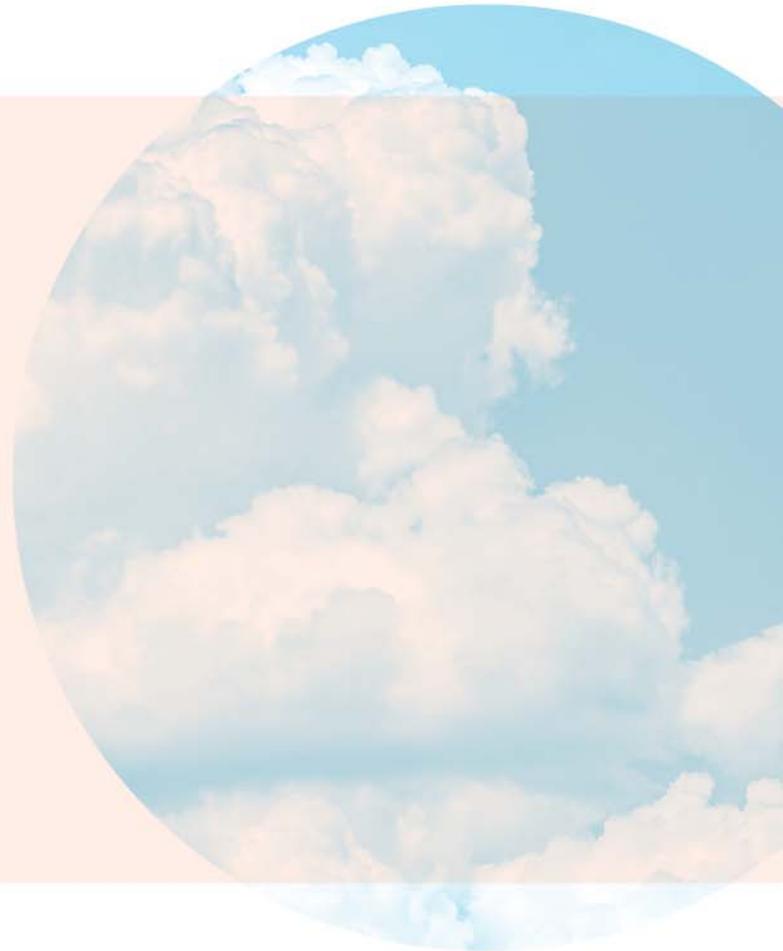




# Management Discussion and Analysis Report

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GULF AND FRASER FISHERMEN'S CREDIT UNION  
YEAR ENDED DECEMBER 31, 2018



**Gulf and Fraser Fishermen's Credit Union  
2018 ANNUAL REPORT**

# Management Discussion and Analysis Report

## Introduction

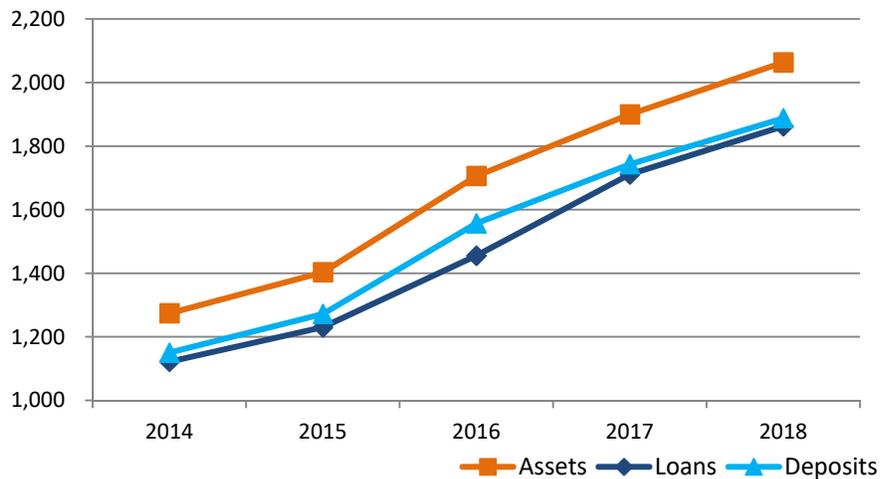
Gulf and Fraser Fishermen's Credit Union, operating as G&F Financial Group ("G&F" or "the credit union") is a BC based credit union serving members in the Lower Mainland for 78 years offering a full range of products and services including personal and business banking, wealth management and retail and commercial lending solutions. G&F serves over 32 thousand members and administers close to \$2.4 billion in assets under administration through a network of 16 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

