



MCAN MORTGAGE CORPORATION

**MANAGEMENT'S DISCUSSION AND
ANALYSIS OF OPERATIONS**

SEPTEMBER 30, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

This Management's Discussion and Analysis of Operations ("MD&A") should be read in conjunction with the interim unaudited consolidated financial statements and accompanying notes for the quarter ended September 30, 2018 and the audited consolidated financial statements, accompanying notes and MD&A for the year ended December 31, 2017. These items and additional information regarding MCAN Mortgage Corporation ("MCAN", the "Company" or "we"), including continuous disclosure materials such as the Annual Information Form are available on the System for Electronic Document Analysis and Retrieval ("SEDAR") at www.sedar.com and our website at www.mcanmortgage.com. Except as indicated below, all other factors discussed and referred to in the MD&A for fiscal 2017 remain substantially unchanged. Information has been presented as at November 8, 2018.

Effective January 1, 2018, MCAN prospectively adopted IFRS 9, *Financial Instruments* and did not restate prior period information. Accordingly, financial information as at September 30, 2018 and for the quarter and nine months ended September 30, 2018 is based on IFRS 9 and prior periods are based on IAS 39, *Financial Instruments: Recognition and Measurement*. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

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A CAUTION ABOUT FORWARD-LOOKING INFORMATION AND STATEMENTS

This MD&A contains forward-looking information within the meaning of applicable Canadian securities laws. All information contained in this MD&A, other than statements of current and historical fact, is forward-looking information. All of the forward-looking information in this MD&A is qualified by this cautionary note. Often, but not always, forward-looking information can be identified by the use of words such as “may,” “believe,” “will,” “anticipate,” “expect,” “planned,” “estimate,” “project,” “future,” and variations of these or similar words or other expressions that are predictions of or indicate future events and trends and that do not relate to historical matters. Forward-looking information in this MD&A includes, among others, statements and assumptions with respect to:

- the current business environment and outlook;
- possible or assumed future results;
- our ability to create shareholder value;
- our business goals and strategy;
- the potential impact of changes to regulations;
- the stability of home prices;
- the effect of challenging conditions on us;
- factors affecting our competitive position within the housing markets;
- the price of oil and its impact on housing markets in Western Canada;
- sufficiency of our access to capital resources; and
- the timing of the effect of interest rate changes on our cash flows.

Forward-looking information is not, and cannot be, a guarantee of future results or events. Forward-looking information reflects management’s current beliefs and is based on information currently available to management. Forward-looking information is based on, among other things, opinions, assumptions, estimates and analyses that, while considered reasonable by us at the date the forward-looking information is provided, inherently are subject to significant risks, uncertainties, contingencies and other factors that may cause actual results and events to be materially different from those expressed or implied by the forward-looking information.

The material factors or assumptions that we identified and were applied by us in drawing conclusions or making forecasts or projections set out in the forward-looking information include, but are not limited to:

- our ability to successfully implement and realize on our business goals and strategy;
- factors and assumptions regarding interest rates;
- housing sales and residential mortgage borrowing activities;
- the effect of competition;
- government regulation of our business;
- computer failure or security breaches;
- the availability of funding and capital to meet our requirements;
- the value of mortgage originations;
- the expected margin between interest earned on mortgage portfolios and interest paid on deposits;
- the relative continued health of real estate markets;
- acceptance of our products in the marketplace;
- our ability to forecast future changes to borrower credit and credit scores, loan to value ratios and other forward-looking factors used in assessing expected credit losses;
- availability of key personnel;
- our operating cost structure; and
- the current tax regime.

Reliance should not be placed on forward-looking information because it involves known and unknown risks, uncertainties and other factors, which may cause actual results to differ materially from anticipated future results expressed or implied by such forward-looking information. Factors that could cause actual results to differ materially from those set forth in the forward-looking information include, but are not limited to:

- global market activity;
- worldwide demand for and related impact on oil and other commodity prices;
- changes in government and economic policy;
- changes in general economic, real estate and other conditions;
- changes in interest rates;
- changes in Canada Mortgage Bonds (“CMB”) and mortgage-backed securities (“MBS”) spreads and swap rates;
- MBS and mortgage prepayment rates;
- mortgage rate and availability changes;

- adverse legislation or regulation;
- availability of CMB and MBS issuer allocation;
- technology changes;
- confidence levels of consumers;
- our ability to raise capital and term deposits on favourable terms;
- our debt and leverage;
- competitive conditions in the homebuilding industry, including product and pricing pressures;
- our ability to retain our executive officers and other employees;
- litigation risk;
- our relationships with our mortgage originators;
- additional risks and uncertainties, many of which are beyond our control, referred to in this MD&A and our other public filings with the applicable Canadian regulatory authorities.

Subject to applicable securities law requirements, we undertake no obligation to publicly update or revise any forward-looking information after the date of this MD&A whether as a result of new information, future events or otherwise or to explain any material difference between subsequent actual events and any forward-looking information. However, any further disclosures made on related subjects in subsequent reports should be consulted.

ACRONYMS

AFS	<i>Available for Sale</i>	FVOCI	<i>Fair Value Through Other Comprehensive Income</i>	MBS	<i>Mortgage Backed Securities</i>
ALCO	<i>Asset and Liability Committee</i>	FVPL	<i>Fair Value Through Profit and Loss</i>	MD&A	<i>Management's Discussion & Analysis</i>
BCBS	<i>Basel Committee on Banking Supervision</i>	HELOC	<i>Home Equity Line of Credit</i>	MIC	<i>Mortgage Investment Corporation</i>
CAR	<i>Capital Adequacy Requirements</i>	IAS	<i>International Accounting Standard</i>	NHA	<i>National Housing Act</i>
CDIC	<i>Canada Deposit Insurance Corporation</i>	IASB	<i>International Accounting Standards Board</i>	NSFR	<i>Net Stable Funding Ratio</i>
CET 1	<i>Common Equity Tier 1</i>	ICB	<i>Investment Committee of the Board</i>	OSFI	<i>Office of the Superintendent of Financial Institutions</i>
CHT	<i>Canada Housing Trust</i>	IFRIC	<i>IFRS Interpretations Committee</i>	PD	<i>Probability of Default</i>
CMB	<i>Canada Mortgage Bonds</i>	IFRS	<i>International Financial Reporting Standards</i>	RAF	<i>Risk Appetite Framework</i>
CMHC	<i>Canada Mortgage and Housing Corporation</i>	LAR	<i>Liquidity Adequacy Requirements</i>	RMBS	<i>Residential Mortgage Backed Securities</i>
DRIP	<i>Dividend Reinvestment Plan</i>	LCR	<i>Liquidity Coverage Ratio</i>	SEDAR	<i>System for Electronic Document Analysis and Retrieval</i>
EAD	<i>Exposure at Default</i>	LGD	<i>Loss Given Default</i>	SPPI	<i>Solely Payment of Principal and Interest</i>
ECL	<i>Expected Credit Losses</i>	LP ARA	<i>Limited Partner's At-Risk Amount</i>	TSX	<i>Toronto Stock Exchange</i>
EIM	<i>Effective Interest Rate Method</i>	LTV	<i>Loan to Value (ratio)</i>		

As of the Third Quarter Report, we have renamed "Financial Investments" as "Non-Marketable Securities".

SELECTED FINANCIAL INFORMATION

Table 1: Income Statement Highlights

(in thousands except for per share amounts and %)	Q3	Q2	Change	Q3	Change	YTD	YTD	Change
For the Periods Ended	2018 ¹	2018 ¹	(%)	2017	(%)	2018 ¹	2017	(%)
Income Statement Highlights								
Net investment income - corporate assets	\$ 13,116	\$ 15,063	(13%)	\$ 12,918	2%	\$ 40,252	\$ 38,054	6%
Net investment income - securitization assets	1,276	1,317	(3%)	1,532	(17%)	3,894	4,197	(7%)
	14,392	16,380	(12%)	14,450	-	44,146	42,251	4%
Other income	314	-	-	-	-	2,015	876	130%
Operating expenses	3,637	5,142	(29%)	4,689	(22%)	13,410	13,916	(4%)
Net income before income taxes	11,069	11,238	(2%)	9,761	13%	32,751	29,211	12%
Provision for (recovery of) income taxes	63	113	(44%)	(157)	1%	5	90	(94%)
Net income	\$ 11,006	\$ 11,125	(1%)	\$ 9,918	11%	\$ 32,746	\$ 29,121	12%
Basic and diluted earnings per share	\$ 0.47	\$ 0.47	-	\$ 0.42	12%	\$ 1.39	\$ 1.25	11%
Dividends per share	\$ 0.37	\$ 0.37	-	\$ 0.32	16%	\$ 1.11	\$ 0.94	18%
Next quarter's dividend per share	\$ 0.32							
Return on average shareholders' equity ²	14.29%	14.54%	(0.25%)	13.63%	0.66%	14.31%	13.45%	0.86%
Taxable income per share ^{2,4}	\$ 0.13	\$ 0.48	(73%)	\$ 0.36	(64%)	\$ 0.80	\$ 1.17	(32%)
Yields								
Average mortgage portfolio yield - corporate ³	5.53%	5.65%	(0.12%)	5.25%	0.28%	5.63%	5.22%	0.41%
Term deposit average interest rate ³	2.61%	2.48%	0.13%	2.25%	0.36%	2.49%	2.22%	0.27%
Spread of mortgages over term deposits	2.92%	3.17%	(0.25%)	3.00%	(0.08%)	3.14%	3.00%	0.14%
Average mortgage portfolio yield - securitized ³	2.57%	2.59%	(0.02%)	2.63%	(0.06%)	2.58%	2.61%	(0.03%)
Financial liabilities from securitization - average interest rate ³	1.83%	1.83%	0.00%	1.83%	0.00%	1.83%	1.88%	(0.05%)
Spread of mortgages over liabilities	0.74%	0.76%	(0.02%)	0.80%	(0.06%)	0.75%	0.73%	0.02%
Average term to maturity (in months)								
Mortgages - corporate	12.8	13.2	(3%)	10.6	21%			
Term deposits	19.2	17.4	10%	18.1	6%			

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

² Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

³ Refer to "Average Interest Rate" in the "Non-IFRS Measures" section of this MD&A for a definition of this measure.

⁴ For further information refer to the "Taxable Income" section of this MD&A.

Table 2: Balance Sheet Highlights

(in thousands except for per share amounts)	September 30 2018 ¹	June 30 2018 ¹	December 31 2017	September 30 2017	Change from Prior Quarter (\$)	
					(%)	(%)
Balance Sheet Highlights						
Assets						
Corporate	\$ 1,239,181	\$ 1,212,078	\$ 1,182,371	\$ 1,147,544	\$ 27,103	2%
Securitization	950,200	993,992	1,034,404	1,048,244	(43,792)	(4%)
Total assets	\$ 2,189,381	\$ 2,206,070	\$ 2,216,775	\$ 2,195,788	\$ (16,689)	(1%)
Mortgages - corporate	\$ 965,674	\$ 919,053	\$ 863,384	\$ 867,069	\$ 46,621	5%
Mortgages - securitized	\$ 919,176	\$ 964,507	\$ 1,016,724	\$ 1,026,657	\$ (45,331)	(5%)
Liabilities						
Corporate	\$ 953,405	\$ 923,205	\$ 904,099	\$ 878,428	\$ 30,200	3%
Securitization	933,553	976,769	1,015,699	1,027,090	(43,216)	(4%)
Total liabilities	\$ 1,886,958	\$ 1,899,974	\$ 1,919,798	\$ 1,905,518	\$ (13,016)	(1%)
Shareholders' equity ⁷	\$ 302,423	\$ 306,096	\$ 296,977	\$ 290,270	\$ (3,673)	(1%)
Capital Ratios ²						
Income Tax Assets to Capital Ratio	4.90	4.60	4.60	4.50		7%
Common Equity Tier 1 Capital Ratio ⁴	20.58%	21.47%	21.26%	21.34%		(0.89%)
Tier 1 Capital Ratio ⁴	20.58%	21.47%	21.26%	21.34%		(0.89%)
Total Capital Ratio ⁴	20.58%	21.47%	21.26%	21.34%		(0.89%)
Leverage ratio ³	11.35%	11.55%	11.31%	11.31%		(0.20%)
Credit Quality						
Impaired mortgage ratio (total) ^{2,5}	0.03%	0.02%	0.09%	0.14%		0.01%
Impaired mortgage ratio (corporate) ^{2,5}	0.06%	0.03%	0.20%	0.31%		0.03%
Mortgage Arrears ⁶						
Corporate	\$ 8,398	\$ 6,739	\$ 8,766	\$ 11,317	\$ 1,659	25%
Securitized	8,472	13,979	8,803	7,782	(5,507)	(39%)
Total	\$ 16,870	\$ 20,718	\$ 17,569	\$ 19,099	\$ (3,848)	(19%)
Common Share Information (end of period)						
Number of common shares outstanding	23,746	23,652	23,378	23,378		-
Book value per common share ²	\$ 12.74	\$ 12.94	\$ 12.70	\$ 12.42	\$ (0.20)	(2%)
Common share price - close	\$ 17.50	\$ 17.90	\$ 17.84	\$ 15.60	\$ (0.40)	(2%)
Market capitalization ²	\$ 415,555	\$ 423,371	\$ 417,064	\$ 364,697	\$ (7,816)	(2%)

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

² Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

³ Mortgages securitized through the market MBS program and CMB program for which derecognition has not been achieved are included in regulatory assets in the leverage ratio. For further information, refer to the "Capital Management" section of this MD&A.

⁴ These ratios are presented on the "all-in" basis, with certain regulatory capital deductions fully phased in.

⁵ Incorporates impaired (stage 3) mortgages under IFRS 9 and impaired mortgages under IAS 39.

⁶ The calculation of mortgage arrears was not impacted by the adoption of IFRS 9 as it represents mortgages that are at least one day past due.

⁷ Shareholders' equity as at September 30, 2018 is calculated net of the fourth quarter dividend payable January 2, 2019 due to the fact that this dividend was declared prior to quarter end and therefore has been accrued as at September 30, 2018.

HIGHLIGHTS

Financial Performance

Q3 2018

- Net income of \$11.0 million in Q3 2018, up \$1.1 million (11%) from \$9.9 million in Q3 2017 and down \$0.1 million from \$11.1 million in Q2 2018.
- Earnings per share totalled \$0.47 per share in Q3 2018, up \$0.05 (12%) from \$0.42 per share in Q3 2017 and unchanged from Q2 2018.
- Return on average shareholders' equity¹ was 14.29% in Q3 2018 compared to 13.63% in Q3 2017 and 14.54% in Q2 2018.
- Operating expenses decreased significantly from Q2 2018 and Q3 2017 as a result of a reduction in variable compensation accruals and a non-recurring reimbursement of previously incurred and accrued legal expenses.

Year to Date 2018

- For 2018 year to date, we earned net income of \$32.7 million, up \$3.6 million (12%) from \$29.1 million in 2017.
- Earnings per share were \$1.39 for 2018 year to date, up \$0.14 (11%) from \$1.25 in 2017.
- Return on average shareholders' equity¹ was 14.31% for 2018 year to date compared to 13.45% in 2017.

Corporate Activity

- Corporate assets, which totalled \$1.24 billion at September 30, 2018, increased by \$27 million (2%) from June 30, 2018.
- Corporate mortgage portfolio increased by \$47 million (5%) during Q3 2018 to \$966 million from \$919 million, which included increases of \$20 million in construction loans, \$17 million in uninsured single family and \$15 million in insured single family, partially offset by a decrease of \$5 million in completed inventory loans.
- Corporate mortgage originations increased to \$83 million in Q3 2018 from \$48 million in Q3 2017, including increases of \$21 million in insured single family and \$22 million in uninsured single family.

Dividends ⁴

- On September 24, 2018, the Board of Directors (the "Board") declared a fourth quarter dividend of \$0.32 per share to be paid on January 2, 2019 to shareholders of record as of December 14, 2018.
- This dividend has been accrued as a liability as at September 30, 2018 due to the fact that it was declared prior to the end of the quarter. Shareholders' equity as at September 30, 2018 is calculated net of both this dividend and the third quarter dividend that was paid September 28, 2018.
- The dividend decrease reflects the expected impact from shifting to a more conservative asset mix, the slower than expected growth in our single family originations to date and the related impact on our net interest income.

