MCAN MORTGAGE CORPORATION

BASEL III PILLAR 3 DISCLOSURES

SEPTEMBER 30, 2018

1. Scope of Application

This document represents the Basel III Pillar 3 disclosures for MCAN Mortgage Corporation (the "Company" or "MCAN") as at September 30, 2018. These disclosures are made pursuant to the Pillar 3 Disclosure Requirements of the Office of the Superintendent of Financial Institutions Canada ("OSFI").

The amounts disclosed in the tables below represent the carrying amounts included in the Company's consolidated financial statements, which are prepared in accordance with International Financial Reporting Standards ("IFRS") and use the accounting policies described therein. This document is unaudited and is reported in thousands of Canadian dollars, unless otherwise noted.

The Basel III capital adequacy framework is applied to the consolidated operations of the Company, which include the Company's wholly-owned subsidiary XMC Mortgage Corporation ("XMC").

MCAN is a Loan Company under the *Trust and Loan Companies Act* (Canada) (the "Trust Act") and a Mortgage Investment Corporation ("MIC") under the *Income Tax Act* (Canada) (the "Tax Act"). As a Loan Company under the Trust Act, the Company is subject to the guidelines and regulations set by OSFI.

The Company invests its corporate funds in a portfolio of mortgages (including single family residential, residential construction, non-residential construction and commercial loans), as well as other types of securities, loans and real estate investments, while employing leverage by issuing term deposits eligible for Canada Deposit Insurance Corporation ("CDIC") deposit insurance. We manage our capital and asset balances based on the regulations and limits of both the Tax Act and OSFI. The Company also participates in the National Housing Act ("NHA") mortgage-backed securities ("MBS") program. XMC focuses on the origination and sale of residential first-charge mortgage products across Canada.

2. Capital Structure and Capital Adequacy

The Company's Common Equity Tier 1 ("CET 1") capital consists of share capital, contributed surplus, retained earnings and accumulated other comprehensive income. The Company does not hold any additional Tier 1 or Tier 2 capital instruments, therefore its CET 1 capital is equal to its Tier 1 and Total capital. The Company's authorized share capital is unlimited common shares with no par value. As at September 30, 2018, the Company had 23,745,727 common shares outstanding.

As a Loan Company under the Trust Act, OSFI oversees the adequacy of the Company's capital. OSFI expects all federally regulated institutions to attain capital-to-regulatory (or risk-weighted) assets ratios of 7% CET 1, 8.5% Tier 1 and 10.5% Total and a minimum leverage ratio which is calculated on a different basis from the aforementioned MIC leverage ratio. The risk-weighting of all on-balance sheet assets and all off-balance sheet assets is based on a prescribed percentage of the underlying asset position, in addition to adjustments for other items such as impaired mortgages. Risk-weighted assets also include an operational risk charge, which is based on certain components of the Company's net investment income over the past 12 quarters. The Company uses the standardized approach for credit risk and the basic indicator approach for operational risk. The Company's internal target minimum CET 1, Tier 1 and Total Capital ratios are 20%.

The Company maintains prudent capital planning practices to ensure that it is adequately capitalized and continues to satisfy minimum standards and internal targets. In conjunction with the annual strategic planning and budgeting process, the Company completes an Internal Capital Adequacy Assessment Process ("ICAAP") in order to ensure that it has the capital adequacy to support its business plan and risk appetite. The ICAAP assesses the capital necessary to support the various inherent risks that the Company faces, including credit, liquidity, interest rate, market, geographic concentration and reputational risks. The Company's business plan is also stress tested under various adverse scenarios in order to determine the impact on its results from operations and financial condition. The ICAAP is reviewed by both management and the Board of Directors (the "Board") and is submitted to OSFI annually. In addition, the Company performs stress testing on its internal forecasts for capital adequacy on a quarterly basis, and the results of such testing are reported to the Board.

