Desjardins Group Management's Discussion and Analysis

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SECTION 1.0 Desjardins Group

This section gives a brief overview of Desjardins Group and its 2017 financial highlights. It also includes material events, priority financial objectives, a description of the economic environment in 2017, and the economic and financial outlook for 2018.

SECTION 2.0 Review of financial results

This section provides an analysis of Desjardins Group's results for the year ended December 31, 2017. It contains information on each of Desjardins Group's business segments, including a profile, a description of the industry, the strategy and priorities for 2018, and an analysis of financial results. An analysis of fourth quarter results and quarterly trends is also included.

SECTION 3.0 Balance sheet review

This section provides commentary on Desjardins Group's balance sheet. It mainly addresses financing activities and recruitment of savings, as well as capital management and off-balance sheet arrangements.

SECTION 4.0 Risk management

This section focuses on the risk management framework and presents the various risks associated with Desjardins Group's operations. It also presents risk factors that could impact its future results.

SECTION 5.0 Additional information

This section presents controls and procedures, related party disclosures, critical accounting policies and estimates, future accounting changes and various annual statistics.

Note to the reader

Desjardins Group (hereinafter also referred to as Desjardins) comprises the Desjardins caisse network in Quebec and Ontario (the caisses), the *Fédération des caisses Desjardins du Québec* (the Federation) and its subsidiaries (including Desjardins Capital Inc.), the *Fédération des caisses populaires de l'Ontario Inc.* and the *Fonds de sécurité Desjardins*.

The Management's Discussion and Analysis (MD&A) dated February 26, 2018, presents the analysis of the results of and main changes to Desjardins Group's balance sheet for the year ended December 31, 2017, in comparison to previous fiscal years. Desjardins Group reports financial information in compliance with *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings* prescribed by the Canadian Securities Administrators (CSA). Desjardins Group is not a reporting issuer, on a combined basis, under this regulation. However, it has chosen to apply the provisions provided in this regulation to demonstrate its willingness to comply with best practices in financial governance. Information about Desjardins Group's controls and procedures is presented in the "Additional information" section of this MD&A.

The MD&A should be read in conjunction with the Combined Financial Statements, including the Notes thereto, as at December 31, 2017.

Additional information about Desjardins Group is available on the website of the System for Electronic Document Analysis and Retrieval (SEDAR) at **www.sedar.com** (under the Desjardins Capital Inc. profile). The Annual Information Form of the Federation (under the *Fédération des caisses Desjardins du Québec* profile) can be found on SEDAR as well. Further information is available on the Desjardins website at **www.desjardins.com/ca/about-us/investor-relations**. None of the information presented on these sites is incorporated by reference into this MD&A.

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

Desjardins Group's public communications often include oral or written forward-looking statements. Such forward-looking statements are contained in this MD&A and may be incorporated in other filings with Canadian regulators or in any other communications. Forward-looking statements include, but are not limited to, comments about Desjardins Group's objectives regarding financial performance, priorities, operations, the review of economic conditions and markets, as well as the outlook for the Canadian, U.S., European and other international economies. These forward-looking statements include those appearing in sections 1.3 "Financial strategy and objectives," 1.4 "Changes in the economy," 2.0 "Review of financial results", 3.0 "Balance sheet review" and 5.0 "Additional information" of this MD&A. Such statements are typically identified by words or phrases such as "believe", "expect", "anticipate", "intend", "estimate", "plan" and "may", words and expressions of similar import, and future and conditional verbs.

By their very nature, such statements involve assumptions, uncertainties and inherent risks, both general and specific. It is therefore possible that, due to many factors, the assumptions made may be incorrect, or that the predictions, forecasts or other forward-looking statements as well as Desjardins Group's objectives and priorities may not materialize or may prove to be inaccurate and that actual results differ materially. Desjardins Group cautions readers against placing undue reliance on these forward-looking statements since actual results, conditions, actions and future events could differ significantly from the targets, expectations, estimates or intents in the forward-looking statements, either explicitly or implicitly.

A number of factors, many of which are beyond Desjardins Group's control and the effects of which can be difficult to predict, could influence the accuracy of the forward-looking statements in this MD&A. These factors include those discussed in Section 4.0 "Risk management," such as credit, market, liquidity, operational, insurance, strategic and reputation risk. Additional factors include legal and regulatory environment risk, including legislative or regulatory developments in Quebec, Canada or globally, such as changes in fiscal and monetary policies, reporting guidance, liquidity regulatory guidance and capital guidelines, or interpretations thereof. There is also environmental risk, which is the risk of financial, operational or reputational loss for Desjardins Group as a result of environmental impacts or issues, whether they are a result of Desjardins Group's credit or investment activities or its operations. Lastly, there is the risk related to pension plans, which is the risk of losses resulting from pension plan commitments made by Desjardins Group for the benefit of its employees arising essentially from interest rate, price, foreign exchange and longevity risks.

Additional factors that may affect the accuracy of the forward-looking statements in this MD&A also include factors related to cyber threats, technological advancement and regulatory developments, household indebtedness and real estate market trends, the low interest rate environment and geopolitical risks. Furthermore, there are factors related to general economic and business conditions in regions in which Desjardins Group operates; changes in the economic and financial environment in Quebec, Canada and globally, including short- and long-term interest rates, inflation, debt market fluctuations, foreign exchange rates, the volatility of capital markets, tighter liquidity conditions in certain markets, the strength of the economy and the volume of business conducted by Desjardins Group in a given region; monetary policies; the accuracy and completeness of information concerning clients and counterparties; the critical accounting estimates and accounting standards applied by Desjardins Group; new products and services to maintain or increase Desjardins Group's market share; geographic concentration; acquisitions and joint arrangements; credit ratings; catastrophes and climate change.

Other factors that could influence the accuracy of the forward-looking statements in this MD&A include amendments to tax laws, unexpected changes in consumer spending and saving habits, the ability to implement Desjardins Group's disaster recovery plan within a reasonable time, the potential impact of international conflicts or natural disasters, and Desjardins Group's ability to anticipate and properly manage the risks associated with these factors, despite a disciplined risk management environment.

It is important to note that the above list of factors that could influence future results is not exhaustive. Other factors could have an adverse effect on Desjardins Group's results. Additional information about these and other factors is found in Section 4.0, "Risk management" of this MD&A. Although Desjardins Group believes that the expectations expressed in these forward-looking statements are reasonable, it cannot guarantee that these expectations will prove to be correct. Desjardins Group cautions readers against placing undue reliance on forward-looking statements when making decisions. Readers who rely on these statements must carefully consider these risk factors and other uncertainties and potential events.

