

CANADA MORTGAGE AND HOUSING CORPORATION

Quarterly Financial Report

THIRD QUARTER
September 30, 2018
(Unaudited)

Table of Contents

| | |
|--|-----------|
| MANAGEMENT’S DISCUSSION AND ANALYSIS | 3 |
| OVERVIEW..... | 3 |
| THE OPERATING ENVIRONMENT AND OUTLOOK FOR 2018 | 4 |
| CONDENSED CONSOLIDATED FINANCIAL RESULTS | 7 |
| FINANCIAL RESULTS BY REPORTABLE BUSINESS SEGMENT | 9 |
| ASSISTED HOUSING..... | 9 |
| MORTGAGE LOAN INSURANCE..... | 11 |
| SECURITIZATION | 16 |
| RISK MANAGEMENT | 18 |
| HISTORICAL QUARTERLY INFORMATION | 19 |
| UNAUDITED QUARTERLY CONSOLIDATED FINANCIAL STATEMENTS | 20 |



Management's Discussion and Analysis

OVERVIEW

The following Management's Discussion and Analysis (MD&A) of the financial condition and results of operations as approved by the Audit Committee on 27 November 2018 is prepared for the third quarter ended 30 September 2018 and is intended to provide readers with an overview of our performance including comparatives against the same three and nine month period in 2017. The MD&A includes explanations of significant deviations in actual financial results from the targets outlined in the Corporate Plan Summary that may impact the current and future quarters of our fiscal year. This MD&A should be read in conjunction with the unaudited quarterly consolidated financial statements as well as the 2017 Annual Report. The unaudited quarterly consolidated financial statements have been prepared in accordance with International Accounting Standard 34 Interim Financial Reporting (IAS 34) and do not include all of the information required for full annual consolidated financial statements. The unaudited quarterly consolidated financial statements have been reviewed by Ernst & Young LLP. All amounts are expressed in millions of Canadian dollars, unless otherwise stated.

Information related to our significant accounting policies, judgments and estimates can be found in our 2017 Annual Report. Except for the adoption of International Financial Reporting Standards (IFRS) 9 and IFRS 15, as disclosed in note 3 of our unaudited quarterly financial statements there have been no material changes to our significant accounting policies, judgments or estimates to the end of the third quarter of 2018.

Forward-looking statements

Our Quarterly Financial Report (QFR) contains forward-looking statements including, but not limited to, statements made in the "The Operating Environment and Outlook for 2018", and "Financial Results by Reportable Business Segment" sections of the report. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties which may cause actual results to differ materially from expectations expressed in these forward-looking statements.

Non-IFRS measures

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 with other institutions. These non-IFRS measures are presented to supplement the information disclosed in the unaudited quarterly consolidated financial statements which are prepared in accordance with IFRS and may be useful in analyzing performance and understanding the measures used by management in its financial and operational decision making. Definitions of the non-IFRS measures used throughout the quarterly financial report can be found in the Glossary for Non-IFRS Financial Measures section of the 2017 Annual Report.



THE OPERATING ENVIRONMENT AND OUTLOOK FOR 2018

The following events can be expected to have an impact on our business going forward:

Economic conditions and housing indicators

In spite of an uncertain operating environment, the outlook for economic growth in Canada is roughly unchanged from July, with a moderate pace of expansion expected. On an average annual basis, real GDP is projected to grow by 2% in 2018 and 1.9% in 2019¹, with the economy operating close to its potential rate.

The strength of the Canadian economy continues to be underpinned by domestic demand. Following a softer start to the year, consumer spending rebounded in the second quarter and should remain a key driver of economic activity, although not to the same extent as in recent years. Its contribution to growth is supported by still-tight labour markets reflecting both employment and wage gains.

Exports have been the other main factor behind Canada's economic performance. During the NAFTA negotiations, a relatively resilient export sector was expected to hold up well over the near term, broadly in line with a stronger U.S. economy, our largest trading partner. Now with the NAFTA replacement deal, a backdrop of reduced uncertainty should further support trade growth. Coupled with higher levels of capacity utilization and stronger business confidence, these trends would also help stimulate businesses investment.

Meanwhile, the current economic environment suggests that interest rates are expected to continue to rise. Additional rate increases could put upward pressure on debt service costs, implying that an increasing share of household income would be required to service higher debt repayments. Overall, Canada's mortgage debt service ratio rose to 6.5% in the second quarter of 2018, up from 6.3% in its equivalent year-earlier period.

Although debt levels remain elevated, these trends are expected to curb borrowing activity, while also reducing dependence on debt to fuel economic growth in Canada. Even though labour market conditions continue to spur a pickup in wages, these gains are not expected to offset the hit to disposable income from higher debt service. All told, household spending growth is projected to ease from 3.5% last year to a pace closer to the 2% range in 2018.

After years of strong activity, the national housing market started to show signs of cooling during the first half of the year. Taken together—tighter mortgage rules, rising interest rates and a slowing economy—are expected to underpin reduced demand for housing, resulting in slower price growth over the near term.

All this put Canada's average MLS® price at \$452,233 during the first eight months of 2018, just below its 2016 level when price growth hit a twenty-year high of nearly 13%. This represents a drop of 3.7% from the same period a year earlier, marking the first decline in home prices since the 2009 recession. Meanwhile, MLS® sales activity also moderated, dropping 11.7% to 327,206 units. Still, national housing starts were virtually unchanged over the period, at about 144,644 units.

National Housing Strategy

In Q3, Canada Mortgage and Housing Corporation continued delivery of National Housing Strategy (NHS) initiatives that launched earlier in the year and continued the in-take of funding applications. In this quarter specifically, we also launched the Collaborative Housing Research Network (jointly with the Social Sciences and Humanities Research Council of Canada) and the CMHC Housing Scholarship Program (in collaboration with Tri-Agency) to build research capacity in the housing and academic sectors. The Federal Lands Initiative was also launched to make surplus federal lands and buildings available for affordable housing. Financial authorities for these federal NHS initiatives, and for provincially and territorially delivered initiatives, were obtained through Treasury Board in Q2.

¹ Consensus Economics survey of private sector forecasters, as of September 2018.



We continued bilateral negotiations with provinces and territories in Q3 for new agreements that will be effective 1 April 2019, securing an agreement with New Brunswick on 5 July 2018. We also continued discussions with provinces and territories to co-develop the Canada Housing Benefit, set to launch on 1 April 2020. Additionally, following public consultations that concluded in Q2, we are developing recommendations towards the Human-Rights Based Approach to Housing and a *What We Heard* report is expected to be released in Q4. Finally, planning continued for the first National Housing Conference held on 21-22 November 2018.

Office of the Superintendent of Financial Institutions (OSFI) guidelines

Changes to capital requirements for Mortgage Insurers

On 9 August 2018, OSFI issued the Mortgage Insurer Capital Adequacy Test (MICAT) guideline that combines the 1 January 2017 advisory on Capital Requirements for Federally Regulated Mortgage Insurers and the relevant portions of the 2018 Minimum Capital Test for Federally Regulated Property and Casualty Insurance Companies. The MICAT has an effective date of 1 January 2019.

With this new guideline OSFI simplified the calculation of insurance risk, streamlined the requirements for single-family residential mortgages, included accommodations for IFRS 16 - Leases, and specified credit risk factors for securitized assets.

Changes in the MICAT framework predominately relate to streamlining the requirements for single-family residential mortgages as follows:

- Base total asset requirements will require the mortgage insurer to use the borrower's credit score at origination and remove the use of updated credit scores, and;
- Increases of the base total asset requirements uniformly by 5%, with a corresponding 1% increase in operational risk, to allow for deterioration in borrower credit scores after origination.

CMHC expects its capital required to decrease on transition and to increase over the planning horizon as new business is written.

Updates on future changes to accounting standards

Information relating to all standards issued by the International Accounting Standards Board (IASB) affecting the Corporation can be found in note 2 of our 2017 audited consolidated financial statements.

IFRS 16 Leases – effective date of 1 January 2019

IFRS 16 *Leases* replaces IAS 17 *Leases* and related interpretations and provides greater transparency about leverage, the assets an entity uses in its operations, and the risks to which it is exposed from entering into lease transactions.

Under IFRS 16, the core principle is that a lessee recognizes assets and liabilities for the rights and obligations created by all leases where the term of the lease is greater than 12 months, unless the underlying asset is of low value. A lessee would recognize a liability to make lease payments and a right-of-use asset representing its right to use the leased asset for the lease term. Depreciation of the leased assets is recognized separately from interest on lease liabilities in the statement of income. The accounting requirements for lessors are substantially unchanged.

We have completed our preliminary detailed assessment of the impact of adopting IFRS 16. The primary impact to the Corporation is that right-of-use assets and lease liabilities will be recognized for its leases of office space, which are currently accounted for as operating leases under IAS 17. We intend to apply the standard using the modified retrospective approach. Based on the current facts and circumstances, we expect to recognize right-of-use assets and lease liabilities totaling approximately \$70 million upon transition, with no adjustment to equity. In addition, straight-line operating lease expenses will be replaced by depreciation on right-of-use assets and interest on lease liabilities, but this impact will be significantly smaller. The final quantitative impact will depend on future economic conditions, including the Corporation's borrowing rate at 1 January 2019 and our updated assessment of whether various renewal and early termination options will be exercised.



OSFI Advisory on IFRS 17 Insurance contracts

On 4 May 2018, OSFI issued an Advisory entitled IFRS 17 Transition and Progress Report Requirements for Federally Regulated Insurers (IFRS 17 Advisory). The IFRS 17 Advisory removes an insurer's option to early adopt IFRS 17, establishes a requirement for semi-annual progress reporting to OSFI and requires the use of IFRS 17 for financial guarantee contracts, where the insurer, if applicable, would have had the option to account for its insurance contracts under IFRS 17 or IFRS 9.

IFRS 17 Insurance Contracts – effective date of 1 January 2021

In May 2017, the IASB issued IFRS 17 Insurance Contracts (IFRS 17), which will replace IFRS 4 Insurance Contracts. Our insurance contracts meet the definition of financial guarantee contracts under IFRS 9 Financial Instruments and as insurance contracts under IFRS 17, but as discussed above, we will be required to apply IFRS 17 and believe it is the appropriate accounting standard for our insurance contracts.

Under IFRS 17, insurance contract liabilities will include the present value of future insurance cash flows adjusted for risk as well as contractual service margin. Contractual service margin will represent the difference between the present value of the risk adjusted cash flows and the premium received at inception and will be released over the coverage period. Should the difference between the premium received and the present value of future cash outflows be negative at inception, the insurance contract would be considered onerous and the difference would be recorded immediately in income. There will also be a new income statement presentation for insurance contracts and additional disclosure requirements.

We have a multi-disciplinary team dedicated to analyzing and implementing the new accounting standard, and a detailed project plan is in place. We are currently evaluating the standard and identifying where changes to our existing accounting and reporting processes will be required, and the potential impact on our consolidated financial statements.

Changes to the presentation of parliamentary appropriations and housing program expenses

In accordance with Treasury Board's *Policy on Results*, starting 1 April 2018, CMHC is required to report appropriated funds following the Departmental Results Framework (DRF). The DRF is the structure against which resources and performance information are reported to Parliament and Canadians. A DRF describes, at a high level, the domains in which an organisation acts, the changes it seeks to contribute to, and how it will assess progress. CMHC's activities are presented into the following three core responsibilities.

Assistance for housing needs: encompasses programs where CMHC provides federal funding to improve access to affordable housing for Canadians in housing need, including Indigenous peoples, Canadians with special or distinct needs, and certain vulnerable groups.

Financing for housing: encompasses programs whereby CMHC makes financing available for new and existing housing-related initiatives.

Housing expertise and capacity development: encompasses a variety of programs whereby CMHC supports capacity and skills development activities within the housing sector and conducts research and analysis as well as disseminates information on a range of issues that support the housing sector and informed decision making by government and other sectors.

CONDENSED CONSOLIDATED FINANCIAL RESULTS

Condensed consolidated balance sheets

| <i>(in millions)</i> | As at | |
|------------------------|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Total assets | 272,513 | 267,115 |
| Total liabilities | 256,839 | 249,374 |
| Total equity of Canada | 15,674 | 17,741 |

Our total equity of Canada decreased by \$2,067 million (11.7%) primarily as a result of the declaration of \$3,000 million in dividends partially offset by comprehensive income of \$988 million during the period.

An increase in our total assets of \$5,398 million (2.0%) was driven by an increase of \$8,695 million (3.7%) in loans at amortized cost, mainly due to the issuance of Canada Mortgage Bonds (CMB), offset by a decrease in our investment balances as we paid \$4,500 million of dividends.

Total liabilities increased by \$7,465 million (3.0%) mainly due to a \$9,260 million (4.0%) increase in borrowings at amortized cost in line with the increases in our loans at amortized costs, the declaration of \$3,000 million in dividends, offset by the payments of \$4,500 million of dividends referred to above.

Condensed consolidated statements of income and comprehensive income

| <i>(in millions)</i> | Three months ended 30 September | | Nine months ended 30 September | |
|-----------------------------------|---------------------------------|-------|--------------------------------|-------|
| | 2018 | 2017 | 2018 | 2017 |
| Total revenues | 1,049 | 1,266 | 3,776 | 4,722 |
| Total expenses | 536 | 648 | 2,363 | 3,089 |
| Income taxes | 126 | 151 | 345 | 399 |
| Net income | 387 | 467 | 1,068 | 1,234 |
| Other comprehensive income (loss) | (23) | (118) | (80) | (277) |
| Comprehensive income | 364 | 349 | 988 | 957 |

Q3 2018 vs. Q3 2017

Total revenues decreased by \$217 million (17.1%) from the same quarter last year mainly due to decreases in parliamentary appropriations for housing programs, investment income, premiums and fees earned and net gains (losses) on financial instruments.

- Parliamentary appropriations for housing programs decreased by \$105 million (20.2%) primarily due to decline in Budget 2016 expenditures.
- Investment income decreased by \$19 million (13.1%) mainly as a result of a decrease in average portfolio size as a result of dividend payments to the Government of Canada.
- Premiums and fees earned decreased by \$13 million (2.6%) because of lower volumes and the slowing down of recognition of revenue based on recent claims occurrence experience in our Mortgage Loan Insurance Activity. This was partially offset by higher National Housing Act Mortgage Backed Securities (NHA MBS) guarantee fees earned following the pricing policy changes which came into effect on 1 July 2016 in the Securitization Activity.
- Net gains (losses) on financial instruments decreased by \$74 million (113.8%) mainly as a result of negative fair market value fluctuations in Q1 2018 on common equities and higher loss on sales of fixed income security due to increasing interest rates. Fair value fluctuations on our common equities now flow through profit and loss following the implementation of IFRS 9 Financial Instruments: Recognition and Measurement. In the prior year, unrealized gains and losses on common equities flowed through other comprehensive income (OCI).



Total expenses decreased by \$112 million (17.3%) from the same quarter last year mainly due to a decrease in Housing program expenses of \$105 million (20.2%) in accordance with the decline in parliamentary appropriations for housing and a decrease in insurance claims of \$6 million (14.6%) primarily due to lower incurred claims as a result of continued low areas and unemployment rate at a national level.

YTD 2018 vs. YTD 2017

Total revenues decreased by \$946 million (20.0%) from the same nine month period last year due to decreases in parliamentary appropriations for housing programs, investment income, premiums and fees earned and net gains (losses) on financial instruments as described above

Total expenses decreased by \$726 million (23.5%) from the same nine month period last year primarily due to a decrease in Housing program expenses and a decrease in operating expenses.



FINANCIAL RESULTS BY REPORTABLE BUSINESS SEGMENT

Financial analysis is provided for the following activities: Assisted Housing, Mortgage Loan Insurance and Securitization.

ASSISTED HOUSING

We provide federal funding in support of housing programs for Canadians in need, including on-reserve. Our activities also include Lending programs for social housing. The ultimate outcome of our activities is to help Canadians in need have access to affordable and suitable housing.

Financial analysis

| <i>(in millions)</i> | Three months ended | | Nine months ended | |
|---|----------------------|----------------------|----------------------|----------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Net interest income | 2 | 4 | 10 | 8 |
| Parliamentary appropriations for housing programs | 416 | 521 | 1,905 | 2,635 |
| Other income ¹ | 13 | 4 | 18 | 17 |
| Total revenues | 431 | 529 | 1,933 | 2,660 |
| Housing programs expenses | 416 | 521 | 1,905 | 2,635 |
| Operating expenses | 4 | 5 | 17 | 19 |
| Total expenses | 420 | 526 | 1,922 | 2,654 |
| Income (loss) before income taxes | 11 | 3 | 11 | 6 |
| Income taxes | 1 | (1) | (2) | (3) |
| Net income (loss) | 10 | 4 | 13 | 9 |

¹ Other income includes net gains (losses) on financial instruments and other income.

Q3 2018 vs. Q3 2017

Total expenses decreased by \$106 million (20.2%) from the same quarter last year due to a decrease in housing program expenses. This expenditure decrease is primarily driven by the expiry of Budget 2016 initiatives, fewer expenses claimed in the first nine months related to the Prepayment Flexibility initiative, advances to provinces for Investment in Affordable Housing (IAH) and transactions for Non-Profit housing. This decrease in expenses is partially offset by an increase in administrative expenses resulting from the launch of National Housing Strategy programing.

Total revenues decreased by \$98 million (18.5%) primarily due to a decrease in housing programs expenses as explained above.

YTD 2018 vs. YTD 2017

Total expenses decreased by \$732 million (27.6%) from the same nine month period last year primarily due to fewer expenses claimed for the delivery of the Innovation Fund and the expiry of the majority of Budget 2016 programs starting Q2 2018.

Total revenues decreased by \$727 million (27.3%) primarily driven by a decrease in housing programs expenses as explained above.

Financial condition

| | As at | |
|------------------------|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Total assets | 9,185 | 9,949 |
| Total liabilities | 8,875 | 9,715 |
| Total equity of Canada | 310 | 234 |



Total assets and liabilities have decreased by \$764 million (7.7%) and \$840 million (8.6%), respectively, primarily due to the net repayments on our current Lending programs. Proceeds received from repayments and our investment activities were used primarily to repay matured Government Borrowings leading also to a decrease in liabilities.

Capital management

We maintain a reserve fund pursuant to Section 29 of the CMHC Act. A portion of the Lending program's earnings are retained in this reserve fund as part of our strategy to address interest rate and credit risk exposure on our loans. Unrealized fair value market fluctuations as well as remeasurement losses on defined benefit plans are absorbed in retained earnings.

We do not hold capital² for Housing programs, as this activity does not present risks to the Corporation that would require capital to be set aside.

Refer to the unaudited quarterly consolidated financial statements Note 9 – Capital Management for complete disclosure on capital management.

Reporting on use of appropriations

The following table reconciles the amount of appropriations authorized by Parliament as available to us during the Government fiscal year (31 March) with the total amount recognized by us in our calendar year.

| <i>(in millions)</i> | Nine months ended 30 September | |
|---|--------------------------------|--------------|
| | 2018 | 2017 |
| Amounts provided for housing programs: | | |
| Amounts authorized in 2017/18 (2016/17) | | |
| Main estimates | 2,735 | 2,028 |
| Supplementary estimates A ^{1,2} | 41 | 1,070 |
| Supplementary estimates B ^{1,2,3} | 1 | 78 |
| Supplementary estimates C ^{1,3} | 1 | - |
| Less: Portion recognized in calendar 2017 (2016) | (1,663) | (1,563) |
| Less: Appropriations lapsed for 2017/18 (2016/17) ^{4,5} | (89) | (47) |
| 2017/18 (2016/17) portions recognized in 2018 (2017) | 1,026 | 1,566 |
| Amounts authorized in 2018/19 (2017/18) | | |
| Main estimates | 2,427 | 2,735 |
| Supplementary estimates A ^{1,2} | - | 41 |
| Supplementary estimates B ^{1,3} | - | 1 |
| Supplementary estimates C ^{1,3} | - | 1 |
| Total fiscal year appropriations | 2,427 | 2,778 |
| Less: Portion to be recognized in subsequent quarters | (1,548) | (1,709) |
| 2018/19 (2017/18) portions recognized in 2018 (2017) | 879 | 1,069 |
| Total appropriations recognized – nine months ended 30 September | 1,905 | 2,635 |

¹ Supplementary estimates are additional appropriations voted on by Parliament during the Government's fiscal year.

² Budget 2016 provided funding over two years for investments in social infrastructure, as well as funding over five years for a new Affordable Rental Housing Innovation Fund. Years one and two of these investments are reflected within the 2016-17 and 2017-18 appropriations.

³ Transfers received in 2017/18 from other government departments as a result of in-year reallocation of resources related to the Youth Employment Strategy. This additional funding will be used to support the Housing Internship Initiative for First Nations and Inuit Youth program.

