

GULF AND FRASER FISHERMEN'S CREDIT UNION  
YEAR ENDED DECEMBER 31, 2017

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# Management Discussion and Analysis Report

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**Gulf and Fraser Fishermen's Credit Union  
2017 ANNUAL REPORT**

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## Introduction

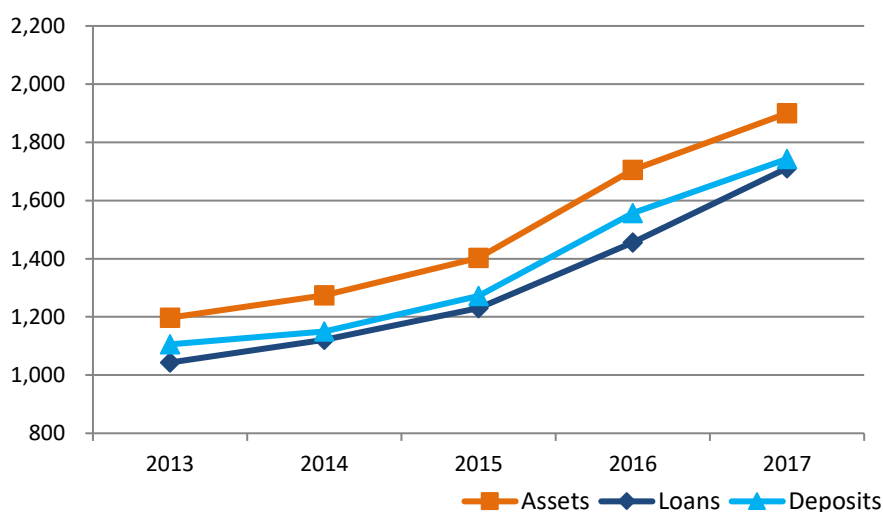
Gulf and Fraser Fishermen's Credit Union, operating as G&F Financial Group ("G&F" or "the credit union") is a BC based credit union serving members in the Lower Mainland for over 75 years offering a full range of products and services including personal and business banking, wealth management and retail and commercial lending solutions. G&F serves approximately 31 thousand members and administers over \$2.2 billion in assets under administration through a network of 15 branches, a locally based Member Hub, online, mobile, and telephone banking channels as well as a mobile team of experts who meet with members at their convenience.

This Management Discussion and Analysis provides an overview of the credit union's financial and operating performance. It is intended to complement our audited consolidated financial statements and should be read in conjunction with those financial statements. The discussion may contain forward looking statements concerning G&F's activities and strategies. Readers are cautioned that such statements may involve risk and uncertainties with respect to the economic, legislative, regulatory and competitive environments, which could cause actual results to differ from the forward-looking statements in this report.

## Highlights

G&F achieved record-breaking loan growth and exceptional financial performance in 2017. Assets increased by \$194 million or 11.4%, while our membership reached 30,969 as we welcomed 942 net new members into our network. Loan growth hit a record high of \$256 million or 17.6%, while deposits grew by \$186 million or 11.9%. In addition, wealth management assets under administration grew by a notable \$25 million, or 12.6%. We continued expanding our branch network with the opening of a new boutique branch in the Metrotown neighbourhood of Burnaby.

**Assets, Loans and Deposits** (in \$millions)



Earnings from operations for 2017 of \$11.4 million was also a record high for G&F, an increase of 79.0% over 2016 as a result of improved operating margin (net interest income and other income) due to the growth in our loan, deposit and wealth management portfolios. While operating expenses increased on an absolute dollar basis by 6.3% year over year, it decreased as a percentage of assets from 1.90% to 1.73% as the credit union continued to realize efficiencies through engaging in collaborative opportunities, growth and economies of scale. Furthermore, the operating efficiency improved from 80.92% in 2016 to 72.09% in 2017.