The significant economic assumptions underlying the forward-looking statements in this MD&A are described in the section "Economic outlook for 2018" of this MD&A. These assumptions may also be updated in the quarterly MD&As. Any forward-looking statements contained in this MD&A represent the views of management only as at the date hereof, and are presented for the purpose of assisting readers in understanding and interpreting Desjardins Group's balance sheet as at the dates indicated or its results for the periods then ended, as well as its strategic priorities and objectives. These statements may not be appropriate for other purposes. Desjardins Group does not undertake to update any oral or written forward-looking statements that could be made from time to time by or on behalf of Desjardins Group, except as required under applicable securities legislation.

BASIS OF PRESENTATION OF FINANCIAL INFORMATION

The Combined Financial Statements have been prepared by Desjardins Group's management in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec, which do not differ from IFRS. The accounting policies used did not differ from those used in 2016. For more information about the accounting policies used, see the Combined Financial Statements.

This MD&A was prepared in accordance with the regulations in force on continuous disclosure obligations issued by the CSA. Unless otherwise indicated, all amounts are presented in Canadian dollars ($) and are primarily from Desjardins Group's Combined Financial Statements.

To assess its performance, Desjardins Group uses IFRS measures and various non-IFRS financial measures. Non-IFRS financial measures, other than the regulatory ratios, do not have a standardized definition and are not directly comparable to similar measures used by other companies, and may not be directly comparable to any IFRS measures. Investors, among others, may find these non-IFRS measures useful in analyzing financial performance. They are defined as follows:

Average assets – Average loans and acceptances – Average deposits – Average equity

The average balance for these items is used to measure growth. It is equal to the average of the amounts presented in the Combined Financial Statements at the end of the previous five quarters, calculated starting from December 31.

Growth differential between adjusted operating income and adjusted non-interest expense

The growth differential between operating income and non-interest expense is used to measure sustainability and profitability. It is the difference between the growth rate for operating income and for non-interest expense.

The following table presents the calculation of the growth differential between adjusted operating income and adjusted non-interest expense.

(in millions of dollars and as a percentage)	**2017**	2016	2015
Operating income	**$ 15,413**	$ 14,082	$ 13,880
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company[(1)]	**(278)**	-	-
Gain related to the acquisition of State Farm's Canadian operations[(1)]	**-**	-	(52)
Adjusted operating expenses	**$ 15,135**	$ 14,082	$ 13,828
Growth in adjusted operating income	**7.5%**	1.8%	9.6%
Non-interest expense	**$ 7,348**	$ 7,204	$ 6,959
Expenses related to the acquisition of State Farm's Canadian operations[(1)]	**(44)**	(45)	(45)
Adjusted non-interest expense	**$ 7,304**	$ 7,159	$ 6,914
Growth in adjusted non-interest expense	**2.0%**	3.5%	7.0%
Growth differential between adjusted operating income and adjusted non interest expense	**5.5%**	(1.7)%	2.6%

(1) Amounts before income taxes.

Adjusted surplus earnings of Desjardins Group before member dividends

The concept of adjusted surplus earnings is used to exclude specific items in order to present financial performance based on operating activities. These specific items, such as acquisitions and disposals, are unrelated to operations.

Desjardins Group's surplus earnings before member dividends are adjusted to exclude the following specific items: the gain and expenses, net of income taxes, related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017, as well as the gain as at the acquisition date and expenses, net of income taxes, incurred as part of the acquisition of the Canadian operations of State Farm Mutual Automobile Insurance Company (State Farm), completed on January 1, 2015. These latter expenses include the costs related to the transaction and the integration of operations as well as processing expenses.

The following table presents a reconciliation of surplus earnings before member dividends as presented in the Combined Financial Statements and the adjusted surplus earnings as presented in the MD&A.

(in millions of dollars)	2017	2016	2015
Presentation of the surplus earnings before member dividends in the Combined Financial Statements	**$ 2,151**	$ 1,772	$ 1,959
Specific items, net of income taxes			
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company[1]	**(249)**	-	-
Gain and expenses related to the acquisition of State Farm's Canadian operations	**32**	33	(19)
Presentation of the adjusted surplus earnings before member dividends	**$ 1,934**	$ 1,805	$ 1,940

(1) The amount before income taxes was $278 million for the year ended December 31, 2017, as presented in Note 20, "Significant disposals" to the Combined Financial Statements.

Adjusted net surplus earnings − Property and Casualty Insurance segment

The net surplus earnings of the Property and Casualty Insurance segment (P&C) are adjusted to exclude the following specific items: the gain and expenses, net of income taxes, related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017, as well as the gain as at the acquisition date and expenses, net of income taxes, incurred as part of the acquisition of State Farm's Canadian operations, completed on January 1, 2015. These latter expenses include the costs related to the transaction and the integration of operations as well as processing expenses.

The following table presents a reconciliation of the net surplus earnings of the Property and Casualty Insurance segment as presented in the Combined Financial Statements, and the adjusted net surplus earnings as presented in the MD&A.

(in millions of dollars)	2017	2016	2015
Presentation of the net surplus earnings of the Property and Casualty Insurance segment in the Combined Financial Statements	**$ 446**	$ 296	$ 360
Specific items, net of income taxes			
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company[1]	**(241)**	-	-
Gain and expenses related to the acquisition of State Farm's Canadian operations[2]	**32**	33	(22)
Presentation of the adjusted net surplus earnings of the Property and Casualty segment	**$ 237**	$ 329	$ 338

(1) The difference with the data presented in the table for adjusted surplus earnings of Desjardins Group before member dividends is related to intersegment transaction expenses.

(2) The difference with the data presented in the table for adjusted surplus earnings of Desjardins Group before member dividends is related to an amount from the Wealth Management and Life and Health Insurance segment.

Productivity index and adjusted productivity index

The productivity index is used to measure efficiency and is equal to the ratio of non-interest expense to total income, net of expenses related to claims, benefits, annuities and changes in insurance contract liabilities, expressed as a percentage. A lower ratio indicates greater productivity.

The following table presents the calculation of the productivity index as presented in the MD&A.

(in millions of dollars and as a percentage)	2017	2016[1]	2015[1]
Non-interest expense	**$ 7,348**	$ 7,204	$ 6,959
Total income	**17,101**	15,201	15,242
Claims, benefits, annuities and changes in insurance contract liabilities	**(6,717)**	(5,446)	(5,431)
Total income excluding claims	**$ 10,384**	$ 9,755	$ 9,811
Productivity index	**70.8%**	73.8%	70.9%
Adjusted productivity index[2]	**72.3**	73.4	70.8

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.

(2) Takes into account the specific items presented under "Adjusted surplus earnings of Desjardins Group before member dividends" subsection of this section.

Net interest margin

Net interest margin is used to measure profitability. It is equal to net interest income expressed as a percentage of average interest-bearing assets.

Table 6 of Desjardins Group's MD&A provides more detailed information on the net interest margin.

Gross impaired loans/gross loans and acceptances ratio

The gross impaired loans/gross loans and acceptances ratio is used to measure loan portfolio quality and is equal to gross impaired loans expressed as a percentage of total gross loans and acceptances.