⁴ Included in our appropriations lapsed for fiscal year 2016/17 of \$47 million is a frozen allotment in the amount of \$35 million to reflect the transfer of delivery of the Inuit Housing Funding from CMHC to Indigenous and Northern Affairs Canada. When netted against this frozen allotment, CMHC's lapse was \$12 million.

⁵ Included in our appropriations lapsed for fiscal year 2017/18 of \$89 million is frozen funding in the amount of \$15 million to reflect the reduction in CMHC's authorities due to the expiry of long-term operating agreements for existing social housing programs and the reprofiling of funding under the Investment in Affordable Housing program to fiscal year 2019/2020. When netted against this frozen funding, CMHC's lapse is \$74 million.

² References to "capital" in this QFR are to the accounting term, and are not limited to "capital" as provided for in the CMHC Act, National Housing Act and Financial Administration Act.

Total appropriations approved by Parliament for fiscal year 2018/19 are \$2,427 million. The total spending against the reference level as at 30 September, 2018, was \$879 million (36.2%).

MORTGAGE LOAN INSURANCE

We provide mortgage loan insurance for transactional homeowner, portfolio and multi-unit residential units in all parts of Canada. We operate these programs on a commercial basis. Revenues from premiums, fees and investments cover all expenses, including insurance claim losses, and we are expected to generate a reasonable return for the Government with due regard for loss.

Our mortgage loan insurance business is exposed to some seasonal variation. While premiums earned and net gains (losses) on financial instruments vary from quarter to quarter as underlying balances change, premiums received for some insurance products vary each quarter because of seasonality in housing markets. Variations are driven by the level of mortgage originations and related mortgage policies written, which for purchase transactions typically peak in the spring and summer months. Losses on claims vary from quarter to quarter primarily as the result of prevailing economic conditions as well as the characteristics of the insurance-in-force portfolio, such as size and age.

Financial metrics

| <i>(in billions)</i> | As at | |
|---------------------------|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Insurance-in-force | 453 | 480 |
| Transactional homeowner | 240 | 249 |
| Portfolio | 141 | 162 |
| Multi-unit residential | 72 | 69 |

Under Section 11 of the National Housing Act (NHA), the total of outstanding insured amounts of all insured loans may not exceed \$600 billion (2017 – \$600 billion). At 30 September 2018, insurance-in-force was \$453 billion, a \$27 billion (5.6%) decrease from 31 December 2017. New loans insured were \$36 billion, while estimated loan amortization and pay-downs were \$63 billion.

| <i>(in millions, unless otherwise indicated)</i> | Three months ended | | Nine months ended | |
|--|--------------------|-------------------|-------------------|-------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Total insured volumes (units) | 65,679 | 67,915 | 186,525 | 211,891 |
| Transactional homeowner | 30,481 | 32,942 | 80,479 | 88,402 |
| Portfolio ¹ | 6,980 | 5,765 | 28,943 | 35,741 |
| Multi-unit residential | 28,218 | 29,208 | 77,103 | 87,748 |
| Total insured volumes (\$) | 13,305 | 12,539 | 35,575 | 38,187 |
| Transactional homeowner | 8,244 | 8,893 | 21,153 | 23,036 |
| Portfolio ¹ | 1,674 | 987 | 5,536 | 7,087 |
| Multi-unit residential | 3,387 | 2,659 | 8,886 | 8,064 |
| Premiums and fees received² | 409 | 414 | 1,065 | 1,085 |
| Transactional homeowner | 290 | 309 | 745 | 768 |
| Portfolio | 6 | 7 | 15 | 45 |
| Multi-unit residential | 113 | 98 | 305 | 272 |
| Claims Paid³ | 60 | 74 | 182 | 245 |
| Transactional homeowner | 54 | 61 | 164 | 195 |
| Portfolio | 5 | 4 | 13 | 12 |
| Multi-unit residential | 1 | 9 | 5 | 38 |
| Arrears rate (%) | 0.29 | 0.30 | 0.29 | 0.30 |

¹ Portfolio volumes include Lender substitutions along with new business volumes. Portfolio substitutions were 1,172 units and \$162 million and 15,352 units and \$2,106 million for the three and nine months ended 30 September 2018 (4,022 units and \$485 million and 22,517 units and \$3,831 million for the three and nine months ended 30 September 2017)

² Premiums and fees received may not equal premiums and fees deferred on contracts written during the period due to timing of receipts.

³ Claims paid does not include social housing and index-linked mortgage claims.

Q3 2018 vs. Q3 2017

Our total insured volumes in the third quarter of 2018 were 2,236 units (3.3%) lower than the same quarter last year primarily due to decreases in transactional homeowner and multi-unit residential volumes.

- Transactional homeowner volumes decreased by 2,461 units (7.5%) largely due to Government and OSFI regulations that have decreased the size of the insured market.
- Portfolio volumes (new and substitutions) increased by 1,215 units (21.1%) mainly due to some significant portfolio approvals partially offset by a decrease in portfolio substitution driven by lower eligible volumes.
- Multi-unit residential volumes decreased by 990 units (3.4%) primarily due to a decrease in refinance volumes partially driven by higher interest rates and lower new construction in Quebec, partially offset by increased purchases in Ontario and the Atlantic regions. Although the unit volumes are decreasing, we are experiencing higher volumes of insured dollars as there have been higher unit prices insured.

Premiums and fees received decreased by \$5 million (1.2%) from the same quarter last year primarily due to lower transactional homeowner insurance volumes partially offset by higher multi-unit insured dollars driven by higher loan amounts as previously stated.

Claims paid decreased by \$14 million (18.9%) attributable to lower reported claims in Ontario, Atlantic and Quebec regions, a lower number of policies in force and sustained low arrears and unemployment rates at a national level.

YTD 2018 vs. YTD 2017

Our total insured volumes in the first nine months of 2018 were 25,366 units (12.0%) lower than the same nine month period last year due to decreases in all product volumes.

- Transactional homeowner volumes decreased by 7,923 units (9.0%), and multi-unit residential volumes decreased by 10,645 units (12.1%) for the same reasons noted above.
- Portfolio volumes (new and substitutions) decreased by 6,798 units (19.0%) due to a decrease in portfolio substitution driven by lower eligible volumes.

Premiums and fees received decreased by \$20 million (1.8%) from the same nine month period last year due to lower premiums and fees received for transactional homeowner and portfolio products caused by lower volumes and changing customers behaviours driven by recent price adjustment from regulatory requirements. This was partially offset by an increase in multi-unit products driven by higher dollar volumes.

Claims paid decreased by \$63 million (25.7%) from the same nine month period last year for the same reasons noted above.

| | As at | | | |
|-------------------------|----------------------------|-----------------|----------------------------|-----------------|
| | 30 September 2018 | | 31 December 2017 | |
| | No. of Delinquent Loans | Arrears Rate | No. of Delinquent Loans | Arrears Rate |
| Transactional homeowner | 5,087 | 0.42% | 5,376 | 0.43 % |
| Portfolio | 1,327 | 0.13% | 1,362 | 0.13 % |
| Multi-unit residential | 83 | 0.35% | 106 | 0.48 % |
| Total | 6,497 | 0.29% | 6,844 | 0.29 % |

Our arrears rate is calculated on the basis of all loans that are more than 90 days past due over the number of outstanding insured loans.

Our overall arrears rate and total number of delinquent loans as at 30 September 2018 has decreased mainly due to a decrease in the number of transactional homeowner delinquent loans in the Quebec and Alberta.

Financial analysis

| <i>(in millions)</i> | Three months ended | | Nine months ended | |
|-----------------------------------|----------------------|----------------------|----------------------|----------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Premiums and fees earned | 358 | 394 | 1,070 | 1,167 |
| Investment income | 130 | 153 | 405 | 457 |
| Other income ¹ | (9) | 69 | (47) | 89 |
| Total revenues | 479 | 616 | 1,428 | 1,713 |
| Insurance claims | 35 | 41 | 172 | 169 |
| Operating expenses | 67 | 69 | 227 | 228 |
| Total expenses | 102 | 110 | 399 | 397 |
| Income before income taxes | 377 | 506 | 1,029 | 1,316 |
| Income taxes | 94 | 124 | 254 | 324 |
| Net income | 283 | 382 | 775 | 992 |

¹ Other income includes net gains (losses) on financial instruments and other income.

Q3 2018 vs. Q3 2017

Premiums and fees earned decreased by \$36 million (9.1%) due to lower homeowner and portfolio insurance volumes in recent years and revised expectations of claim occurrence based on recent experience slowing down the rate at which revenue is recognized on certain products.

Investment income decreased by \$23 million (15.0%) primarily as a result of a decrease in average portfolio size as a result of dividend payments to the Government of Canada.

Other income decreased by \$78 million (113.0%) primarily due to an increase in losses on financial instruments resulting from weaker market performance of our equities.

Insurance claims decreased by \$6 million (14.6%) primarily due to continued low arrears and unemployment rate at a national level.

YTD 2018 vs. YTD 2017

Premiums and fees earned and investment income decreased by \$97 million (8.3%) and \$52 million (11.4%) respectively from the same nine month period last year due for the same reasons noted above.

Other income decreased by \$136 million (152.8%) primarily due to an increase in losses on financial instruments mainly due to weaker market performance of equities.

Insurance claims increased slightly by \$3 million (1.8%) from the same nine month period last year and remains low due to continuing low arrears and unemployment rates nationally.

Ratios

To supplement financial results of the Mortgage Loan Insurance Activity, we also use financial measures and ratios to analyze our financial performance.

| <i>(in percentages)</i> | Three months ended | | Nine months ended | |
|--|--------------------|--------------|-------------------|--------------|
| | 30 September | 30 September | 30 September | 30 September |
| | 2018 | 2017 | 2018 | 2017 |
| Severity ratio | 32.1 | 30.3 | 31.4 | 31.4 |
| Loss ratio ¹ | 9.8 | 10.4 | 16.1 | 14.5 |
| Operating expense ratio | 18.7 | 17.5 | 21.2 | 19.5 |
| Combined ratio | 28.5 | 27.9 | 37.3 | 34.0 |
| Return on equity | 8.8 | 10.1 | 7.3 | 7.8 |
| Return on required equity ² | 9.1 | 10.2 | 8.2 | 8.6 |

¹ Loss ratio on transactional homeowner and portfolio products excluding multi-unit residential was 17.6% and 20.5% for the three and nine months ended 30 September 2018 (14.7% and 16.1% for the three and nine months ended 30 September 2017)

² Return on required equity is calculated as the annualized net income, adjusted to remove investment income earned on equity in excess of required equity, divided by the average required equity for the period. Required equity is determined at our operating MCT level of 165%.

Q3 2018 vs. Q3 2017 and YTD 2018 vs. YTD 2017

The severity ratio increased by 1.8 percentage points from the same quarter last year due to fluctuations in the Corporation's deficiency sales rates, housing prices and recovery levels.

The loss ratio decreased by 0.6 percentage points from the same quarter last year mainly due to the decrease in insurance claims partially offset by lower premiums and fees earned as discussed above. The ratio increased by 1.6 percentage points from the same nine month period last year, primarily due to the decrease in earned premium as discussed above.

The operating expense ratio increased by 1.2 percentage points and 1.7 percentage points from the same quarter and nine month period last year, respectively, due to the decrease in earned premiums and fees as previously discussed.

The return on equity ratio decreased by 1.3 percentage points and 0.5 percentage points from the same quarter and nine month period last year, respectively, due to increases in losses on financial instruments and decrease in earned premiums as noted above partially offset due to the declaration of dividends.

The return on required equity ratio decreased by 1.1 percentage points and 0.4 percentage points from the same quarter and nine month period last year, respectively, mainly due to the increases in losses on financial instruments as well as a decrease in premiums earned as noted above.

Capital management

Our capital management framework follows OSFI regulations with respect to the use of the Minimum Capital Test (MCT) for insurance companies. The MCT is the ratio of capital available to minimum capital required. Refer to the unaudited quarterly consolidated financial statements Note 9 – Capital Management for complete disclosure on capital management.

| <i>(in percentages)</i> | As at | |
|--|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Capital available to minimum capital required (% MCT) ¹ | 175 | 184 |

¹ We have not made use of transitional arrangements as provided by the OSFI Advisory. Our MCT ratio as at 30 September 2018 would be 183% with transitional arrangements (31 December 2017 – 211%).

Capital available to minimum capital required decreased by 9 percentage points mainly due to the declaration of \$3 billion of dividends since 1 January 2018.

Financial resources

The Mortgage Loan Insurance investment portfolio is funded by cash flow generated by premiums, fees and interest received, net of claims and operating expenses. The investment objective and asset allocation for the Mortgage Loan Insurance investment portfolio focuses on maximizing risk-adjusted return while minimizing the need to liquidate investments. As at 30 September 2018 total investments had a fair value of \$18.6 billion (31 December 2017 - \$22.8 billion).

SECURITIZATION

We facilitate access to funds for residential mortgage financing through securitization guarantee products and the administration of the legal framework for Canadian covered bonds.

Financial metrics

Under Section 15 of the NHA, the aggregate outstanding amount of principal guarantees may not exceed \$600 billion. Total guarantees-in-force represents the maximum principal obligation related to this timely payment guarantee, and is broken down as follows.

| <i>(in billions)</i> | As at | |
|----------------------------------|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Total guarantees-in-force | 484 | 477 |
| NHA MBS | 242 | 244 |
| CMB | 242 | 233 |

Guarantees-in-force were \$484 billion as at 30 September 2018, an increase of \$7 billion (1.5%) as new CMB guarantees provided by CMHC exceeded CMB maturities.

| <i>(in millions)</i> | Three months ended | | Nine months ended | |
|--|--------------------|-------------------|-------------------|-------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Total new securities guaranteed | 43,766 | 41,172 | 118,318 | 113,082 |
| NHA MBS | 33,766 | 31,672 | 88,818 | 82,832 |
| CMB | 10,000 | 9,500 | 29,500 | 30,250 |
| Guarantee and application fees received | 156 | 134 | 397 | 370 |
| MBS guarantee and application fees received | 119 | 100 | 289 | 260 |
| CMB guarantee fees received | 37 | 34 | 108 | 110 |

Q3 2018 vs. Q3 2017

New securities guaranteed increased by \$2,594 million (6.3%) from the same quarter last year primarily driven by issuers' liquidity needs.

Guarantee and application fees received were \$22 million (16.4%) higher than the same quarter last year mainly due to higher NHA MBS volumes securitized and due to higher average premiums rates. In Q3 2018 certain issuers exceeded the annual guarantee fee threshold above which carries a higher premium rate.

YTD 2018 vs. YTD 2017

New securities guaranteed increased by \$5,236 million (4.6%) from the same nine month period last year mainly due to higher securitization activity by NHA MBS issuers. The NHA MBS guarantee limit in 2018 is \$5 billion higher than it was in 2017 (\$135 billion in 2018 vs \$130 billion in 2017).

Guarantee and application fees received were \$27 million (7.3%) higher than the same nine month period last year as a result of the higher NHA MBS guaranteed volumes and higher average premiums rates as discussed above.

Financial analysis

| <i>(in millions)</i> | Three months ended | | Nine months ended | |
|---------------------------------------|----------------------|----------------------|----------------------|----------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Net interest income | 2 | 2 | 8 | 8 |
| Premiums and fees earned ¹ | 121 | 98 | 351 | 276 |
| Investment income | 17 | 13 | 44 | 36 |
| Other income ² | (1) | 1 | (1) | 5 |
| Total revenues | 139 | 114 | 402 | 325 |
| Total expenses | 14 | 12 | 42 | 38 |
| Income before income taxes | 125 | 102 | 360 | 287 |
| Income taxes | 31 | 26 | 90 | 72 |
| Net income | 94 | 76 | 270 | 215 |

¹ Securitization Activity is comprised of guarantee and application fees earned.

² Other income includes net gains (losses) on financial instruments and other income.

Q3 2018 vs. Q3 2017 and YTD 2018 vs. YTD 2017

Net income increased by \$18 million (23.7%) from the same quarter and \$55 million (25.6%) from the same nine month period last year primarily due to increases in premiums and fees earned of \$23 million (23.5%) and \$75 million (27.2%), respectively. The increase in fees earned is mainly driven by NHA MBS fees earned and is a result of the increasing guarantee limit following the policy change which came into effect on 1 July 2016, and which introduced an NHA MBS guarantee fee on NHA MBS sold to CHT.

Ratios

To supplement financial results of the Securitization programs (excluding Canada Housing Trust (CHT)), we also use financial measures and ratios to analyze our financial performance.

| <i>(in percentages)</i> | Three months ended | | Nine months ended | |
|--|----------------------|----------------------|----------------------|----------------------|
| | 30 September 2018 | 30 September 2017 | 30 September 2018 | 30 September 2017 |
| Operating expense ratio | 8.4 | 10.4 | 9.2 | 10.7 |
| Return on equity | 15.1 | 13.5 | 14.8 | 13.2 |
| Return on required equity ¹ | 21.2 | 15.4 | 20.3 | 13.8 |

¹ Return on required equity is calculated as the annualized net income, adjusted to remove investment income earned on equity in excess of required equity, divided by the average required equity for the period.

Q3 2018 vs. Q3 2017 and YTD 2018 vs. YTD 2017

The operating expense ratio decreased by 2 percentage points and 1.5 percentage points from the same quarter and nine month period last year, respectively, mainly due to higher guarantee and application fees earned.

Return on equity increased by 1.6 percentage points from the same quarter and nine month period last year due to higher net income as noted above.

The return on required equity increased by 5.8 percentage points and 6.5 percentage points from the same quarter and nine month period last year, respectively. This is due to a combined effect of a 23% increase in adjusted net income, and a 16% decrease in average required equity for the nine month period.

Capital management

Our Capital Management Framework for the Securitization Activity follows industry best practices and incorporates regulatory principles from OSFI, including those set out in OSFI's E19 – Own Risk and Solvency Assessment (ORSA) guideline, and the Basel Committee on Banking Supervision.

Our capital adequacy assessment uses an integrated approach to evaluate our capital needs from both a regulatory and economic capital basis to establish capital targets that take into consideration our strategy and risk appetite. Refer to the unaudited quarterly consolidated financial statements Note 9 – Capital Management for complete disclosure on capital management.

| <i>(in percentages)</i> | As at | |
|---------------------------------------|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Capital available to capital required | 149 | 135 |

Capital available to capital required was 14 percentage points higher due to the combined effect of an increase in equity available and a decrease in required equity. Required equity decreased from 31 December 2017 levels mainly due to lower market risk as a result of lower durations in our securitization investment portfolio.

Financial resources

The Securitization investment portfolio is funded by guarantee and application fees and interest received net of expenses. The portfolio is intended to cover risk exposures associated with our securitization guarantee programs. The objective of the Securitization investment portfolio is to maximize our capacity to meet liquidity needs of the timely payment guarantee and to preserve capitalization amounts through investments in Government of Canada securities. As at 30 September 2018, total investments under management had a fair value of \$3.9 billion (31 December 2017 - \$3.6 billion).

RISK MANAGEMENT

We are exposed to a variety of risks in our operating environment that could have an impact on the achievement of our objectives. These risks are discussed in detail in our 2017 Annual Report. There have been no material developments impacting our risk management approaches during this reporting period.