Total comprehensive income for 2017 was \$9.2 million resulting in a 10.3% growth in members' equity. G&F was honoured to be able to share this success with the local communities we serve by distributing \$598 thousand from both the credit union and G&F Financial Group Foundation. In 2017, G&F also introduced investment equity shares giving members an opportunity to further share in the success of their credit union while enhancing G&F's capital for ongoing investment and growth. The Board of Directors approved a dividend return of 4% on member equity shares and 5% on investment equity shares. G&F remains well capitalized with a capital adequacy ratio of 13.20% at the end of 2017, well above the 8% regulatory requirement.

## 2017 Financial Performance

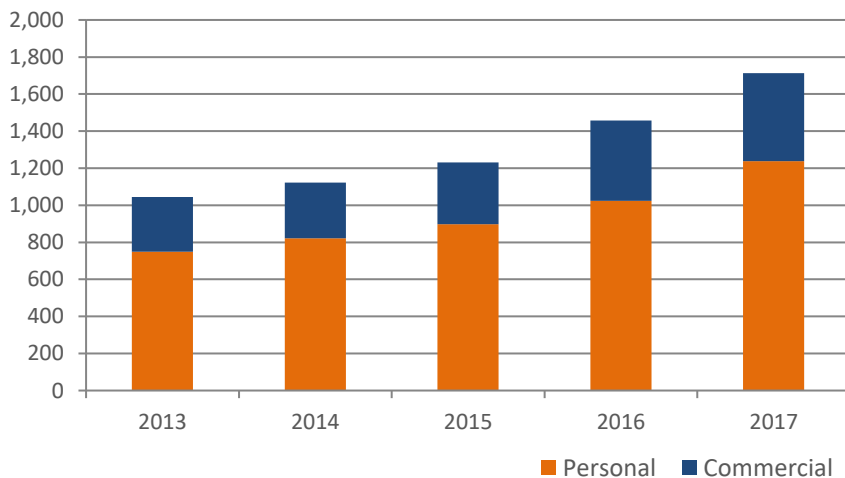
Total assets grew by \$194 million, or 11.4%, due to growth in both our loan and deposit portfolios. Assets now total \$1.90 billion versus \$1.71 billion in 2016. As loan growth outpaced deposit growth, cash and financial investments decreased by \$62 million totaling \$177 million at the end of 2017. Our liquidity position ended the year at 9.4%, which was in compliance with the statutory requirement of 8%. We also saw our membership grow by 3.1% and now have 30,969 members connecting and doing business with G&F.

### LOANS

Loans to members grew by \$256 million, or 17.6%, reaching \$1.71 billion at the end of 2017 versus \$1.46 billion at the end of 2016. The loan growth was fueled by an ongoing low interest rate environment and an active real estate market in the Lower Mainland, particularly for condos and townhomes.

The residential mortgages and personal loans portfolio increased by \$214 million (20.9%) totaling \$1.24 billion at the end of 2017. The commercial lending portfolio, which equates to 28% of our total loan portfolio, grew by \$41 million (9.6%) totaling \$475 million at the end of 2017. G&F's Investment and Lending Policy has established a limit on the commercial lending portfolio (funded and unfunded) of 35% of the credit union's asset base with which the credit union was in compliance.