Table 36 of Desjardins Group's MD&A provides more detailed information on this indicator.

Loss ratio – Expense ratio – Combined ratio

These ratios are used to measure the profitability of the Property and Casualty Insurance segment.

The loss ratio is equal to incurred claims, net of reinsurance, expressed as a percentage of net premiums earned, excluding the market yield adjustment. Market yield adjustment is defined as the impact of changes in the discount rate on the provisions for claims and adjustment expenses, based on the change in the market-based yield of the underlying assets for these provisions.

The loss ratio is comprised of the following ratios:

- Current year loss ratio, which is the loss ratio excluding catastrophe and major event claims expenses for the current year as well as changes in prior year claims, net of related reinsurance, not including reinstatement premiums, as applicable.
- Loss ratio related to catastrophes and major events, which is the loss ratio including catastrophe and major event claims expenses for the current year, net of reinsurance and including the impact of reinstatement premiums, as applicable.
- Ratio of changes in prior year claims, which is the loss ratio including, in the numerator, the effect of changes in total prior year claims for a given period, net of related reinsurance, not including, in the denominator, reinstatement premiums, as applicable.

The expense ratio is equal to operating expenses expressed as a percentage of net premiums earned.

The combined ratio is equal to the sum of the loss ratio and the expense ratio.

The following table presents the calculation of the loss ratio, the expense ratio and the combined ratio, as presented in the MD&A.

(in millions of dollars and as a percentage)	**2017**	2016	2015
Net premiums	**$ 3,896**	$ 3,207	$ 3,113
Premiums excluded from the loss ratio[1]	**(61)**	(149)	(117)
Net premiums considered in the ratio denominators	**$ 3,835**	$ 3,058	$ 2,996
Claims, benefits, annuities, and changes in insurance contract liabilities	**$ 2,555**	$ 1,838	$ 1,922
Market yield adjustment (MYA)	**62**	39	(27)
Other items excluded from the loss ratio[1]	**(20)**	(36)	(34)
Claims, benefits, annuities and changes in insurance contract liabilities excluding the MYA	**$ 2,597**	$ 1,841	$ 1,861
Loss ratio	**67.7%**	60.2%	62.1%
Non-interest expense	**$ 1,099**	$ 1,132	$ 1,070
Other expenses excluded from the expense ratio[2]	**(158)**	(329)	(306)
Operating expenses	**$ 941**	$ 803	$ 764
Expense ratio	**24.5%**	26.3%	25.5%
Combined ratio	**92.2**	86.5	87.6

[1] Due mainly to the life insurance activities of Western Life Assurance Company, the sale of which was completed on July 1, 2017.
[2] Due mainly to the life insurance and insurance product distribution activities of Western Life Assurance Company and Western Financial Group Inc., including expenses related to the sale of these two entities on July 1, 2017, and expenses related to the acquisition of State Farm's Canadian operations on January 1, 2015.

Return on equity and adjusted return on equity

Return on equity is used to measure profitability resulting in value creation for members and clients. Expressed as a percentage, it is equal to surplus earnings before member dividends, excluding the non-controlling interests' share, divided by average equity before non-controlling interests.

The following table presents the reconciliation of return on equity with surplus earnings before member dividends as presented in the MD&A.

(in millions of dollars and as a percentage)	**2017**	2016	2015
Surplus earnings before member dividends	**$ 2,151**	$ 1,772	$ 1,959
Non-controlling interests' share	**(43)**	(76)	(172)
Group's share	**2,108**	1,696	1,787
Average equity before non-controlling interests' share	**$ 23,228**	$ 21,236	$ 19,667
Return on equity	**9.1%**	8.0%	9.1%
Adjusted return on equity[1]	**8.1**	8.1	9.0

[1] Takes into account the specific items presented under "Adjusted surplus earnings of Desjardins Group before member dividends" subsection in this section.

Income

Operating income

The concept of operating income is used to analyze financial results. This concept allows for better structuring of financial data and makes it easier to compare operating activities from one period to the next by excluding the volatility of results specific to investments, particularly regarding the extent of life and health insurance and P&C insurance operations, for which a very large proportion of investments are recognized at fair value through profit or loss. The analysis therefore breaks down Desjardins Group's income into two parts, namely operating income and investment income, which make up total income. This measure is not directly comparable to similar measures used by other companies.

Operating income includes net interest income, generated mainly by the Personal and Business Services segment and the Other category, net premiums and other operating income such as deposit and payment service charges, lending fees and credit card service revenues, income from brokerage and investment fund services, management and custodial service fees, foreign exchange income as well as other income. These items, taken individually, correspond to those presented in the Combined Financial Statements.

Investment income

Investment income includes net income on securities at fair value through profit or loss, net income on available-for-sale securities and net other investment income. These items, taken individually, correspond to those presented in the Combined Financial Statements. The life and health insurance and P&C insurance subsidiaries' matching activities, which include changes in fair value, gains and losses on disposals and interest and dividend income on securities, are presented with investment income, given that these assets back insurance liabilities, which are recognized under expenses related to claims, benefits, annuities and changes in insurance contract liabilities in the Combined Financial Statements. In addition, this investment income includes changes in the fair value of investments for the Personal and Business Services segment, recognized at fair value through profit or loss.

The following table shows the correspondence of total income between the MD&A and the Combined Financial Statements:

(in millions of dollars)	**2017**	2016[1]	2015[1]
Presentation of income in the Combined Financial Statements			
Net interest income	**$ 4,405**	$ 4,273	$ 4,279
Net premiums	**8,049**	7,168	6,907
Other income			
Deposit and payment service charges	**458**	488	489
Lending fees and credit card service revenues	**660**	574	550
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**428**	376	365
Net income on securities at fair value through profit or loss	**1,079**	533	809
Net income on available-for-sale securities	**408**	388	318
Net other investment income	**201**	198	235
Foreign exchange income	**77**	70	88
Other	**249**	27	165
Total income	**$ 17,101**	$ 15,201	$ 15,242
Presentation of income in the Management's Discussion and Analysis			
Net interest income	**$ 4,405**	$ 4,273	$ 4,279
Net premiums	**8,049**	7,168	6,907
Other operating income			
Deposit and payment service charges	**458**	488	489
Lending fees and credit card service revenues	**660**	574	550
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**428**	376	365
Foreign exchange income	**77**	70	88
Other	**249**	27	165
Operating income	**15,413**	14,082	13,880
Investment income			
Net income on securities at fair value through profit or loss	**1,079**	533	809
Net income on available-for-sale securities	**408**	388	318
Net other investment income	**201**	198	235
	1,688	1,119	1,362
Total income	**$ 17,101**	$ 15,201	$ 15,242

[1] Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.

Provisioning rate

The provisioning rate is used to measure loan portfolio quality, and is equal to the provision for credit losses divided by average gross loans and acceptances.