HISTORICAL QUARTERLY INFORMATION

| <i>(in millions, unless otherwise indicated)</i> | Q3 2018 | Q2 2018 | Q1 2018 ¹ | Q4 2017 | Q3 2017 | Q2 2017 | Q1 2017 | Q4 2016 |
|--|---------|---------|----------------------|---------|---------|---------|---------|---------|
| Consolidated Results | | | | | | | | |
| Total assets | 272,513 | 268,185 | 270,522 | 267,115 | 268,771 | 264,713 | 266,188 | 259,532 |
| Total liabilities | 256,839 | 251,875 | 253,627 | 249,374 | 251,209 | 247,260 | 244,782 | 238,542 |
| Total equity of Canada | 15,674 | 16,310 | 16,895 | 17,741 | 17,562 | 17,453 | 21,406 | 20,990 |
| Total revenues | 1,049 | 1,151 | 1,576 | 1,430 | 1,266 | 1,224 | 2,232 | 1,186 |
| Total expenses (including income taxes) | 662 | 763 | 1,283 | 861 | 799 | 827 | 1,862 | 790 |
| Net income | 387 | 388 | 293 | 569 | 467 | 397 | 370 | 396 |
| Assisted Housing | | | | | | | | |
| Parliamentary appropriations for housing programs expenses | 416 | 463 | 1,026 | 594 | 521 | 548 | 1,566 | 570 |
| Net income (loss) | 10 | 4 | (1) | 71 | 4 | (1) | 6 | (29) |
| Total equity of Canada | 310 | 275 | 235 | 234 | 203 | 151 | 186 | 196 |
| Mortgage Loan Insurance | | | | | | | | |
| Insurance-in-force (\$B) | 453 | 463 | 472 | 480 | 484 | 496 | 502 | 512 |
| Total insured volumes | 13,304 | 14,005 | 8,265 | 15,382 | 12,539 | 17,395 | 8,253 | 20,528 |
| Premiums and fees received | 409 | 415 | 241 | 353 | 414 | 443 | 228 | 374 |
| Premiums and fees earned | 358 | 359 | 353 | 390 | 394 | 396 | 377 | 344 |
| Claims paid | 60 | 53 | 69 | 84 | 74 | 94 | 77 | 82 |
| Insurance claims | 35 | 72 | 65 | (22) | 41 | 51 | 77 | (13) |
| Net income | 283 | 289 | 203 | 412 | 382 | 321 | 289 | 364 |
| Arrears rate | 0.29 % | 0.27 % | 0.29 % | 0.29 % | 0.30 % | 0.29 % | 0.32 % | 0.32 % |
| Loss ratio | 9.8 % | 20.1 % | 19.8 % | (5.6) % | 10.4 % | 12.9 % | 20.4 % | (3.8) % |
| Operating expense ratio | 18.7 % | 22.8 % | 22.1 % | 23.1 % | 17.5 % | 19.7 % | 21.5 % | 21.2 % |
| Combined ratio | 28.5 % | 42.9 % | 41.9 % | 17.5 % | 27.9 % | 32.6 % | 41.9 % | 17.4 % |
| Severity ratio | 32.1 % | 29.1 % | 31.9 % | 31.9 % | 31.6 % | 27.5 % | 30.5 % | 29.9 % |
| Return on equity | 8.8 % | 8.3 % | 5.5 % | 10.3 % | 10.1 % | 7.5 % | 6.1 % | 7.7 % |
| Return on required equity | 9.1 % | 8.7 % | 6.0 % | 11.4 % | 10.2 % | 8.5 % | 6.9 % | 15.8 % |
| Capital available to minimum capital required (% MCT) | 175 % | 177 % | 177 % | 184 % | 179 % | 173 % | 215 % | 384 % |
| % Estimated outstanding Canadian residential mortgages with CMHC insurance coverage | 29.7 % | 30.6 % | 31.0 % | 31.9 % | 32.7 % | 34.3 % | 34.9 % | 36.0 % |
| Securitization | | | | | | | | |
| Guarantees-in-force (\$B) | 484 | 479 | 481 | 477 | 459 | 456 | 457 | 452 |
| Securities guaranteed | 43,766 | 37,819 | 36,733 | 54,149 | 41,172 | 37,730 | 34,180 | 52,117 |
| Guarantee and application fees received | 156 | 120 | 121 | 257 | 134 | 121 | 115 | 240 |
| Guarantee and application fees earned | 121 | 117 | 113 | 108 | 98 | 91 | 87 | 66 |
| Net income | 94 | 88 | 88 | 80 | 76 | 71 | 68 | 53 |
| Operating expense ratio | 8.4 % | 9.6 % | 9.5 % | 11.2 % | 10.4 % | 10.7 % | 10.7 % | 14.2 % |
| Return on equity | 15.1 % | 14.7 % | 14.9 % | 14.1 % | 13.5 % | 13.0 % | 12.9 % | 9.9 % |
| Return on required equity | 21.2 % | 19.9 % | 19.7 % | 16.8 % | 15.4 % | 14.3 % | 13.2 % | 12.4 % |
| Capital available to capital required | 149 % | 143 % | 137 % | 136 % | 112 % | 120 % | 106 % | 100 % |
| % Estimated outstanding Canadian residential mortgages with CMHC securitization guarantees | 31.7 % | 31.7 % | 32.0 % | 32.2 % | 31.2 % | 31.9 % | 32.6 % | 32.6 % |

¹ We implemented IFRS 9 and IFRS 15 in Q1 2018. Prior quarters were based off International Accounting Standard (IAS) 39 and IAS 18.

Unaudited Quarterly Consolidated Financial Statements

CONTENTS

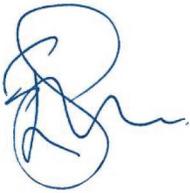
| | |
|--|----|
| MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING..... | 21 |
| CONSOLIDATED BALANCE SHEET..... | 22 |
| CONSOLIDATED STATEMENT OF INCOME AND COMPREHENSIVE INCOME | 23 |
| CONSOLIDATED STATEMENT OF EQUITY OF CANADA..... | 24 |
| CONSOLIDATED STATEMENT OF CASH FLOWS..... | 25 |
| NOTES TO UNAUDITED QUARTERLY CONSOLIDATED FINANCIAL STATEMENTS | 26 |
| 1. CORPORATE INFORMATION | 26 |
| 2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES..... | 26 |
| 3. CURRENT AND FUTURE ACCOUNTING CHANGES..... | 27 |
| 4. CRITICAL JUDGMENTS IN APPLYING ACCOUNTING POLICIES AND MAKING ESTIMATES | 38 |
| 5. SEGMENTED INFORMATION..... | 39 |
| 6. PARLIAMENTARY APPROPRIATIONS AND HOUSING PROGRAMS EXPENSES | 42 |
| 7. MORTGAGE LOAN INSURANCE..... | 42 |
| 8. SECURITIZATION | 44 |
| 9. CAPITAL MANAGEMENT | 44 |
| 10. FAIR VALUE MEASUREMENT..... | 47 |
| 11. CASH AND CASH EQUIVALENTS | 51 |
| 12. INVESTMENT SECURITIES..... | 51 |
| 13. LOANS | 52 |
| 14. BORROWINGS | 56 |
| 15. FINANCIAL INSTRUMENTS INCOME AND EXPENSES..... | 58 |
| 16. MARKET RISK | 61 |
| 17. CREDIT RISK..... | 62 |
| 18. PENSION AND OTHER POST-EMPLOYMENT BENEFITS | 62 |
| 19. INCOME TAXES..... | 63 |
| 20. RELATED PARTY TRANSACTIONS..... | 63 |
| 21. COMMITMENTS AND CONTINGENT LIABILITIES..... | 63 |
| 22. COMPARATIVE FIGURES | 63 |

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

Period ended 30 September 2018

Management is responsible for the preparation and fair presentation of these unaudited quarterly consolidated financial statements in accordance with International Accounting Standard 34 *Interim Financial Reporting*, and for such internal controls as Management determines are necessary to enable the preparation of unaudited quarterly consolidated financial statements that are free from material misstatement. Management is also responsible for ensuring all other information in this quarterly financial report is consistent, where appropriate, with the unaudited quarterly consolidated financial statements.

Based on our knowledge, these unaudited quarterly consolidated financial statements present fairly, in all material respects, our financial position, results of operations and cash flows, as at the date of and for the periods presented in the unaudited quarterly consolidated financial statements.



Evan Siddall, BA, LL.B
President and Chief Executive Officer



Lisa Williams, CPA, CA
Chief Financial Officer

27 November 2018

CONSOLIDATED BALANCE SHEET

| (in millions of Canadian dollars) | Notes | As at | |
|---|-------|-------------------|------------------|
| | | 30 September 2018 | 31 December 2017 |
| Assets | | | |
| Cash and cash equivalents | 11 | 817 | 887 |
| Accrued interest receivable | | 1,301 | 705 |
| Investment securities: | 12 | | |
| Fair value through profit or loss | | 1,871 | 1,234 |
| Fair value through other comprehensive income | | 18,313 | - |
| Available for sale | | - | 22,112 |
| Derivatives | | 45 | 61 |
| Due from the Government of Canada | 6 | 174 | 126 |
| Loans: | 13 | | |
| Fair value through profit or loss | | 2,191 | 2,906 |
| Amortized cost | | 246,639 | 237,944 |
| Accounts receivable and other assets | | 857 | 835 |
| Investment property | | 305 | 305 |
| | | 272,513 | 267,115 |
| Liabilities | | | |
| Securities sold under repurchase agreements | | 458 | 297 |
| Accounts payable and other liabilities | | 410 | 561 |
| Accrued interest payable | | 1,142 | 545 |
| Dividend payable | 9 | 500 | 2,000 |
| Derivatives | | 46 | 39 |
| Provision for claims | 7 | 523 | 555 |
| Borrowings: | 14 | | |
| Fair value through profit or loss | | 3,714 | 4,564 |
| Amortized cost | | 242,852 | 233,592 |
| Defined benefit plans liability | | 255 | 450 |
| Unearned premiums and fees | 7, 8 | 6,812 | 6,687 |
| Deferred income tax liabilities | | 127 | 84 |
| | | 256,839 | 249,374 |
| Commitments and contingent liabilities | 21 | | |
| Equity of Canada | | | |
| Contributed capital | | 25 | 25 |
| Accumulated other comprehensive income (loss) | | (112) | 490 |
| Retained earnings | | 15,761 | 17,226 |
| | | 15,674 | 17,741 |
| | | 272,513 | 267,115 |

The accompanying notes are an integral part of these quarterly consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME AND COMPREHENSIVE INCOME

| <i>(in millions of Canadian dollars)</i> | Notes | Three months ended 30 September | | Nine months ended 30 September | |
|---|-------|------------------------------------|-------|-----------------------------------|-------|
| | | 2018 | 2017 | 2018 | 2017 |
| Interest income | 15 | 1,347 | 1,173 | 3,903 | 3,452 |
| Interest expense | 15 | 1,317 | 1,138 | 3,805 | 3,347 |
| Net interest income | | 30 | 35 | 98 | 105 |
| Parliamentary appropriations for housing programs | 6 | 416 | 521 | 1,905 | 2,635 |
| Premiums and fees earned | | 479 | 492 | 1,421 | 1,443 |
| Investment income | 15 | 126 | 145 | 388 | 432 |
| Net gains (losses) on financial instruments | 15 | (9) | 65 | (59) | 80 |
| Other income | | 7 | 8 | 23 | 27 |
| Total revenues and parliamentary appropriations | | 1,049 | 1,266 | 3,776 | 4,722 |
| Non-interest expenses | | | | | |
| Housing programs | 6 | 416 | 521 | 1,905 | 2,635 |
| Insurance claims | | 35 | 41 | 172 | 169 |
| Operating expenses | | 85 | 86 | 286 | 285 |
| | | 536 | 648 | 2,363 | 3,089 |
| Income before income taxes | | 513 | 618 | 1,413 | 1,633 |
| Income taxes | 19 | 126 | 151 | 345 | 399 |
| Net income | | 387 | 467 | 1,068 | 1,234 |
| Other comprehensive income (loss), net of tax | | | | | |
| Items that will be subsequently reclassified to net income | | | | | |
| Net unrealized losses from available for sale financial instruments | | - | (204) | - | (230) |
| Net unrealized losses from debt instruments held at fair value through other comprehensive income | | (75) | - | (225) | - |
| Reclassification of gains on available for sale instruments to net income on disposal in the period | | - | (34) | - | (42) |
| Reclassification of gains on debt instruments held at fair value through other comprehensive income in the period | | (7) | - | (9) | - |
| Total items that will be subsequently reclassified to net income | | (82) | (238) | (234) | (272) |
| Items that will not be subsequently reclassified to net income | | | | | |
| Net unrealized losses from equity securities designated at fair value through other comprehensive income | | - | - | (1) | - |
| Remeasurement gains (losses) on defined benefit plans | | 59 | 120 | 155 | (5) |
| Total items that will not be subsequently reclassified to net income | | 59 | 120 | 154 | (5) |
| | | (23) | (118) | (80) | (277) |
| Comprehensive income | | 364 | 349 | 988 | 957 |

The accompanying notes are an integral part of these quarterly consolidated financial statements.

CONSOLIDATED STATEMENT OF EQUITY OF CANADA

| <i>(in millions of Canadian dollars)</i> | Notes | Three months ended 30 September | | Nine months ended 30 September | |
|--|-------|------------------------------------|--------|-----------------------------------|---------|
| | | 2018 | 2017 | 2018 | 2017 |
| Contributed capital | | 25 | 25 | 25 | 25 |
| Accumulated other comprehensive income | | | | | |
| Balance reported at the end of previous period | | (30) | 727 | 490 | 761 |
| Impact of adopting IFRS 9 | 3 | - | - | (368) | - |
| Restated opening balance | | (30) | 727 | 122 | 761 |
| Other comprehensive loss | | (82) | (238) | (234) | (272) |
| Balance at end of period | | (112) | 489 | (112) | 489 |
| Retained earnings | | | | | |
| Balance reported at the end of previous period | | 16,315 | 16,701 | 17,226 | 20,204 |
| Impact of adopting IFRS 9 | 3 | - | - | 366 | - |
| Impact of adopting IFRS 15 | 3 | - | - | (53) | - |
| Restated opening balance | | 16,315 | 16,701 | 17,539 | 20,204 |
| Net income | | 387 | 467 | 1,068 | 1,234 |
| Other comprehensive income (loss) | | 59 | 120 | 154 | (5) |
| Dividend | 9 | (1,000) | (240) | (3,000) | (4,385) |
| Balance at end of period | | 15,761 | 17,048 | 15,761 | 17,048 |
| Equity of Canada | | 15,674 | 17,562 | 15,674 | 17,562 |

The accompanying notes are an integral part of these quarterly consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

| <i>(in millions of Canadian dollars)</i> | Notes | Three months ended | | Nine months ended | |
|---|-------|--------------------|---------|-------------------|----------|
| | | 30 September | | 30 September | |
| | | 2018 | 2017 | 2018 | 2017 |
| Cash flows from operating activities | | | | | |
| Net income | | 387 | 467 | 1,068 | 1,234 |
| Adjustments to determine cash flows from operating activities | | | | | |
| Amortization of premiums and discounts on financial instruments | | 25 | (9) | 85 | 79 |
| Net (gains) losses on financial instruments | | 48 | (52) | 10 | (55) |
| Deferred income taxes | | 30 | 6 | 24 | 30 |
| Changes in operating assets and liabilities | | | | | |
| Derivatives | | (76) | 28 | 23 | 22 |
| Accrued interest receivable | | (605) | (663) | (596) | (608) |
| Due from the Government of Canada | | 42 | 26 | (48) | (219) |
| Accounts receivable and other assets | | (11) | 45 | (76) | (17) |
| Accounts payable and other liabilities | | (53) | (76) | (153) | (74) |
| Accrued interest payable | | 569 | 666 | 597 | 575 |
| Provision for claims | | (15) | (22) | (32) | (68) |
| Defined benefit plans liability | | 9 | (14) | (8) | (47) |
| Unearned premiums and fees | | 74 | 48 | 53 | 27 |
| Other | | (7) | 13 | (4) | 10 |
| Loans | 13 | | | | |
| Repayments | | 5,185 | 5,214 | 21,839 | 20,607 |
| Disbursements | | (10,063) | (9,584) | (29,666) | (30,493) |
| Borrowings | 14 | | | | |
| Repayments | | (5,349) | (5,860) | (22,429) | (22,681) |
| Issuances | | 10,306 | 10,130 | 30,213 | 32,337 |
| | | 496 | 363 | 900 | 659 |
| Cash flows from investing activities | | | | | |
| Investment securities | | | | | |
| Sales and maturities | | 2,615 | 2,579 | 8,340 | 5,512 |
| Purchases | | (1,576) | (1,913) | (4,971) | (5,626) |
| Securities purchased under resale agreements | | 38 | - | 0 | 17 |
| Securities sold under repurchase agreements | | (164) | (64) | 161 | (300) |
| | | 913 | 602 | 3,530 | (397) |
| Cash flows from financing activities | | | | | |
| Dividends paid | 9 | (1,500) | (1,240) | (4,500) | (1,385) |
| Change in cash and cash equivalents | | (91) | (275) | (70) | (1,123) |
| Cash and cash equivalents | | | | | |
| Beginning of period | | 908 | 1,147 | 887 | 1,995 |
| End of period | | 817 | 872 | 817 | 872 |
| Represented by | | | | | |
| Cash | | - | (1) | - | (1) |
| Cash equivalents | | 817 | 873 | 817 | 873 |
| | | 817 | 872 | 817 | 872 |
| Supplementary disclosure of cash flows from operating activities | | | | | |
| Amount of interest received during the period | | 932 | 767 | 3,948 | 3,527 |
| Amount of interest paid during the period | | 799 | 556 | 3,361 | 2,939 |
| Amount of dividends received during the period | | 8 | 11 | 27 | 35 |
| Amount of income taxes paid during the period | | 111 | 72 | 367 | 327 |

The accompanying notes are an integral part of these quarterly consolidated financial statements.

NOTES TO UNAUDITED QUARTERLY CONSOLIDATED FINANCIAL STATEMENTS

1. Corporate Information

Canada Mortgage and Housing Corporation (CMHC or Corporation) was established in Canada as a Crown corporation in 1946 by the *Canada Mortgage and Housing Corporation Act* (CMHC Act) to carry out the provisions of the *National Housing Act* (NHA). We are also subject to Part X of the *Financial Administration Act* (FAA) by virtue of being listed in Part 1 of Schedule III, wholly owned by the Government of Canada (Government), and an agent Crown corporation. Our Corporation's National Office is located at 700 Montreal Road, Ottawa, Ontario, Canada, K1A 0P7.

These consolidated financial statements are as at and for the three and nine months ended 30 September 2018 and were approved and authorized for issue by our Audit Committee on 27 November 2018.

2. Basis of Preparation and Significant Accounting Policies

Our unaudited quarterly consolidated financial statements have been prepared in accordance with *International Accounting Standard (IAS) 34 Interim Financial Reporting (IAS 34)* and do not include all of the information required for full annual consolidated financial statements. Except as indicated in Note 3, we follow the same accounting policies and methods of application as disclosed in Note 2 of our audited consolidated financial statements for the year ended 31 December 2017 and should be read in conjunction with those financial statements.

Seasonality

We have concluded that our business is not highly seasonal in accordance with IAS 34; however, our mortgage loan insurance (MLI) business is exposed to some seasonal variation. Premiums received for some insurance products vary each quarter because of seasonality in housing markets. Variations are driven by the level of mortgage originations and related mortgage policies written, which, for purchase transactions, typically peak in the spring and summer months. Insurance claims vary from quarter to quarter primarily as the result of prevailing economic conditions as well as the characteristics of the insurance-in-force portfolio, such as size and age.

3. Current and future accounting changes

Current accounting changes

International Financial Reporting Standard 15 Revenue from Contracts with Customers (IFRS 15)

We adopted IFRS 15, with an initial application date of 1 January 2018, using the cumulative catch-up method. Therefore the comparative information for 2017 is reported under IAS 18 *Revenue* and is not comparable to the information presented in 2018. The net effect of transitioning to IFRS 15 was recognized in Equity of Canada on 1 January 2018. The application of IFRS 15 impacted how we account for application fees on timely payment guarantees (TPG) in our Securitization activity. There were no other material changes as a result of the adoption of IFRS 15.

Whereas the application fees were previously recognized as revenue on payment date, under IFRS 15, the application fee and the TPG fee are considered one performance obligation and the corresponding revenue should be recognized as the performance obligation is satisfied. The application fees are recognized on the same basis as the TPG.

As a consequence, the unearned premiums and fees balance on 1 January 2018 was \$72 million higher than the balance under the previous policy. The corresponding net of tax adjustment to retained earnings was \$53 million.

International Financial Reporting Standard 9 *Financial Instruments* (IFRS 9)

We adopted IFRS 9, which replaced IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39), on 1 January 2018. IFRS 9 addresses the recognition and derecognition, classification and measurement and impairment of financial instruments and hedge accounting. We have not restated comparative figures for financial instruments for dates and periods before 1 January 2018 as permitted by IFRS 9. Therefore the comparative information for 2017 is reported in accordance with IAS 39 and is not comparable to the information presented in 2018. The net effect of transitioning to IFRS 9 was recognized in Equity of Canada on 1 January 2018. CMHC does not apply hedge accounting.

Amendments were also made to *IFRS 7 Financial Instruments: Disclosures* to reflect the differences between IAS 39 and IFRS 9. These changes include transitional disclosures which we have disclosed below along with expanded quantitative and qualitative credit risk disclosures which we will adopt for the annual period ending 31 December 2018.

Classification and measurement of financial instruments

With the adoption of IFRS 9, we now classify our financial assets in the following categories: financial assets at fair value through profit or loss (FVTPL), fair value through other comprehensive income (FVOCI) and amortized cost. Classification is determined at initial recognition based on our business model for managing the asset and the contractual cash flow characteristics of the asset.

Financial liabilities are classified as either financial liabilities at FVTPL or amortized cost which is essentially unchanged from IAS 39, with the exception that changes in fair value of liabilities designated at FVTPL due to our own credit risk are presented in other comprehensive income (OCI), rather than profit or loss.