Credit Quality

- The impaired total mortgage ratio^{1,2,5} increased slightly to 0.03% at September 30, 2018 from 0.02% at June 30, 2018.
- The impaired corporate mortgage ratio^{1,2,5} increased slightly to 0.06% at September 30, 2018 from 0.03% at June 30, 2018.
- Total mortgage arrears^{1,3} were \$17 million at September 30, 2018, down from \$21 million at June 30, 2018. The September 30, 2018 balance consists entirely of single family mortgages, \$5.7 million of which were uninsured.
- Net write-offs were nil basis points of the average corporate portfolio in Q3 2018 compared to 4.3 basis points in Q3 2017.
- Average loan to value ratio ("LTV") of our uninsured single family portfolio based on an industry index of current real estate values was 57.1% at September 30, 2018 compared to 56.9% at June 30, 2018 and 51.1% at September 30, 2017.

Capital ⁴

- Common Equity Tier 1, Tier 1 and Total Capital to risk-weighted assets ratios¹ were 20.58% at September 30, 2018 compared to 21.47% at June 30, 2018.
- The leverage ratio¹ was 11.35% at September 30, 2018 compared to 11.55% at June 30, 2018.
- The income tax assets to capital ratio¹ was 4.90 at September 30, 2018 compared to 4.60 at June 30, 2018.
- Capital and asset balances are managed based on the regulations and limits of both the Tax Act and OSFI.

¹ Considered to be a "Non-IFRS Measure". For further details, refer to the "Non-IFRS Measures" section of this MD&A.

² Represents impaired (stage 3) mortgages under IFRS 9 and impaired mortgages under IAS 39.

³ The mortgage arrears balance was not impacted by the adoption of IFRS 9 as it represents mortgages that are at least one day past due.

⁴ The Common Equity Tier 1, Tier 1 and Total Capital to risk-weighted assets ratios, the leverage ratio and the income tax assets to capital ratio are calculated net of the fourth quarter dividend payable January 2, 2019 due to the fact that this dividend was declared prior to quarter end and therefore has been deducted from shareholders' equity as at September 30, 2018. This deduction has contributed to the decrease in these metrics as at September 30, 2018.

⁵ The impaired mortgage ratios do not include insured mortgages since credit risk is mitigated by mortgage insurance.

OUTLOOK

Regulatory Changes

Effective January 1, 2018, additional granularity was added to Guideline B-20, *Residential Mortgage Underwriting Practices and Procedures* ("Guideline B-20") by OSFI, including a stress test for uninsured mortgages. We estimate that the uninsured stress test has impacted approximately 10-15% of mortgages that we underwrite based on the borrower's ability to service the higher mortgage rates used in the stress test. We expect that this stress test, amongst other changes to Guideline B-20, will continue to have some impact on the proportion of mortgages that we approve.

Real Estate Conditions

Canadian residential real estate markets continue to have a mixed performance as regional markets adjust to both regulatory changes and local economic conditions. We expect Canadian housing market conditions to experience downward pressure and uncertainty for the remainder of 2018 and continue to encounter headwinds into 2019 as consumers face a rising interest rate environment, challenging affordability.

Consistent with our expectation last quarter, we saw some signs of recovery in home sale levels during the third quarter as buyers continued to adjust to the new mortgage rules. However, we have observed weakness in resale markets and construction starts through 2018, and we expect this to continue into 2019. In October 2018, the Bank of Canada announced a further increase to its benchmark interest rate to 1.75%. We expect interest rates to continue to increase into 2019, which we believe will place further pressures on consumer spending and housing/mortgage affordability.

Impact on MCAN

MCAN has historically repositioned itself during times of uncertainty to adapt its portfolio to changing market dynamics. Consistent with our disclosures in the Second Quarter outlook, we continue to reposition our mortgage portfolio to focus more on single family mortgages and less on construction lending given the uncertainty in the housing market, the impact of increasing rates, the overall economy and related risk factors.

Our construction lending activity, as discussed in the "Risk Governance and Management" section of this MD&A, is considered a higher risk lending activity and we believe that it is prudent to moderate lending activities in this business segment as we believe that we are approaching the end of a real estate cycle. For further information on our construction lending activities, refer to the "Construction and commercial lending" sub-section of the "Financial Position" section of this MD&A. We believe that single family lending provides a more moderate risk profile as uncertainties remain with respect to the housing market and the broader economy. Accordingly, we will focus on continuing to grow our uninsured single family origination volumes compared to the past two years.

Given competitive market conditions and the recent regulatory changes related to Guideline B-20, we believe that there will be challenges in originating adequate volumes to grow the single family portfolio. Notwithstanding these challenges, to assist with our single family growth plans we have launched programs to attract potential loans through the brokerage community and have increased our internal sales capabilities. In addition, through MCAP Commercial LP ("MCAP") and other originators, we have accelerated discussions to acquire additional single family mortgages. Additionally, we expect to experience mortgage rate pressures in our single family lending business as we compete with other lenders for originations. As a result of this rebalancing, we are observing historically low spread levels in our mortgage originations. We expect to invest in sustainable internal operating platforms to ensure that there are sufficient processes and monitoring in place to support growth, rebalancing and risk management. Collectively, we believe that this strategy may impact our net interest margins, while at the same time increasing the strength and stability of our balance sheet.

As noted above, recent announcements by the Bank of Canada to increase interest rates may provide an environment in which mortgage spreads could improve. However, improving mortgage spreads are also highly dependent on the overall rates offered by larger competitors in the space in addition to the broader market impact of housing ownership costs relative to household income.

Our corporate assets have increased by 5% year to date, compared to our stated annual growth target of 10%. We maintain our stated annual growth target for corporate assets of 10% per annum, as we believe that this target provides our shareholders with a measure of the long term expected pace of annual growth for the Company. As market conditions change, we may choose to deviate from this target to exercise prudent risk management, or tactically seize appropriate opportunities if they arise.

As volatility in the current market evolves, we believe that our strong capital position and asset capacity can be deployed if and when opportunities arise. Overall, we believe that our strategy in the near term is prudent given our review of the current state of the Canadian economy and housing markets. Over the longer term we will focus on a strategy that effectively grows our balance sheet and returns to our shareholders.

RESULTS OF OPERATIONS

Table 3: Net Income

(in thousands except for per share amounts)								
For the Periods Ended	Q3 2018 ¹	Q2 2018 ¹	Change (%)	Q3 2017	Change (%)	YTD 2018 ¹	YTD 2017	Change (%)
Net Investment Income - Corporate Assets								
Mortgage interest	\$ 13,094	\$ 12,867	2%	\$ 12,006	9%	\$ 37,961	\$ 35,656	6%
Equity income from MCAP Commercial LP	3,263	3,194	2%	3,260	0%	9,896	8,970	10%
Non-marketable securities ⁴	1,316	1,321	(0%)	2,244	(41%)	4,127	7,418	(44%)
Marketable securities	821	867	(5%)	924	(11%)	2,566	2,868	(11%)
Fees	882	267	230%	326	171%	1,512	918	65%
Interest on cash and other income	372	208	79%	357	4%	931	646	44%
Unrealized gain (loss) on securities ^{1,3}	359	3,341	(89%)	-	-	3,644	-	-
	20,107	22,065	(9%)	19,117	5%	60,637	56,476	7%
Term deposit interest and expenses	6,334	5,643	12%	5,447	16%	17,224	15,604	10%
Mortgage expenses	1,008	1,024	(2%)	972	4%	2,983	2,926	2%
Interest on loans payable	-	96	(100%)	-	-	116	36	222%
Provision for (recovery of) credit losses ^{1,2}	(351)	239	(247%)	(220)	60%	62	(144)	(143%)
	6,991	7,002	(0%)	6,199	13%	20,385	18,422	11%
	13,116	15,063	(13%)	12,918	2%	40,252	38,054	6%
Other Income - Corporate Assets								
Gain on dilution of investment in MCAP Commercial LP	314	-	-	-	-	314	91	245%
Gain on sale of investment in MCAP Commercial LP	-	-	-	-	-	1,701	785	117%
	314	-	-	-	-	2,015	876	130%
Net Investment Income - Securitization Assets								
Mortgage interest	6,015	6,375	(6%)	6,786	(11%)	18,883	20,579	(8%)
Other securitization income	111	23	383%	66	68%	206	139	48%
	6,126	6,398	(4%)	6,852	(11%)	19,089	20,718	(8%)
Interest on financial liabilities from securitization	4,346	4,558	(5%)	4,781	(9%)	13,585	14,939	(9%)
Mortgage expenses	512	534	(4%)	539	(5%)	1,614	1,582	2%
Provision for (recovery of) credit losses ^{1,2}	(8)	(11)	(27%)	-	-	(4)	-	-
	4,850	5,081	(5%)	5,320	(9%)	15,195	16,521	(8%)
	1,276	1,317	(3%)	1,532	(17%)	3,894	4,197	(7%)
Operating Expenses								
Salaries and benefits	2,294	3,179	(28%)	2,775	(17%)	8,418	7,958	6%
General and administrative	1,343	1,963	(32%)	1,914	(30%)	4,992	5,958	(16%)
	3,637	5,142	(29%)	4,689	(22%)	13,410	13,916	(4%)
Net income before income taxes	11,069	11,238	(2%)	9,761	13%	32,751	29,211	12%
Provision for (recovery of) income taxes	63	113	(44%)	(157)	(140%)	5	90	(94%)
Net Income	\$ 11,006	\$ 11,125	(1%)	\$ 9,918	11%	\$ 32,746	\$ 29,121	12%
Basic and diluted earnings per share	\$ 0.47	\$ 0.47	-	\$ 0.42	12%	\$ 1.39	\$ 1.25	11%
Dividends per share	\$ 0.37	\$ 0.37	-	\$ 0.32	16%	\$ 1.11	\$ 0.94	18%

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

² Under IFRS 9, the methodology for the calculation of mortgage allowances and provisions has changed from IAS 39, therefore provisions under IFRS 9 are not directly comparable to prior periods.

³ Under IFRS 9, fair value changes in certain reclassified financial assets are presented in the income statement and are therefore not directly comparable to prior periods. Under IAS 39, these fair value changes were recorded through other comprehensive income.

⁴ Prior to Q3 2018, non-marketable securities were referred to as financial investments.

Net Investment Income - Corporate Assets

Mortgage interest income

Table 4: Interest Income and Average Rate by Mortgage Portfolio - Quarterly

For the Quarters Ended	September 30, 2018			June 30, 2018			September 30, 2017		
	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹
(in thousands except %)									
Single family									
- Uninsured	\$ 217,645	\$ 2,499	4.59%	\$ 203,052	2,356	4.65%	\$ 211,218	\$ 2,393	4.52%
- Insured	128,440	983	3.06%	94,847	734	3.10%	81,821	696	3.40%
- Uninsured - completed inventory	5,111	85	6.59%	12,065	159	5.29%	63,510	875	5.45%
Construction loans									
- Residential	436,632	7,116	6.47%	440,870	7,076	6.44%	399,689	5,566	5.51%
- Non residential	6,927	110	6.30%	5,291	77	5.87%	7,200	96	5.29%
Commercial loans									
- Multi family residential	74,185	993	5.25%	74,034	1,014	5.43%	44,999	528	4.64%
- Other commercial	73,116	1,308	7.12%	82,753	1,451	7.05%	99,798	1,852	7.36%
Mortgages - corporate portfolio	\$ 942,056	\$ 13,094	5.53%	\$ 912,912	12,867	5.65%	\$ 908,235	\$ 12,006	5.25%
Term deposits	903,136	6,334	2.61%	856,680	5,643	2.48%	893,865	5,447	2.25%
Spread of mortgages over term deposits			2.92%			3.17%			3.00%
Average term to maturity (months)									
Mortgages - corporate	12.8			13.2			10.6		
Term deposits	19.2			17.4			18.1		

Table 5: Interest Income and Average Rate by Mortgage Portfolio - Year to Date

For the Nine Months Ended September 30	2018			2017		
	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹
(in thousands except %)						
Single family						
- Uninsured	\$ 207,011	\$ 7,175	4.62%	\$ 226,685	\$ 7,702	4.52%
- Insured	96,658	2,254	3.11%	89,822	2,286	3.38%
- Uninsured - completed inventory	11,452	489	5.71%	42,178	1,690	5.34%
Construction loans						
- Residential	424,032	20,343	6.41%	396,452	16,307	5.48%
- Non residential	5,449	247	6.06%	7,413	295	5.30%
Commercial loans						
- Multi family residential	73,822	2,936	5.32%	41,797	1,421	4.53%
- Other commercial	83,082	4,517	7.27%	105,811	5,955	7.50%
Mortgages - corporate portfolio	\$ 901,506	\$ 37,961	5.63%	\$ 910,158	\$ 35,656	5.22%
Term deposits	866,083	17,224	2.49%	878,101	15,604	2.22%
Spread of mortgages over term deposits			3.14%			3.00%

¹ Average interest rate is equal to income/expense divided by the average balance on an annualized basis. The average interest rate as presented may not necessarily be equal to "Income/Expense" divided by "Average Balance", as non-recurring items such as discount income, deferred interest and prior period adjustments are excluded from the calculation of the average interest rate as applicable. Non-recurring items were immaterial for the nine months ended September 30, 2018 and September 30, 2017. Average interest rate is considered to be a non-IFRS measure. Refer to the "Non-IFRS Measures" section of this MD&A for a definition of this measure.

Overview

In our Second Quarter outlook, we discussed our strategy to reposition our mortgage portfolio through a shift in focus towards single family mortgages from construction lending. We believe that it is prudent to moderate construction loan originations given the recent weakening in sales levels and property values, while the single family segment provides a more moderate risk profile.

The Bank of Canada has increased the overnight rate by 1.00% since June 30, 2017 and increased it a further 0.25% subsequent to quarter end. These increases have had and will continue to have a positive impact on future mortgage interest income related to the floating rate component of our corporate mortgage portfolio. Approximately 98% of the construction portfolio and 57% of the total corporate portfolio were floating rate as at September 30, 2018.

Average mortgage portfolio yield is a non-IFRS measure. For a definition of this measure, refer to the “Non-IFRS Measures” section of this MD&A.

Single family

Our uninsured single family portfolio grew by 8% during Q3 2018, driven by continued increases in both internal originations and acquisition from external origination sources. During the same period, the insured single family portfolio has increased by 12%. The combined insured and uninsured single family origination volumes increased by \$44 million from Q3 2017. On a combined basis, the portfolios have grown by \$82 million for the year to date. These increases are due to both market dynamics and improved internal sales and productivity initiatives.

We also noted in the prior quarter outlook that we believe there will be challenges in originating adequate volumes to grow the single family portfolio and that we expect to see reduced spreads as a result of competitive pressures. While we still believe that these risks exist, we were able to grow the portfolio in Q3 2018.

In light of the adoption of Guideline B-20 effective January 1, 2018, we continue to monitor our underwriting criteria in the context of the lending market while maintaining a conservative approach given home valuations in certain single family markets. We will continue to look to external sources for uninsured single family mortgage originations that are consistent with our internal risk and quality standards to assist in the continued growth of the portfolio.

During 2018, we have experienced a significant decrease in the completed inventory portfolio as the volume of loans transferred from the construction portfolio has decreased significantly from 2017.

Construction and commercial

The growth in our construction portfolio during Q3 2018 was driven by further advances on existing loans. While we are strategically shifting away from growth in this portfolio, we will continue to evaluate new loans in markets that are balanced between new home sales and unsold resale inventory and have affordable price points in the markets in which we invest.

Our commercial loan portfolio has had minimal change during 2018.