The following table presents the calculation of the provisioning rate as presented in the MD&A.

(in millions of dollars and as a percentage)	2017	2016	2015
Provision for credit losses	**$ 349**	$ 319	$ 377
Average gross loans	**171,737**	162,979	155,431
Average gross acceptances	**69**	108	483
Average gross loans and acceptances	**$ 171,806**	$ 163,087	$ 155,914
Provisioning rate	**0.20%**	0.20%	0.24%

REGULATORY ENVIRONMENT

Regulatory environment

Desjardins Group's operations are governed in particular by the *Act respecting financial services cooperatives* and the *Act respecting the Mouvement Desjardins*. The AMF is the main government agency that oversees and monitors deposit-taking institutions (other than banks) and insurance companies that do business in Quebec and are governed by Quebec law, including the caisses and the Federation and its insurance subsidiaries. Other federal and provincial regulations, in addition to those of regulators, may also govern some operations of Desjardins Group entities, such as the Office of the Superintendent of Financial Institutions (OSFI) related to property and casualty insurance, custodial and trust services and banking services provided by Zag Bank.

Moreover, Desjardins Group complies with the minimum regulatory capital requirements issued by the AMF, which reflect the provisions of the Basel III Accord. As mentioned on page 13, although Desjardins Group is not a reporting issuer under AMF *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings*, it has chosen to apply the provisions in the regulation to demonstrate its willingness to comply with sound practices in financial governance. Desjardins Group's financial and corporate governance are discussed on page 108 of this MD&A and in the "Corporate governance" section of the 2017 Desjardins Group Annual Report.

In June 2013, the AMF determined that Desjardins Group met the criteria to be designated a domestic systemically important financial institution (D-SIFI), which subjects Desjardins Group to higher capital requirements and enhanced disclosure requirements, among other things, as instructed by the AMF. Since January 1, 2016, Desjardins Group has therefore been subject, as a D-SIFI, to an additional capital requirement of 1% on its minimum capital ratios. Also, based on the recommendations issued by the Enhanced Disclosure Task Force (EDTF) of the Financial Stability Board contained in the document "Enhancing the Risk Disclosures of Banks", Desjardins Group is continuing to develop its external disclosures and integrating all these recommendations into its risk management disclosure framework. Desjardins Group also continues to adapt its disclosure to comply with the principles of risk data aggregation and risk reporting (RDARR), which will strengthen governance as well as risk data aggregation and risk reporting capabilities. Furthermore, Desjardins Group developed a living will, detailing the actions it will take to restore its financial position in the event of a crisis. Note that the OSFI also determined in 2013 that Canada's six major financial institutions meet the criteria for designation as D-SIFI.

It should also be mentioned that Desjardins Bank, National Association, a subsidiary of the Federation incorporated under U.S. federal laws, is supervised by the Office of the Comptroller of the Currency of the United States (OCC), and that the Federation's operations in the United States, as a bank holding company, are subject to the supervisory and regulatory authority of the Board of Governors of the Federal Reserve System. Desjardins Florida Branch, the branch of the Federation operating in the State of Florida and incorporated under U.S. federal laws, is also supervised by the OCC. Desjardins Group is further governed by the U.S. *Bank Holding Company Act* and has the status of financial holding company (FHC) in the U.S. In order to maintain such status, Desjardins Group must continue to meet capital requirements and certain other requirements to be considered "well capitalized" and be deemed "well managed" in accordance with the regulations of the U.S. Federal Reserve (the Fed).

Changes in the regulatory environment

Desjardins Group closely monitors regulations for financial products and services, as well as new developments in fraud, corruption, tax evasion, protection of personal information, money laundering and terrorist financing in order to mitigate any negative impact on its operations, and aims to comply with best practices in this regard. Additional information on changes in regulatory capital is provided in the "Capital management" section.

The *Act respecting financial services cooperatives* and the *Act respecting the Mouvement Desjardins*

On October 5, 2017, the Quebec Minister of Finance tabled Bill 141, *An Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions* (the Bill) in the National Assembly. The Bill will have significant impacts on all institutions and intermediaries operating in Quebec's financial sector. Bill 141 is intended to update and modernize the legislative framework for Quebec's financial sector so that the financial institutions that it governs will have all the levers they need to operate in a very competitive environment and governance that is consistent with best practices. The Bill will have impacts on a series of laws, including the *Act respecting insurance*, the *Act respecting financial services cooperatives*, the *Act respecting the distribution of financial products and services* and the *Deposit Insurance Act*. The *Act respecting financial service cooperatives* will be amended to, among other things, prescribe the rules for organizing a network of financial services cooperatives and a financial group, as well as the rules for issuing capital shares and investment shares.

The Bill will also add a chapter concerning the *Groupe coopératif Desjardins* to replace the *Act respecting the Mouvement Desjardins* and strengthen financial solidarity mechanisms within Desjardins, among other things. In this way, the Bill will affirm the Federation's mission to manage Desjardins Group's risks and look after the financial health and sustainability of the cooperative group. The Federation and the *Fonds de sécurité Desjardins* will therefore be given additional special powers of supervision and intervention regarding the protection of creditors, including depositors, and the public interest. The proposed amendments to the *Deposit Insurance Act* include a proposal to have this Act govern the supervision and control of deposit-taking activities and the activities of authorized deposit-taking institutions, as well as recovery and resolution mechanisms in the event of failure of deposit-taking institutions. Furthermore, the Bill will provide for revised supervision for Quebec insurers, including the introduction of a modern regime for selling insurance over the Internet. The government's parliamentary leader has not provided a specific timeline for passage of the Bill in its definitive version. Desjardins Group continues to closely monitor the legislative process and analyze the impacts of this Bill.

Defined benefit pension plan legislation

The *Act to amend the Supplemental Pension Plans Act mainly with respect to the funding of defined benefit pension plans* came into force on January 1, 2016. The changes to the funding rules are intended to promote the sustainability of private pension plans by ensuring funding that must include an explicit stabilization provision determined according to the plan's investment policy. Funding on a solvency basis is no longer required. On December 20, 2017, the Quebec government issued a regulation to set out the requirements applicable to the elements introduced in 2016, particularly the funding policy and the annuity purchase policy. Desjardins Group continues to monitor developments in legislation that could affect pension plans.

Rules concerning capital instruments

The Capital Adequacy Requirements (CAR) Guideline of the Office of the Superintendent of Financial Institutions (OSFI) applicable to Canadian financial institutions includes requirements for Non-Viability Contingent Capital as part of regulatory capital. Desjardins Group, under the AMF's guideline on adequacy of capital base standards, is subject to similar rules applicable to non-viability contingent capital in its regulatory capital. However, Desjardins Group has not issued any instrument subject to these rules since discussions with the AMF are still underway on how Desjardins Group will apply these rules.