The following table presents a description of all our financial instruments along with their classification under IFRS 9 and the criteria for classifying them as such:

| Classification | Financial Instruments (Activity) ¹ | Description | Criteria and accounting treatment |
|---|--|---|---|
| Financial assets at amortized cost | Cash and cash equivalents (AH, MLI, SEC) | highly liquid investments with a term to maturity of 98 days or less from the date of acquisition that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value | Financial assets are classified at amortized cost if the assets: <ol style="list-style-type: none"> are held within a business model whose objective is to collect contractual cash flows; generate cash flows on specified dates that are solely payment of principal and interest (SPPI); and have not been designated as FVTPL in order to eliminate or significantly reduce an accounting mismatch that would otherwise arise from classifying them as at amortized cost. |
| | Securities purchased under resale agreements (Reverse Repurchase Agreements) (AH, MLI) | purchase of securities, typically Government treasury bills or bonds, with the commitment to resell the securities to the original seller at a specified price and future date in the near term | Financial assets at amortized cost are initially recognized at fair value plus transaction costs. They are subsequently measured at amortized cost using the effective interest rate method (EIRM), net of an allowance for expected credit losses (ECL). |
| | Loans – Canada Mortgage Bonds Program (CMB) (SEC) | amounts due from Canadian financial institutions as a result of the sale of their beneficial interest in National Housing Act Mortgage Backed Securities (NHA MBS) to Canada Housing Trust (CHT) | Interest income is recognized using the EIRM in interest income in AH and investment income under MLI and SEC. ECL are recognized in profit or loss on financial assets at amortized cost. |
| | Loans - Lending Programs (AH) | loans not economically hedged within our AH Activity | |
| | Loans (MLI) | mortgages or loans (workouts) that benefit from the MLI supported default management activities that enable borrowers to work through their financial difficulties | |
| Debt instruments at FVOCI | Cash equivalents (MLI, SEC) | highly liquid investments with a term to maturity of 98 days or less from the date of acquisition that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value consists of Corporate, Federal, Provincial and Sovereign debt instruments | Debt instruments are classified as at FVOCI if the assets: <ol style="list-style-type: none"> are held within a business model whose objective is achieved by collecting contractual cash flows and selling assets; generate cash flows on specified dates that are SPPI; and have not been designated as FVTPL in order to eliminate or significantly reduce an accounting mismatch that would otherwise arise from classifying them as at FVOCI. |
| | Investment Securities – debt instruments (MLI, SEC) | | Financial assets at FVOCI are initially recognized at fair value plus transaction costs. They are subsequently measured at fair value. Unrealized gains and losses arising from changes in fair value are recorded in other comprehensive income (OCI) until the financial asset is derecognized at which point, cumulative gains or losses previously recognized in OCI are reclassified from accumulated other comprehensive income (AOCI) to net gains (losses) on financial instruments. Unrealized foreign exchange gains (losses) are recognized in net gains (losses) on financial instruments. Interest income is recognized using the EIRM. ECL are recognized on financial assets held at FVOCI. The cumulative ECL allowance is recorded in OCI and does not reduce the carrying amount of the financial asset on the balance sheet. The change in the ECL allowance is recognized in profit and loss. |

Denotes in which Activity we hold the instruments: Assisted Housing (AH), Mortgage Loan Insurance (MLI) or Securitization (SEC)

| Classification | Financial Instruments (Activity) | Description | Criteria and accounting treatment |
|---|--|--|--|
| Financial assets at FVTPL | Cash equivalents, loans, investment securities designated at FVTPL (AH) | for certain portfolios of loans and associated borrowings originated prior to August 2016, the AH Activity uses derivatives to manage refinancing and reinvestment risks, as well as mismatches between the timing of receipts from assets and payments of liabilities. These assets form part of the lending economic hedging structure and are designated at FVTPL | Financial assets that do not meet the criteria for classification as financial assets at amortized cost or financial assets at FVOCI are classified as at FVTPL, unless an irrevocable election has been made at initial recognition for certain equity investments to have their changes in fair value be presented in OCI. Financial assets at FVTPL include any financial assets whose contractual cash flows are not SPPI, or any financial assets that are not held within a business model whose objective is achieved by collecting contractual cash flows or collecting cash flows and selling assets. Financial assets at FVTPL also include derivatives or instruments that have been irrevocably designated upon initial recognition as at FVTPL in order to eliminate or significantly reduce an accounting mismatch that would otherwise arise from classifying them in those categories. |
| | Derivatives – Interest rate swaps (AH) and FX contracts (MLI) | interest rate swaps and foreign exchange contracts used to economically hedge foreign exchange risks on US Dollar denominated debt instruments | Financial assets at FVTPL are initially recognized and subsequently measured at fair value. Unrealized gains and losses arising from changes in fair value and gains and losses realized on disposition are recorded in net gains (losses) on financial instruments. Transaction costs are expensed as incurred. |
| | Investment Securities – Common equity securities and limited partnership units (MLI) | mandatorily classified at FVTPL | Interest income using the EIRM and dividend income is recognized in profit and loss. ECL are not recognized on financial instruments measured at FVTPL. |
| | Investment Securities – debt instruments (MLI) | subordinated debt securities whose contractual cash flows do not give rise to cash flows that are SPPI | |
| | Loans – (AH, MLI) | workout loans which contain interest adjustment clauses and therefore fail the SPPI test as well as assignment of mortgages for which we only expect to recover the value of the underlying collateral | |
| Equity instruments designated at FVOCI | Investment Securities - Preferred equity securities (MLI) | Preferred shares | <p>An irrevocable election is available upon initial recognition to present changes in the fair value of equity instruments in OCI if the instruments are not held for trading and is not a contingent consideration in a business combination. An instrument that is held for trading is:</p> <ul style="list-style-type: none"> a) acquired principally for the purpose of selling in the near term; b) on initial recognition part of a portfolio of identified financial instruments that are managed together and for which there is evidence of recent actual short-term profit-taking; or c) a derivative (other than financial guarantee derivatives or designated effective hedging instruments). <p>The election is made upon initial recognition on an instrument-by-instrument basis. Amounts recognized in OCI shall not be transferred to profit or loss; however, they may be transferred to a different category within equity (e.g. retained earnings) upon derecognition.</p> <p>We have elected to present cumulative OCI directly in retained earnings.</p> <p>ECL are not recognized on equity instruments.</p> <p>Dividend income is recognized in profit and loss.</p> |

| Classification | Financial Instruments (Activity) | Description | Criteria and accounting treatment |
|--|---|--|---|
| Financial liabilities at FVTPL | Borrowings (AH – Lending programs) | borrowings that are economically hedged as part of our lending hedging structure | <p>A financial liability is classified at FVTPL if it is held for trading or designated as at FVTPL.</p> <p>A financial liability may be irrevocably designated upon initial recognition as at FVTPL if:</p> <ul style="list-style-type: none"> a) doing so eliminates or reduces significantly an accounting match; or b) its performance is evaluated on a fair value basis in accordance with risk management policies. <p>Unrealized gains and losses arising from changes in fair value are recognized in profit or loss except for changes in fair value attributable to an entity's own credit risk which are recognized in OCI unless doing so would create an accounting mismatch, in which case, the entire fair value change is presented in profit or loss.</p> <p>Interest expense is recognized using the EIRM.</p> |
| Financial liabilities at amortized cost | <p>Borrowings – Canada Mortgage Bonds (SEC)</p> <p>Borrowings from the Government of Canada (AH)</p> <p>Securities sold under repurchase agreements (MLI)</p> | <p>interest-bearing bullet bonds issued by CHT and guaranteed by CMHC</p> <p>borrowings incurred to fund loans in the Assisted Housing Activity that are not part of the lending hedging structure</p> <p>sale of securities with the commitment to repurchase the securities from the original buyer at a specified price and future date in the near term. Proceeds received from these agreements are generally invested in Reverse Repurchase Agreements or cash equivalents for the purpose of generating additional income. These transactions are entered into simultaneously with matching terms to maturity</p> | <p>Financial liabilities are classified at amortized cost unless they have been classified at FVTPL.</p> <p>Financial liabilities are initially recognized at fair value plus transaction costs. They are subsequently measured at amortized cost using the EIRM.</p> <p>Interest expense is recognized using the EIRM.</p> |
| Financial guarantee contracts | <i>National Housing Act</i> Mortgage-Backed Securities (NHA MBS) and Canada Mortgage Bonds (CMB) (SEC) | guarantee to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due | <p>NHA MBS TPG and application fees and CMB TPG fees are initially recognized in unearned premiums and fees at fair value (the premium received). Subsequently, they are measured at the higher of i) amount initially recognized less the amortization of guarantee and application fee revenue; and ii) the amount of the allowance for ECL.</p> |

Classification and measurement of debt instruments

The classification and measurement of debt instruments is based on the business model for managing the assets and whether contractual cash flows are SPPI.

Business model assessment

The business model reflects how we manage assets in order to generate cash flows. That is, whether the objective is solely to collect contractual cash flows, or to collect both contractual cash flows and cash flows arising from the sale of assets. If neither is applicable, then the financial asset is measured at FVTPL. We assess our business models at a level that reflects how our financial instruments are managed to achieve our business objectives. This assessment begins at the operating segment level, and where applicable, by sub-portfolios of instruments that are managed together within a particular activity to achieve common business objectives.

Upon initial and subsequent application of IFRS 9, we perform our business model assessment based on the following main criteria:

- management's strategic objectives of the business model and how these objectives are carried out in practice;
- how performance of the business model is evaluated and reported to key management personnel;
- the risks that affect the performance of the business model and how we manage those risks. Key risks include credit, market and liquidity risks as described in detail in our consolidated financial statements for the year ended 31 December 2017;
- how managers of the business model are compensated;
- the frequency, value and timing of historical sales activity and expectations for future sales activities;

Assessment of whether contractual cash flows are SPPI

We assess whether the cash flows of our debt instruments meet the SPPI criteria based on the asset's contractual terms. For this assessment, we define principal as the fair value of the asset upon initial recognition and interest as consideration for the time value of money, the credit risk of the transaction and for other lending risks and costs as well as a profit margin.

Contractual terms that introduce exposure to risk or volatility to the contractual cash flows that are inconsistent with a basic lending agreements do not satisfy the SPPI requirement. Equity instruments and derivatives fail the SPPI test.

Impairment of financial instruments

We recognize an allowance for ECL on all debt instruments not carried at FVTPL. We also recognize an allowance for ECL for our financial guarantees to the extent they exceed the balance of unearned fees associated with the guarantees. Changes in our estimate of ECL, for all instruments except our workout loans, are recognized in expected credit losses on financial assets in net gains (losses) on financial instruments. Changes in our estimate of ECL, on our workout loans are recognized in insurance claims expense.

Credit losses are defined as the difference between all contractual cash flows due to the Corporation over the maximum contractual period, including extension options, and the cash flows that we expect to receive (cash shortfalls), discounted at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired assets). ECL are the weighted average of credit losses determined by evaluating a range of possible outcomes using reasonable, supportable information about past events and current and forecasted future economic conditions.

Measurement of expected credit losses

The Corporation has developed an impairment model to determine the allowance for ECL on our debt securities classified as amortized cost or FVOCI, loans classified as amortized cost and our financial guarantee contracts. We determine an allowance for ECL at initial recognition of the financial instrument (or the date we become party to a financial guarantee) that is updated at each reporting period throughout the life of the instrument.

The ECL allowance is based on the ECL over the life of the financial instrument (lifetime ECL), unless there has been no significant increase in credit risk (SICR) since initial recognition, in which case the ECL allowance is measured at an amount equal to the portion of lifetime ECL that result from default events possible within the next 12 months (12-month ECL). ECL are determined based on three main drivers: probability of default, loss given default and exposure at default:

- Probability of default (PD): a point in time estimate of the likelihood of default either over the next 12 months (12-month ECL) or over the remaining life of the instrument (lifetime ECL). Our PD's are determined by mapping internal credit ratings to point-in-time PD tables based on statistical models derived from a large data set of publicly traded entities.
- Loss given default (LGD): is the percentage of the gross carrying amount of the instrument that will be lost on default at a given point in time. It is based on the difference between contractual cash flows due and those expected to be received, including the realization of collateral;
- Exposure at default (EAD): the gross carrying amount of the instrument at a given point in time and is calculated as the present value of the outstanding contractual cash flows using the EIRM.
- The ECL is calculated using a scenario based approach where, for each scenario, the PD, LGD and EAD are projected for each individual exposure at each cash flow date over the next 12 months (12-month ECL) or remaining life of the instrument (lifetime ECLs). The components are multiplied together at each future date and discounted back using the original effective interest rate to the reporting date and summed. A probability-weighted average ECL is then determined across the multiple scenarios. We have modelled all ECLs at the individual instrument level.

Significant increase in credit risk

We have established a policy to perform an assessment at the end of each reporting period, of whether the instrument's credit risk has increased significantly since initial recognition (or the date we become party to a financial guarantee).

Based on this assessment, we group the instruments into the following categories:

- Stage 1: instruments which have not experienced a SICR since initial recognition. ECL are recognized based on 12-month ECL;
- Stage 2: instruments which have experienced a SICR since initial recognition. In subsequent periods, if the credit risk of an instrument has improved such that there is no longer a SICR since initial recognition, the ECL allowance will revert to stage 1. ECLs are recognized based on lifetime ECLs;
- Stage 3: instruments are considered credit-impaired as one or more events that have a detrimental impact on estimated future cash flows have occurred. ECL are recognized based on lifetime ECL;
- Purchased or originated credit-impaired (POCI) – instruments that are credit impaired on initial recognition. ECL are recognized based on lifetime ECL.

Interest revenue on stage 3 or POCI financial instruments is calculated based on the carrying amount of the asset, net of the loss allowance, rather than the gross carrying amount.

For instruments that we assess as having low credit risk at the reporting date, we applied the low credit risk exemption and have presumed that credit risk has not increased significantly since initial recognition. We use our internal credit ratings at the reporting date to assess whether the instrument has low credit risk. Our internal ratings are based on internal assessments of counterparty creditworthiness and generally correspond to those provided by credit rating agencies. We consider an instrument to have low credit risk when our internal rating is BBB- or higher.

We consider an instrument in default, which is fully aligned with the definition of credit-impaired, when it meets the following criteria:

- Observable data exists that has a detrimental impact on the estimated future cash flows such as:
 - significant financial difficulty of the issuer;
 - the granting of a new loan to assist the borrower work through financial difficulties;
 - it becomes probable that the issuer will enter bankruptcy or other financial reorganization, and
 - the disappearance of an active market due to financial difficulties.
- Borrower becomes 90 days past due on its contractual payments.

An instrument is no longer considered impaired when all past due amounts, including interest, have been recovered and it is determined that the principal and interest are fully collectable in accordance with the original contractual terms of the instrument. We write off instruments, either partially or in full, against the related ECL allowance when we judge that there is no realistic prospect of future recovery.

We apply the following policies in determining whether there has been a SICR on our financial instruments subject to ECL:

Debt instruments at amortized cost / FVOCI

The Corporations' credit risk policies restricts the investment in debt instruments to an internal rating of BBB- or higher and therefore all debt instruments held are presumed to have low credit risk and we have applied the low credit risk exemption (stage 1). A backstop is applied where the financial instrument is considered to have experienced a SICR if the counterparty is more than 30 days past due on its contractual payments.

Loans under the CMB program

Loans under the CMB program represent amounts due from Canadian financial institutions as a result of the sale of their beneficial interest in NHA MBS securities to us. The loans are collateralized by the NHA MBS and associated reinvestment securities acquired in the transactions. The NHA MBS, reinvestment assets and swaps represent the sole source of repayment on the loans, and thus directly affect the probability of a default occurring. Therefore, our assessment of SICR is based on the credit risk of these supporting assets.

The supporting assets are limited to NHA MBS and reinvestment assets rated R-1 (high) or AAA and swap counterparties with a minimum rating of BBB-. As such, all loans under the CMB program are presumed to have low credit risk and we have applied the low credit risk exemption (stage 1).

Assisted Housing Activity loans / Mortgage Loan Insurance Activity loans

Loans with an internal rating of BBB- or higher are presumed to have low credit risk and the low credit risk exemption has been applied (stage 1). These loans consist of those issued to municipalities under the Municipal Infrastructure Lending Program and loans indemnified by provinces and territories through provisions under Social Housing Agreements (SHA) where the credit rating of the province or territory is considered in the SICR assessment. This credit enhancement is relevant to assessing changes in credit risk since it directly impacts the probability of default. The province or territory is responsible for collecting loan payments from the borrower and, in turn, makes all payments to CMHC directly in accordance with the contractual terms of the loan on behalf of the borrower. These payment are made to CMHC, irrespective of the borrower's payment status.

A backstop is applied to these loans where the financial instrument is considered to have experienced a SICR if the borrower is more than 30 days past due on its contractual payments.

All remaining loans issued under our Assisted Housing or Mortgage Loan Insurance activities have not been internally rated and therefore the low credit risk presumption will not be used. Our SICR assessment of these loans is based on the following criteria which is primarily based on days past due:

- Stage 1: All current loans to 30 days past due.
- Stage 2: Loans between 30 and 90 days past due;
- Stage 3: Loans more than 90 days past due. Note, a loan that is not past due, but has been issued a workout loan to assist with financial difficulties will be considered credit impaired irrespective of days past due.

Based on analysis of internal data, we have determined there is a correlation between loans that are more than 30 days past due and loans that are 90 days past due (default threshold).

Under the terms of certain construction loans issued by our Assisted Housing Activity or workout loans issued by our Mortgage Loan Insurance Activity, there may be a period of time where the loan has been advanced but not under repayment and therefore days past due cannot be used in the SICR assessment. For these loans that are not under repayment, we will assess SICR by applying the following criteria:

- days past due on loans issued by the same borrower;
- collective assessment by reviewing past due status of borrowers with shared credit risk characteristics;
- qualitative assessment of specific indicators of the construction project such as: project delays, performance against budget and remaining costs to complete.

Financial guarantees

CMHC issues financial guarantees for NHA MBS and CMB whereby CMHC guarantees the timely payment of principal and interest to NHA MBS and CMB investors. Upon issuance of a guarantee, CMHC collects a fee which is considered the fair value of the guarantee and is deferred and recognized as revenue over the expected life of the guarantee.

Under the NHA MBS program, a financial institution (the “NHA MBS issuer”) creates a pool of eligible mortgages and sells the pool to investors. The underlying pool of mortgages is designed to provide sufficient cash flows to fund the NHA MBS with the issuer having the obligation to fund any shortfalls that may arise, thus exposing the Corporation to credit risk of the issuer with the underlying pool of mortgages serving as a credit enhancement. This credit enhancement directly affects the likelihood of the issuer defaulting since shortfalls only occur if the underlying pool has provided insufficient cash flows to fund NHA MBS payments to investors. Our assessment of SICR is therefore based on both the credit risk of the issuer and the credit risk of the pool of mortgages underlying the NHA MBS. The pool of mortgages are considered low credit risk since only mortgages insured by CMHC or by approved private mortgage insurers are eligible to be pooled in NHA MBS, all of which carry investment grade credit ratings.

Under the CMB program, the credit risk exposures are, by design, the CMB loans that are the sole source of funds to fulfill CHT’s CMB obligations. As discussed above, the NHA MBS, reinvestment assets and swaps represent the sole source of repayment on the loans. The SICR assessment for the CMB guarantee is based on the credit risk of these supporting assets all of which have been assessed as low credit risk.

We have assessed the TPG under both the NHA MBS and CMB programs as having low credit risk and will apply the low credit risk exemption (stage 1).

Forward looking macroeconomic variables

The Corporation has incorporated forward looking economic information into its ECL by performing the calculation under multiple scenarios resulting in a probability-weighted average ECL based on the weightings of each scenario. We have used three sets of economic scenarios for all instruments representing a baseline, upside and downside scenario.

We performed an economic variable selection process to identify the sets of macroeconomic variables that had the highest correlation with our portfolios. This process resulted in three sets of economic variables that are most highly correlated to our portfolios dependent on the geographic and industry sector of the exposure that include the following variables: unemployment rates, oil prices, 10-year corporate bond spreads and the CBOE Volatility Index.

All macroeconomic variables are projected over a five year period, subsequently reverting to long-run averages. Forecasts and scenarios weightings are prepared by the Corporation annually and reviewed quarterly by a cross-functional committee represented by members of our Capital Markets, Finance, Risk and Market Analysis sectors with recommendations presented to an executive committee for approval.