Equity income from MCAP

Equity income from MCAP was unchanged from Q3 2017 and Q2 2018. In Q3 2018, MCAP’s origination volumes were \$4.7 billion compared to \$4.2 billion in Q2 2018 and \$4.9 billion in Q3 2017. As at August 31, 2018, MCAP had \$72.0 billion of assets under administration compared to \$68.7 billion as at May 31, 2018 and \$64.2 billion as at August 31, 2017.

We recognize equity income from MCAP on a one-month lag such that our Q3 2018 equity income from MCAP is based on MCAP’s net income for the quarter ended August 31, 2018. For further information on our equity investment in MCAP, refer to the “Equity investment in MCAP” sub-section of the “Financial Position” section of this MD&A.

Other net investment income – Corporate assets

The decrease in income from non-marketable securities (formerly financial investments) from Q3 2017 was a result of higher distribution income from our investment in the Crown Realty II Limited Partnership (“Crown LP”) in Q3 2017. In Q3 2017, we received additional distribution income from the sale of one of the properties held within Crown LP.

Fees increased compared to Q2 2018 and Q3 2018 as a result of \$0.5 million of non-recurring income recognized from construction letter of credit fees.

We recorded a small unrealized gain on securities in Q3 2018, consisting of fair value changes relating to our marketable securities portfolio and our investment in Crown LP. Q2 2018 activity consisted of \$1.3 million relating to marketable securities and \$2.0 million relating to Crown LP. Fair value changes in the investment in Crown LP are primarily driven by changes in the fair value of the properties held within Crown LP.

The change in the average term deposit balance is generally similar to that of the average corporate mortgage portfolio as we primarily use term deposits to fund our corporate assets. We issue term deposits that are eligible for Canada Deposit Insurance Corporation (“CDIC”) deposit insurance. We do not accept deposits that can be cashed prior to maturity or paid on demand except in the event of the death of a depositor. For further details, refer to the “Liquidity Management” section of this MD&A.

Mortgage expenses consist primarily of mortgage servicing fees paid to third party mortgage servicers.

Details of the provision for (recovery of) credit losses are discussed in the “Credit Quality” sub-section below.

For further information on corporate and securitization net investment income, refer to the “Net Interest Income” sub-section below.

Other Income - Corporate Assets

In Q3 2018, MCAP issued additional class B units to other partners of MCAP which decreased our equity interest from 13.83% to 13.71%. As a result of the issuance of the new units at a price in excess of the per-unit carrying value of the investment, we recorded a dilution gain of \$0.3 million.

In Q1 2018, we sold 200,000 partnership units in MCAP at a price of \$22.60 per unit (compared to a net book value of \$14.10 per unit), recognizing a gain on sale of \$1.7 million.

Net Investment Income - Securitization Assets

Net investment income from securitization assets relates to our participation in the market MBS program and CMB program, which involve the securitization of insured mortgages through the Canada Mortgage and Housing Corporation (“CMHC”) NHA MBS program. In Q3 2018, our total securitization volumes were \$32 million (Q3 2017 - \$20 million). For further details on these programs, refer to the “Securitization Programs” section of this MD&A.

Table 6: Interest Income and Average Rate by Mortgage Portfolio - Quarterly

For the Quarters Ended	September 30, 2018			June 30, 2018			September 30, 2017		
	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹
(in thousands except %)									
Mortgages - securitized portfolio	\$ 934,759	\$ 6,015	2.57%	\$ 985,757	\$ 6,375	2.59%	\$ 1,028,172	\$ 6,784	2.63%
Financial liabilities from securitization	951,222	4,346	1.83%	997,584	4,558	1.83%	1,042,893	4,780	1.83%
Spread of mortgages over liabilities			0.74%			0.76%			0.80%

Table 7: Interest Income and Average Rate by Mortgage Portfolio - Year to Date

For the Nine Months Ended September 30	2018			2017		
	Average Balance	Interest Income	Average Rate ¹	Average Balance	Interest Income	Average Rate ¹
(in thousands except %)						
Mortgages - securitized portfolio	\$ 978,319	\$ 18,883	2.58%	\$ 1,045,816	\$ 20,576	2.61%
Financial liabilities from securitization	990,577	13,585	1.83%	1,058,476	14,939	1.88%
Spread of mortgages over liabilities			0.75%			0.73%

¹ Average interest rate is equal to income/expense divided by the average balance on an annualized basis. The average interest rate as presented may not necessarily be equal to “Income/Expense” divided by “Average Balance”, as non-recurring items such as discount income, deferred interest and prior period adjustments are excluded from the calculation of the average interest rate as applicable. Non-recurring items were immaterial for the nine months ended September 30, 2018 and September 30, 2017. Average interest rate is considered to be a non-IFRS measure. Refer to the “Non-IFRS Measures” section of this MD&A for a definition of this measure.

The main driver of the variance in the quarterly spread of securitized mortgages over liabilities has been penalty income collected upon the early prepayment of a mortgage, which can be volatile.

Net Interest Income – Summary

Table 8: Net Interest Income - Q3

For the Quarters Ended September 30 (in thousands except %)	2018			2017		
	Average Balance ¹	Income / Expense	Average Rate ³	Average Balance ¹	Income / Expense	Average Rate ³
Corporate						
Cash and cash equivalents	\$ 85,101	\$ 343	1.60%	\$ 99,772	\$ 264	1.05%
Mortgages	942,056	13,094	5.53%	908,235	11,973	5.25%
Other loans	2,184	29	5.27%	3,004	38	5.03%
Corporate interest earning assets	1,029,341	13,466	5.20%	1,011,011	12,275	4.83%
Term deposits	903,136	6,334	2.61%	893,865	5,447	2.25%
Corporate interest bearing liabilities	\$ 903,136	6,334	2.61%	\$ 893,865	5,447	2.25%
Net interest income (Corporate)		\$ 7,132	2.59%		\$ 6,828	2.58%
Securitization						
Cash held in trust	\$ 28,289	\$ 111	1.56%	\$ 20,197	\$ 42	0.83%
Mortgages	934,759	6,015	2.57%	1,028,172	6,784	2.63%
Securitization interest earning assets	963,048	6,126	2.54%	1,048,369	6,826	2.60%
Securitization interest bearing liabilities	\$ 951,222	4,346	1.83%	\$ 1,042,893	4,780	1.83%
Net interest income (Securitization)		\$ 1,780	0.71%		\$ 2,046	0.77%
Net Interest Income²		\$ 8,912	1.71%		\$ 8,874	1.67%

Table 9: Net Interest Income - YTD

For the Nine Months Ended September 30 (in thousands except %)	2018			2017		
	Average Balance ¹	Income / Expense	Average Rate ³	Average Balance ¹	Income / Expense	Average Rate ³
Corporate						
Cash and cash equivalents	\$ 87,978	\$ 838	1.27%	\$ 84,369	\$ 563	0.89%
Mortgages	901,506	37,961	5.63%	910,158	35,531	5.22%
Other loans	2,412	93	5.16%	3,474	132	5.09%
Corporate interest earning assets	991,896	38,892	5.24%	998,001	36,226	4.85%
Term deposits	866,083	17,224	2.49%	878,101	15,604	2.22%
Loans payable	3,689	116	4.20%	1,774	36	2.71%
Corporate interest bearing liabilities	\$ 869,772	17,340	2.50%	\$ 879,875	15,640	2.22%
Net interest income (Corporate)		\$ 21,552	2.74%		\$ 20,586	2.63%
Securitization						
Cash held in trust	\$ 19,327	\$ 206	1.43%	\$ 17,335	\$ 63	0.49%
Mortgages	978,319	18,883	2.58%	1,045,816	20,576	2.61%
Securitization interest earning assets	997,646	19,089	2.56%	1,063,151	20,639	2.58%
Securitization interest bearing liabilities	\$ 990,577	13,585	1.83%	\$ 1,058,476	14,939	1.88%
Net interest income (Securitization)		\$ 5,504	0.73%		\$ 5,700	0.70%
Net Interest Income²		\$ 27,056	1.75%		\$ 26,286	1.64%

¹ The average balances (excluding cash and cash equivalents, mortgages and term deposits) are calculated with reference to opening and closing monthly balances and as such may not be as precise as if daily balances were used. The average cash and cash equivalents, mortgage and term deposit balances are calculated using daily balances.

² Net interest income is equal to net investment income less equity income from MCAP, income from non-marketable securities, marketable securities income, fees, unrealized gain/loss on financial instruments, other securitization income, mortgage expenses and provision for credit losses. Net interest income is a non-IFRS measure. Refer to the "Non-IFRS Measures" section of this MD&A for a definition of this measure.

³ Average rate is equal to income/expense divided by the average balance on an annualized basis. The average rate as presented may not necessarily be equal to "Income/Expense" divided by "Average Balance", as non-recurring items such as discount income, one-time gains/losses, asset write-downs and fees not associated with the asset/liability yield are excluded from the calculation of the average rate. Non-recurring items were immaterial for the nine months ended September 30, 2018 and September 30, 2017. Average rate is considered to be a non-IFRS measure. Refer to the "Non-IFRS Measures" section of this MD&A for a definition of this measure.

Credit Quality

Table 10: Provisions for Credit Losses and Write-offs

(in thousands except basis points)	IFRS 9 Q3 2018	IAS 39 Q3 2017	Change (%)	IFRS 9 YTD 2018	IAS 39 YTD 2017	Change (%)
For the Periods Ended September 30						
Provision (recovery) on impaired corporate mortgages ¹						
Single family uninsured	\$ 20	\$ 104	(81%)	\$ 174	\$ 133	31%
Provision (recovery) on performing corporate mortgages ²						
Single family insured	-	-	-	10	-	-
Single family uninsured	(312)	(58)	438%	426	(206)	(307%)
Single family uninsured - completed inventory	(32)	1	(3,300%)	(376)	183	(306%)
Construction	29	(122)	(124%)	115	41	181%
Commercial						
Multi family residential	7	-	-	65	66	(2%)
Other commercial	(54)	(85)	(37%)	(291)	(195)	49%
	(362)	(264)	37%	(51)	(111)	(54%)
Other provisions (recoveries)	(9)	(60)	(85%)	(61)	(166)	(63%)
Corporate provision for credit losses	(351)	(220)	60%	62	(144)	(143%)
Provision (recovery) on performing securitized mortgages ²	(8)	-	-	(4)	-	-
Total provisions for (recoveries of) credit losses	\$ (359)	\$ (220)	63%	\$ 58	\$ (144)	(140%)
Corporate mortgage portfolio data:						
Provisions for (recoveries of) credit losses, net	\$ (342)	\$ (160)	114%	\$ 123	\$ 22	459%
Net write offs	\$ -	\$ 98	(100%)	\$ 256	\$ 475	(46%)
Net write offs (basis points)	-	4.3	(100%)	3.8	7.0	(46%)

¹ Represents impaired (stage 3) provision for credit losses on mortgages and mortgage commitments under IFRS 9 and individual provisions for credit losses under IAS 39.

² Represents performing (stage 1 and 2) provision for credit losses on mortgages and mortgage commitments under IFRS 9 and collective provisions for credit losses under IAS 39.

Earlier in 2018, we recorded an allowance relating to the Alberta and Saskatchewan geographical sub-segment of the uninsured single family portfolio. During Q3 2018, we reduced this allowance in line with the reduction in the outstanding balance in this segment of the portfolio, which led to a recovery of provisions during the quarter. The provision activity in other lines of business is primarily driven by changes in the respective portfolio balances.

Write-offs in all periods presented above relate entirely to uninsured single family mortgages, except for 2017 year to date which includes a \$220,000 write-off relating to the construction portfolio.

Operating Expenses

Table 11: Operating Expenses

(in thousands)								
	Q3	Q2	Change	Q3	Change	YTD	YTD	Change
For the Periods Ended	2018	2018	(%)	2017	(%)	2018	2017	(%)
Salaries and benefits	\$ 2,294	\$ 3,179	(28%)	\$ 2,775	(17%)	\$ 8,418	\$ 7,958	6%
General and administrative	1,343	1,963	(32%)	1,914	(30%)	4,992	5,958	(16%)
	\$ 3,637	\$ 5,142	(29%)	\$ 4,689	(22%)	\$ 13,410	\$ 13,916	(4%)

The decrease in salaries and benefits in Q3 2018 was primarily due to a reduction to our variable compensation accruals recorded during the quarter, partially offset by an increase in regular salary expense driven by an increase in the number of employees from 2017. For 2018 year to date, the impact of the increased headcount has exceeded that of the reduction to the variable compensation accrual.

The decrease in general and administrative expenses from Q2 2018 and Q3 2017 was primarily driven by a non-recurring \$0.6 million reimbursement of previously incurred and accrued legal expenses. These legal expenses related to ongoing litigation discussed further in the "Off-Balance Sheet Arrangements" section of this MD&A.

Provision for Income Taxes

Table 12: Income Taxes

(in thousands)								
	Q3	Q2	Change	Q3	Change	YTD	YTD	Change
For the Periods Ended	2018	2018	(%)	2017	(%)	2018	2017	(%)
Current tax provision (recovery)	\$ 4	\$ 457	(99%)	\$ -	-	\$ 461	\$ -	-
Deferred tax provision (recovery)	59	(344)	(117%)	(157)	(138%)	(456)	90	(607%)
	\$ 63	\$ 113	(44%)	\$ (157)	(140%)	\$ 5	\$ 90	(94%)

The 2018 year to date current tax provision recorded relates to estimated current taxes payable in a subsidiary of MCAN as a result of taxable income earned from the sale of properties within the Crown LP investment.

As at September 30, 2018, we had \$8 million of losses available for carry-forward in the MCAN mortgage investment corporation ("MIC") parent company on a non-consolidated basis (June 30, 2018 - \$8 million). As a MIC, we do not account for deferred taxes therefore the benefit of these loss carry-forwards is not reflected in the consolidated balance sheet. For further information, refer to Notes 4 and 14 to the consolidated financial statements.

Taxable Income

The table below provides a reconciliation between net income for accounting purposes and taxable income. The adjustments below represent the difference between the individual components of net income for accounting and tax purposes. Taxable income is presented on a non-consolidated basis and does not incorporate taxable income from XMC and other subsidiaries as it does not directly impact MCAN's non-consolidated taxable income.

As a MIC, we typically pay out all of our taxable income to shareholders through dividends as our MIC status allows us to deduct dividends paid within 90 days of year end from taxable income. MCAN's dividend objective is to provide shareholders with a consistent and stable regular dividend, wherein dividend changes over time follow MCAN's long term growth. From quarter to quarter, timing differences between taxable income and accounting income are considered by the Board in the determination of the quarterly dividend.

Dividends that are deducted in the calculation of taxable income are not included in the table below.

Taxable income is considered to be a non-IFRS measure. For further details, refer to the "Non-IFRS Measures" section of this MD&A.

Table 13: Taxable Income Reconciliation ¹

(in thousands)	Q3 2018	Q3 2017	YTD 2018	YTD 2017
For the Periods Ended September 30				
Net income for accounting purposes	\$ 11,006	\$ 9,918	\$ 32,746	\$ 29,121
Adjustments:				
Deduct: Equity income from MCAP - accounting purposes	(3,263)	(3,260)	(9,896)	(8,970)
Add: MCAP taxable income (loss)	(3,682)	2,308	(3,276)	7,713
Provision for (recovery of) credit losses ²	(390)	(264)	(78)	(155)
Amortization of upfront securitization program costs ³	1,777	1,711	5,313	5,058
Securitization program mortgage origination costs ³	(696)	(310)	(1,713)	(1,522)
Unrealized gain on financial instruments ²	88	-	(641)	-
Equity income from subsidiaries ²	(782)	(557)	(2,585)	(1,953)
Deduct: Accounting gain on partial sale of MCAP ⁴	-	-	(1,701)	(785)
Add: Taxable gain on partial sale of MCAP ⁴	-	-	1,425	536
Gain on dilution of investment in MCAP ²	(314)	-	(314)	(91)
Other securitization program cash outflows	(358)	(346)	(627)	(995)
Other items	(356)	(690)	119	(713)
	\$ 3,030	\$ 8,510	\$ 18,772	\$ 27,244

¹ Taxable income is presented above on a non-consolidated basis for the MIC entity. The current year amounts presented above represent estimates as they are not finalized until the completion of our corporate tax filings.