Proceeds of Crime (Money Laundering) and Terrorist Financing Act

On June 19, 2014, to strengthen the Canadian regime to fight money laundering and terrorist financing as well as improve the effectiveness of its financial sanctions, the Parliament of Canada passed the *Economic Action Plan 2014 Act, No. 1*. The Act includes, in particular, amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* and the regulations thereunder. Some of these amendments came into effect in June 2016. The rest will come into effect gradually. The transitional period for the application of the new measures for ascertaining identity has been extended to January 23, 2018. Furthermore, on June 22, 2017, the Parliament of Canada passed an *Act to implement certain provisions of the budget tabled in Parliament on March 22, 2017 and other measures*. This Act includes amendments to the P*roceeds of Crime (Money Laundering) and Terrorist Financing Act*. Desjardins Group is preparing to implement these legislative changes and is closely monitoring developments to assess their impact on its operations.

Recapitalization regime for domestic systemically important banks

On June 16, 2017, the Department of Finance Canada pre-published three draft regulations to implement the Bank Recapitalization (Bail-in) Regime and the OSFI issued a draft guideline on Total Loss Absorbing Capacity (TLAC) for comments. The introduction of the regulations and the TLAC guideline are intended to ensure that a non-viable domestic systemically important bank (D-SIB) has sufficient loss absorbing capacity to support its recapitalization. The D-SIBs will be required to issue the ratios specified in the TLAC guideline as of the quarter commencing November 1, 2018 and comply with the requirements of the TLAC guideline no later than November 1, 2021. This regime is not applicable immediately to Desjardins Group because it is regulated by the AMF. Furthermore, the bill tabled by the Quebec government on October 5, 2017, as mentioned above, provides for certain recovery and resolution mechanisms in the event of failure of deposit-taking institutions.

Financial reforms in the U.S.

Should reform initiatives in the U.S. pertaining to financial regulation become a reality, they may affect non-U.S. financial institutions operating in the U.S., including Desjardins Group. It should be noted that the future of the reforms being considered is still uncertain when it comes to the U.S. Congress. The rules resulting from the *Dodd-Frank Wall Street Reform and Consumer Protection Act* which affect, in particular, the implementation of provisions on swap trading, proprietary trading and ownership interests in hedge funds (the Volcker rule), as well as those concerning the Enhanced Prudential Standards and the submission of a resolution plan, could be affected. Desjardins Group continues to closely monitor developments in these requirements and the reform initiatives.

Standard for automatic exchange of financial information in tax matters

The Organisation for Economic Co-operation and Development (OECD) has set up a "Standard for Automatic Exchange of Financial Information in Tax Matters", based on the same general principles and obligations as those of the *Foreign Account Tax Compliance Act*, but globally. The standard took effect in Canada on July 1, 2017, with the first exchange of information between Canada and the competent authorities scheduled for May 1, 2018. Desjardins Group has implemented various solutions to ensure its compliance while minimizing the impact on member and client experience.

Data confidentiality and security

Data confidentiality and security is a rapidly changing area. In Canada, new provisions of the *Personal Information Protection and Electronic Documents Act* (PIPEDA) will soon come into force. They will, in particular, require businesses to give notice of any breaches of security safeguards and impose the keeping of a register. Failure to give notice will result in a fine. It should be noted that in Europe, the *General Data Protection Regulation* (GDPR), which will come into force in May 2018, provides for new obligations that will apply internationally to entities that control or process the personal data of citizens of the European Union. Several of these obligations, if applicable, could require changes to the processes used by Desjardins Group. In Quebec, consultations are currently underway concerning amendments to *An Act respecting the protection of personal information in the private sector* (ARPPIPS). Desjardins Group can expect that stricter rules will be adopted, and it is closely monitoring developments to assess the impacts on its operations.

New standard related to the third pillar of the Basel Committee on Banking Supervision

Desjardins Group continues to monitor changes in capital and liquidity requirements under global standards developed by the Basel Committee on Banking Supervision (BCBS). To this end, in January 2015, the Committee issued a new standard related to the third pillar, which aims to enhance comparability across financial institutions, transparency and disclosure with regard to regulatory capital adequacy and risk exposure. In December 2016, the AMF filed an update of its guideline on the adequacy of capital base standards, which includes provisions with respect to the third pillar. Desjardins Group is currently working to ensure compliance with these new requirements, which will take effect on December 31, 2018. In addition, in March 2017, the BCBS issued the second phase of the standard related to the third pillar. The OSFI has not yet announced the effective date of the second phase, nor has the AMF.

Capital adequacy requirements for life and health insurers

In October 2016, the AMF issued the new *Capital Adequacy Requirements Guideline (CARLI) – Insurance of persons*. This new regulatory framework replaces the current *Capital Adequacy Requirements Guideline (CAR) – Life and Health Insurance* as of January 1, 2018. Based on information currently available, the subsidiary Desjardins Financial Security Life Assurance Company plans to comply with the requirements of the new guideline.

Report on Ontario's auto insurance plan

On April 11, 2017, a report by David Marshall on the province of Ontario's automobile insurance system was released, with 35 recommendations for improving it and thereby strengthening consumer protection. The report was also the subject of a public consultation aimed at obtaining various opinions on what the government could do to protect persons injured in collisions. Desjardins Group welcomes this measure and supports the Ontario government in seeking to offer affordable products and services.

Guideline B-20 – Residential Mortgage Underwriting Practices and Procedures

In October 2017, the OSFI issued the revised guideline B-20, *Residential Mortgage Underwriting Practices and Procedures*. The changes made reaffirm the OSFI's expectations by encouraging mortgage lenders to remain prudent in their mortgage underwriting practices. The OSFI in particular sets a new minimum interest rate or "stress test" for uninsured mortgages. Desjardins Group has applied these practices since January 1, 2018 even though the equivalent requirements of the AMF's guideline on granting residential mortgages does not go into effect until March 2018.

Modernization of the Canadian payments system

Technological progress and innovation affect the payments ecosystem, which is undergoing major changes. In 2016, Payments Canada launched a multi-year initiative to modernize the Canadian payments system. The Department of Finance Canada unveiled its project for a retail payments oversight framework in 2017. In December 2017, the Competition Bureau issued the final report from its market study concerning technology-led innovation in the Canadian financial services sector. The report suggests modernizing laws and regulations and provides recommendations for regulators. Desjardins Group continues to monitor work by the industry, the federal government and Payments Canada.

Qualified Intermediary Agreement

The U.S. Qualified Intermediary regime allows clients of financial intermediaries to benefit from more streamlined administrative procedures and more readily take advantage of the reduced tax rates allowed under tax agreements concerning taxable U.S source income. For their part, financial institutions must comply with the sometimes-complex provisions of an agreement established by the U.S. tax authorities. This agreement has undergone several significant changes in the past few years with very short implementation deadlines. Desjardins Group entities that are QIs are continuing their efforts to take the necessary measures to comply with the last agreement issued in January 2017 and monitor developments.