Impact of adoption of IFRS 9

Reclassifications

The following table compares the carrying amount of financial assets and liabilities under IAS 39 with those under IFRS 9 upon transition at 1 January 2018. We have not restated 2017 comparative information presented under IAS 39. Differences upon transition have been recorded directly in retained earnings.

| Financial instrument type | Notes | IAS 39 | | | IFRS 9 | | |
|--|--------|--------------------------|-----------------|------------------|---------------|-----------------------------|-----------------|
| | | Classification | Carrying Amount | Reclassification | Remeasurement | Classification | Carrying Amount |
| Assets: | | | | | | | |
| Cash and cash equivalents | 1, 7 | Designated at FVTPL | 55 | - | - | Designated at FVTPL | 55 |
| | 1 | Available for sale (AFS) | 67 | - | - | Debt instruments at FVOCI | 67 |
| | 1 | Loans and receivables | 765 | - | - | Amortized cost | 765 |
| Total cash and cash equivalents | | | 887 | - | - | | 887 |
| Accrued interest receivable | 1 | Loans and receivables | 705 | - | - | Amortized Cost | 705 |
| Investment securities | | | | | | | |
| Debt instruments | 1, 7 | Designated at FVTPL | 1,234 | - | - | Designated at FVTPL | 1,234 |
| | 1 | AFS | 20,842 | - | - | Debt instruments at FVOCI | 20,842 |
| | 2 | AFS | 97 | - | - | FVTPL | 97 |
| Common equities | 4 | AFS | 1,105 | - | - | FVTPL | 1,105 |
| Preferred equities | 5 | AFS | 68 | - | - | Equity instruments at FVOCI | 68 |
| Total investment securities | | | 23,346 | - | - | | 23,346 |
| Derivatives Due from government of Canada | 1, 7 | FVTPL | 61 | - | - | FVTPL | 61 |
| Loans | 1, 7 | Designated at FVTPL | 2,906 | - | - | Designated at FVTPL | 2,906 |
| | 1,3, 6 | Loans and receivables | 237,944 | 102 | (5) | Amortized Cost | 238,041 |
| | 3 | Loans and receivables | - | 26 | (6) | FVTPL | 26 |
| | 6 | Loans and receivables | - | 15 | 2 | FVTPL | 17 |
| Total loans | | | 240,850 | 143 | (3) | | 240,990 |
| Accounts receivable and other assets | 3 | | | | | | |
| | 1 | Loans and receivables | 193 | (143) | - | Amortized cost | 50 |
| | | N/A | 642 | - | - | N/A | 642 |
| Total accounts receivable and other assets | | | 835 | (143) | - | | 692 |
| Investment property | | N/A | 305 | - | - | N/A | 305 |
| Total assets | | | 267,115 | - | (3) | | 267,112 |

| Financial instrument type | Notes | IAS 39 | | Reclassification | Remeasurement | IFRS 9 | |
|--|-------|-----------------------------|-----------------|------------------|---------------|---------------------|-----------------|
| | | Classification | Carrying Amount | | | Classification | Carrying Amount |
| Liabilities: | | | | | | | |
| Securities sold under repurchase agreements | 1 | Other financial liabilities | 297 | - | - | Amortized cost | 297 |
| Accrued interest payable | 1 | Other financial liabilities | 545 | - | - | Amortized cost | 545 |
| Dividends payable | 1 | Other financial liabilities | 2,000 | - | - | Amortized cost | 2,000 |
| Derivatives | 1, 7 | FVTPL | 39 | - | - | FVTPL | 39 |
| Borrowings | 1, 7 | Designated at FVTPL | 4,564 | - | - | Designated at FVTPL | 4,564 |
| | 1 | Other financial liabilities | 233,592 | - | - | Amortized cost | 233,592 |
| Total | | | 238,156 | - | - | | 238,156 |
| Total borrowings | 1 | Other financial liabilities | | | | Amortized cost | |
| Accounts payable and other liabilities | | N/A | 481 | | | N/A | 481 |
| | | | 80 | | | | 80 |
| Total accounts payable and other liabilities | | | 561 | | | | 561 |
| Other | | N/A | 7,776 | - | - | N/A | 7,776 |
| Total liabilities | | | 249,374 | - | - | | 249,374 |

Reconciliation of impairment allowance from IAS 39 to IFRS 9

The following table reconciles our opening loss allowance under IAS 39's incurred loss model to our expected credit loss allowance under IFRS 9's expected credit loss model, before tax.

| Measurement Category | Loan loss allowance under IAS 39 ⁸ | Reclassification ⁹ | Remeasurement ¹⁰ | ECL allowance under IFRS 9 |
|--|---|-------------------------------|-----------------------------|----------------------------|
| | 39 ⁸ | | | 9 |
| Debt instruments at AFS (IAS 39) / FVOCI (IFRS 9) Loans and receivables (IAS 39) / Amortized cost (IFRS 9) | - | - | 9 | 9 |
| | 113 | (17) | 5 | 101 |
| Total | 113 | (17) | 14 | 110 |

Impact of transition on Equity of Canada

The following table presents the IFRS 9 and IFRS 15 transitional impacts on accumulated OCI and retained earnings as at January 1, 2018.

| Accumulated other comprehensive income | |
|--|---------------|
| Closing Balance as at 31 December 2017 | 490 |
| Impact of adopting IFRS 9, net of tax: | |
| Impact of reclassifying equity securities from AFS to FVTPL ⁴ | (371) |
| Impact of reclassifying debt instruments from AFS to FVTPL ² | (3) |
| Recognition of ECL on debt instruments at FVOCI ¹⁰ | 6 |
| Total impact of adopting IFRS 9, net of tax | (368) |
| Restated opening balance as at 1 January | 122 |
| 2018 Retained earnings | |
| Closing Balance as at 31 December 2017 | 17,226 |
| Impact of adopting IFRS 15, net of tax | (53) |
| Impact of adopting IFRS 9, net of tax: | |
| Impact of reclassifying equity securities from AFS to FVTPL ⁴ | 371 |
| Impact of reclassifying debt instruments from AFS to FVTPL ² | 3 |
| Recognition of ECL on debt instruments at FVOCI ¹⁰ | (6) |
| Re-measurement of loans reclassified from amortized cost to FVTPL | 2 |
| Re-measurement of ECL on loans at amortized cost ¹⁰ | (4) |
| Total impact of adopting IFRS 9, net of tax | 366 |
| Restated opening balance as at 1 January 2018 | 17,539 |

¹ Financial instruments reclassified to new categories under IFRS 9, as their previous categories under IAS 39 were 'retired', with no changes to their measurement basis.

² In our MLI Activity, at January 1, 2018, we held \$97 million in subordinated debt instruments which were classified as AFS and measured at FVOCI under IAS 39. These instruments fail the SPPI test and are classified as at FVTPL under IFRS 9. Upon transition, \$3 million, net of tax, was reclassified from AOCI to retained earnings.

³ In our MLI Activity, at January 1, 2018, we held \$143 million of loans presented in accounts receivable and other assets that have been reclassified to loans. Of these loans, \$26 million fail the SPPI test and were classified as at FVTPL and \$117 million were classified as amortized cost under IFRS 9.

⁴ Under IAS 39, our common share equity securities and limited partnership units held in our MLI Activity were classified as AFS. Under IFRS 9, equity securities are mandatorily classified as financial assets at FVTPL unless an irrevocable election is made to present fair value changes in OCI. We have not made use of this election and therefore our common equity securities and limited partnership units were re-classified from AFS to FVTPL. Upon transition, \$371 million in unrealized gains (losses), net of tax, were reclassified from AOCI to retained earnings.

⁵ Under IAS 39, preferred equity securities of \$68 million held in our MLI Activity were classified as AFS. Under IFRS 9, we have elected to present fair value changes in OCI. Under this election, there is no recycling of gains and losses from OCI to net income upon derecognition. This differs from our previous practices under AFS where realized gains and losses are recycled to net income when the investment is sold or derecognized.

⁶ Under IAS 39, loans held under the Municipal Infrastructure Lending Program (MILP) within our Assisted Housing Activity were classified as loans and receivables. Under IFRS 9, one loan of \$15 million within this portfolio contains contractual cash flows that fail the SPPI test and has been reclassified to FVTPL. All other loans held within the MILP program pass the SPPI test and are classified and measured at amortized cost under IFRS 9.

⁷ As at the transition date of 1 January 2018, all of our loans, investment securities and borrowings that were previously designated at FVTPL to eliminate an accounting mismatch with derivatives used in economic hedges of interest rate risk will remain so under IFRS 9 as there have been no changes in the structure of the hedges.

⁸ Under IAS 39, loss allowance was recognized against related loan balance and presented in accounts receivable and other assets.

⁹ Reclassification represents the impact to the impairment allowances from classification and measurement changes.

¹⁰ Re-measurement represents the before tax impact to the impairment allowance from the adoption of the IFRS 9 ECL model.

Future accounting changes

There have been no new standards or amendments to existing standards issued by the International Accounting Standards Board (IASB) that would affect CMHC in the future other than those disclosed in Note 3 of our audited consolidated financial statements for the year ended 31 December 2017, and the Conceptual Framework for Financial Reporting indicated below. As disclosed in Note 3 of our audited consolidated financial statements for the year ended 31 December 2017, we will implement IFRS 16 *Leases* and IFRIC 23 *Uncertainty over Income Tax Treatments* on 1 January 2019 and IFRS 17 *Insurance Contracts* on 1 January 2021.

Conceptual Framework for Financial Reporting

In March 2018 the IASB issued the revised *Conceptual Framework for Financial Reporting*, replacing the previous version of the *Conceptual Framework* issued in 2010.

The revised *Conceptual Framework* has an effective date of 1 January 2020, with earlier application permitted, for companies that use the *Conceptual Framework* to develop accounting policies when no IFRS Standard applies to a particular transaction. The revised *Conceptual Framework* includes: a new chapter on measurement, guidance on reporting financial performance, improved definitions and guidance, in particular the definitions of an asset and a liability and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting. We have not yet determined the full impact on our consolidated financial statements.

4. Critical Judgments in Applying Accounting Policies and Making Estimates

The preparation of financial statements requires Management to make various judgments, estimates and assumptions that can significantly affect the amounts recognized in the financial statements. Actual results may differ from these estimates. Where these differ, the impact will be recorded in future periods. Significant judgments and estimates at 30 September 2018 were consistent with those disclosed in Note 4 of our audited consolidated financial statements for the year ended 31 December 2017, with the exception of those related to IFRS 9 effective 1 January 2018 which are described below.

Classification and measurement of financial assets

Business model assessment

The classification and measurement of our debt instruments is dependent on our determination of the business model which is based on the objectives under which our portfolios of financial assets are managed and is based on reasonably expected scenarios. Judgement is required in assessing the business model which considers the criteria described in Note 3.

Solely payments of principal and interest test

As a second step in the classification process of our debt instruments, we assess the contractual terms of our debt instruments to determine whether the cash flows meet the SPPI criteria. To make this assessment we apply judgement and consider relevant factors such as, but not limited to: non-cash distributions; performance-linked features; period for which the interest rate is set; conversion options; equity linked payments; limits on claims to specified assets (non-recourse items).

Measurement of expected credit losses

The measurement of ECL on our financial assets is an area that requires the use of complex models and significant assumptions and judgements that are driven by a number of factors, changes in which can result in different levels of allowances.

Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is described in Note 3.

Elements of the ECL model that are considered accounting judgements and estimates include:

- determining criteria for SICR;
- development of appropriate models and assumptions for the measurement of ECL;
- determination of the economic variables most highly correlated to our portfolios of financial assets; and
- establishing the number and relative weightings of forward-looking macroeconomic scenarios and their effect on economic inputs in the ECL model

5. Segmented Information

The quarterly consolidated financial statements include the Assisted Housing, Mortgage Loan Insurance and Securitization Activities, each of which provides different programs in support of our objectives. The accounts for Canada Housing Trust (CHT), a separate legal entity, are included within the Securitization Activity. The financial results of each activity are determined using the accounting policies described in Note 2 of our audited consolidated financial statements for the year ended 31 December 2017. Revenues are generated and assets are located in Canada.

Revenues for the reportable segments are generated as follows:

- Assisted Housing revenues include parliamentary appropriations and interest income on loans;
- Mortgage Loan Insurance revenues include premiums, fees and investment income; and
- Securitization revenues include guarantee and application fees, investment income and interest income on loans.

| Three months ended 30 September (in millions) | Assisted Housing Activity | | Mortgage Loan Insurance Activity | | Securitization Activity | | Eliminations ¹ | | Total | |
|--|------------------------------|------------|-------------------------------------|------------|----------------------------|------------|---------------------------|-----------|--------------|--------------|
| | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 |
| Interest income | 82 | 93 | - | - | 1,266 | 1,082 | (1) | (2) | 1,347 | 1,173 |
| Interest expense | 80 | 89 | - | - | 1,264 | 1,080 | (27) | (31) | 1,317 | 1,138 |
| Net interest income | 2 | 4 | - | - | 2 | 2 | 26 | 29 | 30 | 35 |
| Parliamentary appropriations for housing programs | 416 | 521 | - | - | - | - | - | - | 416 | 521 |
| Premiums and fees earned | - | - | 358 | 394 | 121 | 98 | - | - | 479 | 492 |
| Investment income (losses) | - | - | 130 | 153 | 17 | 13 | (21) | (21) | 126 | 145 |
| Net gains (losses) on financial instruments | 6 | (2) | (9) | 69 | (1) | (1) | (5) | (1) | (9) | 65 |
| Other income | 7 | 6 | - | - | - | 2 | - | - | 7 | 8 |
| Total revenues and parliamentary appropriations | 431 | 529 | 479 | 616 | 139 | 114 | - | 7 | 1,049 | 1,266 |
| Non-interest expenses | | | | | | | | | | |
| Housing programs | 416 | 521 | - | - | - | - | - | - | 416 | 521 |
| Insurance claims | - | - | 35 | 41 | - | - | - | - | 35 | 41 |
| Operating expenses | 4 | 5 | 67 | 69 | 14 | 12 | - | - | 85 | 86 |
| Total expenses | 420 | 526 | 102 | 110 | 14 | 12 | - | - | 536 | 648 |
| Income before income taxes | 11 | 3 | 377 | 506 | 125 | 102 | - | 7 | 513 | 618 |
| Income taxes | 1 | (1) | 94 | 124 | 31 | 26 | - | 2 | 126 | 151 |
| Net income | 10 | 4 | 283 | 382 | 94 | 76 | - | 5 | 387 | 467 |
| Total revenues and parliamentary appropriations | 431 | 529 | 479 | 616 | 139 | 130 | - | 7 | 1,049 | 1,282 |
| Inter-segment income (loss) ¹ | (1) | - | (26) | (24) | 27 | 31 | - | (7) | - | - |
| External revenues and parliamentary appropriations | 430 | 529 | 453 | 592 | 166 | 161 | - | - | 1,049 | 1,282 |

¹ Inter-segment income relates to the following:

- The Assisted Housing Activity recognizes revenues from investing in holdings of CMB;
- The Mortgage Loan Insurance Activity recognizes revenues from investing in holdings of CMB; and
- Within the Securitization Activity, CHT recognizes interest expense on CMBs held by the Assisted Housing and Mortgage Loan Insurance Activities.

| Nine months ended 30 September (in millions) | Assisted Housing Activity | | Mortgage Loan Insurance Activity | | Securitization Activity | | Eliminations ¹ | | Total | |
|--|------------------------------|--------------|-------------------------------------|--------------|----------------------------|------------|---------------------------|-----------|--------------|--------------|
| | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 |
| Interest income | 253 | 284 | - | - | 3,653 | 3,172 | (3) | (4) | 3,903 | 3,452 |
| Interest expense | 243 | 276 | - | - | 3,645 | 3,164 | (83) | (93) | 3,805 | 3,347 |
| Net interest income | 10 | 8 | - | - | 8 | 8 | 80 | 89 | 98 | 105 |
| Parliamentary appropriations for housing programs | 1,905 | 2,635 | - | - | - | - | - | - | 1,905 | 2,635 |
| Premiums and fees earned | - | - | 1,070 | 1,167 | 351 | 276 | - | - | 1,421 | 1,443 |
| Investment income (losses) | - | - | 405 | 457 | 44 | 36 | (61) | (61) | 388 | 432 |
| Net gains (losses) on financial instruments | (2) | (3) | (46) | 87 | (5) | - | (6) | (4) | (59) | 80 |
| Other income | 20 | 20 | (1) | 2 | 4 | 5 | - | - | 23 | 27 |
| Total revenues and parliamentary appropriations | 1,933 | 2,660 | 1,428 | 1,713 | 402 | 325 | 13 | 24 | 3,776 | 4,722 |
| Non-interest expenses | | | | | | | | | | |
| Housing programs | 1,905 | 2,635 | - | - | - | - | - | - | 1,905 | 2,635 |
| Insurance claims | - | - | 172 | 169 | - | - | - | - | 172 | 169 |
| Operating expenses | 17 | 19 | 227 | 228 | 42 | 38 | - | - | 286 | 285 |
| Total expenses | 1,922 | 2,654 | 399 | 397 | 42 | 38 | - | - | 2,363 | 3,089 |
| Income before income taxes | 11 | 6 | 1,029 | 1,316 | 360 | 287 | 13 | 24 | 1,413 | 1,633 |
| Income taxes | (2) | (3) | 254 | 324 | 90 | 72 | 3 | 6 | 345 | 399 |
| Net income | 13 | 9 | 775 | 992 | 270 | 215 | 10 | 18 | 1,068 | 1,234 |
| Total revenues and parliamentary appropriations | 1,933 | 2,660 | 1,428 | 1,713 | 402 | 376 | 13 | 24 | 3,776 | 4,773 |
| Inter-segment income (loss) ¹ | (3) | (1) | (67) | (68) | 83 | 93 | (13) | (24) | - | - |
| External revenues and parliamentary appropriations | 1,930 | 2,659 | 1,361 | 1,645 | 485 | 469 | - | - | 3,776 | 4,773 |

¹ Inter-segment income relates to the following:

- The Assisted Housing Activity recognizes revenues from investing in holdings of CMB;
- The Mortgage Loan Insurance Activity recognizes revenues from investing in holdings of CMB; and
- Within the Securitization Activity, CHT recognizes interest expense on CMBs held by the Assisted Housing and Mortgage Loan Insurance Activities.

| As at 30 September 2018 and 31 December 2017 (in millions) | Assisted Housing Activity | | Mortgage Loan Insurance Activity | | Securitization Activity | | Eliminations ¹ | | Total | |
|---|---------------------------|-------|----------------------------------|--------|-------------------------|---------|---------------------------|---------|---------|---------|
| | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 |
| Assets | | | | | | | | | | |
| Cash and cash equivalents | 352 | 519 | 464 | 342 | 1 | 26 | - | - | 817 | 887 |
| Securities purchased under resale agreements | - | - | - | - | - | - | - | - | - | - |
| Accrued interest receivable | 114 | 140 | 142 | 140 | 1,062 | 439 | (17) | (14) | 1,301 | 705 |
| Investment securities: | | | | | | | | | | |
| Fair value through profit or loss | 1,573 | 1,630 | 694 | 1 | - | - | (396) | (397) | 1,871 | 1,234 |
| Fair value through other comprehensive income | - | - | 17,899 | - | 3,904 | - | (3,490) | - | 18,313 | - |
| Available for sale | - | - | - | 22,689 | - | 3,608 | - | (4,185) | - | 22,112 |
| Derivatives | 34 | 51 | 11 | 10 | - | - | - | - | 45 | 61 |
| Due from the Government of Canada | 174 | 126 | - | - | - | - | - | - | 174 | 126 |
| Loans: | | | | | | | | | | |
| Fair value through profit or loss | 2,172 | 2,906 | 19 | - | - | - | - | - | 2,191 | 2,906 |
| Amortized cost | 4,321 | 4,158 | 111 | - | 242,207 | 233,786 | - | - | 246,639 | 237,944 |
| Accounts receivable and other assets | 189 | 163 | 614 | 618 | 54 | 54 | - | - | 857 | 835 |
| Investment property | 256 | 256 | 49 | 49 | - | - | - | - | 305 | 305 |
| | 9,185 | 9,949 | 20,003 | 23,849 | 247,228 | 237,913 | (3,903) | (4,596) | 272,513 | 267,115 |
| Liabilities | | | | | | | | | | |
| Securities sold under repurchase agreements | - | - | 458 | 297 | - | - | - | - | 458 | 297 |
| Accounts payable and other liabilities | 293 | 429 | 94 | 101 | 23 | 31 | - | - | 410 | 561 |
| Accrued interest payable | 117 | 129 | - | - | 1,042 | 430 | (17) | (14) | 1,142 | 545 |
| Dividend payable | - | - | 500 | 2,000 | - | - | - | - | 500 | 2,000 |
| Derivatives | 24 | 26 | 22 | 13 | - | - | - | - | 46 | 39 |
| Provision for claims | - | - | 523 | 555 | - | - | - | - | 523 | 555 |
| Borrowings: | | | | | | | | | | |
| Fair value through profit or loss | 3,714 | 4,564 | - | - | - | - | - | - | 3,714 | 4,564 |
| Amortized cost | 4,573 | 4,350 | - | - | 242,207 | 233,786 | (3,928) | (4,544) | 242,852 | 233,592 |
| Defined benefit plans liability | 111 | 181 | 150 | 266 | (6) | 3 | - | - | 255 | 450 |
| Unearned premiums and fees | - | - | 5,359 | 5,352 | 1,453 | 1,335 | - | - | 6,812 | 6,687 |
| Deferred income tax liabilities | 43 | 36 | 102 | 68 | (27) | (8) | 9 | (12) | 127 | 84 |
| | 8,875 | 9,715 | 7,208 | 8,652 | 244,692 | 235,577 | (3,936) | (4,570) | 256,839 | 249,374 |
| Equity of Canada | 310 | 234 | 12,795 | 15,197 | 2,536 | 2,336 | 33 | (26) | 15,674 | 17,741 |
| | 9,185 | 9,949 | 20,003 | 23,849 | 247,228 | 237,913 | (3,903) | (4,596) | 272,513 | 267,115 |

¹ Eliminations remove inter-segment holdings of CMB.