**Loans** (in \$millions)

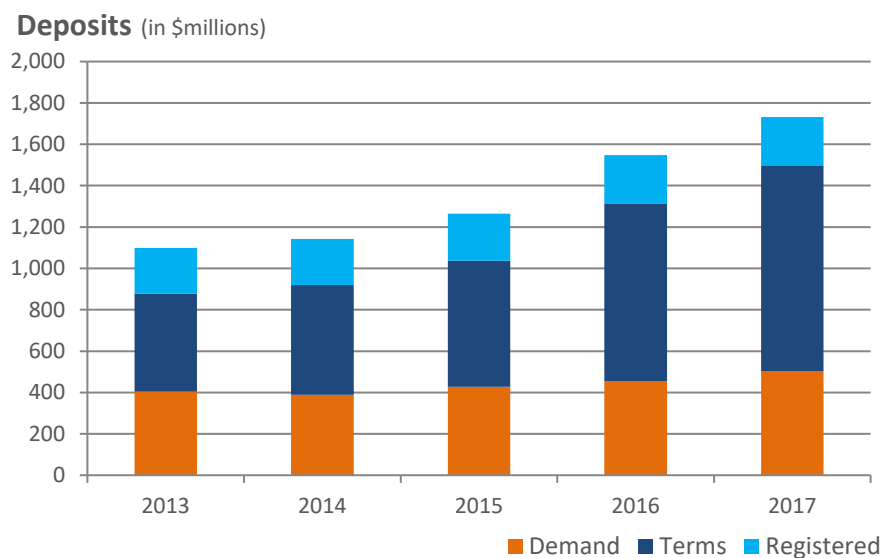


## ALLOWANCE FOR IMPAIRED LOANS

The allowance for impaired loans increased by \$608 thousand to \$4.5 million at the end of 2017 from \$3.9 million at the end of 2016. The increase in the allowance for impaired loans during the year included a provision for impaired loans of \$769 thousand to support a larger loan portfolio, offset by loans written off (net of recoveries) of \$161 thousand. The allowance for impaired loans allocated to the residential mortgages and personal loans portfolio is \$603 thousand or 13.3% while the allowance for impaired loans allocated to the commercial portfolio is \$3.9 million or 86.7%.

## DEPOSITS

Member deposits increased by \$186 million or 11.9% totaling \$1.74 billion at the end of 2017 versus \$1.56 billion at the end of 2016. Demand deposits grew by \$46.8 million, term deposits grew by \$137.1 million, registered deposits (i.e., RRSP, RRIF, RESP and TFSA) grew by \$1.2 million and accrued interest payable grew by \$782 thousand during the year. The significant growth in term deposits reflects members taking advantage of the higher yields associated with term deposit investments and the rising interest rate environment.



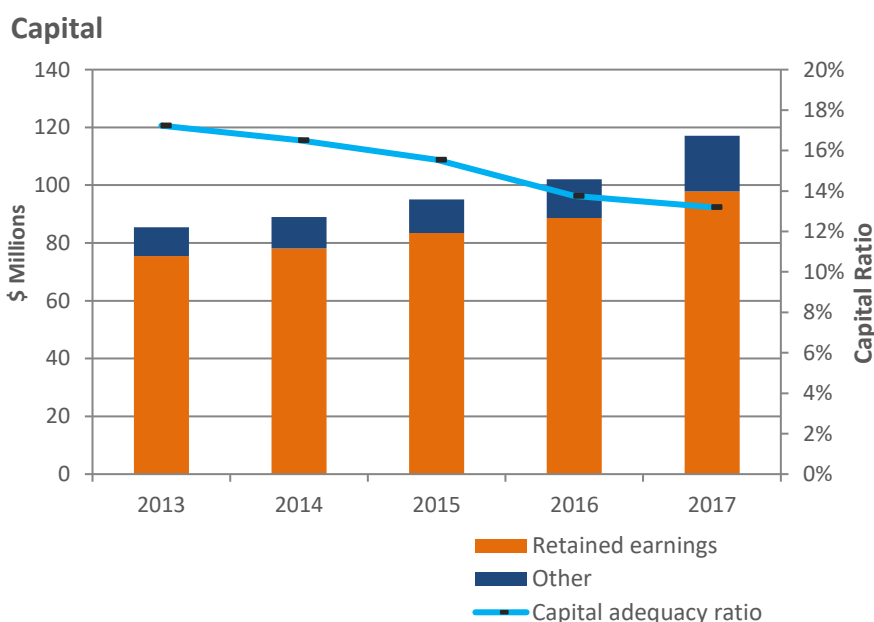
## SECURED BORROWING

During 2017, G&F increased its available operating line and term facility with Central 1 to \$104.8 million from \$84.8 million at the end of 2016. In addition, G&F maintains a credit facility agreement with Fédérations des caisses Desjardins du Québec of \$30.0 million. As at December 31, 2017, no amounts were drawn against these credit facilities. As part of the credit union's program of liquidity, capital, and interest rate risk management, G&F securitizes residential mortgages thereby entering into a secured borrowing arrangement with Central 1. The outstanding secured borrowing with Central 1 was \$45.3 million at the end of 2017, a decrease from the balance at the end of 2016 of \$49.8 million.