(in thousands except %)

As at September 30, 2018	**OSFI Row #**	
On-Balance sheet items	1	$ 2,160,597
Total on-Balance Sheet Exposures	3	2,160,597
Mortgage and investment funding commitments	17	440,844
Less: conversion to credit equivalent amount (50%)	18	(220,422)
Letters of credit	17	43,715
Less: conversion to credit equivalent amount (50%)	18	(21,858)
Off-Balance Sheet Items	19	242,279
Tier 1 Capital	20	272,734
Total Exposures	21	$ 2,402,876
Leverage ratio	22	11.35%

The Company's regulatory capital information as at September 30, 2018 is presented in the table below. OSFI's Basel III guidance[1] for non-Domestic Systemically Important Banks (non-DSIBs) prescribes standardized row numbers when disclosing certain capital information to facilitate comparability across regulated entities.

(in thousands except %)

As at September 30, 2018	**OSFI Row #**	
Share capital and contributed surplus	1	$ 221,636
Retained earnings	2	80,787
Accumulated other comprehensive income	3	-
Common Equity Tier 1 capital before regulatory adjustments	6	302,423
Total regulatory adjustments to Common Equity Tier 1 capital	28	(29,689)
Common Equity Tier 1 capital (CET1)	29	272,734
Tier 1 capital	45	272,734
Tier 2 capital	58	-
Total capital	59	$ 272,734
Total risk-weighted assets	60	$ 1,325,068
Capital ratios (as a percentage of risk-weighted assets)		
Common Equity Tier 1 capital	61	20.58%
Tier 1 capital	62	20.58%
Total capital	63	20.58%

[1] Public Capital Disclosure Requirements related to Basel III Pillar 3 effective July, 2003

The Company's assets, analyzed on a risk-weighted basis, are as outlined in the table below.

(in thousands)		
As at September 30, 2018		
On-Balance Sheet Assets		
Cash and cash equivalents	$	15,228
Cash held in trust		5,505
Marketable securities		58,447
Mortgages - corporate		687,342
Mortgages - securitized		28,121
Non-marketable securities		156,603
Other loans		2,104
Equity investment in MCAP Commercial LP		30,242
Foreclosed real estate		435
Deferred tax asset		2,971
Other assets		7,153
		994,151
Off-Balance Sheet Assets		
Letters of credit		21,857
Commitments		198,135
		219,992
Charge for operational risk		110,925
Total Risk-Weighted Assets	**$**	**1,325,068**

3. Credit Risk

Credit risk is the risk of financial loss resulting from the failure of a counterparty, for any reason, to fully honour its financial or contractual obligations to the Company, primarily arising from our mortgage and lending activities. Fluctuations in real estate values may increase the risk of default and may also reduce the net realizable value of the collateral property to the Company. Fluctuations in the fair market value of other financial assets may also increase the risk of credit loss to the Company. These risks may result in defaults and credit losses, which may result in a loss of earnings. Credit losses occur when a counterparty fails to meet its obligations to the Company and the value realized on the sale of the underlying security deteriorates below the carrying amount of the exposure.

Credit risk management

Credit and commitment exposure is closely monitored through a reporting process that includes a formal monthly review involving the Asset and Liability Committee ("ALCO"), which is comprised of management and a formal quarterly review involving the Board. A Chief Risk Officer ("CRO") Report, which identifies, assesses, ranks and provides trending analysis on all material risks to the Company, is provided to the Enterprise Risk Management and Compliance Committee ("ERMCC") on a quarterly basis. Monitoring also takes place through our Capital Commitments Committee and Executive Committee, which are both comprised of certain members of management.

The Company's exposure to credit risk is managed through prudent risk management policies and procedures that emphasize the quality and diversification of its investments and sufficiency and quality of collateral. Credit limits, based on the Company's risk appetite, which is approved by the Board at least annually, have been established for concentration by asset class, geographic region, dollar amount and borrower. These policies are amended on an ongoing basis to reflect changes in market conditions and risk appetite. All members of management are subject to limits on their ability to commit the Company to credit risk.

The Company identifies potential risks in its mortgage portfolio by way of regular review of market and portfolio metrics, which are a key component of quarterly market reports provided to the Board. The Company also undertakes site visits of active mortgage properties as part of its construction lending. Existing risks in the mortgage portfolio are identified by arrears reporting, portfolio diversification analysis, annual reviews of large loans and risk rating trends of the entire

mortgage portfolio. The aforementioned reporting and analysis provides adequate monitoring of and control over the Company's exposure to credit risk.