6. Parliamentary Appropriations and Housing Programs Expenses

Parliamentary appropriations were used to fund the following housing programs expenses, including operating expenses incurred to support these programs.

| <i>(in millions)</i> | Three months ended 30 | | Nine months ended 30 | |
|--|-----------------------|------------|----------------------|--------------|
| | September | | September | |
| | 2018 | 2017 | 2018 | 2017 |
| Assistance for housing needs | 390 | 486 | 1,809 | 2,537 |
| Financing for housing | 8 | 17 | 28 | 33 |
| Housing expertise and capacity development | 18 | 18 | 68 | 65 |
| Total | 416 | 521 | 1,905 | 2,635 |

The following table presents the change in the due from the Government of Canada account. The outstanding balance as at 30 September 2018 is mainly composed of Housing programs expenses incurred but not yet reimbursed.

| <i>(in millions)</i> | Three months ended 30 | | Nine months ended 30 | |
|---|-----------------------|------------|----------------------|------------|
| | September | | September | |
| | 2018 | 2017 | 2018 | 2017 |
| Balance at beginning of period | 216 | 304 | 126 | 59 |
| Total appropriations recognized in revenues during the period | 416 | 521 | 1,905 | 2,635 |
| Total appropriations received during the period | (457) | (547) | (1,856) | (2,417) |
| Third party remittances (owing) to the Government of Canada | (1) | - | (1) | 1 |
| Balance at end of period | 174 | 278 | 174 | 278 |

7. Mortgage Loan Insurance

Unearned premiums and fees

The following table presents the changes in the unearned premiums and fees balance.

| <i>(in millions)</i> | Three months ended 30 | | Nine months ended 30 | |
|--|-----------------------|--------------|----------------------|--------------|
| | September | | September | |
| | 2018 | 2017 | 2018 | 2017 |
| Balance at beginning of period | 5,320 | 5,393 | 5,352 | 5,472 |
| Premiums deferred on contracts written in the period | 390 | 399 | 1,056 | 1,076 |
| Premiums earned in the period | (351) | (388) | (1,049) | (1,146) |
| Application fees deferred on contracts written in the period | 4 | 4 | 11 | 13 |
| Application fees earned in the period ¹ | (4) | (4) | (11) | (11) |
| Balance at end of period | 5,359 | 5,404 | 5,359 | 5,404 |

¹ Only includes earned application fees on multi-unit residential loans during the period. Application fee revenue earned on low loan-to-value transactional homeowner application fees are earned immediately as they are received.

Deferred acquisition costs

Deferred acquisition costs (DAC) are included in accounts receivable and other assets. The following table presents the changes in the DAC balance.

| <i>(in millions)</i> | Three months ended 30 | | Nine months ended 30 | |
|---------------------------------|-----------------------|------------|----------------------|------------|
| | September | | September | |
| | 2018 | 2017 | 2018 | 2017 |
| Balance at beginning of period | 172 | 157 | 165 | 149 |
| Acquisition costs deferred | 14 | 15 | 45 | 45 |
| Amortization of DAC | (12) | (11) | (36) | (33) |
| Balance at end of period | 174 | 161 | 174 | 161 |

Provision for claims

The provision for claims includes amounts set aside for claims incurred but not reported (IBNR), claims incurred but not enough reported (IBNER), claims in process (CIP) and social housing and index-linked mortgages (SH/ILM).

Provision for claims comprises the following:

| <i>(in millions)</i> | As at | | | | | |
|--|---------------------------|------------|------------|---------------------------|------------|------------|
| | 30 September 2018 | | | 31 December 2017 | | |
| | IBNR, IBNER and CIP | SH/ILM | Total | IBNR, IBNER and CIP | SH/ILM | Total |
| Undiscounted estimated losses | 352 | 145 | 497 | 364 | 158 | 522 |
| Discounting | (7) | (19) | (26) | (6) | (17) | (23) |
| Discounted provision for adverse deviation | 26 | 26 | 52 | 27 | 29 | 56 |
| Total provision for claims | 371 | 152 | 523 | 385 | 170 | 555 |

The following table presents the changes in the provision for claims balance.

| <i>(in millions)</i> | Three months ended 30 September | | | | | |
|--|---------------------------------|------------|------------|---------------------------|------------|------------|
| | 2018 | | | 2017 | | |
| | IBNR, IBNER and CIP | SH/ILM | Total | IBNR, IBNER and CIP | SH/ILM | Total |
| Provision for claims, beginning of period | 380 | 158 | 538 | 444 | 164 | 608 |
| Net claims (paid) recovered during the period | (60) | 1 | (59) | (74) | (1) | (75) |
| Provision for claims provided for and losses incurred during the period ¹ | 58 | - | 58 | 68 | (3) | 65 |
| Unfavourable (favourable) development on prior period claims | (7) | (7) | (14) | (12) | - | (12) |
| Provision for claims, end of period | 371 | 152 | 523 | 426 | 160 | 586 |

¹ Included as part of insurance claims on the consolidated statements of income and comprehensive income. Provision for claims provided for and losses may not equal insurance claims expense as certain expenses incurred do not impact the provision for claims.

| <i>(in millions)</i> | Nine months ended 30 September | | | | | |
|--|--------------------------------|------------|------------|---------------------------|------------|------------|
| | 2018 | | | 2017 | | |
| | IBNR, IBNER and CIP | SH/ILM | Total | IBNR, IBNER and CIP | SH/ILM | Total |
| Provision for claims, beginning of period | 385 | 170 | 555 | 475 | 179 | 654 |
| Net claims (paid) recovered during the period | (182) | (3) | (185) | (245) | - | (245) |
| Provision for claims provided for and losses incurred during the period ¹ | 174 | 1 | 175 | 201 | (2) | 199 |
| Unfavourable (favourable) development on prior period claims | (6) | (16) | (22) | (5) | (17) | (22) |
| Provision for claims, end of period | 371 | 152 | 523 | 426 | 160 | 586 |

¹ Included as part of insurance claims on the consolidated statements of income and comprehensive income. Provision for claims provided for and losses may not equal insurance claims expense as certain expenses incurred do not impact the provision for claims.

Insurance policy liability adequacy

We perform a liability adequacy test on the premium liabilities and claim liabilities quarterly. Premium liabilities represent a provision for future claims and expenses that are expected to arise from the unearned portion of the policies in-force. Thus, this provision is for claims that have not yet occurred and, therefore, covers the period from the date of the valuation to the date of default (the assumed claim occurrence date).

The liability adequacy test for the Corporation as at 30 September 2018 has identified that no premium deficiency reserve is required.

8. Securitization

We guarantee the timely payment of principal and interest of CMB issued by CHT under the CMB program and NHA MBS issued by Approved Issuers on the basis of housing loans under the NHA MBS program in the event that an issuer is unable to satisfy its obligations under these programs. In that circumstance, we will mitigate our loss by realizing on the collateral securing the obligations under each of the programs.

At the balance sheet date, the Corporation has not received a claim on its TPG. As such, no provision in addition to the remaining unearned premium is required.

ECL on our TPG's have been assessed as immaterial at 30 September 2018 and are lower than the balance of unearned fees and therefore have not been recognized.

The following table presents the changes in the unearned premiums and fees balance.

| (in millions) | Three months ended 30 September | | | | | |
|-----------------------------------|---------------------------------|------------|--------------|------------|------------|--------------|
| | 2018 | | | 2017 | | |
| | NHA MBS | CMB | Total | NHA MBS | CMB | Total |
| Balance at beginning of period | 933 | 485 | 1,418 | 687 | 463 | 1,150 |
| TPG and application fees received | 119 | 37 | 156 | 100 | 34 | 134 |
| TPG and application fees earned | (89) | (32) | (121) | (70) | (28) | (98) |
| Balance at end of period | 963 | 490 | 1,453 | 717 | 469 | 1,186 |

| (in millions) | Nine months ended 30 September | | | | | |
|--|--------------------------------|------------|--------------|------------|------------|--------------|
| | 2018 | | | 2017 | | |
| | NHA MBS | CMB | Total | NHA MBS | CMB | Total |
| Balance reported at the end of the previous year | 859 | 476 | 1,335 | 648 | 444 | 1,092 |
| IFRS 15 adjustment for application fees | 72 | - | 72 | - | - | - |
| Restated opening balance | 931 | 476 | 1,407 | 648 | 444 | 1,092 |
| TPG and application fees received | 289 | 108 | 397 | 260 | 110 | 370 |
| TPG and application fees earned | (257) | (94) | (351) | (191) | (85) | (276) |
| Balance at end of period | 963 | 490 | 1,453 | 717 | 469 | 1,186 |

9. Capital Management

For capital management, we consider our capital available to be equal to the total equity of Canada less assets with a capital requirement of 100%.

Our primary objective with respect to capital management is to ensure that our commercial operations have adequate capital to deliver their mandate while remaining financially self-sustaining and also to follow prudent business practices and guidelines existing in the private sector as appropriate. Beyond the \$25 million capital prescribed by the CMHC Act, we currently have no externally imposed minimal capital requirements; however, we voluntarily follow guidelines set out by the Office of the Superintendent of Financial Institutions (OSFI).

We perform an Own Risk & Solvency Assessment, which is an integrated process that evaluates capital adequacy on both a regulatory and economic capital basis and is used to establish capital targets taking into consideration our strategy and risk appetite. Our 'Own View' of capital needs is determined by identifying our risks and evaluating whether or not an explicit amount of capital is necessary to absorb losses from each risk. With the above we have also met the requirements of the CMHC Act and the NHA.

We set an internal target for our commercial operations at a level that is expected to cover all material risks. The internal target is calibrated using specified confidence intervals and is designed to provide Management with an early indication of the need to resolve financial problems. Under our Capital Management Policy, we operate at available capital levels above the internal target on all but unusual and infrequent occasions. Accordingly, we have established an operating level (holding target) for our commercial operations in excess of our internal target. The operating level is calibrated using confidence

intervals specified by our Capital Management Policy and is designed to provide Management with adequate time to resolve financial problems before available capital decreases below the internal target.

Beginning in 2017, we started making dividend payments to the Government from our Mortgage Loan Insurance Activity to the extent there are profits and retained earnings not allocated to reserves, capitalization or to meet the needs of the Corporation for purposes of the NHA, CMHC Act or any other purpose authorized by Parliament relating to housing. However, our capital is not managed to issue a dividend. The following table presents the change in the dividend payable balance.

| <i>(in millions)</i> | Dividend declarations ¹ | | Amount payable | Amount paid | Dividend payable |
|-----------------------|------------------------------------|--------|---------------------|-------------------|----------------------|
| | Date | Amount | at 31 December 2017 | during the period | at 30 September 2018 |
| 2017 Special dividend | 29 June 2017 | 4,000 | 2,000 | 2,000 | - |
| Quarterly dividend | 22 March 2018 | 1,000 | - | 1,000 | - |
| Quarterly dividend | 24 May 2018 | 1,000 | - | 1,000 | - |
| Quarterly dividend | 23 August 2018 | 1,000 | - | 500 | 500 |
| | | | 2,000 | 4,500 | 500 |

¹ Dividends declared in 2017 and paid in full by 31 December 2017 have been excluded from the table.

The components of consolidated capital available are presented below.

| <i>(in millions)</i> | As at | |
|---|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Contributed capital | 25 | 25 |
| Accumulated other comprehensive income (loss) | (112) | 490 |
| Appropriated retained earnings | 13,974 | 14,918 |
| Unappropriated retained earnings ¹ | 1,787 | 2,308 |
| Total equity of Canada² | 15,674 | 17,741 |
| Less: assets with a capital requirement of 100% | (20) | (10) |
| Total capital available | 15,654 | 17,731 |

¹ Unappropriated retained earnings represents retained earnings in excess of our operating level for the Mortgage Loan Insurance and Securitization Activities.

² Equity of Canada includes the impact of eliminations.

Mortgage Loan Insurance capital

The following table presents the components of capital available.

| <i>(in millions, unless otherwise indicated)</i> | As at | |
|--|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Appropriated capital ¹ | 12,069 | 13,648 |
| Unappropriated capital | 726 | 1,549 |
| Total mortgage loan insurance capital | 12,795 | 15,197 |
| Less: assets with a capital requirement of 100% | (20) | (10) |
| Total mortgage loan insurance capital available | 12,775 | 15,187 |
| Internal target | 155% | 155% |
| Operating level | 165% | 165% |
| Capital available to minimum capital required (% MCT) ² | 175% | 184% |

¹ We appropriate retained earnings and AOCI at the operating level of 165% of MCT.

² We have not made use of transitional arrangements as provided by the OSFI Advisory. Our MCT ratio as at 30 September 2018 would be 183% (31 December 2017 – 211%) with transitional arrangements.

Securitization capital

The following table presents the components of the capital available.

| <i>(in millions, unless otherwise indicated)</i> | As at | |
|--|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Appropriated capital ¹ | 1,705 | 1,724 |
| Unappropriated capital | 831 | 612 |
| Total securitization capital available | 2,536 | 2,336 |
| Capital available to capital required (%) | 149% | 135% |

¹ We appropriate retained earnings and AOCI at the operating level (capital required) which is set at 110% of economic capital. Our internal target is set at 105% of economic capital.

Assisted Housing capital

Lending programs

We maintain a reserve fund pursuant to Section 29 of the CMHC Act. A portion of the Lending programs' earnings is retained in this reserve fund as part of our strategy to address interest rate risk exposure on pre-payable loans as well as credit risk exposure on unsecured loans. The reserve fund is subject to a statutory limit of \$240 million (2017 – \$240 million). Should the statutory limit be exceeded, we would be required to pay the excess to the Government.

Unrealized fair value fluctuations as well as remeasurement losses on defined benefit plans are absorbed in retained earnings. The Housing programs' portion of remeasurements is recorded in retained earnings until it is reimbursed by the Government through housing programs appropriations.

The following table presents the components of the capital available.

| <i>(in millions)</i> | As at | |
|---|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Reserve fund | 112 | 116 |
| Retained earnings | 173 | 93 |
| Total Lending programs capital available | 285 | 209 |

Housing programs

We do not hold capital for housing programs as this activity does not present risks to the Corporation that would require capital to be set aside.

10. Fair Value Measurement

We measure certain financial instruments and non-financial assets at fair value in the consolidated balance sheet and disclose the fair value of certain other items. Fair value is determined using a consistent measurement framework.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. Fair value measurement of non-financial assets (i.e. investment property) takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use. For financial instruments, accrued interest is separately recorded and disclosed.

Fair value hierarchy

The methods used to measure fair value make maximum use of relevant observable inputs and minimize the use of unobservable inputs. Fair value measurements are classified in a fair value hierarchy as level 1, 2 or 3 according to the observability of the most significant inputs used in making the measurements.

Level 1: Assets and liabilities that are measured based on unadjusted quoted prices in active markets for identical assets or liabilities. An active market is one where transactions are occurring with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2: Assets and liabilities that are measured based on observable inputs other than level 1 prices. Level 2 inputs include prices obtained from third-party pricing services based on independent dealers' quotes for identical assets or liabilities in markets that are not considered sufficiently active. Level 2 also includes fair values obtained by discounting expected future cash flows, making maximum use of directly or indirectly observable market data such as yield curves and implied forward curves constructed from foreign exchange rates, benchmark interest rates and credit spreads of identical or similar assets or liabilities.

Level 3: Assets and liabilities not quoted in active markets that are measured using valuation techniques. Where possible, inputs to the valuation techniques are based on observable market data, such as yield curves and implied forward curves constructed from benchmark interest rates and credit spreads of similar assets or liabilities. Where observable inputs are not available, unobservable inputs are used. For level 3 assets and liabilities, unobservable inputs are significant to the overall measurement of fair value.

Generally, the unit of account for a financial instrument is the individual instrument, and valuation adjustments are applied at an individual instrument level, consistent with that unit of account.

Comparison of carrying and fair values for financial instruments not carried at fair value

The following table compares the carrying and fair values of financial instruments not carried at fair value. Carrying value is the amount at which an item is measured in the consolidated balance sheet.

| (in millions) | As at | | | | | |
|---|-------------------|------------|---------------------------------|------------------|------------|--------------------------------|
| | 30 September 2018 | | | 31 December 2017 | | |
| | Carrying value | Fair value | Fair value under carrying value | Carrying value | Fair value | Fair value over carrying value |
| Financial assets | | | | | | |
| Loans at amortized cost ¹ | 246,639 | 245,007 | (1,632) | 237,944 | 239,137 | 1,193 |
| Financial liabilities | | | | | | |
| Borrowings at amortized cost ² | 242,852 | 241,374 | (1,478) | 233,592 | 234,918 | 1,326 |

¹ \$244,896 million (31 December 2017 – \$239,137 million) fair value categorized as level 2, \$111 million (31 December 2017 – nil) fair value categorized as level 3.

² \$115,264 million (31 December 2017 – \$111,380 million) fair value categorized as level 1, \$126,110 million (31 December 2017 – \$123,538 million) fair value categorized as level 2.

Fair value hierarchy for items carried at fair value

The following table presents the fair value hierarchy for assets and liabilities carried at fair value in the consolidated balance sheet.

| <i>(in millions)</i> | As at | | | | | | | |
|--|-------------------|---------------|------------|---------------|------------------|---------------|------------|---------------|
| | 30 September 2018 | | | | 31 December 2017 | | | |
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | | | | | |
| Cash equivalents | | | | | | | | |
| Interest bearing deposits with banks | - | 14 | - | 14 | - | 55 | - | 55 |
| Federal government issued | 4 | - | - | 4 | 67 | - | - | 67 |
| Total cash equivalents | 4 | 14 | - | 18 | 67 | 55 | - | 122 |
| Investment securities | | | | | | | | |
| FVTPL | | | | | | | | |
| Debt instruments | | | | | | | | |
| Corporate/other entities | - | 426 | - | 426 | - | 373 | - | 373 |
| Provinces/municipalities | 176 | 255 | - | 431 | 78 | 399 | - | 477 |
| Sovereign and related entities | - | 365 | - | 365 | - | 384 | - | 384 |
| Equities | | | | | | | | |
| Canadian common shares | 554 | - | - | 554 | - | - | - | - |
| Limited partnership units | - | - | 95 | 95 | - | - | - | - |
| Total at FVTPL | 730 | 1,046 | 95 | 1,871 | 78 | 1,156 | - | 1,234 |
| FVOCI | | | | | | | | |
| Debt instruments | | | | | | | | |
| Corporate/other entities | 1,482 | 7,462 | - | 8,944 | - | - | - | - |
| Federal government issued | 4,186 | 52 | - | 4,238 | - | - | - | - |
| Provinces/municipalities | 2,006 | 2,748 | - | 4,754 | - | - | - | - |
| Sovereign and related entities | - | 266 | - | 266 | - | - | - | - |
| Equities | | | | | | | | |
| Canadian preferred shares | 111 | - | - | 111 | - | - | - | - |
| Total at FVOCI | 7,785 | 10,528 | - | 18,313 | - | - | - | - |
| AFS | | | | | | | | |
| Debt instruments | | | | | | | | |
| Corporate/other entities | - | - | - | - | 1,010 | 9,663 | - | 10,673 |
| Federal government issued | - | - | - | - | 4,105 | 86 | - | 4,191 |
| Provinces/municipalities | - | - | - | - | 2,054 | 3,734 | - | 5,788 |
| Sovereign and related entities | - | - | - | - | - | 287 | - | 287 |
| Equities | | | | | | | | |
| Canadian common shares | - | - | - | - | 1,017 | - | - | 1,017 |
| Limited partnership units | - | - | - | - | - | - | 88 | 88 |
| Canadian preferred shares | - | - | - | - | 68 | - | - | 68 |
| Total AFS | - | - | - | - | 8,254 | 13,770 | 88 | 22,112 |
| Loans designated at FVTPL | - | 2,156 | - | 2,156 | - | 2,906 | - | 2,906 |
| Loans mandatorily at FVTPL | - | 16 | 19 | 35 | - | - | - | - |
| Derivatives | - | 45 | - | 45 | - | 61 | - | 61 |
| Investment property | - | - | 305 | 305 | - | - | 305 | 305 |
| Total assets carried at fair value | 8,519 | 13,805 | 419 | 22,743 | 8,399 | 17,948 | 393 | 26,740 |
| Liabilities | | | | | | | | |
| Borrowings designated at FVTPL | - | 3,714 | - | 3,714 | - | 4,564 | - | 4,564 |
| Derivatives | - | 46 | - | 46 | - | 39 | - | 39 |
| Total liabilities carried at fair value | - | 3,760 | - | 3,760 | - | 4,603 | - | 4,603 |

Transfers between fair value hierarchy levels

For assets and liabilities measured at fair value on a recurring basis, we determine if reclassifications have occurred between levels in the hierarchy by re-assessing categorization at the end of each reporting period. Transfers are dependent on our assessment of market trading activity of the last month of each reporting period using internal classification criteria. Transfers between levels are deemed to occur at the beginning of the quarter in which the transfer occurs. During the three and nine months ended 30 September 2018, there were \$494 million and \$2,187 million of transfers from level 2 to level 1, respectively (three and nine months ended 30 September 2017 - \$334 million and \$1,993 million). During the three and nine months ended 30 September 2018, there were \$1,347 million and \$1,769 million of transfers from level 1 to level 2 respectively (three and nine months ended 30 September 2017 - \$687 million and \$2,600 million).

