial services cooperatives.

**Securitization**

Process by which financial assets, such as mortgage loans, are converted into asset-backed securities and transferred to a trust.

**Security borrowed or purchased**

Security typically borrowed or purchased to cover a short position. The borrowing or purchase usually requires that an asset, taking the form of cash or highly rated securities, be pledged as collateral by the borrower.

**Security lent or sold**

Security typically lent or sold to cover a short position of the borrower. The loan or sale usually requires that an asset, taking the form of cash or highly rated securities, be pledged as collateral by the borrower.

**Security sold short**

Commitment by a seller to sell a security it does not own. Typically, the seller initially borrows the security to deliver it to the purchaser. At a later date, the seller buys an identical security to replace the borrowed security.

**Segregated fund**

Type of fund offered by insurance companies through a variable contract that provides the contract holder with a number of guarantees, such as principal repayment upon death. Segregated funds encompass a range of categories of securities and are designed to meet a variety of investment objectives. Segregated fund deposits represent amounts invested by clients. Segregated funds are comprised of investment funds with capital guaranteed upon death or at maturity.

**Segregated fund deposits**

Amounts paid by annuity contract holders in order to invest in segregated funds. Individual annuity contracts provide for a guarantee of the principal on death or at maturity.

**Standardized Approach**- Credit risk

Default approach used to calculate risk-weighted assets. Under this method, the financial institution uses valuations performed by external credit assessment institutions recognized by the AMF to determine the risk-weighting factors related to the various exposure categories.

- Market risk

Default approach used to calculate risk-weighted assets for the four areas of market risk: interest rate risk, equity price risk, foreign exchange risk and commodity risk. The calculation is based on predefined rules such as those on the size and nature of the financial instruments held.

- Operational risk

Risk measurement approach used to assess the capital charge for operational risk. For this measurement, activities are divided into predefined business lines for a financial institution. The capital charge is calculated by multiplying each business line's gross income by a specific factor. The total capital charge represents the three-year average of the summation of the capital charges across each of the business lines in each year.

**Strategic risk**

Risk of loss attributable to an inability to adapt to a changing environment because of failure to act, an inappropriate strategic choice or the inability to effectively implement strategies.

**Stressed Value at Risk (VaR)**

Value calculated in the same way as the Value at Risk, except for the historical data used, which are for a one-year stress period.

**Structural interest rate risk**

Risk related to the potential impact of interest rate fluctuations on net interest income and the economic value of equity.

**Structured entity**

Entity that has been designed so that voting rights or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: restricted activities, a narrow and well-defined objective, insufficient equity to permit it to finance its activities without subordinated financial support, or financing in the form of multiple contractually linked instruments to investors.

**Subordinated note**

Unsecured note whose repayment in the event of liquidation is subordinated to the prior repayment of certain other creditors.

**Subsidiary**

Company controlled by the Federation.

**Swap**

Derivative financial instrument under which two parties agree to exchange interest rates or currencies for a specified period according to predetermined rules.

**Underwriting experience**

In life and health insurance, the difference between actual results and actuarial assumptions used to determine premiums or actuarial liabilities, as applicable.

**Value at Risk (VaR)**

Estimate of the potential loss over a certain period of time at a given confidence level, calculated using historical data for a one-year interval.

**Written premiums**

In life and health insurance, insurance or annuity premiums for the policies or certificates issue during the year.