² Not deductible/recognizable in the calculation of taxable income. Individual mortgage allowances are 90% deductible for tax purposes.

³ Deductible in full for tax purposes as mortgages securitized; capitalized and amortized for accounting purposes, however amortization is added back in calculation of taxable income.

⁴ For tax purposes, the accounting gain is excluded and only 50% of the taxable gain is included.

The decrease in taxable income in 2018 for both the quarter and year to date has been driven primarily by timing differences between accounting and taxable income in respect of a number of securitization transactions that MCAP has executed year to date. These timing differences are expected to reverse over the duration of the associated transactions.

In Q3 2018, we incurred \$0.7 million of origination costs on securitized mortgages (including market MBS held by MCAN) (Q3 2017 - \$0.3 million). These costs are deductible for income tax purposes in the period that the mortgages are securitized, while for accounting purposes they are capitalized and amortized over the term of the associated mortgages. As at September 30, 2018, the unamortized origination cost balance was \$9.4 million (June 30, 2018 - \$10.1 million), which represents costs that are still to be expensed for non-consolidated accounting purposes but will be added back in the calculation of taxable income in future periods.

Cash Flows

Operating Activities

- Used cash flows of \$16 million in Q3 2018; used cash flows of \$7 million in Q3 2017
- Used cash flows of \$25 million for 2018 year to date; provided \$4 million for 2017 year to date
- Variances primarily due to significant net mortgage inflows in 2017 compared to small net outflows in 2018.

Investing Activities

- Provided cash flows of \$2 million in Q3 2018; provided cash flows of \$2 million in Q3 2017
- Provided cash flows of \$11 million for 2018 year to date; provided \$5 million for 2017 year to date
- 2018 year to date includes higher net inflows relating to distributions from MCAP and \$4.5 million of proceeds from a partial sale of our equity investment in MCAP.

Financing Activities

- Used cash flows of \$7 million in Q3 2018; used cash flows of \$6 million in Q3 2017
- Used cash flows of \$28 million for 2018 year to date; used \$24 million for 2017 year to date
- In 2018, there were higher outflows from dividends paid partially offset by higher inflows from the issuance of common shares through the Dividend Reinvestment Plan ("DRIP").

FINANCIAL POSITION

Table 14: Assets

(in thousands except %)					
As at	September 30 2018 ¹	June 30 2018 ¹	December 31 2017	Change from Prior Quarter (\$) (%)	
Corporate Assets					
Cash and cash equivalents	\$ 75,236	\$ 96,985	\$ 117,571	\$ (21,749)	(22%)
Marketable securities	58,447	58,534	62,518	(87)	-
Mortgages	965,674	919,053	863,384	46,621	5%
Non-marketable securities ²	70,727	70,191	68,190	536	1%
Other loans	2,104	2,426	2,612	(322)	(13%)
Equity investment in MCAP Commercial LP	59,931	57,954	59,189	1,977	3%
Foreclosed real estate	435	435	435	-	-
Deferred tax asset	2,971	3,005	2,672	(34)	(1%)
Other assets	3,656	3,495	5,800	161	5%
	1,239,181	1,212,078	1,182,371	27,103	2%
Securitization Assets					
Cash held in trust	27,527	25,740	13,441	1,787	7%
Mortgages	919,176	964,507	1,016,724	(45,331)	(5%)
Other assets	3,497	3,745	4,239	(248)	(7%)
	950,200	993,992	1,034,404	(43,792)	(4%)
	\$ 2,189,381	\$ 2,206,070	\$ 2,216,775	\$ (16,689)	(1%)

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

² As of Q3 2018, we renamed Financial Investments as Non-Marketable Securities.

Mortgages - Corporate & Securitized

Table 15: Mortgage Summary

(in thousands)					
As at	September 30 2018 ¹	June 30 2018 ¹	December 31 2017	Change from Prior Quarter (\$) (%)	
Corporate portfolio:					
Single family mortgages					
- Uninsured	\$ 221,220	\$ 203,897	\$ 198,354	\$ 17,323	8%
- Insured	139,860	125,330	80,377	14,530	12%
- Uninsured - completed inventory	4,095	9,314	51,190	(5,219)	(56%)
Construction loans					
- Residential	445,335	429,855	386,562	15,480	4%
- Non-residential	10,357	5,496	4,840	4,861	88%
Commercial loans					
- Multi family residential	73,547	73,830	64,655	(283)	-
- Other commercial	71,260	71,331	77,406	(71)	-
	965,674	919,053	863,384	46,621	5%
Securitized portfolio:					
Single family insured - Market MBS program	780,036	821,807	867,406	(41,771)	(5%)
Single family insured - CMB program	139,140	142,700	149,318	(3,560)	(2%)
	919,176	964,507	1,016,724	(45,331)	(5%)
	\$ 1,884,850	\$ 1,883,560	\$ 1,880,108	\$ 1,290	-

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

Corporate and Securitized Mortgage Portfolio Analysis

Q3 2018 Summary

As discussed in the Outlook section of this MD&A, we have shifted our corporate mortgage portfolio strategy to focus more on single family mortgages. Given the position of the current real estate cycle, we believe that it is prudent to moderate our construction lending. The single family segment provides a more moderate risk profile given the uncertainty in the housing market.

The uninsured single family portfolio balance has exhibited improved growth over the past two quarters after levelling off in the second half of 2017. While we continuously monitor our underwriting criteria in the context of the lending market, we have maintained a conservative underwriting approach in recent quarters given home valuations in certain single family markets. We continue to look to external sources for uninsured single family mortgage originations that are consistent with our internal risk and quality standards to assist in the continued growth of the portfolio.

Our insured single family portfolio has also increased over the past two quarters after remaining largely unchanged since mid-2017. Origination volumes have increased from 2017, and we have used these volumes to issue market MBS to retain on our corporate balance sheet for liquidity purposes, or to sell to third parties. Mortgages retained as market MBS remain in the insured single family corporate mortgage classification since the transaction associated with the retention of MBS fails mortgage derecognition criteria under IFRS.

Although we are strategically shifting away from growth in the construction portfolio, we will continue to evaluate new loans in markets that are balanced between new home sales and unsold resale inventory and have affordable price points in the markets in which we invest. For further information on the construction portfolio, refer to the “Construction and commercial lending” sub-section of this MD&A.

Our commercial loan portfolio has remained consistent during 2018. This portfolio provides a different risk profile from single family while providing appropriate risk-adjusted returns. Since 2017 we have focused on the lower-risk segments of the commercial lending market, such as loans secured by apartment buildings. Certain segments of the commercial loan portfolio also include non-conventional loans that may have some construction exposure.

The graph below highlights the impact of the recent initiatives noted above. Our improved single family origination volumes have been the primary driver behind corporate mortgage growth in the past two quarters, with construction also experiencing seasonal growth earlier in the year. The steady decrease in the securitization portfolio has been a result of a reduction in our securitization volumes due to tightened spreads and reduced economics and a more recent focus on retaining insured single family originations on the corporate balance sheet for liquidity purposes.

Figure 1: Total Corporate and Securitized Mortgage Portfolio (in thousands)

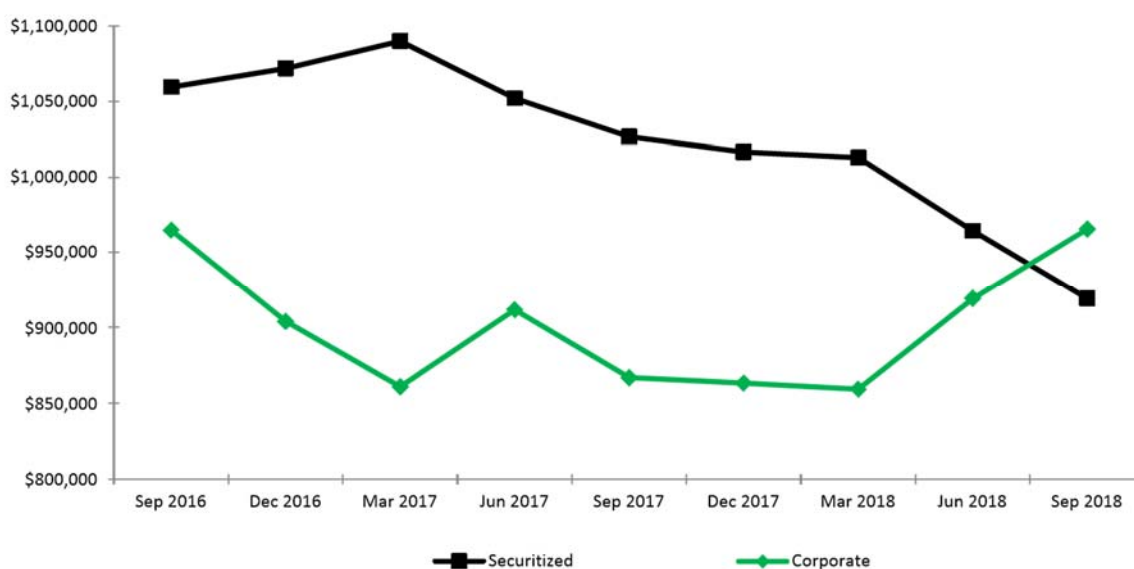
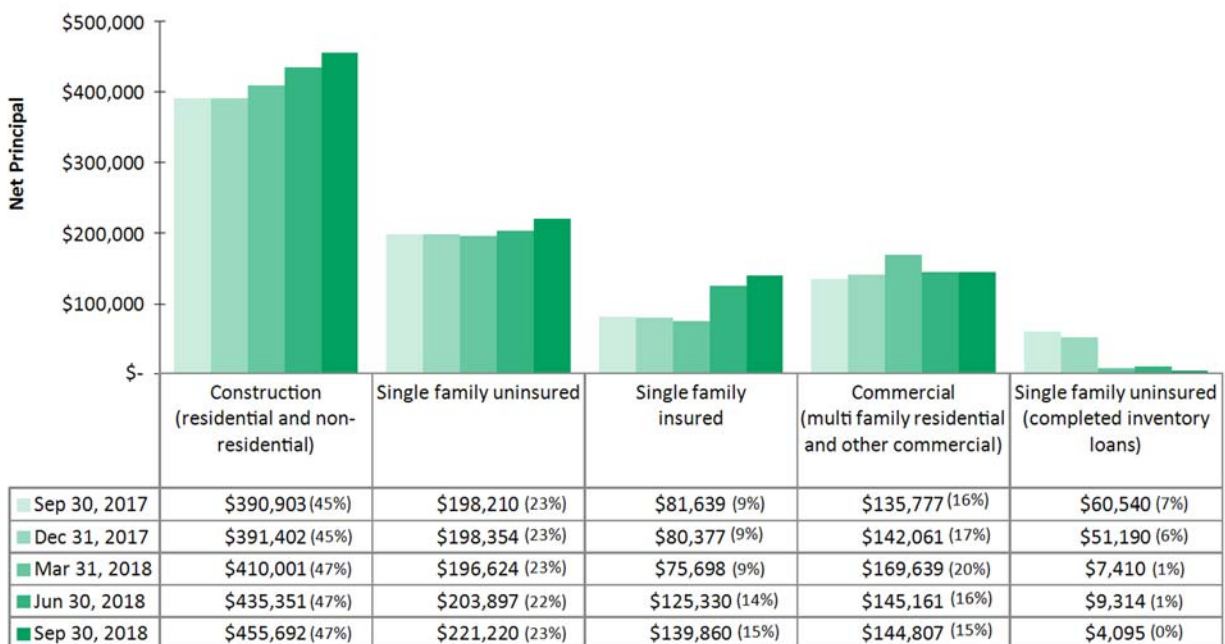
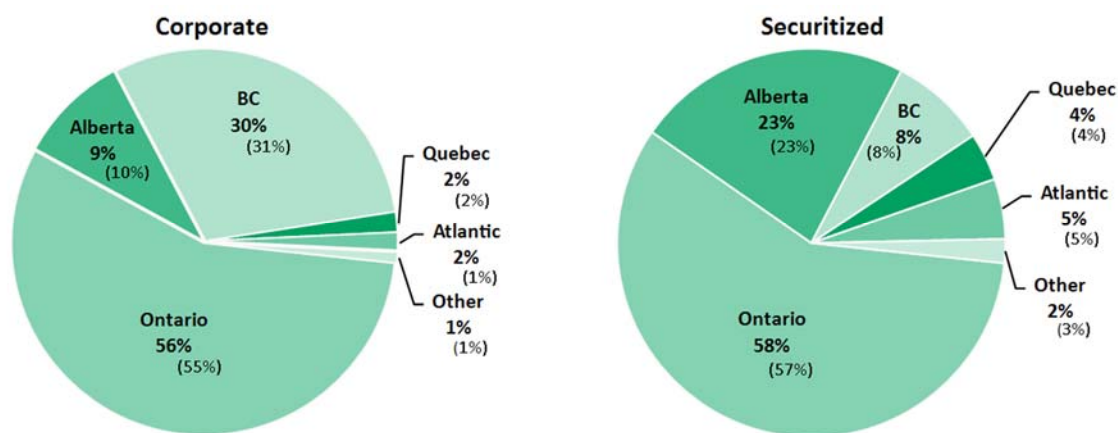


Figure 2: Corporate Mortgage Portfolio Composition by Product Type (in thousands)



Note: Amounts in parentheses represent the percentage of the corporate portfolio represented by the individual mortgage portfolio.

Figure 3: Mortgage Portfolio Geographic Distribution as at September 30, 2018 (June 30, 2018)



Arrears and Impaired Mortgages

Table 16: Arrears and Impaired Mortgages - Summary

(in thousands except %)	IFRS 9 September 30 2018	IFRS 9 June 30 2018	Change (%)	IFRS 9 March 31 2018	IAS 39 December 31 2017
As at					
Impaired mortgages ²					
Corporate					
Single family - uninsured	\$ 581	\$ 292	99%	\$ 1,873	\$ 1,696
Single family - insured	1,592	1,939	(18%)	1,945	832
	2,173	2,231	(3%)	3,818	2,528
Securitized	2,305	1,458	58%	966	-
Total impaired mortgages	\$ 4,478	\$ 3,689	21%	\$ 4,784	\$ 2,528
Impaired mortgage ratio (total) ^{1,6}	0.03%	0.02%	0.01%	0.10%	0.09%
Impaired mortgage ratio (corporate) ^{1,6}	0.06%	0.03%	0.03%	0.22%	0.20%
Mortgage arrears (past due) ⁵					
Corporate					
Single family - uninsured	\$ 5,707	\$ 3,813	50%	\$ 6,978	\$ 5,912
Single family - insured	2,691	2,926	(8%)	2,226	2,854
Total corporate mortgage arrears ¹	8,398	6,739	25%	9,204	8,766
Total securitized mortgage arrears ¹	8,472	13,979	(39%)	9,554	8,803
Total mortgage arrears ¹	\$ 16,870	\$ 20,718	(19%)	\$ 18,758	\$ 17,569
IFRS 9 staging analysis - corporate portfolio					
Stage 2					
Single family - uninsured	\$ 34,188	\$ 27,717	23%	\$ 34,408	n/a
Single family - insured	15,222	9,724	57%	5,182	n/a
Construction - residential	60,631	58,089	4%	45,629	n/a
Commercial - multi-family residential	2,100	2,621	(20%)	2,626	n/a
Commercial - other	4,934	11,170	(56%)	27,147	n/a
	117,075	109,321	7%	114,992	n/a
Stage 3					
Single family - uninsured	581	292	99%	1,873	n/a
Single family - insured	1,592	1,939	(18%)	1,945	n/a
	2,173	2,231	(3%)	3,818	n/a
Total stage 2 and 3 corporate mortgages	\$ 119,248	\$ 111,552	7%	\$ 118,810	n/a
Allowance for credit losses					
Corporate					
Allowance on performing mortgages ³	\$ 4,678	\$ 5,040	(7%)	\$ 4,865	\$ 4,748
Allowance on impaired mortgages ⁴	51	31	65%	173	62
	4,729	5,071	(7%)	5,038	4,810
Securitized - allowance on performing mortgages ³	13	21	(38%)	32	-
Total allowance for credit losses	\$ 4,742	\$ 5,092	(7%)	\$ 5,070	\$ 4,810

¹ Refer to the "Non-IFRS Measures" section of this MD&A for a definition of this measure.