Change in fair value measurement for items classified as level 3

The following table presents the change in fair value for items carried at fair value and classified as level 3.

| <i>(in millions)</i> | Investment securities | | | Loans - FVTPL ³ | Investment property | Total |
|---|--|--|-----------------------------------|-------------------------------|------------------------|-------|
| | FVTPL – asset backed securities | Equities at FVTPL – limited partnership units ⁴ | Total investment securities | | | |
| Three months ended 30 September 2018 | | | | | | |
| Fair value as at 1 July 2018 | - | 92 | 92 | 22 | 305 | 419 |
| Purchases | - | 3 | 3 | 9 | - | 12 |
| Net gains in net income ^{1,2} | - | - | - | - | - | - |
| Cash receipts on settlements/disposals | - | - | - | (12) | - | (12) |
| Fair value as at 30 September 2018 | - | 95 | 95 | 19 | 305 | 419 |
| Nine months ended 30 September 2018 | | | | | | |
| Fair value as at 1 January 2018 | - | 88 | 88 | 26 | 305 | 419 |
| Purchases | - | 9 | 9 | 34 | - | 43 |
| Net gains in net income ^{1,2} | - | 3 | 3 | - | - | 3 |
| Cash receipts on settlements/disposals | - | (5) | (5) | (41) | - | (46) |
| Fair value as at 30 September 2018 | - | 95 | 95 | 19 | 305 | 419 |
| Three months ended 30 September 2017 | | | | | | |
| Fair value as at 1 July 2017 | - | 49 | 49 | - | 267 | 316 |
| Purchases | - | 4 | 4 | - | - | 4 |
| Net gains in net income ^{1,2} | - | - | - | - | - | - |
| Gains in OCI | - | 2 | 2 | - | - | 2 |
| Cash receipts on settlements/disposals | - | (2) | (2) | - | - | (2) |
| Fair value as at 30 September 2017 | - | 53 | 53 | - | 267 | 320 |
| Nine months ended 30 September 2017 | | | | | | |
| Fair value as at 1 January 2017 | 137 | 38 | 175 | - | 267 | 442 |
| Purchases | - | 13 | 13 | - | - | 13 |
| Net gains in net income ^{1,2} | - | - | - | - | - | - |
| Gains in OCI | - | 5 | 5 | - | - | 5 |
| Cash receipts on settlements/disposals | (137) | (3) | (140) | - | - | (140) |
| Fair value as at 30 September 2017 | - | 53 | 53 | - | 267 | 320 |

¹ Included in net gains (losses) on financial instruments for investment securities; other income for investment property.

² Solely relates to unrealized gains for assets held at the end of the respective periods.

³ Consists of MLI Activity loans that were reclassified from accounts receivable and other assets to loans at FVTPL as at 1 January 2018.

⁴ Under IAS 39, limited partnership units were previously classified as AFS.

Unobservable inputs for items classified as level 3

The valuations of items classified as level 3 use unobservable inputs, changes in which may significantly affect the measurement of fair value. Valuations were based on assessments of the prevailing conditions at 30 September 2018, which may change materially in subsequent periods. The following table presents quantitative information about the significant unobservable inputs used in level 3 fair value measurements for items carried at fair value.

| <i>(in millions, unless otherwise indicated)</i> | Valuation technique | Unobservable inputs | 30 September 2018 | | 31 December 2017 | |
|--|-----------------------------|---|---------------------|------------------------------------|---------------------|------------------------------------|
| | | | Asset fair value | Weighted average input/range | Asset fair value | Weighted average input/range |
| Investment securities | | | | | | |
| Equities at FVTPL - Limited partnership units ¹ | Share of partnership equity | Reported partnership equity | 95 | n.a. | 88 | n.a. |
| Investment property | | | | | | |
| Mortgage Loan Insurance Activity | Discounted cash flow | Estimated rental value per square foot Discount rate | 49 | \$16 - \$42 7% | 49 | \$16 - \$42 7% |
| Assisted Housing Activity | Discounted cash flow | Estimated rental value per square foot | 21 | \$25 - \$149 | 21 | \$25 - \$149 |
| | | Discount rate | | 4% - 6% | | 4% - 6% |
| | Market approach | Value per square foot | 235 | \$0 - \$491 | 235 | \$0 - \$491 |
| Total investment property | | | 305 | | 305 | |
| Loans at FVTPL | | | | | | |
| MLI activity workout loans | Discounted cash flow | Loss rate | 10 | - | - | - |
| MLI activity mortgage assignments | Market approach | Value per square foot | 9 | \$11-330 | - | - |
| Total loans at FVTPL | | | 19 | | | |
| Total level 3 items carried at fair value | | | 419 | | 393 | |

¹ Under IAS 39, limited partnership units were previously classified as AFS

Level 3 sensitivity analysis

Investment property

For investment property, increases (decreases) in estimated rental value and price per square foot could result in a significantly higher (lower) fair value of the properties. Increases (decreases) in discount rates could result in a significantly lower (higher) fair value.

11. Cash and Cash Equivalents

The following table provides a breakdown of our cash and cash equivalents:

| <i>(in millions)</i> | As at | | | | | | | |
|--|-------------------|----------|-----------|------------|-----------------------|-----------|-----------|------------|
| | 30 September 2018 | | | | 31 December 2017 | | | |
| | Amortized cost | FVOCI | FVTPL | Total | Loans and receivables | AFS | FVTPL | Total |
| Cash | - | - | - | - | 3 | - | - | 3 |
| Interest-bearing deposits with banks | 301 | - | 14 | 315 | 450 | - | 55 | 505 |
| Corporate/other entities | 198 | - | - | 198 | 208 | - | - | 208 |
| Federal government issued | - | 4 | - | 4 | - | 67 | - | 67 |
| Provinces/municipalities | 300 | - | - | 300 | 104 | - | - | 104 |
| Total cash and cash equivalents | 799 | 4 | 14 | 817 | 765 | 67 | 55 | 887 |

We have \$78 million of cash and cash equivalents as at 30 September 2018 (31 December 2017 – \$80 million) that relates to funds received from the Government that may only be used as part of the Affordable Rental Housing Innovation Fund.

We also have \$198 million of cash and cash equivalents (31 December 2017 – \$75 million) that may only be used as part of the Rental Construction Financing initiative.

12. Investment Securities

The following table shows the cumulative unrealized gains (losses) on investment securities recorded at fair value.

| <i>(in millions)</i> | As at | | | | | | | |
|----------------------|-----------------------------|-----------------------------------|------------------------------------|------------|-----------------------------|-----------------------------------|------------------------------------|------------|
| | 30 September 2018 | | | | 31 December 2017 | | | |
| | Amortized cost ¹ | Gross cumulative unrealized gains | Gross cumulative unrealized losses | Fair value | Amortized cost ¹ | Gross cumulative unrealized gains | Gross cumulative unrealized losses | Fair value |
| Debt instruments | | | | | | | | |
| FVTPL | 1,232 | 2 | (13) | 1,221 | 1,242 | 2 | (10) | 1,234 |
| FVOCI ² | 18,387 | 115 | (300) | 18,202 | - | - | - | - |
| AFS | - | - | - | - | 20,837 | 264 | (162) | 20,939 |
| Equities | | | | | | | | |
| FVTPL | 384 | 269 | (3) | 650 | - | - | - | - |
| FVOCI | 110 | 3 | (2) | 111 | - | - | - | - |
| AFS | - | - | - | - | 670 | 504 | (1) | 1,173 |

¹ Amortized cost for equities is acquisition cost less impairment losses, if any.

² Includes debt instruments denominated in U.S. dollars with a carrying value of \$2,148 million (31 December 2017 - \$1,792 million)

We have investment securities of \$452 million (31 December 2017 – \$295 million) that are part of securities sold under repurchase agreements with terms that do not exceed 93 days. We continue to earn investment income and recognize in OCI changes in fair value on these investment securities during the period, with the exception of investments in CHT-issued CMB, which are eliminated from the consolidated financial statements.

Credit quality – FVOCI

The following table presents the credit quality of debt instruments held at FVOCI, all of which have an ECL allowance based on 12-month ECL. Credit ratings are based on our internal credit rating system and amounts in the table represent the fair value of the financial asset.

| <i>(in millions)</i> | As at 30 September 2018 | | | | |
|------------------------------------|-------------------------|------------|----------|--------------|--------|
| | AAA | AA- to AA+ | A- to A+ | BBB- to BBB+ | Total |
| Investment securities ¹ | 5,072 | 2,030 | 9,523 | 1,577 | 18,202 |

¹ The internal credit ratings are based upon internal assessments of the counterparty creditworthiness. These ratings correspond to those provided by the credit rating agencies except in cases where stand-alone ratings exist. A counterparty internal credit rating cannot be higher than the highest stand-alone rating from any of the agencies. A stand-alone rating removes the assumption of Government support from the rating.

Expected credit losses – FVOCI

The ECL allowance for debt instruments held at FVOCI was \$6 million at 30 September 2018 and there was a decrease of \$1 million and \$3 million in ECL recognized in net gains (losses) on financial instruments for these securities during the three and nine months ended 30 September 2018 respectively.

There were no impairment losses recognized in net gains (losses) on financial instruments for investment securities during the three or nine months ended 30 September 2017 and no reversals of previously realized debt instrument impairments.

13. Loans

The following table presents the cash flows and non-cash changes for loans.

| <i>(in millions)</i> | Three months ended 30 September | | | | | | | Balance at end of period |
|--|---------------------------------------|----------------|---------------|--------------------|-----------|----------|------------------------|--------------------------|
| | Restated opening balance ⁴ | Cash flows | | Non-cash changes | | | | |
| | | Repayments | Disbursements | Fair value changes | Accretion | ECL | Transfers ¹ | |
| 2018 | | | | | | | | |
| FVTPL | | | | | | | | |
| Lending programs designated at FVTPL | 2,351 | (84) | - | (8) | - | - | (104) | 2,155 |
| Loans mandatorily at FVTPL ² | 39 | (12) | 9 | - | - | - | - | 36 |
| Total at FVTPL | 2,390 | (96) | 9 | (8) | - | - | (104) | 2,191 |
| Amortized cost³ | | | | | | | | |
| Loans under the CMB program | 237,170 | (4,950) | 9,977 | - | 10 | - | - | 242,207 |
| Lending programs | 4,273 | (131) | 75 | - | - | - | 104 | 4,321 |
| MLI Activity loans ² | 110 | (8) | 2 | - | 2 | 5 | - | 111 |
| Total amortized cost | 241,553 | (5,089) | 10,054 | - | 12 | 5 | 104 | 246,639 |
| Total | 243,943 | (5,185) | 10,063 | (8) | 12 | 5 | - | 248,830 |
| 2017 | | | | | | | | |
| Designated at FVTPL | | | | | | | | |
| Lending programs | 3,389 | (115) | - | (24) | - | - | (153) | 3,097 |
| Loans and receivables³ | | | | | | | | |
| Loans under the CMB program | 229,333 | (4,948) | 9,552 | - | 10 | - | - | 233,947 |
| Lending programs | 4,114 | (151) | 32 | - | - | - | 153 | 4,148 |
| Total loans and receivables | 233,447 | (5,099) | 9,584 | - | 10 | - | 153 | 238,095 |
| Total | 236,836 | (5,214) | 9,584 | (24) | 10 | - | - | 241,192 |

¹ Transfers are matured loans that have been renewed where the new loans are no longer part of a portfolio of economically hedged loans and borrowings and therefore classified at amortized cost

² Includes MLI Activity loans that were previously classified within accounts receivable and other assets but were reclassified to loans at FVTPL and amortized cost as at 1 January 2018.

³ On 1 January 2018, upon adoption of IFRS 9, loans and receivables were renamed to loans at amortized cost.

⁴ Restated opening balances for the 2018 period are presented in accordance with IFRS 9. Reclassifications and remeasurements upon transition from IAS 39 to IFRS 9 are presented in Note 3.

| (in millions) | Nine months ended 30 September | | | | | | | Balance at end of period |
|--|---------------------------------------|-----------------|---------------|--------------------|-----------|------------|------------------------|--------------------------|
| | Restated opening balance ⁴ | Cash flows | | Non-cash changes | | | | |
| | | Repayments | Disbursements | Fair value changes | Accretion | ECL | Transfers ¹ | |
| 2018 | | | | | | | | |
| FVTPL | | | | | | | | |
| Lending programs designated at FVTPL | 2,906 | (278) | - | (17) | - | - | (456) | 2,155 |
| Loans mandatorily at FVTPL ² | 43 | (41) | 34 | - | - | - | - | 36 |
| Total at FVTPL | 2,949 | (319) | 34 | (17) | - | - | (456) | 2,191 |
| Amortized cost³ | | | | | | | | |
| Loans under the CMB program | 233,786 | (21,050) | 29,441 | - | 30 | - | - | 242,207 |
| Lending programs | 4,138 | (455) | 183 | - | - | (1) | 456 | 4,321 |
| MLI Activity loans ² | 117 | (15) | 8 | - | 2 | (1) | - | 111 |
| Total amortized cost | 238,041 | (21,520) | 29,632 | - | 32 | (2) | 456 | 246,639 |
| Total | 240,990 | (21,839) | 29,666 | (17) | 32 | (2) | - | 248,830 |
| 2017 | | | | | | | | |
| Designated at FVTPL | | | | | | | | |
| Lending programs | 4,020 | (356) | - | (53) | - | - | (514) | 3,097 |
| Loans and receivables³ | | | | | | | | |
| Loans under the CMB program | 223,315 | (19,800) | 30,403 | - | 29 | - | - | 233,947 |
| Lending programs | 3,995 | (451) | 90 | - | - | - | 514 | 4,148 |
| Total loans and receivables | 227,310 | (20,251) | 30,493 | - | 29 | - | 514 | 238,095 |
| Total | 231,330 | (20,607) | 30,493 | (53) | 29 | - | - | 241,192 |

¹ Transfers are matured loans whose terms have been renewed where the new loans are no longer part of a portfolio of economically hedged loans and borrowings and therefore classified at amortized cost

² Includes MLI Activity loans that were previously classified within accounts receivable and other assets but were reclassified to loans at FVTPL and amortized cost as at 1 January 2018.

³ On 1 January 2018, upon adoption of IFRS 9, loans and receivables were renamed to loans at amortized cost.

⁴ Restated opening balances for the 2018 period are presented in accordance with IFRS 9. Reclassifications and remeasurements upon transition from IAS 39 to IFRS 9 are presented in Note 3.

Credit quality – amortized cost

The following table presents the credit quality of loans at amortized cost, presented separately for those based on 12-month or lifetime ECL. For loans where past due information is used as the primary criteria in assessing SICR, aging of loans past due from contractual due date is presented. For loans where past due information is not the primary criteria used in assessing SICR, credit quality is presented by credit rating category based on our internal credit rating system. Amounts in the table represent the gross carrying amount of the financial asset.

| Loans at amortized cost (in millions) | As at 30 September 2018 | | | | POCI | Total |
|---|-------------------------|---|---|------------|------------|----------------|
| | Stage 1: 12-month ECL | Stage 2: Lifetime ECL (not credit impaired) | Stage 3: Lifetime ECL (credit impaired) | | | |
| Days past due: | | | | | | |
| 0-30 days | 2,416 | - | - | - | - | 2,416 |
| 30-90 | - | 1 | - | - | - | 1 |
| 90+ | - | - | 102 | - | - | 102 |
| POCI | - | - | - | - | 117 | 117 |
| Total gross carrying amount | 2,416 | 1 | 102 | 117 | 117 | 2,636 |
| Internal credit ratings¹: | | | | | | |
| AAA | - | - | - | - | - | - |
| AA- to AA+ | 714 | - | - | - | - | 714 |
| A- to A+ | 318 | - | - | - | - | 318 |
| BBB- to BBB+ | 867 | - | - | - | - | 867 |
| Total gross carrying amount | 1,899 | - | - | - | - | 1,899 |
| Total | 4,315 | 1 | 102 | 117 | 117 | 4,535 |
| ECL allowance | (1) | - | (42) | (60) | (60) | (103) |
| Total, net of ECL allowance | 4,314 | 1 | 60 | 57 | 57 | 4,432 |
| Loans under the CMB program ² | - | - | - | - | - | 242,207 |
| Total loans at amortized cost | | | | | | 246,639 |

¹ The internal credit ratings are based upon internal assessments of the counterparty creditworthiness. These ratings correspond to those provided by the credit rating agencies except in cases where stand-alone ratings exist. A counterparty internal credit rating cannot be higher than the highest stand-alone rating from any of the agencies. A stand-alone rating removes the assumption of Government support from the rating.

² ECL are not recognized for Loans under the CMB program since the credit risk arising from these loans is reflected in the credit risk of the NHA MBS and CMB TPGs and recognized in unearned premiums and fees. The sole source of repayment on these loans are the NHA MBS securities, reinvestment assets and swaps which are the same credit risk drivers as the NHA MBS and CMB TPGs.

We are assured collection of principal and accrued interest on 99% (31 December 2017 – 99%) of our loans by various levels of government, CMHC mortgage insurance or by investment grade collateral representing the sole source of repayment on our loans under the CMB program. For loans designated at FVTPL, there were no changes in fair value attributable to changes in credit risk.

Total undrawn loan commitments outstanding at 30 September 2018 were \$340 million, of which \$329 million are subject to 12-month ECL and \$11 million are commitments outstanding on purchased or credit impaired loans.

Expected credit losses

The table below presents the change in the ECL allowance recognized in the consolidated statement of income on loans held at amortized cost.

| <i>(in millions)</i> | Three months ended September 30 | | | | | 2017 – IAS 39 ¹ |
|--|---------------------------------|---|--|-----------|------------|----------------------------|
| | 2018 – IFRS 9 | | | | | |
| | Stage1: 12-month ECL | Stage 2: Lifetime ECL not credit impaired | Stage 3: Lifetime ECL credit impaired | POCI | Total | |
| ECL allowance – beginning of period: | | | | | | |
| Lending program loans | 1 | - | 5 | - | 6 | 23 |
| MLI activity loans | - | - | 39 | 63 | 102 | 197 |
| Total ECL allowance – beginning of period | 1 | - | 44 | 63 | 108 | 220 |
| Increase in ECL allowance: | | | | | | |
| Lending program loans | - | - | - | - | - | - |
| MLI activity loans | - | - | (2) | (3) | (5) | (15) |
| Total increase in ECL allowance ² | - | - | (2) | (3) | (5) | (15) |
| ECL allowance – end of period: | | | | | | |
| Lending program loans | 1 | - | 5 | - | 6 | 23 |
| MLI activity loans | - | - | 37 | 60 | 97 | 182 |
| Total ECL allowance – end of period | 1 | - | 42 | 60 | 103 | 205 |

¹ IAS 39 loss allowance for MLI activity loans was presented in accounts receivable and other assets.