The Company assigns a credit score and risk rating for all mortgages at the time of underwriting based on the quality of the borrower and the underlying real estate. Risk ratings are reviewed annually for large exposures, and whenever there is an amendment or a material adverse change such as a default or impairment.

The Company's maximum credit exposure on its individual financial assets is equal to the carrying value of the respective assets, except for the corporate mortgage portfolio and non-marketable securities, where maximum credit exposures also include outstanding commitments for future fundings.

Corporate mortgages by exposure type

	Gross	Allowance				Net
As at September 30, 2018	**Principal**	**Stage 1**	**Stage 2**	**Stage 3**	**Total**	**Principal**
Corporate portfolio:						
Single family mortgages						
- Uninsured	$ 221,959	$ 554	$ 134	$ 51	$ 739	$ 221,220
- Insured	139,861	1	-	-	1	139,860
- Uninsured - completed inventory	4,119	24	-	-	24	4,095
Construction loans						
- Residential	447,985	2,283	367	-	2,650	445,335
- Non-residential	10,420	63	-	-	63	10,357
Commercial loans						
- Multi family residential	74,219	660	12	-	672	73,547
- Other commercial	71,840	538	42	-	580	71,260
	$ 970,403	**$ 4,123**	**$ 555**	**$ 51**	**$ 4,729**	**$ 965,674**

Corporate mortgages by geography

As at September 30, 2018	**Single Family**	**Construction**	**Commercial**	**Total**	
Ontario	$ 229,459	$ 218,409	$ 96,173	$ 544,041	56.3%
Alberta	62,937	24,359	2,100	89,396	9.3%
British Columbia	38,510	207,244	46,534	292,288	30.3%
Quebec	10,693	5,680	-	16,373	1.7%
Atlantic Provinces	14,330	-	-	14,330	1.5%
Other	9,246	-	-	9,246	0.9%
	$ 365,175	**$ 455,692**	**$ 144,807**	**$ 965,674**	**100.0%**

Allowances for credit losses

The allowance for credit losses reduces the carrying value of mortgage assets by an estimate of the principal amounts that borrowers may not repay in the future. In assessing the estimated realizable value of assets, we must rely on estimates and exercise judgment regarding matters for which the ultimate outcome is unknown. A number of factors can affect the amount that we ultimately collect, including the quality of our own underwriting process and credit criteria, the diversification of the portfolio, the underlying security relating to the loans and the overall economic environment. Allowances on impaired mortgages include all of the accumulated provisions for losses to reduce the assets to their estimated realizable value. Allowances depend on asset class, as different classes have varying underlying risks. Future changes in circumstances could materially affect net realizable values and lead to an increase or decrease the allowance for credit losses.

The measurement of impairment losses requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Company's ECL calculations are model outputs with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Company's criteria for assessing if there has been a significant increase in credit risk which results in allowances being measured on a lifetime versus 12 month ECL basis
- The segmentation of financial assets for the purposes of assessing ECL on a collective basis
- Development of ECL models, including the various formulas and the choice of inputs
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs

Corporate mortgage allowance continuity

For the Quarter Ended September 30, 2018	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balance, July 1, 2018	$ 4,366	$ 674	$ 31	$ 5,071
Provisions for (recovery of) losses	(243)	(119)	20	(342)
Balance, September 30, 2018	**$ 4,123**	**$ 555**	**$ 51**	**$ 4,729**

Impaired and past due mortgages

The Company considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments and, in certain cases, where qualitative thresholds indicate unlikeliness to pay as a result of a credit event. When such events occur, the Company carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events include:

- Significant financial difficulty of the borrower
- Breach of contract, such as a default or past due event
- The granting by the lender, for economic or contractual reasons relating to the borrower's financial difficulty, concession(s) that the lender(s) would not otherwise consider
- The increased likelihood that the borrower will enter bankruptcy or other financial reorganization
- The origination or acquisition of a financial asset at a deep discount that reflects the incurred credit losses

The combined impact of several events may cause financial assets to become defaulted as opposed to one discrete event. It is the Company's policy to consider a financial instrument as "cured" and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least twelve consecutive months.