## MEMBERS' EQUITY

G&F achieved net income of \$9.2 million, a net unrealized loss from cash flow hedges (net of tax recovery) of \$975 thousand and a net unrealized gain on financial investments (net of tax expense) of \$947 thousand in 2017 resulting in total comprehensive income of \$9.2 million - a return on members' equity of 10.3%.

Capital adequacy at the end of 2017 was 13.20%, well exceeding the regulatory requirement of 8% and the supervisory target of 10%.



## NET INTEREST INCOME

In 2017, the Canadian economy experienced healthy growth and was running close to capacity which led the Bank of Canada to increase its overnight target rate in July by 0.25% and another 0.25% in September, to end the year at 1.00%. Accordingly, G&F increased its prime rate in July and September to end 2017 at 3.2% compared to 2.70% at the end of 2016.

G&F's net interest income benefited from this rise in interest rates which resulted in the net interest income as a percentage of assets improving from 1.85% in 2016 to 1.90% in 2017. On an absolute dollar basis, the credit union's net interest income (the difference between interest earned on loans and investments and interest paid on deposits and secured borrowings) increased by \$5.7 million, or 19.7% to \$34.5 million reflecting the growth in our asset base as well.

### OTHER INCOME

Other income includes member services income (such as loan fees and penalties, demand account fees, wealth management income and foreign exchange income), hedge ineffectiveness on cash flow hedges, other income earned by Gulf & Fraser Insurance Services Ltd. (a wholly owned subsidiary of the credit union providing life insurance products and services) and provision for impaired loans. Other income totaled \$8.4 million in 2017, an increase of \$1.2 million or 17.3% over 2016 largely due to more loan fees generated associated with the growth experienced in the lending portfolio.

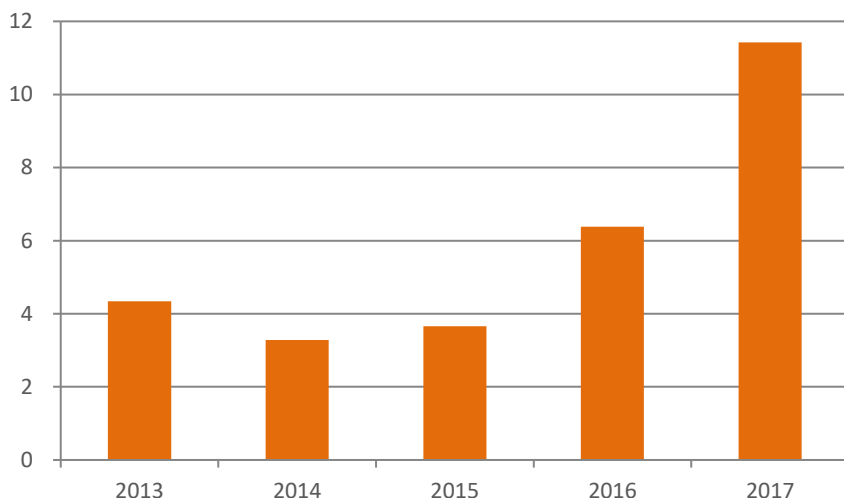
### OPERATING EXPENSES

Operating expenses increased by \$1.9 million or 6.3% to \$31.5 million in 2017 primarily as a result of increases in salaries and employee benefits which includes the first full year of operations for our Brentwood branch as well as the opening of our new Metrotown branch in late 2017. Other operating expenses such as advertising and promotion and dues increased naturally with the growth of the credit union. Notwithstanding, the operating expenses as a percentage of assets decreased from 1.90% in 2016 to 1.73% in 2017 as the credit union continued to realize operating efficiencies through collaborating with other like-minded organizations, growth and economies of scale.