In 2018, G&F surpassed the \$2 billion on-balance sheet asset milestone and had exceptional financial results. Assets increased by \$164 million or 8.6%, while our membership reached 32,388 as we welcomed 1,419 net new members into our network. Loans increased by \$151 million or 8.8%, while deposits grew by \$145 million or 8.3%. Despite a challenging and volatile year in the financial markets, wealth management assets under administration grew by \$1.2 million, or 0.5%. To meet the needs of our growing membership we continued expanding our branch network with the opening of a new boutique branch in the West End of downtown Vancouver.

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



G&F experienced record earnings from operations in 2018 of \$12.8 million, an increase of 12.1% over 2017 as a result of higher net interest income due to the growth in our loan and deposit portfolios and the rising interest rate environment. While operating expenses increased on an absolute dollar basis by 9.4% year over year, it remained relatively flat as a percentage of assets at 1.74%, compared to 1.73% in 2017. G&F was able to accomplish this by realizing efficiencies through growth, economies of scale and engaging in collaborative opportunities in the credit union system. Furthermore, the operating efficiency improved from 72.09% in 2017 to 71.85% in 2018.

Total comprehensive income for 2018 was \$11.0 million resulting in an 11.2% growth in members' equity. G&F was proud to be able to share this success with the local communities we serve by distributing \$389 thousand through the credit union and the G&F Financial Group Foundation. The Board of Directors approved a dividend return of 4.25% on member equity shares and 5.25% on investment equity shares. G&F remains well capitalized with a capital adequacy ratio of 14.52% at the end of 2018, well above the 8% regulatory requirement.

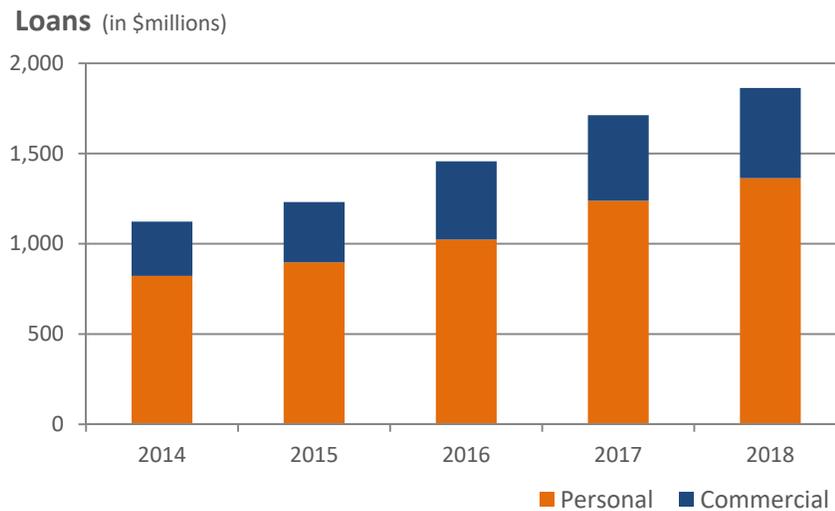
## 2018 Financial Performance

Total assets grew by \$164 million, or 8.6%, due to growth in both our loan and deposit portfolios. Assets now total \$2.06 billion versus \$1.90 billion in 2017. Our liquidity position ended the year at 9.1%, which was above the statutory requirement of 8%. We also saw our membership grow by 4.6% and now have 32,388 members connecting and doing business with G&F.