² Represents impaired (stage 3) mortgages under IFRS 9 and impaired mortgages under IAS 39.

³ Represents performing (stage 1 and 2) allowances for credit losses on mortgages and mortgage commitments under IFRS 9 and collective allowances for credit losses under IAS 39.

⁴ Represents impaired (stage 3) allowances for credit losses on mortgages and mortgage commitments under IFRS 9 and individual allowances for credit losses under IAS 39.

⁵ The calculation of mortgage arrears was not impacted by the adoption of IFRS 9 as it represents mortgages that are at least one day past due.

⁶ The impaired mortgage ratios do not include insured mortgages since credit risk is mitigated by mortgage insurance.

Single family arrears

The increase in uninsured single family arrears related primarily to Ontario-based mortgages and occurred in the 1-30 day and 31-60 day classifications. While higher than recent quarters, these categories are volatile with the majority of borrowers curing arrears subsequent to the end of the period. We will continue to closely monitor this arrears category.

The securitized mortgage arrears balance as at June 30 was significantly higher than that of recent quarters, and the reduction in the balance as at September 30, 2018 brought it to a level more consistent with recent arrears levels. Similar to the uninsured portfolio, the majority of activity between periods occurs in the 1-30 day category, in which the majority of arrears are resolved and do not migrate to arrears categories over 30 days.

Figure 4: Impaired Corporate Mortgage Ratio



The ratio as presented above incorporates impaired (stage 3) mortgages under IFRS 9 for data presented after January 1, 2018, while the data prior to this time incorporates impaired mortgages under IAS 39. The adoption of IFRS 9 did not materially impact the impaired mortgage ratios. Refer to the “Non-IFRS Measures” section of this MD&A for a full definition of impaired mortgage ratios.

Table 17: Corporate Mortgages by Risk Rating

The table below outlines the corporate portfolio by mortgage type that, per MCAN's internal mortgage risk rating system, are considered to be "high", "higher risk" or "monitored/watchlist", including the percentage of the total portfolio that each balance represents. For further information refer to Note 8 to the consolidated financial statements.

(in thousands except %)	September 30 2018		June 30 2018		Change (%)	March 31 2018	
As at							
Insured / Low to Moderate Risk							
Single family - insured	\$ 137,169	98%	\$ 122,400	98%	12%	\$ 73,472	97%
Single family - uninsured	199,662	90%	183,597	90%	9%	172,569	88%
Construction - residential	46,627	10%	41,129	10%	13%	24,964	6%
Commercial - multi-family residential	42,409	58%	42,372	57%	0%	42,319	58%
Commercial - other	33,926	48%	33,904	48%	0%	33,817	35%
	\$ 459,793	48%	\$ 423,402	46%	9%	\$ 347,141	40%
High/Higher Risk							
Single family - uninsured	\$ 15,851	7%	\$ 16,491	8%	(4%)	\$ 17,077	9%
Single family - uninsured completed inventory	4,095	100%	9,314	100%	(56%)	7,410	100%
Construction - residential	357,662	80%	368,463	86%	(3%)	366,787	91%
Construction - non-residential	10,357	100%	5,496	100%	88%	5,014	100%
Commercial - multi-family residential	29,038	39%	28,837	39%	1%	28,081	38%
Commercial - other	37,334	52%	37,427	52%	(0%)	45,202	47%
	\$ 454,337	47%	\$ 466,028	51%	(3%)	\$ 469,571	55%
Monitored/Watchlist							
Construction - residential	\$ 41,046	9%	\$ 20,263	5%	103%	\$ 13,236	3%
Commercial - multi-family residential	2,100	3%	2,621	4%	(20%)	2,626	4%
Commercial - other	-	-	-	-	-	17,594	18%
	\$ 43,146	4%	\$ 22,884	2%	89%	\$ 33,456	4%
Arrears/Impaired							
Single family - insured	\$ 2,691	2%	\$ 2,926	2%	(8%)	\$ 2,226	3%
Single family - uninsured	5,707	3%	3,813	2%	50%	6,978	4%
	\$ 8,398	1%	\$ 6,739	1%	25%	\$ 9,204	1%
	\$ 965,674	100%	\$ 919,053	100%	5%	\$ 859,372	100%

Construction and commercial lending

Our strategy relating to construction lending consists of providing loans to developers to build housing projects. In selecting construction projects to finance, we focus on the affordable component of the housing market, such as first time or first move-up borrowers characterized by lower price points, lower price volatility and steady sales volumes based on continued family formation and immigration. This approach mitigates the impact of price volatility and tightened sales activity in the event of market corrections. We only participate in markets where we have experience and local expertise, consisting primarily of major urban markets and their surrounding areas with a preference for proximity to transit lines. We focus on projects in those markets where the increase in the cost to build new homes has not followed housing price inflation.

Although construction lending is generally riskier than single family lending, we take certain actions to mitigate risk in the portfolio, some examples of which are as follows:

- Evidence of pre-sales prior to loan approval
- Targeting experienced borrowers with a successful track record of project completion and loan repayment
- Targeting smaller multi-phased projects; as at September 30, 2018 the average outstanding construction loan size was \$6 million with a maximum loan commitment of \$30 million
- Preference for infill projects that demonstrate higher market acceptance and absorption
- Monitoring of projects with a "cost-to-complete" structure and usage of independent cost consultants to assess construction progress
- Loan terms are typically 24 months with extensions requiring separate underwriting and approval

- Management of concentration risk by diversifying across product type, loan size, geography and borrower
- Utilization of relationships with strategic partners for loan participation, servicing and workout expertise

As part of our credit risk management process, we monitor our loan portfolio for early indicators of potential concerns. The “monitored/watchlist” category includes 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. Due to factors such as borrower equity, portfolio loan to value ratios and project liquidity, as at September 30, 2018 we have not observed anything specific across the portfolio that we believe would cause a loss of principal in excess of the stage 1 and 2 allowances recorded under IFRS 9. These collective allowances are based on forward-looking economic assumptions and other factors discussed in Note 4 to the consolidated financial statements.

In addition to our construction mortgage portfolio, we are exposed to direct and indirect construction risk in certain segments of the commercial mortgage portfolio and in certain non-marketable securities based on the underlying assets.

Other Mortgage Information

Table 18: Mortgage Originations

(in thousands)					
For the Periods Ended September 30	Q3 2018	Q2 2018	Q3 2017	YTD 2018	YTD 2017
Single family - insured	\$ 35,173	\$ 26,417	\$ 13,888	\$ 74,582	\$ 31,705
Single family - uninsured	33,111	24,963	10,837	70,245	23,563
Single family - uninsured completed inventory	-	6,678	9,000	6,678	9,000
Residential construction	7,645	52,601	14,772	98,224	102,004
Non-residential construction	7,550	-	-	10,196	-
Commercial	-	-	-	44,819	35,869
	\$ 83,479	\$ 110,659	\$ 48,497	\$ 304,744	\$ 202,141

New uninsured single family origination volumes have continued to increase since mid-2017, which led to an 8% increase in the portfolio balance during Q3 2018. The increase has also been driven by external uninsured single family mortgage acquisitions of \$16 million in Q3 2018 and \$32 million for 2018 year to date.

From an internal origination perspective, we continue to monitor our underwriting criteria in the context of the lending market while maintaining a conservative approach given home valuations in certain single family markets. Additionally, we will continue to look to external sources for uninsured single family mortgage originations that are consistent with our internal risk and quality standards to assist in the continued growth of the portfolio.

We have also targeted new insured single family originations during 2018 to be able to grow our insured single family corporate mortgage portfolio (including the retention of market MBS on our corporate balance sheet) and to continue to securitize opportunistically through the NHA MBS program.

Construction, commercial and completed inventory originations represent first advances on newly originated loans, i.e. they exclude additional fundings on existing loans in the portfolio or reclassifications between portfolios.

Table 19: Average Loan to Value (LTV) Ratio for Uninsured Single Family Mortgage Originations

(in thousands except %)								
For the Periods Ended September 30	Q3 Average 2018	LTV	YTD Average 2018	LTV	Q3 Average 2017	LTV	YTD Average 2017	LTV
Ontario	\$ 23,495	69.1%	\$ 49,127	69.0%	\$ 18,919	67.9%	\$ 31,108	68.4%
Alberta	219	80.0%	7,621	63.0%	598	80.0%	743	71.1%
British Columbia	9,167	62.8%	18,350	65.7%	320	75.3%	545	65.1%
Other	230	75.8%	1,825	71.5%	-	-	167	66.8%
	\$ 33,111	67.5%	\$ 76,923	67.6%	\$ 19,837	68.4%	\$ 32,563	68.4%

Table 20: Average Mortgage Loan to Value (LTV) Ratios at Origination

As at	September 30 2018	June 30 2018	December 31 2017
Corporate portfolio:			
Single family mortgages			
- Uninsured ¹	67.3%	67.6%	67.5%
- Uninsured completed inventory	60.0%	57.6%	64.2%
- Insured	81.2%	80.8%	78.1%
Construction loans			
- Residential	58.2%	60.6%	61.6%
- Non-residential	53.1%	52.0%	47.0%
Commercial loans			
- Multi family residential	67.8%	67.9%	67.9%
- Other commercial	64.6%	65.3%	64.6%
	64.7%	65.8%	65.3%
Securitized portfolio:			
Single family insured - Market MBS Program	85.2%	85.4%	85.8%
Single family insured - CMB Program	82.0%	82.1%	82.0%
	84.7%	84.9%	85.3%
	74.4%	75.5%	76.0%

¹ MCAN's corporate uninsured single family mortgage portfolio (including completed inventory loans) is secured with a weighted average LTV at origination of 67.2% as at September 30, 2018 (June 30, 2018 - 67.2%). Based on an industry index that incorporates current real estate values, the ratios would be 57.1% and 56.9%, respectively.

Based on past experience and relative to the specifics of the then prevailing economic conditions, we would expect to observe an increase in overall mortgage default and arrears rates in the event of an economic downturn as realization periods on collateral become longer and borrowers adjust to the new economic conditions and changing real estate values. This would also result in a corresponding increase in our allowance for credit losses. An economic downturn, for example, could include changes to employment and unemployment rates, income levels and consumer spending which would have the above noted impact on our single family mortgage portfolio. MCAN utilizes a number of risk assessment and mitigation strategies to lessen the potential impact for loss on single family mortgages.

Mortgage renewal rights

Through our XMC origination platform, we retain the renewal rights to internally originated single family mortgages that are held as corporate or securitized mortgages or have been sold to third parties and derecognized from the balance sheet. At renewal, we may be able to renew these mortgages by offering clients attractive renewal options, thereby contributing to future revenues.

As at September 30, 2018, we had the renewal rights to \$952 million of single family mortgages (June 30, 2018 - \$936 million). The majority of these renewal rights relate to mortgages held on the consolidated balance sheet as corporate or securitized mortgages.

Other items

In recent years, the Canadian mortgage industry has experienced falsification of supporting documents provided to lenders in the mortgage underwriting process, and during this time we have observed instances of this activity in our own underwriting processes. The implementation of significant changes to OSFI Guideline B-20 effective January 1, 2018 has reduced the number of borrowers that qualify for new mortgages, which increases the risk of document falsification. Accordingly and in consideration of this additional risk, we have made enhancements to our underwriting processes in response to this document falsification, and we continue to monitor our processes and enhance them as part of our rigorous due diligence process.

To date, this document falsification has not had a material impact on MCAN or its financial position or performance. We do not expect to experience any material impact to our financial position or performance in the future relating to such document falsification.

Additional Information on Residential Mortgages and Home Equity Lines of Credit (“HELOCs”)

In accordance with OSFI Guideline B-20, additional information is provided on the composition of MCAN’s single family mortgage portfolio by insurance status and province, as well as amortization periods and LTV by province. LTV is calculated as the ratio of the outstanding loan balance on an amortized cost basis to the value of the underlying collateral at the time of origination.

Insured mortgages include mortgages insured by CMHC or other approved insurers at origination and mortgages that are portfolio insured after origination.

The HELOC balances displayed below relate to insured single family mortgages that have been acquired by MCAN. We do not originate HELOCs.

Table 21: Single Family Mortgages by Province as at September 30, 2018

	Corporate						Securitized		Total	
	Insured	%	Uninsured	%	HELOCs	%	Insured	%	Total	%
Ontario	\$ 87,357	62.6%	\$ 141,978	63.0%	\$ 124	80.0%	\$ 532,050	57.9%	\$ 761,509	59.2%
Alberta	28,538	20.4%	34,368	15.3%	31	20.0%	209,412	22.8%	272,349	21.2%
British Columbia	6,680	4.8%	31,830	14.1%	-	-	71,751	7.8%	110,261	8.6%
Quebec	6,276	4.5%	4,417	2.0%	-	-	35,063	3.8%	45,756	3.6%
Atlantic Provinces	8,450	6.0%	5,880	2.6%	-	-	41,872	4.6%	56,202	4.4%
Other	2,404	1.7%	6,842	3.0%	-	-	29,028	3.1%	38,274	3.0%
Total	\$ 139,705	100.0%	\$ 225,315	100.0%	\$ 155	100.0%	\$ 919,176	100.0%	\$ 1,284,351	100.0%

Table 22: Single Family Mortgages by Province as at June 30, 2018

	Corporate						Securitized		Total	
	Insured	%	Uninsured	%	HELOCs	%	Insured	%	Total	%
Ontario	\$ 77,540	61.9%	\$ 130,376	61.1%	\$ 101	76.5%	\$ 549,428	56.9%	\$ 757,445	58.0%
Alberta	23,279	18.6%	37,429	17.6%	31	23.5%	221,684	23.0%	282,423	21.7%
British Columbia	7,010	5.6%	28,155	13.2%	-	-	79,009	8.2%	114,174	8.8%
Quebec	7,375	5.9%	4,698	2.2%	-	-	38,337	4.0%	50,410	3.9%
Atlantic Provinces	7,246	5.8%	5,920	2.8%	-	-	43,894	4.6%	57,060	4.4%
Other	2,748	2.2%	6,633	3.1%	-	-	32,155	3.3%	41,536	3.2%
Total	\$ 125,198	100.0%	\$ 213,211	100.0%	\$ 132	100.0%	\$ 964,507	100.0%	\$ 1,303,048	100.0%

Table 23: Single Family Mortgages by Amortization Period as at September 30, 2018

(in thousands except %)	Up to 20 Years	>20 to 25 Years	>25 to 30 Years	>30 to 35 Years	Total
Corporate	\$ 60,645 16.6%	\$ 118,565 32.5%	\$ 183,321 50.2%	\$ 2,644 0.7%	\$ 365,175 100.0%
Securitized	\$ 209,707 22.8%	\$ 457,657 49.8%	\$ 205,639 22.4%	\$ 46,173 5.0%	\$ 919,176 100.0%
Total	\$ 270,352 21.0%	\$ 576,222 44.9%	\$ 388,960 30.3%	\$ 48,817 3.8%	\$ 1,284,351 100.0%

Table 24: Single Family Mortgages by Amortization Period as at June 30, 2018

(in thousands except %)	Up to 20 Years	>20 to 25 Years	>25 to 30 Years	>30 to 35 Years	Total
Corporate	\$ 67,494 19.9%	\$ 97,926 28.9%	\$ 171,311 50.7%	\$ 1,810 0.5%	\$ 338,541 100.0%
Securitized	\$ 216,195 22.4%	\$ 468,607 48.6%	\$ 218,197 22.6%	\$ 61,508 6.4%	\$ 964,507 100.0%
Total	\$ 283,689 21.8%	\$ 566,533 43.5%	\$ 389,508 29.8%	\$ 63,318 4.9%	\$ 1,303,048 100.0%

Other Corporate Assets

Cash and cash equivalents

Cash and cash equivalents, which include cash balances with banks and overnight term deposits, provide liquidity to meet maturing term deposit and new mortgage funding commitments and are considered to be Tier 1 liquid assets. For further information, refer to the “Liquidity Management” section of this MD&A.