Corporate mortgages past due but not impaired

As at September 30, 2018	**1 to 30 days**	**31 to 60 days**	**61 to 90 days**	**Total**
Corporate portfolio:				
Single family - uninsured	$ 3,035	$ 2,091	$ -	$ 5,126
Single family - insured	1,099	-	-	1,099
	$ 4,134	**$ 2,091**	**$ -**	**$ 6,225**

The provincial breakdown of mortgages past due but not impaired is as follows: Alberta ($1,213); Ontario ($2,932); British Columbia ($589); New Brunswick ($469); Newfoundland ($183); Manitoba ($166); and Saskatchewan ($673).

Impaired corporate mortgages

As at September 30, 2018	Single family insured	Single family uninsured	Total
Ontario	$ 83	$ -	$ 83
Alberta	1,148	320	1,468
Quebec	117	132	249
Atlantic Provinces	244	-	244
Other	-	129	129
	$ 1,592	**$ 581**	**$ 2,173**

Total corporate assets by maturity

As at September 30, 2018	Within 3 Months	3 Months To 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years	Total
Cash and cash equivalents	$ 75,236	$ -	$ -	$ -	$ -	$ 75,236
Marketable securities	58,418	-	-	29	-	58,447
Mortgages - corporate	215,710	411,825	263,131	69,318	5,690	965,674
Non-marketable securities	-	-	-	-	70,727	70,727
Other loans	1,062	30	1,012	-	-	2,104

4. Securitizations

The Company is an NHA MBS issuer, which involves the securitization of insured mortgages to create MBS. The Company issues MBS through its internal market MBS program and the Canada Housing Trust (“CHT”) Canada Mortgage Bonds (“CMB”) program. In instances where the Company has sold MBS, where applicable, these sales are executed for the purposes of transferring various economic exposures that result in accounting outcomes noted for each program below. In all instances, the mortgage servicing has been outsourced to MCAP.

The primary risks associated with the market MBS program and CMB program are prepayment, liquidity and funding risk, including the obligation to fund 100% of any cash shortfall related to the NHA MBS Timely Payment Guarantee. Prepayment risk includes the acceleration of the amortization of mortgage premiums as a result of early payouts.

Market MBS Program

During the third quarter of 2018, the Company securitized $31,685 of MBS through the market MBS program and sold the MBS to a third party. When the MBS is sold to third parties and the interest-only strip is retained by MCAN, the securitized mortgages remain on MCAN’s consolidated balance sheet while a corresponding financial liability from securitization is incurred, due to the fact that the Company retains significant continuing involvement with the assets.

Securitized mortgages exposure by type

As at September 30, 2018, the company had $919,176 of securitized mortgages which consisted of single family insured mortgages securitized through the market MBS program and CMB program.

Securitized mortgages past due not impaired

As at September 30, 2018	1 to 30 days	31 to 60 days	61 to 90 days	Total
Single family - Market MBS program	$ 3,713	$ 1,665	$ 334	$ 5,712
Single family - CMB program	455	-	-	455
	$ 4,168	**$ 1,665**	**$ 334**	**$ 6,167**

As at September 30, 2018, there were a total of $ 2,305 of impaired securitized mortgages (Alberta - $ 607, British Columbia - $ 204, Ontartio - $ 400, Quebec - $ 509, Atlantic Provinces - $ 262, Other Provinces - $ 323).

5. Operational Risk

Operational risk is the potential for loss resulting from people, inadequate or failed internal processes, systems, or from external events. The risk of loss from people includes internal or external fraud, non-adherence to internal procedures/values/objectives or unethical behaviour. The largest component of this risk has been separately identified as outsourcing risk. The remaining risks arise from the small size and entrepreneurial nature of MCAN, and the legacy systems used within it. The exposure to financial misreporting, inaccurate financial models, fraud, breaches in privacy, information security, attraction and retention of employees, and business continuity and recovery are included within operational risk.

Operational risk management

The Company manages operational risk through various committees and processes. The management team reviews operational measures on a recurring basis as part of the Operating Committee, Compliance Audit and Enterprise Risk Management Committee, and ALCO. Monthly updates are provided to the Board to provide an update on operations and other key factors and issues that arise.

The Company maintains appropriate insurance coverage through a financial institution bond policy, which is reviewed at least annually by the Board for changes to coverage and the Company's operations.

The Company uses the basic indicator approach in the calculation of operational risk, which is based on a specified percentage of average revenues over the past 12 quarters.