### LOANS

Loans to members grew by \$151 million, or 8.8%, reaching \$1.86 billion at the end of 2018 versus \$1.71 billion at the end of 2017. The loan growth was supported by a robust BC economy and a relatively low interest rate environment albeit the introduction of new federal government mortgage stress test rules and rising interest rates contributed to a slowing real estate market in the Lower Mainland in the latter half of 2018.

The residential mortgages and personal loans portfolio increased by \$125 million (10.1%) totaling \$1.36 billion at the end of 2018. The commercial lending portfolio, which equates to 27% of our total loan portfolio, grew by \$25 million (5.3%) totaling \$500 million at the end of 2018. 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.

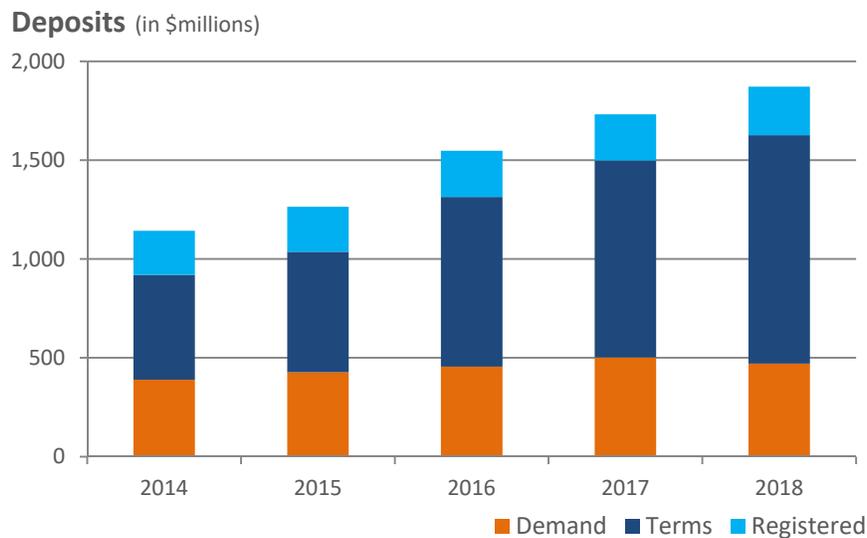


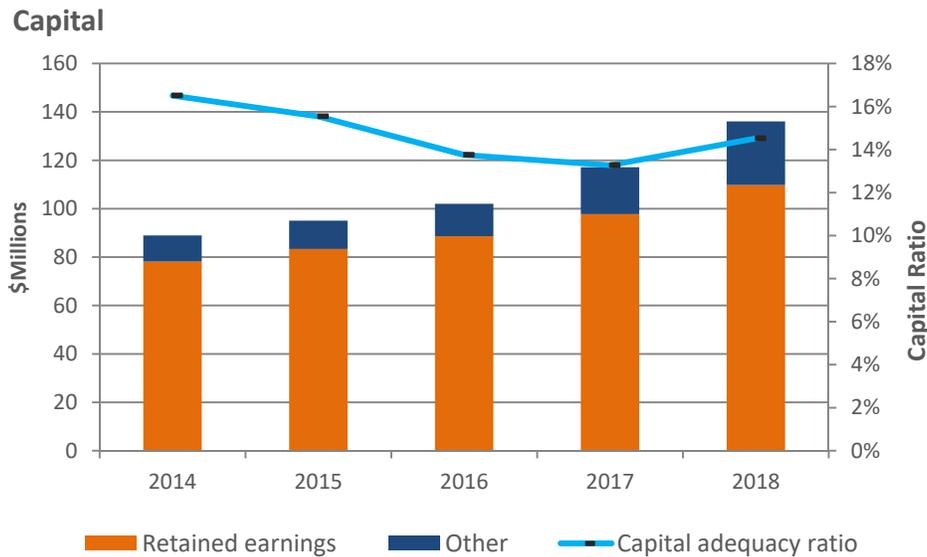
### ALLOWANCE FOR CREDIT LOSSES

The allowance for credit losses decreased by \$301 thousand to \$4.2 million at the end of 2018 from \$4.5 million at the end of 2017. New International Financial Reporting Standards (IFRS 9) for loan impairment that came into effect on January 1, 2018 resulted in an opening transitional reduction of \$868 thousand to the allowance. The increase in the allowance for credit losses during the year included a provision for credit losses of \$697 thousand reflecting a larger loan portfolio, offset by loans written off (net of recoveries) of \$130 thousand. The allowance for credit losses allocated to the residential mortgages and personal loans portfolio was \$1.3 million or 32.2% while the allowance for credit losses allocated to the commercial portfolio was \$2.9 million or 67.8%.

### DEPOSITS

Member deposits increased by \$145 million or 8.3% totaling \$1.89 billion at the end of 2018 versus \$1.74 billion at the end of 2017. Demand deposits decreased by \$31.7 million while term deposits grew by \$160 million, registered deposits (i.e., RRSP, RRIF, RESP and TFSA) grew by \$11.8 million and accrued interest payable grew by \$4.5 million during the year. The decrease in demand deposits and significant growth in term deposits reflected members taking advantage of the higher yields associated with term deposit investments and the rising interest rate environment.





