MCAN MORTGAGE CORPORATION

BASEL III PILLAR 3 DISCLOSURES

DECEMBER 31, 2018

1. Scope of Application

This document represents the Basel III Pillar 3 disclosures for MCAN Mortgage Corporation (the "Company" or "MCAN") as at December 31, 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 diversified portfolio of Canadian 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. The Company employs leverage by issuing term deposits eligible for Canada Deposit Insurance Corporation ("CDIC") deposit insurance up to a maximum of five times capital (on a non-consolidated tax basis in the MIC entity) as limited by the provisions of the Tax Act applicable to a MIC. The Company also participates in the National Housing Act ("NHA") mortgage-backed securities ("MBS") program. XMC is an originator of single family residential 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 consists of an unlimited number of common shares with no par value. As at December 31, 2018, the Company had 23,798,464 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 meet the minimum capital to risk-weighted asset ratios of 7% CET 1 capital, 8.5% Tier 1 capital and 10.5% Total capital and a minimum leverage ratio which is calculated on a different basis from the 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 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 December 31, 2018	OSFI Row #	
On-Balance sheet items	1	$ 2,111,442
Total on-Balance Sheet Exposures	3	2,111,442
Mortgage and investment funding commitments	17	410,020
Less: conversion to credit equivalent amount (50%)	18	(205,010)
Letters of credit	17	43,757
Less: conversion to credit equivalent amount (50%)	18	(21,879)
Off-Balance Sheet Items	19	226,888
Tier 1 Capital	20	275,769
Total Exposures	21	$ 2,338,330
Leverage ratio	22	11.79%

The Company's regulatory capital information as at December 31, 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 December 31, 2018	OSFI Row #	
Share capital and contributed surplus	1	$ 222,379
Retained earnings	2	84,315
Accumulated other comprehensive income	3	-
Common Equity Tier 1 capital before regulatory adjustments	6	306,694
Total regulatory adjustments to Common Equity Tier 1 capital	28	(30,925)
Common Equity Tier 1 capital (CET1)	29	275,769
Tier 1 capital	45	275,769
Tier 2 capital	58	-
Total capital	59	$ 275,769
Total risk-weighted assets	60	$ 1,273,205
Capital ratios (as a percentage of risk-weighted assets)		
Common Equity Tier 1 capital	61	21.66%
Tier 1 capital	62	21.66%
Total capital	63	21.66%

[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 December 31, 2018		
On-Balance Sheet Assets		
Cash and cash equivalents	$	20,028
Cash held in trust		5,200
Marketable securities		53,247
Mortgages - corporate		648,833
Mortgages - securitized		28,368
Non-marketable securities		153,692
Other loans		2,640
Equity investment in MCAP Commercial LP		30,669
Deferred tax asset		2,961
Other assets		14,332
		959,970
Off-Balance Sheet Assets		
Letters of credit		21,878
Commitments		182,744
		204,622
Charge for operational risk		108,613
Total Risk-Weighted Assets	**$**	**1,273,205**

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 its 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. 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 Enterprise Risk Management and Compliance Committee ("ERM&CC") and 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 ERM&CC on a quarterly basis. Monitoring also takes place through our Capital Commitments Committee and Executive Committee, which are both comprised of senior 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. Credit limits, based on the Company's risk appetite, which is approved by the Board periodically, 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 by management. Existing risks in the mortgage portfolio are identified by arrears reporting, portfolio diversification analysis, post funding monitoring 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. In the current economic environment, the Company has increased its monitoring of real estate market values for single family mortgages, with independent assessments of value obtained on individual mortgages.

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

As part of the Company's credit risk management process, the Company monitors its loan portfolio for early indicators of potential concerns. The "monitored/watchlist" category includes construction and commercial loans that may experience events such as slow sales, cost overruns or are located in geographic markets in which risks have increased. Loans in this category are included in stage 2 for IFRS 9 arrears classification purposes. Collective allowances are based on forward-looking economic assumptions and other factors.

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, where maximum credit exposures also include outstanding commitments for future mortgage fundings and the investment in the KingSett High Yield Fund, where maximum credit exposure includes the Company's total remaining commitment.

Corporate mortgages by exposure type

	Gross	Allowance				Net
As at December 31, 2018	**Principal**	**Stage 1**	**Stage 2**	**Stage 3**	**Total**	**Principal**
Corporate portfolio:						
Single family mortgages						
- Insured	$ 111,419	$ -	$ -	$ -	$ -	$ 111,419
- Uninsured	256,687	738	191	213	1,142	255,545
- Uninsured - completed inventory	7,747	44	-	-	44	7,703
Construction loans						
- Residential	425,272	2,146	348	217	2,711	422,561
- Non-residential	11,082	64	-	-	64	11,018
Commercial loans						
- Multi family residential	50,613	468	12	-	480	50,133
- Other commercial	64,424	393	20	-	413	64,011
	$ 927,244	**$ 3,853**	**$ 571**	**$ 430**	**$ 4,854**	**$ 922,390**

Corporate mortgages by geography

As at December 31, 2018	**Single Family**	**Construction**	**Commercial**	**Total**	
Ontario	$ 239,515	$ 195,662	$ 64,891	$ 500,068	54.2%
Alberta	59,245	28,943	2,079	90,267	9.8%
British Columbia	45,701	197,322	47,174	290,197	31.5%
Quebec	8,988	11,652	-	20,640	2.2%
Atlantic Provinces	12,994	-	-	12,994	1.4%
Other	8,224	-	-	8,224	0.9%
	$ 374,667	**$ 433,579**	**$ 114,144**	**$ 922,390**	**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, the Company 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 the Company ultimately collects, including the quality of its 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 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 expected credit loss ("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; and
- Determination of associations between macroeconomic scenarios and economic inputs such as unemployment levels and collateral values, and the effect on the probability of default, exposure at default, and loss given default.