Section 871(m) of the U.S. Internal Revenue Code

Section 871(m) of the U.S. Internal Revenue Code was set up to ensure that non-U.S. investors pay tax on dividend payments on U.S. equity-linked instruments. For 2017 and 2018, the withholding tax and reporting obligations determined in section 871(m) apply basically to transactions issued on or after January 1, 2017 and that have a delta equal to 1. This regulation has undergone several changes in recent years and is subject to further amendment. The Desjardins Group entities concerned are putting measures in place to apply the regulation and monitor future changes.

Gradual implementation of *Regulation 93-101 on Derivatives: Business Conduct*

In April 2017, the Canadian Securities Administrators (CSA) published draft *Regulation 93-101 – Derivatives: Business Conduct* and draft *Policy Statement to Regulation 93-101 respecting Derivatives: Business Conduct* to establish a comprehensive regime for regulating the business conduct of participants in over-the-counter derivatives markets. The CSA should also publish for comment in 2018 a separate set of proposed registration rules for derivatives dealers, derivatives advisers and potentially other derivatives market participants. The various derivatives market participants are furthermore subject directly or indirectly to a certain number of national and international standards resulting from a regulatory reform that is gradually taking effect. The Desjardins Group entities concerned are closely watching this regulatory development.

Application of the new framework for European markets in financial instruments

In May 2014, European legislatures adopted a new framework for markets in financial instruments (MIF 2), in the form of the *Markets in Financial Instruments Directive* and the *Markets in Financial Instruments Regulation*. The regulatory requirements related to the MIF 2 directive have been applicable since January 3, 2018 and change the framework for carrying on market activities in Europe. One purpose of the new framework is to strengthen investor protection and make financial markets more resilient and transparent. The Desjardins Group entities concerned are closely monitoring this regulatory development and the notices issued in this regard by the CSA.

1.0 Desjardins Group

1.1 Profile and structure

WHO WE ARE

Desjardins Group is the largest financial cooperative in Canada, with assets of $275.1 billion. The organization brings together 293 caisses in Quebec and Ontario as at December 31, 2017, the *Fédération des caisses Desjardins du Québec* and its subsidiaries (including Desjardins Capital Inc.), the *Fédération des caisses populaires de l'Ontario Inc.* and the *Fonds de sécurité Desjardins*. A number of its subsidiaries and components are active across Canada, and Desjardins Group maintains a presence in the U.S. through Desjardins Bank, National Association.

Through its Personal and Business Services, Wealth Management and Life and Health Insurance, and Property and Casualty Insurance business segments, Desjardins Group offers a full range of financial services to members and clients designed to meet their needs. As one of the largest employers in the country, Desjardins Group capitalizes on the skills of close to 46,000 employees and the commitment of over 4,300 elected officers.

The Federation is, among other things, the treasurer and official representative of Desjardins Group with the Bank of Canada and the Canadian banking system.

WHAT MAKES US DIFFERENT

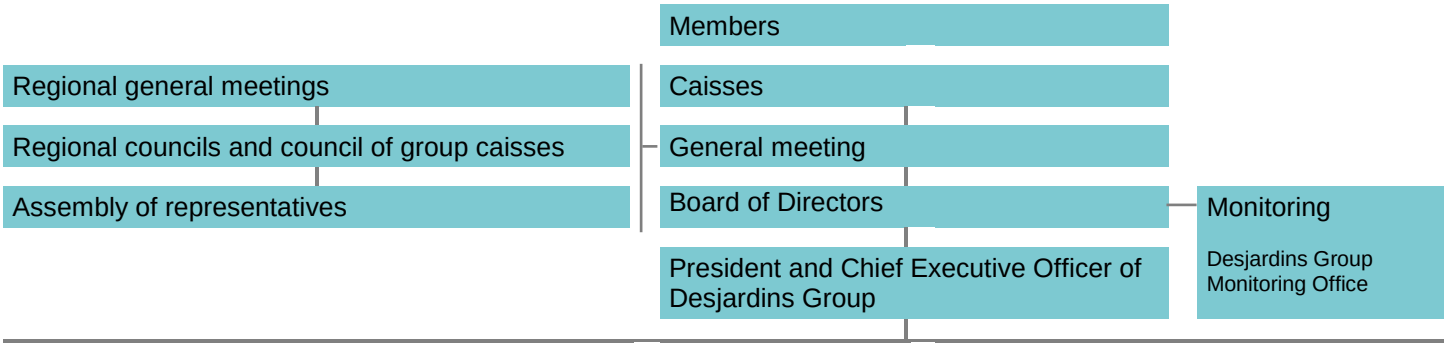
Desjardins Group stands out from other Canadian financial institutions because of its cooperative nature. The resulting mission and values are the driving force for its officers, managers and employees. They are echoed in its orientations, and help Desjardins Group achieve its vision of sustainable prosperity within the communities it serves. Since the first caisse was founded in 1900 in Lévis, Desjardins Group has always been a key player in financial education, and it believes that the cooperative business model is more relevant now than ever in a greatly changing world.

Desjardins Group's ambition is to be first in people's hearts. Thanks to its varied distribution channels, numerous intermediary networks and personnel who strive to always work in the interests of members and clients, Desjardins Group stays close to its members and their communities. In order to best meet members' increasingly diverse needs, Desjardins Group pays special attention to the caisse network and its range of service delivery methods. This process is also part of Desjardins Group's continued commitment to the vitality of cooperation at the caisse level in terms of democratic life, representation, education and training, cooperation with other cooperatives and support for community development.

Another hallmark of Desjardins Group is the active participation of elected officers at the caisse level, and in the organization's decision-making structure through regional general meetings, the regional councils, the council of group caisses, the assembly of representatives and the Board of Directors of the Federation and its various commissions.

STRUCTURE OF DESJARDINS GROUP

Desjardins Group's structure has been designed to take into account the needs of its members and clients, as well as the markets in which it operates. The caisse network in Quebec and Ontario has the support of three main business segments (Personal and Business Services, Wealth Management and Life and Health Insurance, and Property and Casualty Insurance), which reinforces its ability to build on its products and services.