### SECURED BORROWING

During 2018, G&F maintained its available operating line and term facility with Central 1 at \$105 million. In addition, G&F maintains a credit facility agreement with Fédérations des caisses Desjardins du Québec of \$30 million. As at December 31, 2018, \$14.9 million was drawn against the Central 1 credit facilities. As part of the credit union's ongoing management of liquidity, capital, and interest rate risk, G&F securitizes residential mortgages thereby entering into a secured borrowing arrangement with Central 1. The outstanding secured borrowing with Central 1 was \$36.5 million at the end of 2018, a decrease from the balance at the end of 2017 of \$45.3 million.

### MEMBERS' EQUITY

G&F achieved net income of \$10.4 million, and a net unrealized gain from cash flow hedges (net of tax) of \$603 thousand in 2018 resulting in total comprehensive income of \$11.0 million - a return on members' equity of 11.2%. Capital adequacy at the end of 2018 was 14.52%, well exceeding the regulatory requirement of 8% and the supervisory target of 10%.

### NET INTEREST INCOME

In 2018, the Canadian economy experienced healthy growth and was running close to capacity which led the Bank of Canada to increase its overnight target rate three times by 0.25% each in January, July and October to end the year at 1.75%. Accordingly, G&F increased its prime rate in January, July and October to end 2018 at 3.95% compared to 3.20% at the end of 2017.

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 1.90% in 2017 to 1.96% in 2018. 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 \$4.4 million, or 12.6% to \$38.9 million benefiting from 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 provisions for credit losses. Other income of \$8.4 million in 2018 was on par with 2017 at \$8.4 million. Although member services income increased by \$184 thousand or 2.1% in 2018, the other income in 2017 included a realized gain of \$228 thousand on the redemption by Central 1 of Class E shares held by the credit union.