² Included in net gains (losses) on financial instruments for Lending program loans and insurance claims expense for MLI activity loans.

| <i>(in millions)</i> | Nine months ended September 30 | | | | | 2017 – IAS 39 ¹ |
|--|--------------------------------|---|--|-----------|------------|----------------------------|
| | 2018 – IFRS 9 | | | | | |
| | Stage1: 12-month ECL | Stage 2: Lifetime ECL not credit impaired | Stage 3: Lifetime ECL credit impaired | POCI | Total | |
| ECL allowance – beginning of period: | | | | | | |
| Lending program loans | 1 | - | 4 | - | 5 | 23 |
| MLI activity loans | - | - | 33 | 63 | 96 | 187 |
| Total ECL allowance – beginning of period | 1 | - | 37 | 63 | 101 | 210 |
| Increase in ECL allowance: | | | | | | |
| Lending program loans | - | - | 1 | - | 1 | - |
| MLI activity loans | - | - | 4 | (3) | 1 | (5) |
| Total increase in ECL allowance ² | - | - | 5 | (3) | 2 | (5) |
| ECL allowance – end of period: | | | | | | |
| Lending program loans | 1 | - | 5 | - | 6 | 23 |
| MLI activity loans | - | - | 37 | 60 | 97 | 182 |
| Total ECL allowance – end of period | 1 | - | 42 | 60 | 103 | 205 |

¹ IAS 39 loss allowance for MLI activity loans was presented in accounts receivable and other assets.

² Included in net gains (losses) on financial instruments for Lending program loans and insurance claims expense for MLI activity loans.

During the three months ended 30 September 2018, ECLs on loans decreased by \$5 million primarily due to a decrease in the POCI loans balance and during the nine months ended 30 September 2018, ECLs on loan increased by \$2 million primarily due to transfers of loans from stage 1 to stage 3 during the period.

The allowance for expected credit losses on undrawn loan commitments was \$6 million at 30 September 2018, a decrease of \$2 million and increase of \$6 million for the three and nine months ended 30 September 2018 respectively.

14. Borrowings

The following table presents the cash flows and non-cash changes for borrowings.

| <i>(in millions)</i> | Three months ended 30 September | | | | | | Balance at end of period |
|---|---------------------------------|---------------|----------------|--------------------|-----------|--------------|--------------------------|
| | Balance at beginning of period | Cash flows | | Non-cash changes | | | |
| | | Issuances | Repayments | Fair value changes | Accretion | Eliminations | |
| 2018 | | | | | | | |
| Designated at FVTPL | | | | | | | |
| Borrowings from the Government of Canada | 3,913 | 50 | (233) | (16) | - | - | 3,714 |
| Borrowings at amortized cost | | | | | | | |
| Canada mortgage bonds | 233,058 | 9,977 | (4,950) | - | 10 | 184 | 238,279 |
| Borrowings from the Government of Canada | 4,453 | 279 | (166) | (9) | 16 | - | 4,573 |
| Total borrowings at amortized cost | 237,511 | 10,256 | (5,116) | (9) | 26 | 184 | 242,852 |
| Total | 241,424 | 10,306 | (5,349) | (25) | 26 | 184 | 246,566 |
| 2017 | | | | | | | |
| Designated at FVTPL | | | | | | | |
| Borrowings from the Government of Canada | 5,105 | 84 | (401) | (44) | - | - | 4,744 |
| Other financial liabilities | | | | | | | |
| Canada mortgage bonds | 224,610 | 9,552 | (4,948) | - | 10 | 279 | 229,503 |
| Borrowings from the Government of Canada | 4,342 | 494 | (511) | (2) | 7 | - | 4,330 |
| Total other financial liabilities | 228,952 | 10,046 | (5,459) | (2) | 17 | 279 | 233,833 |
| Total | 234,057 | 10,130 | (5,860) | (46) | 17 | 279 | 238,577 |

| <i>(in millions)</i> | Nine months ended 30 September | | | | | | Balance at end of period |
|---|--------------------------------|---------------|-----------------|--------------------|---------------------|--------------|--------------------------|
| | Balance at beginning of period | Cash flows | | Non-cash changes | | | |
| | | Issuances | Repayments | Fair value changes | Accretion and other | Eliminations | |
| 2018 | | | | | | | |
| Designated at FVTPL | | | | | | | |
| Borrowings from the Government of Canada | 4,564 | 50 | (870) | (30) | - | - | 3,714 |
| Borrowings at amortized cost | | | | | | | |
| Canada mortgage bonds | 229,242 | 29,441 | (21,050) | - | 30 | 616 | 238,279 |
| Borrowings from the Government of Canada | 4,350 | 722 | (509) | (13) | 23 | - | 4,573 |
| Total borrowings at amortized cost | 233,592 | 30,163 | (21,559) | (13) | 53 | 616 | 242,852 |
| Total | 238,156 | 30,213 | (22,429) | (43) | 53 | 616 | 246,566 |
| 2017 | | | | | | | |
| Designated at FVTPL | | | | | | | |
| Borrowings from the Government of Canada | 5,632 | 1,083 | (1,889) | (82) | - | - | 4,744 |
| Capital market borrowings | 273 | - | (275) | - | - | 2 | - |
| Total designated at FVTPL | 5,905 | 1,083 | (2,164) | (82) | - | 2 | 4,744 |
| Other financial liabilities | | | | | | | |
| Canada mortgage bonds | 218,829 | 30,403 | (19,667) | - | 29 | (91) | 229,503 |
| Borrowings from the Government of Canada | 4,327 | 851 | (850) | (7) | 9 | - | 4,330 |
| Total other financial liabilities | 223,156 | 31,254 | (20,517) | (7) | 38 | (91) | 233,833 |
| Total | 229,061 | 32,337 | (22,681) | (89) | 38 | (89) | 238,577 |

When CMHC holds CMB to maturity or acquires CMB in the primary market, the related cash flows are excluded from the consolidated statement of cash flows. During the three and nine months ended 30 September 2018, no CMB maturities have been excluded from repayments in the table above and from investment securities – sales and maturities in the consolidated statement of cash flows (three and nine months ended 30 September 2017 – nil and \$133 million). There were no purchases in the primary market during the three and nine months ended 30 September 2018 (30 September 2017 – nil).

15. Financial instruments income and expenses

Interest income, investment income and interest expense

The following table outlines the total interest income and expense calculated using the effective interest method for financial instruments and the dividend income recognized in the consolidated statement of income and comprehensive income.

| | Three months ended | | | | | |
|--|--------------------|-------------------|------------------|-------------------|-------------------|------------------|
| | 30 September 2018 | | | 30 September 2017 | | |
| <i>(in millions)</i> | Interest income | Investment income | Interest expense | Interest income | Investment income | Interest expense |
| Interest for financial instruments not at FVTPL: | | | | | | |
| Cash equivalents | 1 | 2 | - | - | 1 | - |
| Debt instruments – FVOCI | - | 117 | - | - | - | - |
| Debt instruments – AFS | - | - | - | - | 134 | - |
| Loans – amortized cost | 1,327 | - | - | 1,149 | - | - |
| Securities sold under repurchase agreements | - | (1) | - | - | - | - |
| Borrowings – amortized cost | - | - | 1,299 | - | - | 1,114 |
| Total interest for financial instruments not at FVTPL | 1,328 | 118 | 1,299 | 1,149 | 135 | 1,114 |
| Interest for financial instruments at FVTPL: | | | | | | |
| Debt instruments | 6 | 1 | - | 5 | - | - |
| Loans | 9 | - | - | 12 | - | - |
| Borrowings | - | - | 18 | - | - | 24 |
| Derivatives | 4 | - | - | 7 | - | - |
| Total interest for financial instruments at FVTPL | 19 | 1 | 18 | 24 | - | 24 |
| Total Interest | 1,347 | 119 | 1,317 | 1,173 | 135 | 1,138 |
| Dividend income ¹ | - | 7 | - | - | 10 | - |
| Total | 1,347 | 126 | 1,317 | 1,173 | 145 | 1,138 |

¹ All dividend income was recognized on investments still held at the end of the period.

| <i>(in millions)</i> | Nine months ended | | | | | |
|--|-------------------|-------------------|------------------|-------------------|-------------------|------------------|
| | 30 September 2018 | | | 30 September 2017 | | |
| | Interest income | Investment income | Interest expense | Interest income | Investment income | Interest expense |
| Interest for financial instruments not at FVTPL: | | | | | | |
| Cash equivalents | 3 | 6 | - | 1 | 3 | - |
| Debt instruments – FVOCI | - | 358 | - | - | - | - |
| Debt instruments – AFS | - | - | - | - | 397 | - |
| Loans – amortized cost | 3,838 | - | - | 3,374 | - | - |
| Securities sold under repurchase agreements | - | (5) | - | - | (2) | - |
| Borrowings – amortized cost | - | - | 3,748 | - | - | 3,275 |
| Total interest for financial instruments not at FVTPL | 3,841 | 359 | 3,748 | 3,375 | 398 | 3,275 |
| Interest for financial instruments at FVTPL: | | | | | | |
| Debt instruments | 16 | 4 | - | 15 | - | - |
| Loans | 31 | - | - | 43 | - | - |
| Borrowings | - | - | 57 | - | - | 72 |
| Derivatives | 15 | - | - | 19 | - | - |
| Total interest for financial instruments at FVTPL | 62 | 4 | 57 | 77 | - | 72 |
| Total interest | 3,903 | 363 | 3,805 | 3,452 | 398 | 3,347 |
| Dividend income ¹ | - | 25 | - | - | 34 | - |
| Total | 3,903 | 388 | 3,805 | 3,452 | 432 | 3,347 |

¹ In the nine months ended 30 September 2018 dividend income of \$24 million was recognized on investments still held at the end of the period (nine months ended 30 September 2017 - \$34 million).

Gains and losses from financial instruments

The following table presents the gains (losses) related to financial instruments recognized in the consolidated statement of income and comprehensive income

| <i>(in millions)</i> | Three months ended 30 September | | Nine months ended 30 September | |
|---|------------------------------------|-----------|-----------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Financial Instruments designated at FVTPL | | | | |
| Investment securities | (4) | (7) | (5) | (10) |
| Loans | (8) | (24) | (17) | (53) |
| Borrowings | 16 | 42 | 30 | 80 |
| Total financial instruments designated at FVTPL | 4 | 11 | 8 | 17 |
| Financial instruments mandatorily at FVTPL | | | | |
| Equity securities | - | - | (38) | - |
| Debt instruments | (1) | - | (2) | - |
| Derivatives | 26 | 14 | (76) | 22 |
| Total financial instruments mandatorily at FVTPL | 25 | 14 | (116) | 22 |
| Debt instruments held at FVOCI ¹ | (50) | - | 32 | - |
| AFS – investment securities ¹ | - | 37 | - | 32 |
| Loans at amortized cost – prepayments | 3 | 23 | 19 | 63 |
| Borrowings – amortized cost ² | 6 | (20) | (4) | (54) |
| Expected credit loss recoveries (credit losses) on financial assets | 3 | - | 2 | - |
| Total | (9) | 65 | (59) | 80 |

¹ Includes foreign exchange losses of \$39 million and gains of \$53 million in the three and nine months ended 30 September 2018, respectively (losses of \$28 and \$50 million in the three and nine months ended 30 September 2017, respectively) resulting from translation of U.S. dollar-denominated debt instruments.

² Includes losses from the retirement of borrowings during the three and nine months ended 30 September 2018 of nil and \$14 million respectively (three and nine months ended 30 September 2017 – \$22 and \$61 million), net of gains during the three and nine months ended 30 September 2018 from the issuance of borrowings of \$6 and \$10 million, respectively (three and nine months ended 30 September 2017 – \$2 and \$7 million).

16. Market Risk

Market risk is the risk of adverse financial impacts arising from changes in underlying market factors, including interest rates, foreign exchange rates, and equity prices.

Value at risk (VaR)

Market risk for investment securities in the Mortgage Loan Insurance and Securitization Activities is evaluated through the use of VaR models. VaR is a statistical technique used to measure the maximum potential loss of an investment portfolio over a specified holding period with a given level of confidence. The VaR for the Mortgage Loan Insurance and Securitization Activities calculated with 95% confidence over a 22 business day holding period is outlined in the table below. VaR is presented separately for individual market risk factors and for the total portfolio. The effect of diversification results from the fact that market risks are not perfectly correlated and, consequently, there is a benefit from investment diversification. The VaR figures are based on one year of historical prices and correlations of bond and equity markets and 26 weeks of volatility.

| <i>(in millions)</i> | As at | |
|--|-------------------|------------------|
| | 30 September 2018 | 31 December 2017 |
| Investment securities: | | |
| Interest rate risk on debt instruments | 176 | 213 |
| Equity risk | 23 | 43 |
| Effect of diversification | (34) | (50) |
| Total VaR | 165 | 206 |

We are exposed to currency risk from our holdings in foreign currency denominated investment securities. Our internal policies limit the amount of foreign currency investments and require full hedging of currency risk. We held \$2,148 million in debt instruments denominated in U.S. dollars as at 30 September 2018 (31 December 2017 – \$1,792 million).

Our strategy to fully hedge currency risk is to continuously enter into a series of short-term foreign currency forward contracts. Under these contracts, most of which are settled net, we exchange U.S. dollars for Canadian dollars at an exchange rate fixed at the outset of the contract for settlement at a future pre-determined date. Given the short terms of the forward contracts, full hedging of currency risk over the life of the foreign-denominated debt instruments will require continued application of our strategy in the future. The exposures presented in the Value at Risk table above reflect the offsetting effect of the hedging instruments. Currency risk was assessed as immaterial as at 30 September 2018.

Interest rate sensitivity

Market risk for the Assisted Housing Activity portfolio of loans, investments, borrowings and swaps is evaluated by measuring their sensitivity to changes in interest rates.

For the Assisted Housing Activity's financial instruments designated at FVTPL and derivatives, we assessed the impact of a 200 bps shift in interest rates as immaterial as at 30 September 2018.

The Assisted Housing Activity's loans and borrowings measured at amortized cost are also exposed to interest rate risk. The net impact of a shift in interest rates on their fair value is presented below.

| <i>(in millions)</i> | As at | | | |
|--|---------------------|----------|---------------------|----------|
| | 30 September 2018 | | 31 December 2017 | |
| | Interest rate shift | | Interest rate shift | |
| | -200 bps | +200 bps | -200 bps | +200 bps |
| Increase (decrease) to fair value of net assets ¹ | (67) | 56 | (56) | 49 |

¹ The changes in fair value of net assets resulting from interest rate shifts presented in this table would not be recognized in comprehensive income as the underlying financial instruments are measured at amortized cost.

The Assisted Housing Activity's net interest income is also sensitive to interest rate movements. The maximum negative exposure of net interest income is \$0.3 million at 30 September 2018 (31 December 2017 – \$1.2 million). This is calculated by scenario analysis using multiple simulations of interest rate volatility with 95% confidence over a one-year period.

17. Credit Risk

Credit risk is the potential for financial loss arising from failure of a borrower or an institutional counterparty to fulfill its contractual obligations. Full descriptions of credit risks related to our financial instruments and how we manage those risks are disclosed in Note 18 of our audited consolidated financial statements. There has been no change to the nature of the risk and how they are managed for the three and nine month period ended 30 September 2018.

18. Pension and Other Post-Employment Benefits

Expense, remeasurements and contributions for the defined benefit plans are presented below:

| <i>(in millions)</i> | Three months ended 30 September | | | |
|---|---------------------------------|------------|-----------------------------|----------|
| | Pension plans | | Other post-employment plans | |
| | 2018 | 2017 | 2018 | 2017 |
| Current service cost | 10 | 7 | - | - |
| Net interest expense | 4 | 2 | 2 | 2 |
| Expense recognized in net income | 14 | 9 | 2 | 2 |
| Net actuarial gains (losses) arising from changes in financial assumptions | 93 | 152 | 6 | 8 |
| Return on plan assets (excluding amounts included in net interest expense) | (27) | (14) | - | - |
| Net remeasurements recognized in other comprehensive income (loss)¹ | 66 | 138 | 6 | 8 |
| CMHC's contributions | 6 | 24 | 1 | 1 |
| Employee contributions | 4 | 3 | - | - |
| Total contributions | 10 | 27 | 1 | 1 |

¹ The defined benefit plans are remeasured on a quarterly basis for changes in the discount rate and for actual asset returns. All other actuarial assumptions are updated at least annually.

| <i>(in millions)</i> | Nine months ended 30 September | | | |
|---|--------------------------------|------------|-----------------------------|------------|
| | Pension plans | | Other post-employment plans | |
| | 2018 | 2017 | 2018 | 2017 |
| Current service cost | 29 | 22 | 1 | 1 |
| Net interest expense | 10 | 8 | 4 | 4 |
| Expense recognized in net income | 39 | 30 | 5 | 5 |
| Net actuarial gains (losses) arising from changes in financial assumptions | 184 | (23) | 11 | (3) |
| Return on plan assets (excluding amounts included in net interest expense) | (8) | 20 | - | - |
| Net remeasurements recognized in other comprehensive income (loss)¹ | 176 | (3) | 11 | (3) |
| CMHC's contributions | 47 | 79 | 5 | 3 |
| Employee contributions | 12 | 9 | - | - |
| Total contributions | 59 | 88 | 5 | 3 |

¹ The defined benefit plans are remeasured on a quarterly basis for changes in the discount rate and for actual asset returns. All other actuarial assumptions are updated at least annually.

We remeasure our defined benefit obligations and the fair value of plan assets at interim periods. The discount rate is determined in accordance with guidance issued by the Canadian Institution of Actuaries by reference to Canadian AA-Corporate bonds with terms to maturity approximating the duration of the obligation. Effective 31 December 2017, the defined contribution plan was closed and all employees were transferred to the new modified defined benefit pension plan. As a result, expenses for the defined contribution plan were nil for the three and nine months ended 30 September 2018 (three and nine months ended 30 September 2017 - \$0.8 million and \$2.8 million).

19. Income Taxes

The following table presents the components of income tax.

| <i>(in millions)</i> | Three months ended 30 September | | Nine months ended 30 September | |
|--|------------------------------------|-------------|-----------------------------------|-------------|
| | 2018 | 2017 | 2018 | 2017 |
| Current income tax expense | 96 | 145 | 321 | 369 |
| Deferred income tax relating to origination and reversal of temporary differences | 30 | 6 | 24 | 30 |
| Total income tax expense included in net income | 126 | 151 | 345 | 399 |
| Income tax expense (recovery) on other comprehensive income (loss) | | | | |
| Net unrealized losses from FVOCI financial instruments | (27) | - | (75) | - |
| Net unrealized losses from AFS financial instruments | - | (70) | - | (78) |
| Reclassification of prior years' net unrealized gains realized in the period in net income | (4) | (12) | (5) | (15) |
| Remeasurement gains (losses) on defined benefit plans | 13 | 26 | 32 | (1) |
| Total income tax recovery included in other comprehensive income (loss) | (18) | (56) | (48) | (94) |
| Total | 108 | 95 | 297 | 305 |

20. Related Party Transactions

We pay the Government fees in recognition of its financial backing of the Mortgage Loan Insurance and Securitization Activities. The fees, which are recorded in operating expenses, amount to \$10 million and \$29 million for the three and nine months ended 30 September 2018, respectively (three and nine months ended 30 September 2017 – \$10 million and \$27 million) for the Mortgage Loan Insurance Activity and \$6 million and \$17 million for the three and nine months ended 30 September 2018, respectively (three and nine months ended 30 September 2017 – \$5 million and \$15 million) for the Securitization Activity.

All other material related party transactions and outstanding balances are disclosed in relevant notes.

21. Commitments and Contingent Liabilities

Under Section 11 of the NHA, the total of outstanding insured amounts of all insured loans may not exceed \$600 billion (31 December 2017 – \$600 billion). At 30 September 2018, insurance-in-force, which represents the risk exposure of the Mortgage Loan Insurance Activity, totalled \$453 billion (31 December 2017 – \$480 billion). Under Section 15 of the NHA, the aggregate outstanding amount of principal guarantees may not exceed \$600 billion (31 December 2017 – \$600 billion). At 30 September 2018, guarantees-in-force, which represents the risk exposure of the Securitization Activity, totalled \$484 billion (31 December 2017 – \$477 billion).

There are legal claims of \$11 million (31 December 2017 – \$8 million) against CMHC. Due to the uncertainty of the outcome of these claims, no provision for loss has been recorded. We do not expect the ultimate resolution of any of the proceedings to which we are party to have a significant adverse effect on our financial position.

22. Comparative Figures

Certain comparative information in the consolidated statement of income and comprehensive income has been reclassified to conform to the current period's presentation. The same comparative information has been reclassified accordingly in the related notes to the consolidated financial statements.

Parliamentary appropriations presented in Note 6 have been reclassified to conform to the current period's presentation in accordance with Treasury Board's *Policy on Results*. CMHC is required to report appropriated funds following the Departmental Results Framework for the Government beginning April 1, 2018.

CANADA MORTGAGE AND HOUSING CORPORATION
700 Montreal Road
Ottawa, Ontario
K1A 0P7

Available on CMHC's website at www.cmhc.ca or by calling 1-800-668-2642