Desjardins Group Corporate Executive Division

Support functions	Business segments			
Finance, Treasury and Administration	**Personal and Business Services**		**Wealth Management and Life and Health Insurance**	**Property and Casualty Insurance**
Risk Management	Regular and convenience transactions	Payments	Life and health insurance	Automobile insurance
Information Technology	Savings and investment	Development capital and business ownership transfer	Savings and investment	Home insurance
Human Resources and Communications	Financing	Capital markets	Securities brokerage	Business insurance
	Integrated offer for businesses	AccèsD	Private wealth management	
	Specialized services	Payroll services	Institutional asset management	

Desjardins Group 2017 highlights

Surplus earnings before member dividends	Residential mortgages outstanding	Assets under management	Tier 1A capital ratio	Total asset growth
$2,151 million	+ $11.5 billion	+ $6.7 billion	18.0%	+ $16.8 billion

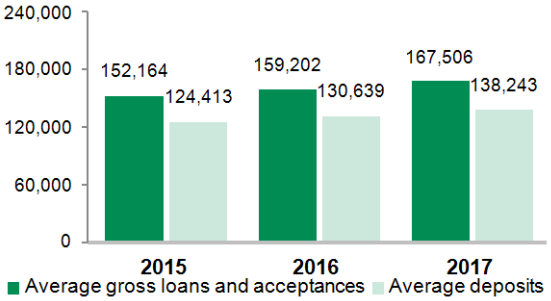
- Surplus earnings before member dividends up $379 million, or 21.4%, compared to 2016.
- Increase of $129 million, or 7.1%, in adjusted surplus earnings[(1)] before member dividends compared to 2016.
- A total of $320 million returned to members and the community, including member dividends, sponsorships, donations and bursaries.
- Operating income[(1)] of $15,413 million, including a gain on the sale of subsidiaries, up 9.5% compared to 2016.
- Adjusted operating income[(1)] of $15,135 million, up 7.5% compared to 2016.
- Sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 to Trimont Financial Ltd., a subsidiary of The Wawanesa Mutual Insurance Company. A $249 million gain, net of expenses and after income taxes, was recorded for the third quarter of 2017.

2017 segment highlights

PERSONAL AND BUSINESS SERVICES

Average gross loans and acceptances and average deposits[(1)]

(in millions of dollars)

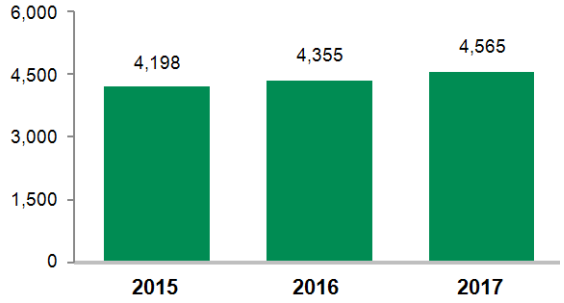


- Quebec's leader in residential mortgages and a leading player in consumer loans, including point-of-sale financing, with estimated market shares of 36.1% and 22.4%, respectively.
- Number one credit and debit card issuer in Quebec and fourth in Canada, Card and Payment Services has issued more than 6.8 million credit cards and 5.9 million debit cards in Canada.
- Leader in agricultural credit in Quebec, with a market share of 39.3%.
- Surplus earnings before member dividends totalled $1,108 million, up 8.1% compared to 2016 due to growth in activities.
- Growth of $3.8 billion in on-balance sheet savings in Quebec in 2017 for an estimated market share of 41.6%.
- Growth of 9.4% compared to 2016 in business volume related to credit card products, Accord D, and auto and durables financing.
- Growth of $8.3 billion compared to 2016 in the entire average portfolio of loans and acceptances.

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

Written premiums

(in millions of dollars)

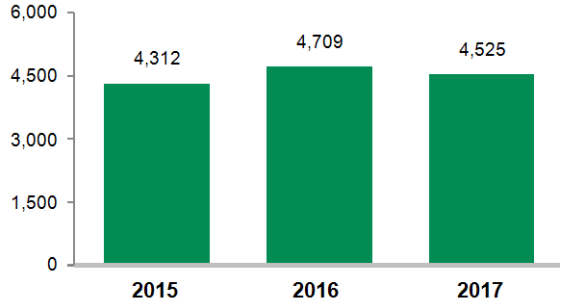


- Quebec's No. 2 life and health insurer and No. 5 in Canada (based on written premiums in 2016).
- Gross insurance premiums of $4.2 billion, up 5.2% compared to 2016.
- Record net sales of $2.5 billion for Desjardins Funds.
- Significant growth in net sales for private wealth management and for full-service and online brokerage, of 51.5% and 25.6%, respectively, in 2017.
- Net surplus earnings of $612 million, up 32.8%, compared to 2016 as a result of favourable adjustments to actuarial assumptions and the solid performance of investments.
- No. 1 for market-linked guaranteed investments and No. 2 for Desjardins Funds, in Quebec (based on 2016 assets under management).
- Announcement of the creation of Aviso Wealth, a partnership that in 2018 will result in one of the largest wealth management companies in Canada.

PROPERTY AND CASUALTY INSURANCE

Gross written premiums

(in millions of dollars)



- Quebec's No. 2 and Canada's No. 3 property and casualty insurer (based on gross direct premiums written in 2016).
- Positive underwriting results for Desjardins General Insurance Group Inc. for the 25th consecutive year.
- Sale on July 1, 2017 of Western Financial Group Inc. and Western Life Assurance Company to Trimont Financial Ltd.
- Launch of new flood coverage for all Canadians as well as the Alert program, a water damage prevention system.
- Net surplus earnings of $446 million for the year, including a $241 million gain, net of expenses and after income taxes, on the sale of subsidiaries.
- Adjusted net surplus earnings[(1)] of $237 million, down 28.0% compared to 2016, on account of the unfavourable current-year claims experience, mainly in automobile insurance
- Growth of $689 million, or 21.5%, compared to 2016, in net premiums to total $3.9 billion.
- Improvement in the expense ratio[(1)] to 24.5% in 2017, compared to 26.3% in 2016.

[(1)] See "Basis of presentation of financial information".

Table 1 – Financial results and indicators
For the years ended December 31

(in millions of dollars and as a percentage)	2017	2016[1]	2015[1]
Results			
Net interest income	**$ 4,405**	$ 4,273	$ 4,279
Net premiums	**8,049**	7,168	6,907
Other operating income[2]	**2,959**	2,641	2,694
Operating income[2]	**15,413**	14,082	13,880
Investment income[2]	**1,688**	1,119	1,362
Total income	**17,101**	15,201	15,242
Provision for credit losses	**349**	319	377
Claims, benefits, annuities and changes in insurance contract liabilities	**6,717**	5,446	5,431
Non-interest expense	**7,348**	7,204	6,959
Income taxes on surplus earnings	**536**	460	516
Surplus earnings before member dividends	**$ 2,151**	$ 1,772	$ 1,959
Adjusted surplus earnings before member dividends[2]	**$ 1,934**	$ 1,805	$ 1,940
Contribution to combined surplus earnings by business segment[3]			
Personal and Business Services	**$ 1,108**	$ 1,025	$ 1,071
Wealth Management and Life and Health Insurance	**612**	461	503
Property and Casualty Insurance	**446**	296	360
Other	**(15)**	(10)	25
	$ 2,151	$ 1,772	$ 1,959
Amount returned to members and the community			
Member dividends	**$ 202**	$ 144	$ 154
Sponsorships, donations and bursaries	**82**	82	81
Desjardins Member Advantages program	**36**	33	29
	$ 320	$ 259	$ 264
Indicators			
Return on equity[2]	**9.1%**	8.0%	9.1%
Adjusted return on equity[2]	**8.1**	8.1	9.0
Productivity index[2]	**70.8**	73.8	70.9
Adjusted productivity index[2]	**72.3**	73.4	70.8
Provisioning rate[2]	**0.20**	0.20	0.24

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".
(3) The breakdown by line item is presented in Note 33, "Segmented information", to the Combined Financial Statements.