6. Marketable Securities

Marketable securities are designated as fair value through profit and loss. Fair values are based on bid prices quoted in active markets, and changes in fair value are recognized in the consolidated statements of income. Marketable securities provide MCAN with additional liquidity at yields in excess of cash and cash equivalents. As at September 30, 2018, the marketable securities portfolio had an unrealized gain of $ 2,380.

As at September 30, 2018	
Real estate investment trusts	$ 58,418
Corporate bonds	29
	$ 58,447

7. Interest Rate Risk

Interest rate risk is the potential impact of changes in interest rates on the Company's earnings and capital. Interest rate risk arises when the Company's assets and liabilities, both on and off-balance sheet, have mismatched repricing and maturity dates. Changes in interest rates where the Company has mismatched repricing and maturity dates may have an adverse effect on its financial condition and results of operations. In addition, interest rate risk may arise when changes in the underlying interest rates on assets do not match changes in the interest rates on liabilities. This potential mismatch may have an adverse effect on the Company's financial condition and results of operations.

Interest rate risk management

The Company evaluates its exposure to a variety of changes in interest rates across the term spectrum of its assets and liabilities, including both parallel and non-parallel changes in interest rates. By strategically managing and matching the terms of corporate assets and term deposits so that they offset each other, the Company seeks to reduce the risks associated with interest rate changes, and in conjunction with liquidity management policies and procedures, the Company also manages cash flow mismatches. ALCO reviews the Company's interest rate exposure on a monthly basis using interest rate spread and gap analysis as well as interest rate sensitivity analysis based on various scenarios. This information is also formally reviewed by the Board each quarter.

Interest rate risk – quantitative impact

An immediate and sustained parallel 1% increase to market interest rates at September 30, 2018 would have an estimated positive effect of $5,296 to net income over the following twelve month period. An immediate and sustained parallel 1% decrease to market interest rates at September 30, 2018 would have an estimated adverse effect of $4,401 to net income over the following twelve month period.

8. Liquidity Risk

Liquidity risk is the risk that cash inflows, supplemented by assets readily convertible to cash, will be insufficient to honour all cash outflow commitments (both on and off-balance sheet) as they come due. The failure of borrowers to make regular mortgage payments increases the uncertainties associated with liquidity management, notwithstanding that the Company may eventually collect the amounts outstanding, and may result in a loss of earnings or capital, or have an otherwise adverse effect on its financial condition and results of operations.

Liquidity Risk Management

The Company closely monitors its liquidity position to ensure that it has sufficient cash to meet liability obligations as they become due. The Board is responsible for the review and approval of liquidity policies. ALCO is responsible for liquidity management. The Company has an internal target of a standard level of liquid investments (cash and cash equivalents, marketable securities, MCAN-issued market MBS retained on the balance sheet, 75% of CMHC-insured single family mortgages, 50% of CMHC-insured single family second mortgages and 50% of privately insured mortgages) of at least 100% of term deposits maturing within 100 days. In addition, all insured single family mortgages are readily marketable within a time frame of one to three months, providing the Company with added flexibility to meet unexpected liquidity needs.

The Company has access to capital through its ability to issue term deposits eligible for Canada Deposit Insurance Corporation ("CDIC") deposit insurance. These term deposits also provide the Company with the ability to fund asset growth as needed.

The Company has a demand loan revolver facility to fund asset growth or meet its short-term obligations as required. The overdraft facility is a component of a $75,000 credit facility that also has a component which guarantees letters of credit used to support the obligations of borrowers to municipalities in conjunction with construction loans. The letters of credit have an individual sub-limit of $50,000. As at September 30, 2018, the total facility and letter of credit sub-limit have been increased to $125,000 and $60,000, respectively, until December 31, 2018.

The Company also has an agreement with a Canadian Schedule I Chartered bank that enables the Company to execute repurchase agreements for liquidity purposes. This facility provides liquidity and allows the Company to encumber certain eligible securities for financing purposes. As part of the agreement, the Company may sell assets to the counterparty at a specified price with an agreement to repurchase at a specified future date. The interest rate on the borrowings is driven by market spot rates at the time of borrowing.

9. Remuneration

For information regarding the remuneration of executives of the Company, refer to the "Statement of Executive Compensation" section of the 2018 Management Information Circular.