Corporate mortgage allowance continuity

For the Year Ended December 31, 2018	Stage 1	Stage 2	Stage 3	Total
Balance, January 1, 2018	$ 3,998	$ 743	$ 121	$ 4,862
Provisions for (recovery of) losses	(133)	(172)	553	248
Write-offs, net	(12)	-	(244)	(256)
Balance, December 31, 2018	**$ 3,853**	**$ 571**	**$ 430**	**$ 4,854**

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. In certain other cases, where qualitative thresholds indicate unlikeliness to pay as a result of a credit event, the Company carefully considers whether the event should result in an assessment at Stage 2 or 3 for ECL calculations.

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. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the assessment of whether the significant increase in credit risk will reverse. The Company has also set probation periods for an asset to return to Stage 1.

Corporate mortgages past due but not impaired

As at December 31, 2018	1 to 30 days	31 to 60 days	61 to 90 days	Total
Corporate portfolio:				
Single family - insured	490	100	-	590
Single family - uninsured	$ 5,097	$ 311	$ 283	$ 5,691
	$ 5,587	**$ 411**	**$ 283**	**$ 6,281**

The provincial breakdown of mortgages past due but not impaired is as follows: Alberta ($2,183); Ontario ($3,915); and British Columbia ($183).

Impaired corporate mortgages

As at December 31, 2018	SF Insured	SF Uninsured	Construction	Total
Ontario	$ 146	$ 323	$ 548	$ 1,017
Alberta	276	312	-	588
British Columbia	-	488	-	488
Quebec	165	-	-	165
Atlantic Provinces	417	-	-	417
Other	-	479	-	479
	$ 1,004	**$ 1,602**	**$ 548**	**$ 3,154**

Total corporate assets by maturity

As at December 31, 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	$ 98,842	$ -	$ -	$ -	$ -	$ 98,842
Marketable securities	53,218	-	-	29	-	53,247
Mortgages - corporate	183,117	436,262	247,661	50,560	4,790	922,390
Non-marketable securities	-	-	-	-	71,813	71,813
Other loans	1,784	-	856	-	-	2,640

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.

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 Timely Payment obligation. Prepayment risk includes the acceleration of the amortization of mortgage premiums, as applicable, as a result of early payouts.

Market MBS Program

During the fourth quarter of 2018, the Company securitized $34,726 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.

CMB Program

During the fourth quarter of 2018, the Company securitized $28,417 of insured single family mortgages through the CMB program.

Securitized mortgages exposure by type

As at December 31, 2018, the Company had $887,252 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 December 31, 2018	1 to 30 days	31 to 60 days	61 to 90 days	Total
Single family - Market MBS program	$ 3,184	$ 797	$ 637	$ 4,618
Single family - CMB program	-	108	-	108
	$ 3,184	**$ 905**	**$ 637**	**$ 4,726**

As at December 31, 2018, there were a total of $ 1,801 of impaired securitized mortgages (Alberta - $ 852, British Columbia - $ 205, Ontartio - $ 311, Other Provinces - $ 433).

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 components of this risk have been separately identified as outsourcing risk, cyber risk, and the risk related to accuracy and completeness of borrower information. The remaining risks arise from the small size and entrepreneurial nature of MCAN. 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. Senior management reviews operational measures on a recurring and regular basis. Monthly updates are provided to the Board 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 periodically 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 December 31, 2018	
Real estate investment trusts	$ 53,218
Corporate bonds	29
	$ 53,247

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.

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 managing and strategically 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.

The Company is exposed to interest rate risk on insured single family mortgages between the time that a mortgage rate is committed to borrowers and the time that the mortgage is funded, or in the case of mortgages securitized through the market MBS or CMB programs, the time that the mortgage is securitized. To manage this risk, the Company may enter into bond forwards or may fund its mortgages with matched-term fixed-rate term deposits.

Interest rate risk – quantitative impact

An immediate and sustained parallel 1% increase to market interest rates at December 31, 2018 would have an estimated positive effect of $5,107 to net income over the following twelve month period. An immediate and sustained parallel 1% decrease to market interest rates at December 31, 2018 would have an estimated adverse effect of $4,682 to net income over the following twelve month period.

8. Liquidity and Funding Risk

Liquidity and funding risk is the risk that cash inflows including the ability to raise deposits and access to other sources of funding, 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

On a daily basis, the Company monitors its liquidity position to ensure that the level of liquid assets held (including insured single family mortgages, which are readily marketable within a time frame of one to three months), together with our ability to raise new deposits, is sufficient to meet its funding commitments, deposit maturity obligations, and other financial obligations. The Board is responsible for the approval of liquidity policies. ALCO is responsible for liquidity management oversight. The Company has an internal target of a standard level of liquid investments. This internal target includes assumptions relating to the value of liquid assets such as the ability to sell these assets in a stressed market scenario. As at December 31, 2018, the Company met this internal target.

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

The Company maintains an overdraft facility to meet its short-term obligations as required. The overdraft facility is a component of a larger credit facility that also has a portion which guarantees letters of credit used to support the obligations of borrowers to municipalities in conjunction with construction loans. Prior to year end, the total facility was temporarily increased from $75 million to $125 million until March 31, 2019.

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.