### EARNINGS FROM OPERATIONS

Earnings from operations was a record \$11.4 million in 2017, up \$5.0 million or 79.0% compared to 2016. G&F has been making long-term strategic investments to improve the sales and service delivery and overall member experience. Specifically, G&F opened the Willoughby branch in Langley and the West Broadway branch in Vancouver in 2014 and the aforementioned Brentwood branch and Metrotown branch in Burnaby in 2016 and 2017 respectively. Although these were significant investments over several years with initial start-up costs, the cumulative benefit of attracting new members and growing the loan, deposit and wealth portfolios contributed to the strong financial performance for 2017.

### Operating Income (in \$millions)



G&F highlights a long history of sharing our profits with the local communities in which we live and serve in the form of donations, sponsorships, educational bursaries, and scholarships. Total distributions from both the credit union and G&F Financial Group Foundation were \$598 thousand or 5.2% of earnings from operations in 2017.

### TOTAL COMPREHENSIVE INCOME

The total comprehensive income for 2017 was \$9.2 million which included a 4% dividend on members' equity shares of \$109 thousand and a 5% dividend on investment equity shares of \$48 thousand approved by the Board of Directors, a provision for income taxes of \$2.1 million, a net unrealized loss from cash flow hedges (net of tax) of \$975 thousand and a net unrealized gain on financial investments (net of tax) of \$947 thousand.

### FUNDS UNDER ADMINISTRATION

Funds under administration by G&F comprise of commercial loans that are administered by the credit union and syndicated with other financial institutions due to the loan amount being above the credit union's single member cap or above the credit union's risk tolerance to fund on its own. The syndicated loan balance ended 2017 at \$98 million, an increase of \$50 million for the year.

Also included in funds under administration are investments and mutual fund accounts that are managed by our wealth management specialists on behalf of members. This portfolio (at market value) grew by \$25 million or 12.6% in 2017 to end the year at \$222 million.



## Risk Management

G&F is subject to a variety of risks that are inherent to the industry in which it operates. The credit union's principal risks are credit risk, liquidity risk and market risk given the nature of our business is holding financial instruments as identified in Note 20 of the audited consolidated financial statements. Other risks the credit union faces are strategic, operational, legal, regulatory and reputational risks. To mitigate these risks the credit union has policies and procedures, controls and monitoring in place. The Board of Directors has overall responsibility for the establishment and oversight of the credit union's strategic direction, risk management framework and risk appetite. The executive management team is responsible for implementing strategies and policies approved by the board and for developing processes that identify, measure, monitor and mitigate risks. The credit union also has internal and external audit functions which are independent of management and report to the Audit Committee.

## 2018 Outlook

Following a strong showing in 2017, the Canadian economy is expected to ease slightly in 2018 with GDP forecasted to rise 2.2% compared to 3.0% in 2017. The BC economy will continue to be Canada's growth leader, spurred by a strong export sector and domestic economic activity. Potential headwinds include the uncertainty with the outcome of the North American Free Trade Agreement (NAFTA) negotiations along with the impact of modest interest rate increases, a tightening of mortgage lending standards and regulatory policy measures on real estate activity which has been a substantial growth driver for the province in recent years.

Within this context, G&F anticipates a year of steady growth in its loans, deposits and wealth management portfolios, and expects to exceed the \$2 billion in assets milestone during 2018. The financial landscape is ever changing and G&F will continue to evolve and innovate to keep pace with how our members wish to interact with us. In addition, G&F will continue to expand its branch network by opening a new West End location in Vancouver. G&F's business plan for 2018 focuses on five strategic areas – Grow the Business, Service Excellence, People and Culture, Financial Strength and Community Investment.

GULF AND FRASER FISHERMEN'S CREDIT UNION

## Five-Year Overview – Financial Highlights

(Expressed in thousands of dollars)