Marketable securities

Marketable securities, consisting of corporate bonds and real estate investment trusts (“REITs”), provide additional liquidity at yields in excess of cash and cash equivalents and are considered to be Tier 2 liquid assets. For further information, refer to the “Liquidity Management” section of this MD&A. In Q3 2018, we recorded a \$0.1 million decrease to the unrealized gain on marketable securities.

Non-marketable securities (formerly Financial Investments)

We hold a \$41 million (June 30, 2018 - \$41 million) investment in the KingSett High Yield Fund (“KSHYF”), in which we have a 7.9% equity interest (June 30, 2018 - 8.0%). Our Q3 2018 return was 11.5% (Q3 2017 - 12.9%). As at September 30, 2018, our total remaining commitment to the KSHYF was \$22 million (June 30, 2018 - \$22 million), consisting of \$1 million (June 30, 2018 - \$1 million) of unfunded capital advances and \$21 million (June 30, 2018 - \$21 million) that supports credit facilities throughout the life of the KSHYF.

We also hold a \$30 million (June 30, 2018 - \$29 million) investment in Crown LP, in which we have a 14.1% equity interest (June 30, 2018 - 14.1%). As at September 30, 2018, the value of the investment in Crown LP for tax purposes was \$4 million (June 30, 2018 - \$4 million). In Q3 2018, we recorded a \$0.4 million increase to the unrealized gain on the investment in Crown LP.

Equity investment in MCAP

We hold a 13.71% equity interest in MCAP (June 30, 2018 - 13.83%), which represents 4.0 million units held by MCAN (June 30, 2018 - 4.0 million) of the 29.2 million total outstanding MCAP partnership units (June 30, 2018 - 28.9 million).

This investment had a net book value of \$60 million as at September 30, 2018 (June 30, 2018 - \$58 million). The Limited Partner’s At-Risk Amount (“LP ARA”), which represents the cost base of the equity investment in MCAP for income tax purposes, was \$31 million as at September 30, 2018 (June 30, 2018 - \$36 million). The difference between the net book value and the LP ARA reflects an unrealized gain that, if realized, would be recognized as a capital gain and applied against MCAN’s tax loss carry forward. For further information on the LP ARA, refer to the “Non-IFRS Measures” section of this MD&A.

During Q3 2018, we received \$1.6 million of unitholder distributions from MCAP (Q3 2017 - \$1.6 million). Since we account for this investment on the equity basis, the receipt of distributions reduces the carrying value of the investment in MCAP.

During the quarter, MCAP announced the retirement of its Chief Executive Officer, Derek Norton, and announced the appointment of Mark Aldridge as MCAP’s new Chief Executive Officer. Mr. Norton remains as a Director on MCAP’s Board alongside Mr. Aldridge.

Amongst the interparty rights in the MCAP partnership agreement, the majority partner in MCAP has the right to acquire MCAN’s entire partnership interest in MCAP at “fair market value”, which would be determined by an independent valuator agreed upon by both parties.

Securitization Assets

Securitization assets consist primarily of single family insured mortgages securitized through the market MBS program and CMB program. For further information, refer to the “Securitization Programs” section of this MD&A.

Table 25: Liabilities and Shareholders' Equity

(in thousands)					
As at	September 30 2018 ¹	June 30 2018 ¹	December 31 2017	Change from Prior Quarter (\$)	Change from Prior Quarter (%)
Corporate Liabilities					
Term deposits	\$ 935,496	\$ 912,223	\$ 884,460	\$ 23,273	3%
Current taxes payable	461	457	-	4	1%
Deferred tax liabilities	3,416	3,390	3,572	26	1%
Other liabilities	14,032	7,135	16,067	6,897	97%
	953,405	923,205	904,099	30,200	3%
Securitization Liabilities					
Financial liabilities from securitization	933,553	976,769	1,015,699	(43,216)	(4%)
	933,553	976,769	1,015,699	(43,216)	(4%)
	1,886,958	1,899,974	1,919,798	(13,016)	(1%)
Shareholders' Equity					
Share capital	221,126	219,456	214,664	1,670	1%
Contributed surplus	510	510	510	-	-
Retained earnings	80,787	86,130	65,365	(5,343)	(6%)
Accumulated other comprehensive income	-	-	16,438	-	-
	302,423	306,096	296,977	(3,673)	(1%)
	\$ 2,189,381	\$ 2,206,070	\$ 2,216,775	\$ (16,689)	(1%)

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

To fund our corporate operations, we issue term deposits that are eligible for CDIC deposit insurance. We do not accept deposits that can be cashed prior to maturity or paid on demand except in the event of the death of a depositor. The role of term deposits in managing liquidity risk is discussed in the “Liquidity and Funding Risk” sub-section of the “Risk Governance and Management” section of this MD&A.

Financial liabilities from securitization relate to our participation in the market MBS program and CMB program, where we have sold MBS to third parties but have not derecognized the related mortgages from our balance sheet. For further information on the market MBS program and CMB program, refer to the “Securitization Programs” section of this MD&A.

Share capital activity for Q3 2018 reflects new common shares issued through the DRIP. The DRIP participation rate for the September 30, 2018 dividend was 19% (June 30, 2018 - 19%). For further information, refer to Note 16 to the consolidated financial statements.

Retained earnings activity for Q3 2018 consists of net income of \$11.0 million less dividends of \$16.3 million. The dividend balance consists of both the third quarter dividend paid on September 28, 2018 and the fourth quarter dividend which is payable on January 2, 2019 but was declared prior to quarter end and has therefore been accrued as at September 30, 2018 and included in other liabilities.

SELECTED QUARTERLY FINANCIAL DATA

Table 26: Selected Quarterly Financial Data

(in thousands except for per share amounts and %)	Q3/18 ²	Q2/18 ²	Q1/18 ²	Q4/17	Q3/17	Q2/17	Q1/17	Q4/16
Net investment income - corporate assets ²	\$ 13,116	\$ 15,063	\$ 12,073	\$ 14,359	\$ 12,918	\$ 12,179	\$ 12,963	\$ 11,684
Other income - corporate assets	314	-	1,701	-	-	-	876	-
Net investment income - securitization assets ²	1,276	1,317	1,301	1,416	1,532	1,374	1,291	1,519
	14,706	16,380	15,075	15,775	14,450	13,553	15,130	13,203
Operating expenses	3,637	5,142	4,631	5,302	4,689	4,616	4,617	4,471
Net income before income taxes	11,069	11,238	10,444	10,473	9,761	8,937	10,513	8,732
Provision for (recovery of) income taxes	63	113	(171)	(334)	(157)	(1)	248	(268)
Net income	\$ 11,006	\$ 11,125	\$ 10,615	\$ 10,807	\$ 9,918	\$ 8,938	\$ 10,265	\$ 9,000
Basic and diluted earnings per share	\$ 0.47	\$ 0.47	\$ 0.45	\$ 0.47	\$ 0.42	\$ 0.39	\$ 0.44	\$ 0.39
Dividends per share	\$ 0.37	\$ 0.37	\$ 0.37	\$ 0.37	\$ 0.32	\$ 0.32	\$ 0.30	\$ 0.30
Return on average shareholders' equity ¹	14.29%	14.54%	14.10%	14.63%	13.63%	12.37%	14.37%	12.94%
Average mortgage portfolio yield - corporate ¹	5.53%	5.65%	5.72%	5.56%	5.25%	5.28%	5.12%	4.99%
Average term deposit interest rate ¹	2.61%	2.48%	2.38%	2.29%	2.25%	2.21%	2.20%	2.20%
Average mortgage portfolio balance - corporate (\$ million)	\$ 942	\$ 913	\$ 849	\$ 866	\$ 908	\$ 914	\$ 908	\$ 954
<u>Average term to maturity (in months)</u>								
Mortgages - corporate	12.8	13.2	11.3	11.1	10.6	10.6	10.8	12.8
Term deposits	19.2	17.4	18.9	19.1	18.1	18.8	17.4	17.4
Average mortgage portfolio yield - securitized ¹	2.57%	2.59%	2.57%	2.57%	2.63%	2.67%	2.61%	2.74%
Average financial liability from securitization rate ¹	1.83%	1.83%	1.83%	1.81%	1.83%	1.93%	1.90%	2.01%
Average mortgage portfolio balance - securitized (\$ million)	\$ 935	\$ 986	\$ 1,015	\$ 1,002	\$ 1,028	\$ 1,057	\$ 1,052	\$ 1,032

¹ Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

² Provisions for credit losses are included in both net investment income from corporate and securitization assets. Effective Q1 2018, we prospectively adopted IFRS 9 and did not restate prior period information. Under IFRS 9, the methodology for the calculation of mortgage allowances and provisions has changed from IAS 39, therefore provisions under IFRS 9 are not directly comparable to prior periods. Additionally, under IFRS 9 fair value changes in certain reclassified financial assets are presented in the income statement and are therefore not directly comparable to prior periods. Under IAS 39, these fair value changes were recorded through other comprehensive income.

Net investment income from corporate and securitization assets is generally driven by the average mortgage portfolio balance and interest rate. Additionally, corporate net investment income was impacted by significant distribution income from Crown LP in Q1 2017 and substantial equity income from MCAP in Q2 2017 and Q4 2017.

Corporate mortgage interest yields have generally increased since Q3 2017 as a result of increases to the overnight rate by the Bank of Canada given that the majority of the corporate portfolio is floating rate, however changes in the portfolio mix have contributed to the slight decrease in the past two quarters.

Since the adoption of IFRS 9 effective January 1, 2018, we have experienced increased volatility in net income as a result of the recognition of unrealized gains on certain securities through net income. This volatility was especially prominent in Q2 2018, generating a positive impact to net income of \$3.3 million. Prior to the adoption of IFRS 9, these unrealized gains were recognized through accumulated other comprehensive income.

The securitized mortgage portfolio has gradually decreased since Q2 2017 as a result of a reduction in securitization volumes.

The decrease in operating expenses in Q3 2018 was a result of a reduction to our variable compensation accruals and a non-recurring \$0.6 million reimbursement of previously incurred and accrued legal expenses related to ongoing litigation. Operating expenses increased in Q4 2017 as a result of non-recurring professional fee accruals.

SECURITIZATION PROGRAMS

We are an NHA MBS issuer, which involves the securitization of insured mortgages to create MBS. We issue MBS through our internal market MBS program and the Canada Housing Trust (“CHT”) CMB program.

Market MBS Program

During Q3 2018, we securitized \$32 million of MBS through the market MBS program (Q3 2017 - \$20 million) and sold the MBS to a third party.

We may issue market MBS through the NHA MBS program and retain the underlying MBS security for liquidity purposes instead of selling it to a third party. As at September 30, 2018, we held \$71 million of retained MBS on our balance sheet (June 30, 2018 - \$73 million), which is included in the insured single family classification within corporate mortgages.

CAPITAL MANAGEMENT

Our primary capital management objectives are to maintain sufficient capital for regulatory purposes and to earn acceptable and sustainable risk-weighted returns for our shareholders. Through our risk management and corporate governance framework, we assess current and projected economic, housing market, interest rate and credit conditions to determine appropriate levels of capital. We typically pay out all taxable income by way of dividends subject to final review and declaration by the Board. Capital growth is achieved through retained earnings, the DRIP, rights offerings and public share offerings. Our capital management is driven by the guidelines set out by the Tax Act and OSFI.

Income Tax Capital

As a MIC under the Tax Act, we are limited to an income tax liabilities to capital ratio of 5:1 (or an income tax assets to capital ratio of 6:1), based on our non-consolidated balance sheet in the MIC entity measured at its tax value. Securitization assets and liabilities (less accrued interest) are both excluded from the calculation of the income tax assets to capital ratio.

We manage our income tax assets to a level of 5.75 times income tax capital on a non-consolidated tax basis to provide a prudent cushion between the maximum permitted assets and total actual assets. Income tax asset capacity represents additional asset growth available to yield a 5.75 income tax assets to income tax capital ratio.

Table 27: Income Tax Capital ¹

(in thousands except ratios)	September 30 2018 ²	June 30 2018 ²	December 31 2017
As at			
Income tax assets ¹			
Consolidated assets	\$ 2,189,381	\$ 2,206,070	\$ 2,216,775
Adjustment for assets in subsidiaries	4,839	5,390	5,435
Non-consolidated assets in MIC entity	2,194,220	2,211,460	2,222,210
Add: mortgage allowances	4,680	5,061	4,750
Less: securitization assets ³	(944,153)	(988,051)	(1,030,020)
Less: equity investments in MCAP and subsidiaries	(56,483)	(48,616)	(42,411)
Other adjustments	(8,436)	(8,139)	(7,475)
	<u>\$ 1,189,828</u>	<u>\$ 1,171,715</u>	<u>\$ 1,147,054</u>
Income tax liabilities ¹			
Consolidated liabilities	\$ 1,886,958	\$ 1,899,974	\$ 1,919,798
Adjustment for liabilities in subsidiaries	(7,963)	(7,588)	(7,852)
Non-consolidated liabilities in MIC entity	1,878,995	1,892,386	1,911,946
Less: securitization liabilities ³	(932,222)	(975,384)	(1,014,258)
	<u>\$ 946,773</u>	<u>\$ 917,002</u>	<u>\$ 897,688</u>
Income tax capital ^{1,4}	<u>\$ 243,055</u>	<u>\$ 254,713</u>	<u>\$ 249,366</u>
Income tax asset capacity ^{1,4}	<u>\$ 207,739</u>	<u>\$ 292,883</u>	<u>\$ 286,801</u>
Income tax capital ratios ^{1,4}			
Income tax assets to capital ratio	4.90	4.60	4.60
Income tax liabilities to capital ratio	3.90	3.60	3.60

¹ Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

² Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

³ The majority of securitization assets and liabilities per balance sheet are excluded from income tax assets, liabilities and capital to the extent that they are held in the MIC entity.

⁴ Income tax capital as at September 30, 2018 is calculated net of the fourth quarter dividend payable January 2, 2019 due to the fact that this dividend was declared prior to quarter end and therefore has been deducted from shareholders' equity as at September 30, 2018. This deduction has contributed to the decrease in income tax asset capacity and the increase in the income tax assets to capital and liabilities to capital ratios as at September 30, 2018.

Regulatory Capital

As a Loan Company under the *Trust and Loan Companies Act* (the "Trust Act"), OSFI oversees the adequacy of our capital. For this purpose, OSFI has imposed minimum capital-to-regulatory (or risk-weighted) assets ratios and a minimum leverage ratio which is calculated on a different basis from the income tax assets to capital ratio discussed in the "Income Tax Capital" subsection above.

During Q3 2018, OSFI released a discussion paper relating to the proposed implementation of final Basel III reforms in Canada. The reforms were published by the Basel Committee on Banking Supervision ("BCBS") in December 2017 and seek to enhance credibility in the calculation of risk-weighted assets and improve the comparability and transparency of the capital ratios of OSFI-regulated financial institutions. These proposed reforms could significantly impact the risk-weighting of the Company's construction and commercial mortgage portfolios, as the new guidelines could potentially increase the risk-weighting of these assets from the current level of 100% to 150%. We are currently investigating the impact of these proposed reforms and the associated potential for higher capital requirements on real estate lending in Canada.

Our internal target minimum CET 1, Tier 1 and Total Capital ratios are 20%. We maintain prudent capital planning practices to ensure that we are adequately capitalized and continue to satisfy minimum standards and internal targets.