### OPERATING EXPENSES

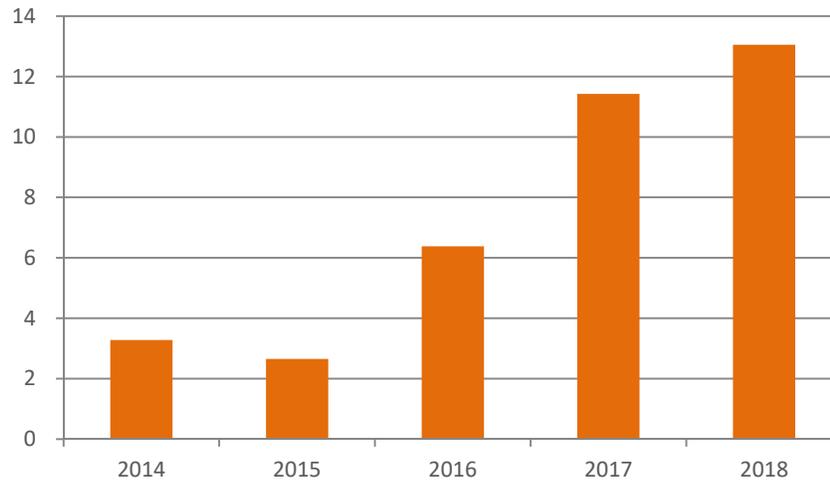
Operating expenses increased by \$3.0 million or 9.4% to \$34.5 million in 2018 as a result of increases in salaries and employee benefits and occupancy costs (which includes the first full year of operations for our Metrotown branch as well as the opening of our new West End branch in late 2018). Other operating expenses such as data processing, dues and advertising and promotion increased naturally with the growth of the credit union. In addition, our strong financial results in 2018 allowed a contribution of \$250 thousand to the G&F Financial Group Foundation continuing our commitment to community investment. As a percentage of assets, the operating expenses remained generally flat at 1.74% in 2018 versus 1.73% in 2017 as the credit union continued to realize operating efficiencies through growth, economies of scale and collaborating with other like-minded organizations.

### EARNINGS FROM OPERATIONS

G&F experienced record earnings from operations of \$12.8 million in 2018, up \$1.4 million or 12.1% compared to 2017. G&F has been making long-term strategic investments by expanding the branch network and improving 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, the Brentwood branch in 2016 and the aforementioned Metrotown branch and West End branch in 2017 and 2018 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 2018.

G&F has a long history of sharing our profits with the local communities in which we live and serve by way of donations, sponsorships, educational bursaries, and scholarships. Total distributions from both the credit union and G&F Financial Group Foundation totaled \$389 thousand or 3.0% of earnings from operations in 2018.

#### Earnings from Operations (in \$millions)



#### TOTAL COMPREHENSIVE INCOME

The total comprehensive income for 2018 was \$11.0 million which included a 4.25% dividend on members' equity shares of \$119 thousand and a 5.25% dividend on investment equity shares of \$196 thousand approved by the Board of Directors, a provision for income taxes of \$2.1 million and a net unrealized gain from cash flow hedges (net of tax) of \$603 thousand.

#### FUNDS UNDER ADMINISTRATION

Funds under administration by G&F comprise of commercial loans that are managed by the credit union and syndicated with other financial institutions for purposes of risk sharing, liquidity management and to service members who have loan amounts above the credit union's single member cap. The syndicated loan balance ended 2018 at \$104 million, an increase of \$6.2 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 \$1.2 million or 0.5% in 2018 to end the year at \$224 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 21 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.

## 2019 Outlook

The Bank of Canada raised its key interest rate three times in 2018 but it is expected to enact a more neutral stance for 2019 as the Canadian and global economy are showing signs of vulnerability. Trade uncertainty between the US and China continues to cast a cloud over global growth and its prospects. The Bank is projecting Canada's GDP growth will slow to 1.7% this year before rebounding to 2.1% in 2020. BC economic growth is softening as well following four years in which growth expanded by more than 3.5% annually. A weakening in the province's housing market combined with lower export momentum are expected to slow BC's GDP growth to 2.9% in 2019.

Given this economic outlook, G&F anticipates a year of steady growth in its loans, deposits and wealth management portfolio. The anticipated slowing BC economic environment, stock market and Lower Mainland real estate market will ease growth rates compared to those experienced in recent years. G&F's business plan for 2019 continues our drive to provide a differentiated member experience focused on relationships and advice while executing on an omni-channel strategy to enhance our member experience across all channels.