*Consolidated Statement of Financial Position (unaudited)*

	2017	2016	2015	2014	2013
<b>ASSETS</b>					
Cash and investments	\$176,694	\$238,253	\$161,000	\$138,179	\$142,032
Loans	1,711,125	1,455,277	1,230,167	1,121,748	1,043,286
Premises, equipment, intangible assets, properties	7,767	7,768	7,516	9,365	8,064
Other assets	4,251	4,434	4,386	4,656	4,188
	<b>\$1,899,837</b>	<b>\$1,705,732</b>	<b>\$1,403,069</b>	<b>\$1,273,948</b>	<b>\$1,197,570</b>
<b>Liabilities and Members' Equity</b>					
Deposits	\$1,742,843	\$1,557,016	\$1,271,819	\$1,150,106	\$1,105,640
Members' shares	6,943	3,522	3,547	3,593	3,682
Secured borrowings	45,299	49,758	37,459	38,755	9,975
Other liabilities	6,468	6,311	5,991	3,021	2,839
	1,801,553	1,616,607	1,318,816	1,195,475	1,122,136
Members' equity					
Accumulated other comprehensive income	496	524	867	318	0
Retained earnings	97,788	88,601	83,386	78,155	75,434
	98,284	89,125	84,253	78,473	75,434
	<b>\$1,899,837</b>	<b>\$1,705,732</b>	<b>\$1,403,069</b>	<b>\$1,273,948</b>	<b>\$1,197,570</b>

*Consolidated Statement of Comprehensive Income (unaudited)*

	2017	2016	2015	2014	2013
Interest income	\$56,655	\$47,735	\$43,265	\$41,940	\$40,310
Interest expense	22,156	18,917	17,204	16,661	15,560
<b>Net Interest Income</b>	<b>34,499</b>	<b>28,818</b>	<b>26,061</b>	<b>25,279</b>	<b>24,750</b>
Other income	8,420	7,177	6,232	5,877	5,452
Operating margin	42,919	35,995	32,293	31,156	30,202
Operating expenses	31,493	29,613	28,638	27,876	25,863
<b>Earnings from operations</b>	<b>11,426</b>	<b>6,382</b>	<b>3,655</b>	<b>3,280</b>	<b>4,339</b>
Gain on sale of premises	0	0	3,348	0	2,372
Loss on sale of assets held-for-sale	0	0	0	0	(84)
Donations to G&F Financial Group Foundation	0	0	(1,000)	0	0
Distributions to members	(157)	(109)	(110)	(109)	(113)
Income before income taxes	11,269	6,273	5,893	3,171	6,514
Provision for income taxes	2,082	1,058	662	450	941
<b>Net income from continuing operations</b>	<b>9,187</b>	<b>5,215</b>	<b>5,231</b>	<b>2,721</b>	<b>5,573</b>
Net loss from assets held-for-sale	0	0	0	0	(178)
Net Income	9,187	5,215	5,231	2,721	5,395
Net unrealized gain (loss) from cash flow hedges (net of tax)	(975)	(343)	549	318	0
Net unrealized gain on financial investments (net of tax)	947	0	0	0	0
<b>Total comprehensive income</b>	<b>\$9,159</b>	<b>\$4,872</b>	<b>\$5,780</b>	<b>\$3,039</b>	<b>\$5,395</b>

*Financial Statistics (unaudited)*

Asset growth	11.4%	21.6%	10.1%	6.4%	10.1%
Loan growth	17.6%	18.3%	9.7%	7.5%	9.0%
Deposit growth	11.9%	22.4%	10.6%	4.0%	10.6%
Operating efficiency	72.09%	80.92%	85.20%	87.92%	84.24%

*Percent of average assets (unaudited)*

Net interest income	1.90%	1.85%	1.93%	2.08%	2.20%
Other income	0.46%	0.46%	0.46%	0.48%	0.48%
Operating expenses	1.73%	1.90%	2.12%	2.29%	2.29%
Earnings from operations	0.63%	0.41%	0.27%	0.27%	0.38%
Net income	0.51%	0.33%	0.39%	0.22%	0.48%

*Other statistics (unaudited)*

Retail branches	15	14	13	13	12
Membership	30,969	30,027	29,247	27,808	26,675
Investment portfolios and mutual funds, at market value	\$222,456	\$197,646	\$179,697	\$160,616	\$132,310
Syndicated loans	\$97,638	\$47,350	\$26,446	\$748	\$1,897
Assets under administration	\$2,219,931	\$1,950,728	\$1,609,212	\$1,435,312	\$1,331,777