Table 28: Regulatory Capital

(in thousands except %)	September 30 2018 ¹	June 30 2018 ¹	December 31 2017
As at			
Regulatory Ratios (OSFI)			
Share capital	\$ 221,126	\$ 219,456	\$ 214,664
Contributed surplus	510	510	510
Retained earnings	80,787	86,130	65,365
Accumulated other comprehensive income	-	-	16,438
Deduction for equity investment in MCAP (Transitional adjustment) ²	n/a	n/a	(23,593)
Common Equity Tier 1, Tier 1 and Total Capital (Transitional) ^{2,3}	n/a	n/a	\$ 273,384
Deduction for equity investment in MCAP (All-in adjustment) ²	(29,689)	(27,344)	(5,898)
Common Equity Tier 1, Tier 1 and Total Capital (All-in) ^{2,3,5}	\$ 272,734	\$ 278,752	\$ 267,486
Total Exposures/Regulatory Assets ³			
Consolidated assets	\$ 2,189,381	\$ 2,206,070	\$ 2,216,775
Less: deductions from all-in Tier 1 Capital ²	(29,689)	(27,344)	(29,491)
Other adjustments ⁴	905	2,222	2,915
Total On-Balance Sheet Exposures	2,160,597	2,180,948	2,190,199
Mortgage and investment funding commitments	440,844	423,043	317,687
Less: conversion to credit equivalent amount (50%)	(220,422)	(211,522)	(158,844)
Letters of credit	43,715	42,236	32,164
Less: conversion to credit equivalent amount (50%)	(21,858)	(21,118)	(16,082)
Total Off-Balance Sheet Items	242,279	232,639	174,925
Total Exposures/Regulatory Assets	\$ 2,402,876	\$ 2,413,587	\$ 2,365,124
Leverage ratio ³	11.35%	11.55%	11.31%
Risk weighted assets (all-in) ^{2,3}	\$ 1,325,068	\$ 1,298,367	\$ 1,258,171
Risk weighted assets (transitional) ^{2,3}	n/a	n/a	1,269,967
Regulatory Capital Ratios ³			
Common Equity Tier 1 capital to risk-weighted assets ratio (all-in)	20.58%	21.47%	21.26%
Tier 1 capital to risk-weighted assets ratio (all-in)	20.58%	21.47%	21.26%
Total capital to risk-weighted assets ratio (all-in)	20.58%	21.47%	21.26%
Common Equity Tier 1 capital to risk-weighted assets ratio (transitional)	n/a	n/a	21.53%
Tier 1 capital to risk-weighted assets ratio (transitional)	n/a	n/a	21.53%
Total capital to risk-weighted assets ratio (transitional)	n/a	n/a	21.53%

¹ Effective January 1, 2018 we adopted IFRS 9, Financial Instruments. Results from periods prior to January 1, 2018 are reported in accordance with IAS 39, Financial Instruments: Recognition & Measurement. For further information on the adoption of IFRS 9, refer to Notes 4 and 6 to the consolidated financial statements.

² The deduction for the equity investment in MCAP on an all-in basis is equal to the equity investment balance less 10% of the Company's shareholders' equity. As of January 1, 2018, the deduction was fully deductible whereas in 2017, the deduction on the transitional basis was equal to 80% of the all-in adjustment.

³ Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

⁴ Certain items, such as negative cash balances, are excluded from total exposures but included in consolidated assets.

⁵ Regulatory capital as at September 30, 2018 is calculated net of the fourth quarter dividend payable January 2, 2019 due to the fact that this dividend was declared prior to quarter end and therefore has been deducted from shareholders' equity as at September 30, 2018. This deduction has contributed to the decrease in the leverage ratio and the Common Equity Tier 1, Tier 1 and Total Capital to Risk Weighted Asset Ratios as at September 30, 2018.

Table 29: Regulatory Risk-Weighted Assets

(in thousands except %)	September 30, 2018			June 30, 2018		
	Per Balance Sheet	Average Rate	Risk Weighted Assets	Per Balance Sheet	Average Rate	Risk Weighted Assets
As at						
On-Balance Sheet Assets						
Cash and cash equivalents	\$ 75,236	20%	\$ 15,228	\$ 96,985	20%	\$ 19,841
Cash held in trust	27,527	20%	5,505	25,740	20%	5,148
Marketable securities	58,447	100%	58,447	58,534	100%	58,534
Mortgages - corporate	965,674	71%	687,342	919,053	72%	665,771
Mortgages - securitized	919,176	3%	28,121	964,507	3%	29,089
Non-marketable securities	70,727	221%	156,603	70,191	229%	161,033
Other loans	2,104	100%	2,104	2,426	100%	2,426
Equity investment in MCAP	59,931	50%	30,242	57,954	53%	30,609
Foreclosed real estate	435	100%	435	435	100%	435
Deferred tax asset	2,971	100%	2,971	3,005	100%	3,005
Other assets	7,153	100%	7,153	7,240	100%	7,240
			<u>994,151</u>			<u>983,131</u>
Off-Balance Sheet Items						
Letters of credit	43,715	50%	21,857	42,236	50%	21,118
Commitments	440,844	45%	198,135	423,043	44%	185,130
			<u>219,992</u>			<u>206,248</u>
Charge for operational risk			<u>110,925</u>			<u>108,988</u>
Risk-Weighted Assets (all-in)			<u>\$ 1,325,068</u>			<u>\$ 1,298,367</u>

LIQUIDITY MANAGEMENT

Our liquidity management process includes a Liquidity Risk Management Framework that incorporates multi scenario stress testing. Results of the stress testing are reviewed by management on a monthly basis and reported to the Board on a quarterly basis.

We fund our corporate operations by issuing term deposits that are eligible for CDIC deposit insurance. We do not accept deposits that can be cashed prior to maturity or paid on demand except in the event of the death of a depositor.

For further information on how we manage liquidity risk, refer to the "Liquidity and Funding Risk" sub-section of the "Risk Governance & Management" section of this MD&A. For information on our credit facilities refer to Note 24 to the consolidated financial statements.

OSFI's Liquidity Adequacy Requirements ("LAR") guideline establishes three minimum standards based on the Basel III framework with national supervisory discretion applied to certain treatments: the Liquidity Coverage Ratio ("LCR") and Net Cumulative Cash Flow ("NCCF") metric, which are both currently in effect, and the Net Stable Funding Ratio ("NSFR"), which is effective January 1, 2020.

As at September 30, 2018, we were in compliance with the LCR and NCCF. Based on our current financial and liquidity position, we believe that we will be able to comply with the NSFR requirements once enacted. These requirements are supplemented by additional supervisory monitoring metrics including the liquidity monitoring tools and the intraday liquidity monitoring tools as considered in the Basel III framework.

The following table shows the composition of our internal liquidity ratios. These internal ratios include assumptions relating to the value of liquid assets such as the ability to sell these assets in a stressed market scenario. We manage our Tier 1 & 2 and Total liquid assets to a minimum of 60% and 100% of term deposit liabilities maturing within 100 days, respectively, and a maximum of 150% for both ratios.

Our liquidity ratios as at September 30, 2018 reduced from the prior quarter to more typical levels. The June 30, 2018 balance was significantly higher than usual as a result of a low volume of term deposit liabilities maturing within 100 days. In recent quarters we have, in some cases, maintained a liquid asset balance above our target maximum as a result of the current uncertainty in housing markets.

Table 30: Liquidity Ratios

(in thousands except %)	September 30 2018	June 30 2018	December 31 2017
As at			
Tier 1 liquid assets ¹			
Cash and cash equivalents	\$ 75,236	\$ 96,985	\$ 117,571
Tier 2 liquid assets ¹			
Marketable securities	58,447	58,534	62,518
Less: marketable securities adjustment ²	(13,900)	(13,952)	(14,391)
Market MBS retained by MCAN ³	71,007	73,123	28,597
	<u>115,554</u>	<u>117,705</u>	<u>76,724</u>
Tier 3 liquid assets ¹			
Single family insured mortgages ⁴	68,278	51,849	51,711
Less: single family insured mortgages adjustment ⁴	(26,216)	(19,008)	(17,713)
	<u>42,062</u>	<u>32,841</u>	<u>33,998</u>
Total liquid assets ¹	<u>\$ 232,852</u>	<u>\$ 247,531</u>	<u>\$ 228,293</u>
100 day term deposit maturities	<u>\$ 111,745</u>	<u>\$ 53,398</u>	<u>\$ 103,632</u>
Liquidity ratios ¹			
Tier 1 & 2 liquid assets to 100 day term deposit maturities	171%	402%	187%
Total liquid assets to 100 day term deposit maturities	<u>208%</u>	<u>464%</u>	<u>220%</u>

¹ Refer to the "Non-IFRS Measures" section of this MD&A for a definition of these measures.

² Adjusted to reflect estimated impact to fair market value in a stressed scenario. Corporate bonds are reduced as follows: BBB- or higher (30%); below BBB- (45%). REITs are reduced as follows: constituent in TSX/S&P Composite Index (20%); not a constituent in TSX/S&P Composite Index (40%).

³ Included in corporate mortgages - insured single family. For further information, refer to the "Securitization Programs" section of this MD&A.

⁴ Single family insured mortgages exclude mortgages pledged as collateral and second mortgages not insured by CMHC. The adjustment reflects lower liquidity than Tier 1 and Tier 2 liquidity, as follows: CMHC insured (25%), CMHC insured second mortgages (50%), privately insured (50%).

Our sources and uses of liquidity are outlined in the table below. We manage our net liquidity surplus/deficit by raising term deposits as mentioned above. For further information on our off-balance sheet commitment associated with our investment in the KSHYF, refer to the "Off-Balance Sheet Arrangements" section of this MD&A.

Table 31: Liquidity Analysis

(in thousands)	Within 3 Months	3 Months To 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years	September 30 2018	June 30 2018
Sources of liquidity							
Cash and cash equivalents	\$ 75,236	\$ -	\$ -	\$ -	\$ -	\$ 75,236	\$ 96,985
Marketable securities	58,418	-	-	29	-	58,447	58,534
Mortgages - corporate	215,710	411,825	263,131	69,318	5,690	965,674	919,053
Non-marketable securities	-	-	-	-	70,727	70,727	70,191
Other loans	1,062	30	1,012	-	-	2,104	2,426
	350,426	411,855	264,143	69,347	76,417	1,172,188	1,147,189
Uses of liquidity							
Term deposits	109,506	255,147	475,169	95,674	-	935,496	912,223
Other liabilities	14,032	-	-	-	-	14,032	7,135
	123,538	255,147	475,169	95,674	-	949,528	919,358
Net liquidity surplus (deficit)	\$ 226,888	\$ 156,708	\$ (211,026)	\$ (26,327)	\$ 76,417	\$ 222,660	\$ 227,831
Off-Balance Sheet							
Unfunded mortgage commitments	\$ 80,139	\$ 159,718	\$ 178,554	\$ -	\$ -	\$ 418,411	\$ 400,610
Commitment - KSHYF	-	-	22,433	-	-	22,433	22,433
	\$ 80,139	\$ 159,718	\$ 200,987	\$ -	\$ -	\$ 440,844	\$ 423,043

Note: The above table excludes securitized assets and liabilities and pledged assets as their use is restricted to securitization program operations.

RISK GOVERNANCE AND MANAGEMENT

We are exposed to a number of risks, including credit risk, liquidity and funding risk, operational risk, strategic and business risk, reputational risk, interest rate risk, market risk and cyber risk, that can adversely affect our ability to achieve our business objectives or execute our business strategies, and which may result in a loss of earnings, capital and/or damage to our reputation. We mitigate these risks through prudent credit limits, established lending policies and procedures, effective monitoring and reporting, investment diversification and by the diligent management of assets and liabilities.

We operate in changing regulatory and economic environments. As a result, we believe that our management team and the Board are particularly diligent in their consideration of all identified and emerging risks. Our goal is not to eliminate risk, as this would result in significantly reduced earnings, but rather to be proactive in our assessment and management of risk, as a means to gain a strategic advantage and ultimately enhance shareholder value.

The risks that have been identified may not be the only risks that we face. Other risks of which we are not aware or which we currently deem to be immaterial may surface in future periods and have a material adverse impact on our business, results from operations and financial condition.

The shaded areas of this section of the MD&A represent a discussion of risk factors and risk management policies and procedures relating to credit, liquidity, interest rate and market risks as required under IFRS 7, *Financial Instruments: Disclosures*. The relevant MD&A sections are identified by shading within boxes and the content forms an integral part of the consolidated financial statements.

For a detailed discussion of risks that the Company is exposed to, refer to the "Risk Governance and Management" section of the 2017 Annual MD&A.

Liquidity and Funding Risk

Liquidity and funding 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 we may eventually collect the amounts outstanding, which may result in a loss of earnings or capital, or have an otherwise adverse effect on our financial condition and results of operations.

For information on the contractual maturities of certain obligations of the Company, refer to notes 13, 15 and 23 to the consolidated financial statements.

Reputational Risk

Reputational risk is the negative consequence of the occurrence of other risks and can occur from an activity undertaken by the Company, its affiliated companies, or its representatives. The loss of reputation can greatly affect shareholder value through reduced public confidence, a loss of business, legal action, or increased regulatory oversight. Reputation refers to the perception of the enterprise by various stakeholders. Typically, key stakeholder groups include investors, customers, depositors, employees, suppliers and regulators. Perceptions may be impacted by various events including financial performance, specific adverse occurrences from events such as cyber security issues, unfavourable media coverage, and changes or actions of the corporation's leadership. Failure to effectively manage reputation risk can result in reduced market capitalization, loss of client loyalty, reduced access to deposit funding and the inability to achieve our strategic objectives.

Strategic and Business Risk

Strategic and business risk is the risk of loss due to fluctuations in the external business environment, the failure of management to adjust its strategies, business model and business activities for external events, business results, changes in the competitive environment or the inability of the business to change its cost levels in response to those changes.

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 for MCAN have been separately identified as outsourcing risk and cyber 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.

Outsourcing Risk

Within operational risk, outsourcing risk is the risk incurred when we contract out a business function to a service provider instead of performing the function ourselves, and the service provider performs at a lower standard than we would have under similar circumstances. We outsource the majority of our mortgage and loan origination, servicing and collections to MCAP and other third parties.

Risk of Accuracy and Completeness of Borrower Information

Within operational risk, in the single family mortgage underwriting process, we rely on information provided by potential borrowers and other third parties, including mortgage brokers. We may also rely on the representations of potential borrowers and third parties as to the accuracy and completeness of that information. Our financial position and performance may be negatively impacted if this information is intentionally misleading or does not fairly represent the financial condition of the potential borrower and is not detected by our internal controls.

Cyber Risk

We collect and store confidential and personal information to the extent needed for operational purposes. Unauthorized access to the Company's computer systems could result in the theft or publication of confidential information or the deletion or modification of records or could otherwise cause interruptions in the Company's operations. In addition, despite the Company's implementation of security measures, its systems are vulnerable to damages from computer viruses, natural disasters, unauthorized access, cyber-attack and other similar disruptions. Any such system failure, accident or security breach could disrupt the Company's delivery of services and make the Company's applications unavailable or cause similar disruptions to the Company's operations. If a person penetrates the Company's network security or otherwise misappropriates sensitive data, we could be subject to liability or our business could be interrupted, and any of these developments could have a material adverse effect on the Company's business, results of operations and financial condition.

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. 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.

Interest Rate Risk

Interest rate risk is the potential impact of changes in interest rates on our earnings and capital. Interest rate risk arises when our assets and liabilities, both on and off-balance sheet, have mismatched repricing dates. Changes in interest rates where we have mismatched repricing dates may have an adverse effect on our 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 our financial condition and results of operations.

Our exposure to interest rate risk is discussed further in Note 25 to the consolidated financial statements.

Subsequent to quarter end, OSFI issued proposed revisions to guideline B-12, *Interest Rate Risk Management*. The draft guideline incorporates most of the Basel Committee on Banking Supervision's ("BCBS") guidance on interest rate risk in the banking book ("IRRBB"), including the methods expected to be used by institutions for measuring, managing and monitoring IRRBB, as well as updated related to supervisory practices. OSFI is targeting implementation of the revised guideline as at January 1, 2020. We are currently assessing the impact of these proposed revisions.

Market Risk

Market risk is the exposure to adverse changes in the value of financial assets. Our market risk factors include price risk on marketable securities, interest rates, real estate values and commodity prices, among others. Any changes in these market risk factors may negatively affect the value of our financial assets, which may have an adverse effect on our financial condition and results of operations. We do not undertake trading activities as part of our regular operations, and therefore are not exposed to risks associated with activities such as market making, arbitrage or proprietary trading.