GULF & FRASER FISHERMEN'S CREDIT UNION

## Five-Year Overview - Financial Highlights

(Expressed in thousands of dollars)

*Consolidated Statement of Financial Position (unaudited)*

	2018	2017	2016	2015	2014
<b>ASSETS</b>					
Cash and investments	\$186,850	\$176,694	\$238,253	\$161,000	\$138,179
Loans	1,862,404	1,711,125	1,455,277	1,230,167	1,121,748
Premises, equipment, intangible assets, properties	8,765	7,767	7,768	7,516	9,365
Other assets	5,603	3,913	4,312	4,386	4,656
	<b>\$2,063,622</b>	<b>\$1,899,499</b>	<b>\$1,705,610</b>	<b>\$1,403,069</b>	<b>\$1,273,948</b>
<b>Liabilities and Members' Equity</b>					
Deposits	\$1,887,475	\$1,742,843	\$1,557,016	\$1,271,819	\$1,150,106
Members' shares	8,047	6,943	3,522	3,547	3,593
Secured borrowings	51,455	45,299	49,758	37,459	38,755
Other liabilities	6,676	6,130	6,189	5,991	3,021
	1,953,653	1,801,215	1,616,485	1,318,816	1,195,475
Members' equity					
Accumulated other comprehensive income	153	496	524	867	318
Retained earnings	109,816	97,788	88,601	83,386	78,155
	109,969	98,284	89,125	84,253	78,473
	<b>\$2,063,622</b>	<b>\$1,899,499</b>	<b>\$1,705,610</b>	<b>\$1,403,069</b>	<b>\$1,273,948</b>

*Consolidated Statement of Comprehensive Income (unaudited)*

	2018	2017	2016	2015	2014
Interest income	\$70,028	\$56,655	\$47,735	\$43,265	\$41,940
Interest expense	31,170	22,156	18,917	17,204	16,661
<b>Net Interest Income</b>	<b>38,858</b>	<b>34,499</b>	<b>28,818</b>	<b>26,061</b>	<b>25,279</b>
Other income	8,404	8,420	7,177	6,232	5,877
Operating margin	47,262	42,919	35,995	32,293	31,156
Operating expenses	34,459	31,493	29,613	29,638	27,876
<b>Earnings from operations</b>	<b>12,803</b>	<b>11,426</b>	<b>6,382</b>	<b>2,655</b>	<b>3,280</b>
Gain on sale of premises	0	0	0	3,348	0
Distributions to members	(315)	(157)	(109)	(110)	(109)
Income before income taxes	12,488	11,269	6,273	5,893	3,171
Provision for income taxes	2,126	2,082	1,058	662	450
<b>Net income</b>	<b>10,362</b>	<b>9,187</b>	<b>5,215</b>	<b>5,231</b>	<b>2,721</b>
Net unrealized gain (loss) from cash flow hedges (net of tax)	603	(975)	(343)	549	318
Net unrealized gain on financial investments (net of tax)	0	947	0	0	0
<b>Total comprehensive income</b>	<b>\$10,965</b>	<b>\$9,159</b>	<b>\$4,872</b>	<b>\$5,780</b>	<b>\$3,039</b>

	2018	2017	2016	2015	2014
<i>Financial Statistics (unaudited)</i>					
Asset growth	8.6%	11.4%	21.6%	10.1%	6.4%
Loan growth	8.8%	17.6%	18.3%	9.7%	7.5%
Deposit growth	8.3%	11.9%	22.4%	10.6%	4.0%
Operating efficiency	71.85%	72.09%	80.92%	88.17%	87.92%
<i>Percent of average assets (unaudited)</i>					
Net interest income	1.96%	1.90%	1.85%	1.93%	2.08%
Other income	0.42%	0.46%	0.46%	0.46%	0.48%
Operating expenses	1.74%	1.73%	1.90%	2.20%	2.29%
Operating return on assets	0.65%	0.63%	0.41%	0.20%	0.27%
Net (after-tax) return on assets	0.52%	0.51%	0.33%	0.39%	0.22%
<i>Other statistics (unaudited)</i>					
Retail branches	16	15	14	13	13
Membership	32,388	30,969	30,027	29,247	27,808
Investment portfolios and mutual funds, at market value	\$223,673	\$222,456	\$197,646	\$179,697	\$160,616
Syndicated loans	\$103,789	\$97,638	\$47,350	\$26,446	\$748
Assets under administration	\$2,391,083	\$2,219,593	\$1,950,606	\$1,609,212	\$1,435,312