Risk Management

For a detailed discussion of how we manage the risks noted above, refer to the "Risk Governance and Management" section of the 2017 Annual MD&A.

Credit Risk - Impairment Assessment Under IFRS 9

The analysis of MCAN's IFRS 9 impairment assessment and measurement approach discussed below should be read in conjunction with Note 4 to the consolidated financial statements.

Probability of Default

The probability of default ("PD") is driven by historical arrears performance, and incorporates the rate at which mortgages move from performing status to defaulted status. Key macroeconomic variables, borrower Beacon scores and internal mortgage risk ratings (where applicable) are also used in calculating this rate. Where historical arrears performance is limited or not available, the Company uses external arrears/default data for similar loans and mortgages.

Exposure at default

The exposure at default ("EAD") represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the borrower's ability to increase its exposure while approaching default and potential early repayments.

To calculate the EAD for a Stage 1 loan, the Company assesses the possible default events within 12 months for the calculation of the 12 month ECL. However, if a Stage 1 loan that is expected to default in the 12 months from the balance sheet date and is also expected to cure and subsequently default again, then all linked default events are taken into account. For Stage 2 and Stage 3 financial assets, the EAD is considered for events over the lifetime of the instruments.

The Company determines EADs by determining the period of exposure and modelling the change in loan exposures over time. Except for some revolving credit facilities, the maximum period over which ECL is measured is the maximum contractual period. For revolving credit facilities that include both a loan component and an undrawn commitment component, assessment is made with respect to whether the Company's exposure to credit losses is not limited to the contractual notice period. Once the period of exposure is determined, EAD is modelled based on loan terms, prepayment assumptions, commitment drawing patterns and other relevant forward-looking information.

Loss given default

Loss given default (“LGD”) is modelled using a common LGD methodology that incorporates specific relevant data where appropriate. The LGD estimation takes into account all relevant and forward-looking information including but not limited to expected EAD, forecast of future collateral valuations including expected sales costs and discounts, debt structure and cross-collateralisation, and varies with macroeconomic scenarios.

The Company segments its corporate mortgage portfolio into individual lines of business, outlined in Note 8. The segmentation is based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and other transaction characteristics as applicable.

Additional data and forward-looking economic scenarios are used in order to determine the IFRS 9 LGD rate for each mortgage. When assessing forward-looking information, the expectation is based on multiple scenarios. Examples of key inputs involve changes in collateral values including property prices for mortgages, regional housing price indexes or other factors that are indicative of losses in the group. Under IFRS 9, LGD rates are estimated for the Stage 1, Stage 2 and Stage 3 IFRS 9 segment of each mortgage. The inputs for these LGD rates are estimated and, where possible, calibrated through back testing against recent recoveries. These are repeated for each economic scenario as appropriate.

Grouping financial assets measured on a collective basis

The Company calculates ECLs either on a collective or individual basis for the corporate mortgage portfolio based on the line of business (per Note 8). ECLs are calculated on an individual basis for all mortgages in Stage 3 and are calculated on a collective basis for all mortgages in Stage 1 and Stage 2.

Analysis of inputs into the ECL model under multiple economic scenarios

An overview of the approach to estimating ECLs is set out in Notes 4 and 5. As part of the model input process, macroeconomic data are obtained from third party sources (e.g. rating agencies, bank economic forecasts), and our Risk Management department verifies the quality of data and assumptions in the Company’s ECL models including determining the weights attributable to the multiple scenarios.

DESCRIPTION OF CAPITAL STRUCTURE

Our authorized share capital consists of an unlimited number of common shares with no par value. At September 30, 2018, there were 23,745,727 common shares outstanding (June 30, 2018 - 23,651,814). As at November 8, 2018, there were 23,745,727 common shares outstanding.

During Q3 2018, we issued 93,913 new common shares under the DRIP (Q3 2017 - 74,496), which provides MCAN with a reliable source of new capital and existing shareholders an opportunity to acquire additional shares at a discount to market value. Under the DRIP, dividends paid to shareholders are automatically reinvested in common shares issued out of treasury at the weighted average trading price for the five days preceding such issue less a discount of 2%.

For additional information related to share capital, refer to Note 16 to the consolidated financial statements.

OFF-BALANCE SHEET ARRANGEMENTS

We have contractual obligations relating to a premises lease, in addition to outstanding commitments for future fundings of corporate mortgages and our investment in the KSHYF. We are obligated to advance additional fundings on the investment at any time subject to capital calls by the KSHYF.

We outsource the majority of our mortgage servicing and continue to pay servicing expenses as long as the mortgages remain on our balance sheet.

Table 32: Contractual Obligations

(in thousands)	Less than one year	One to three years	Three to five years	Over five years	September 30 2018	June 30 2018
Mortgage funding commitments	\$ 239,857	\$ 178,554	\$ -	\$ -	\$ 418,411	\$ 400,610
Commitment - KSHYF	-	22,433	-	-	22,433	22,433
Premises lease	852	1,769	1,769	3,722	8,112	8,325
	\$ 240,709	\$ 202,756	\$ 1,769	\$ 3,722	\$ 448,956	\$ 431,368

We retain mortgage servicing obligations relating to securitized mortgages where balance sheet derecognition has been achieved. For further information, refer to Note 11 to the consolidated financial statements.

We provide letters of credit, which are not reflected on the consolidated balance sheet, for the purpose of supporting developer obligations to municipalities in conjunction with residential construction loans. For further information, refer to Note 24 to the consolidated financial statements.

As at September 30, 2018, our total single family mortgage renewal rights were \$952 million (June 30, 2018 - \$936 million).

MCAP is actively defending a claim arising from a power of sale process with respect to a defaulted land development loan previously funded by MCAN. The plaintiff has claimed improvident sale and has claimed damages of approximately \$6 million. MCAP was awarded a judgment for approximately \$500,000 against the same plaintiff in related proceedings. We may be subject to the indemnification of MCAP for certain liabilities that may be incurred as part of the proceedings under a mortgage servicing agreement between the two parties. Based on, among other things, the current status of the proceedings, we do not expect to incur any material liability arising out of this indemnification obligation to MCAP and accordingly have not recorded a provision. During Q3 2018, we reversed \$0.6 million of previously incurred and accrued legal expenses relating to this litigation after receiving confirmation of reimbursement subsequent to quarter end.

DIVIDENDS

On September 24, 2018, the Board declared a fourth quarter dividend of \$0.32 per share, to be paid on January 2, 2019 to shareholders of record as of December 14, 2018. Since this dividend was declared prior to September 30, 2018, it was accrued as a liability as at that date and deducted from shareholders' equity.

TRANSACTIONS WITH RELATED PARTIES

Related party transactions for the quarters ended September 30, 2018 and September 30, 2017 and related party balances as at September 30, 2018 are discussed in Note 22 to the consolidated financial statements.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

The majority of our consolidated balance sheet consists of financial instruments, and the majority of net income is derived from the related income, expenses, gains and losses. Financial instruments include cash and cash equivalents, cash held in trust, marketable securities, mortgages, non-marketable securities, other loans, financial liabilities from securitization, term deposits and loans payable, which are discussed throughout this MD&A.

The use of financial instruments exposes us to interest rate, credit, liquidity and market risk. A discussion of these risks and how these risks are managed is found in the "Risk Governance and Management" section of this MD&A.

Information on the financial statement classification and amounts of income, expenses, gains and losses associated with the instruments are located in the "Results from Operations" and "Financial Position" sections of this MD&A. Information on the determination of the fair value of financial instruments is located in the "Critical Accounting Estimates and Judgments" section of this MD&A.

PEOPLE

As at September 30, 2018, we had 78 employees (June 30, 2018 - 75).

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of the Company's financial statements requires management to make judgments, estimations and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. Estimates are considered carefully and reviewed at an appropriate level within MCAN. We believe that our estimates of the value of our assets and liabilities are appropriate. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Critical Accounting Estimates

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the consolidated financial statements cannot be derived from active markets, they are determined using a variety of valuation techniques that may include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, estimates are required to establish fair values. These estimates include considerations of liquidity and model inputs such as discount rates, prepayment rates and default rate assumptions for certain investments.

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 both under IFRS 9 and IAS 39 across all categories of financial assets 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; and
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs.

We review our ECL models on a quarterly basis. We continue to monitor asset performance and current economic conditions, focusing on any regionally specific issues to assess the adequacy of the current provisioning policies.

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the consolidated financial statements. To reflect this, we may make temporary qualitative adjustments or overlays using expert credit judgment when such differences are material.

Mortgage prepayment rates

In calculating the rate at which borrowers prepay their mortgages, the Company makes estimates based on its historical experience. These assumptions impact the timing of revenue recognition and the amortization of mortgage premiums using the EIM.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws and the amount and timing of future taxable income in the subsidiaries of the Company. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to the tax treatment of income and expenses already recorded in the subsidiaries of the Company.

The Company establishes provisions, based on reasonable estimates, for possible consequences of audits by relevant tax authorities. The amount of such provisions is based on various factors, such as experience of previous tax audits and interpretations of tax regulations by the responsible tax authority. As the Company assesses the probability of litigation and subsequent cash outflow with respect to taxes as remote, no contingent liability has been recognized.

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable income will be available against which the losses can be used in the subsidiaries of the Company. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized in the subsidiaries of the Company, based upon the likely timing and the level of future taxable income together with future tax planning strategies.

Impairment of financial assets

As applicable, the Company reviews financial assets at each consolidated financial statement date to assess whether an impairment loss should be recorded. In particular, estimates by management are required in the calculation of the amount and timing of future cash flows associated with these assets when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the fair value of the asset.

Critical Accounting Judgments

Going concern

The Company's management has made an assessment of the Company's ability to continue as a going concern and is satisfied that the Company has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Company's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on the going concern basis.

Significant influence

In determining whether it has significant influence over an entity, the Company makes certain judgments based on the applicable accounting standards. These judgments form the basis for the Company's policies in accounting for its equity investments.

Taxes

As a MIC under the Tax Act, the Company is able to deduct from income for tax purposes dividends paid within 90 days of year-end. The Company intends to maintain its status as a MIC and intends to pay sufficient dividends in current and future years to ensure that it is not subject to income taxes in the MIC entity on a non-consolidated basis. Accordingly, the Company does not record a provision for current and deferred taxes within the MIC entity; however provisions are recorded as applicable in all subsidiaries of MCAN.

STANDARDS ISSUED BUT NOT YET EFFECTIVE

Standards issued but not yet effective include IFRS 16, *Leases*, IFRS 2, *Share-based Payment Transactions* and IFRIC 23, *Uncertainty over Income Tax Treatments*. For further information on these standards, refer to Note 4 to the consolidated financial statements.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

As at September 30, 2018, the Interim Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") of MCAN, along with the assistance of the Company's Disclosure Committee comprised of members of senior management, have designed disclosure controls and procedures to provide reasonable assurance that (i) material information relating to MCAN is made known to the CEO and CFO and (ii) information required to be disclosed by us in reports we file or submit is recorded, processed, summarized and reported within the time periods specified in securities legislation, and have designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS.

There were no changes in our internal controls over financial reporting that occurred during the interim period ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

We adopted IFRS 9 effective January 1, 2018 and have updated and modified certain internal controls over financial reporting as a result of the new accounting standard.

All internal control systems, no matter how well designed, have inherent limitations. As a result, even systems determined to be effective may not prevent or detect misstatements on a timely basis, as systems can provide only reasonable assurance that the objectives of the control system are met. In addition, projections of any evaluation of the effectiveness of ICFR to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may change.

Notice required under National Instrument 51-102, “Continuous Disclosure Obligations,” Part 4.3 (3) (a).

The accompanying consolidated interim financial statements of MCAN have not been reviewed by an auditor.

The Company is in compliance with the interim Management’s Discussion and Analysis of Operations requirements set out by National Instrument 51-102.

SUBSEQUENT EVENTS

On October 9, 2018, we announced the departure of William Jandrisits as President, CEO and Director of MCAN. Karen Weaver, a Director of MCAN since November, 2011, Chair of the Audit Committee, was appointed as Interim CEO of MCAN. Subsequent to quarter end, we incurred \$490,000 of severance costs.

On October 19, 2018, we announced the departure of Jeff Bouganim, MCAN’s CFO. Ms. Dipti Patel, MCAN’s Vice President, Operational Effectiveness, will replace Mr. Bouganim as MCAN’s new CFO effective November 9, 2018.

NON IFRS MEASURES

We prepare our consolidated financial statements in accordance with IFRS. We use a number of financial measures to assess our performance. Some of these measures are not calculated in accordance with IFRS, are not defined by IFRS, and do not have standardized meanings that would ensure consistency and comparability between companies using these measures. The non-IFRS measures used in this MD&A are defined as follows:

Return on Average Shareholders' Equity

Return on average shareholders' equity is a profitability measure that presents the annualized net income available to shareholders as a percentage of the capital deployed to earn the income. We calculate return on average shareholders' equity as a monthly average using all components of shareholders' equity.

Taxable Income Measures

Taxable Income Measures include taxable income and taxable income per share. Taxable income represents MCAN's net income on a non-consolidated basis calculated under the provisions of the Tax Act applicable to a MIC. Taxable income is calculated as an estimate until we complete our annual tax returns subsequent to year end, at which point it is finalized.

Average Interest Rate

The average interest rate is a profitability measure that presents the average annualized yield of an asset or liability. Average mortgage portfolio yield (corporate or securitized), term deposit average interest rate, financial liabilities from securitization average interest rate, spread of mortgages over term deposits and spread of securitized assets over liabilities are examples of average interest rates. The average asset/liability balance that is incorporated into the average interest rate calculation is calculated on either a daily or monthly basis depending on the nature of the asset/liability. Please refer to the applicable tables containing average balances for further details.

Net Interest Income

Net interest income is a profitability measure that reflects net interest income earned only from interest-bearing assets and liabilities.

Impaired Mortgage Ratios

The impaired mortgage ratios represent the ratio of impaired uninsured mortgages to both corporate and total (corporate and securitized) mortgage principal.

Mortgage Arrears

Mortgage arrears measures include total corporate mortgage arrears, total securitized mortgage arrears and total mortgage arrears. These measures represent the amount of mortgages from the corporate portfolio, securitized portfolio and the sum of the two, respectively, that are at least one day past due.

Common Equity Tier 1, Tier 1 and Total Capital, Total Exposures, Regulatory Assets, Leverage Ratio, Assets to Capital Multiple and Risk Weighted Assets

These measures provided in this MD&A are in accordance with guidelines issued by OSFI and are located on Table 28 of this MD&A and Note 26 to the consolidated financial statements.

Tier 1, Tier 2, Tier 3 and Total Liquid Assets and Liquidity Ratios

Tier 1, Tier 2, Tier 3 and Total Liquid Assets are internal metrics that quantify the balance sheet assets (or components of assets) that comprise various liquidity levels. Liquidity ratios represent the ratio of select tiers of liquid assets to term deposits maturing within 100 days.

Income Tax Capital Measures

Income tax assets, income tax liabilities and income tax capital represent assets, liabilities and capital as calculated on a non-consolidated basis using the provisions of the Tax Act applicable to a MIC. The calculation of the income tax assets to capital ratio and income tax liabilities to capital ratio are based on these amounts. Income tax asset capacity represents additional income tax asset growth available to yield a 5.75 income tax assets to capital ratio, which is our target ratio.

Market Capitalization

Market capitalization is calculated as the number of common shares outstanding multiplied by the closing common share price as of that date.

Book Value per Common Share

Book value per common share is calculated as total shareholders' equity divided by the number of common shares outstanding.

Limited Partner's At-Risk Amount

The value of our equity investment in MCAP for income tax purposes is referred to as the Limited Partner's At-Risk Amount ("LP ARA"), which represents the cost base of the limited partner's investment in the partnership. The LP ARA is increased (decreased) by the partner's share of partnership income (loss) on a tax basis, increased by the amount of capital contributions into the partnership and reduced by distributions received from the partnership.