Table 2 – Balance sheets and indicators
As at December 31

(in millions of dollars and as a percentage)	2017	2016	2015
Balance sheet			
Assets	**$ 275,095**	$ 258,367	$ 248,128
Net loans and acceptances	**177,521**	166,026	159,881
Deposits	**171,586**	160,546	156,574
Equity	**24,773**	23,293	21,725
Indicators			
Assets under administration	**$ 411,548**	$ 420,166	$ 403,350
Assets under management[1]	**58,220**	51,550	46,053
Tier 1A capital ratio	**18.0%**	17.3%	16.0%
Tier 1 capital ratio	**18.0**	17.3	16.0
Total capital ratio	**18.4**	17.9	17.2
Leverage ratio	**8.5**	8.1	7.8
Gross impaired loans /gross loans and acceptances[2]	**0.25**	0.32	0.34

(1) Assets under management may also be administered by Desjardins Group. When this is the case, they are included in assets under administration.
(2) See "Basis of presentation of financial information".

1.2 Material events

Sale of subsidiaries

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, namely Western Financial Group Inc., a financial services company, and Western Life Assurance Company, a life and health insurance company, to Trimont Financial Ltd., a subsidiary of The Wawanesa Mutual Insurance Company, for a total consideration of $722 million. A gain of $249 million, net of expenses and after income taxes, on the sale of these subsidiaries was recognized in the Combined Statements of Income for the year ended December 31, 2017. The results of these subsidiaries were presented in the Property and Casualty Insurance segment.

It should also be recalled that the sale of Western Financial Insurance Company to Economical Insurance was completed on January 1, 2017.

Additional financial information on these subsidiaries is presented in the "Impact of the sale of subsidiaries" section.

Creation of Aviso Wealth

On December 12, 2017, Desjardins Group and a partnership comprised of Canada's five provincial credit unions (the Centrals) and The CUMIS Group announced that they had entered into an agreement to combine their subsidiaries Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments. The transaction will create Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and a partnership between the Centrals and The CUMIS Group. The transaction is expected to close in the first half of 2018, subject to obtaining the required regulatory approvals and satisfying the usual closing conditions. The results of the subsidiary Qtrade Canada Inc. and the interest held in the associate Northwest & Ethical Investments are presented in the Wealth Management and Life and Health Insurance segment.

1.3 Financial strategy and objectives

ORIENTATIONS AND STRATEGIC PRIORITIES

Fiscal 2017 marked the launch of a new strategic framework. The President and Chief Executive Officer, supported by the Board of Directors and the Management Committee, ratified the new 2020 strategic plan as well as all the master plans for Desjardins Group business sectors and support functions. The organization will therefore be guided by three major orientations until 2020. "Accelerate the shift to a member and client culture" is the first, which focuses on significantly enhancing the quality of the Desjardins member and client experience. The second, "Affirm our cooperative difference", will allow Desjardins to bring the cooperative difference up to date and live it out, as well as to strengthen its fundamental purpose, which is to enrich the lives of people and communities. The third orientation, "Capitalize on the strengths of our expansive cooperative group", will be focused on finding new growth opportunities across Canada along with group synergies. These three orientations will be based on attributes that present Desjardins as a simple, human, modern and capable cooperative for its members and clients, as well as its employees, managers and officers. The strategic priorities to be established for 2020 have been derived from these orientations and will allow Desjardins Group to achieve its ambition of being first in people's hearts. The 2018 strategic priorities for Desjardins Group's business segments may be found in Section 2.3 "Analysis of business segment results" of this MD&A.

FINANCIAL OBJECTIVES

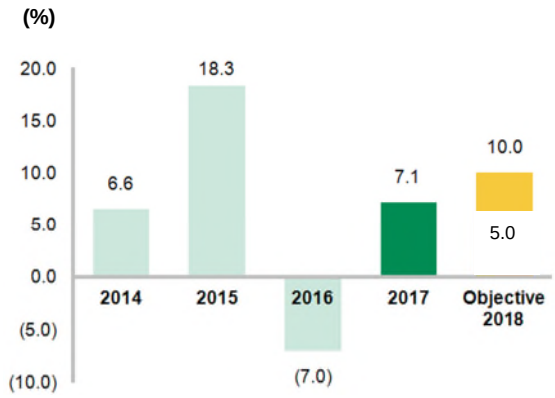
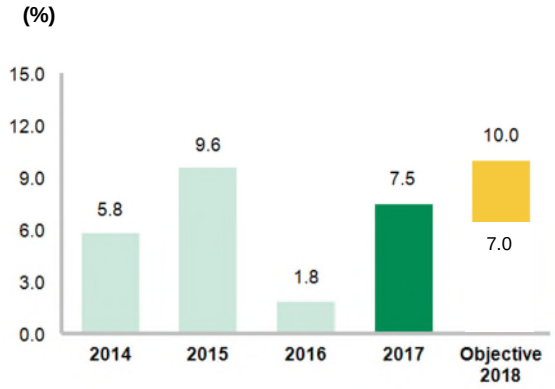
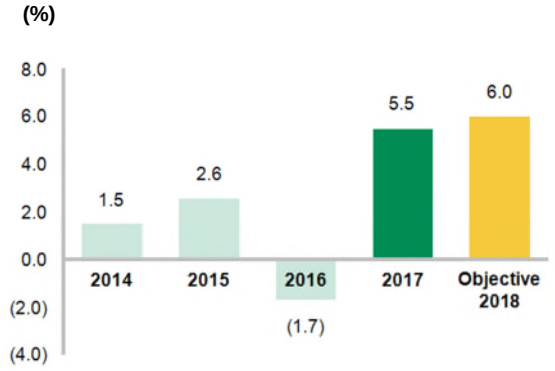
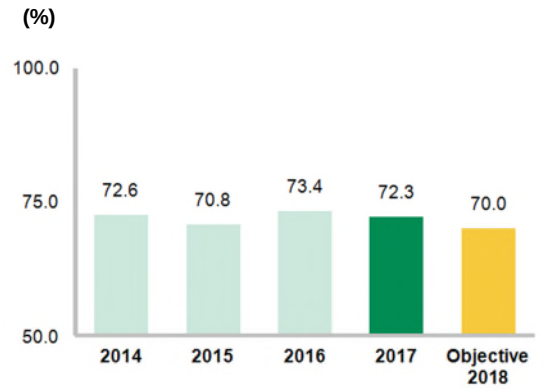
Desjardins Group sets medium-term financial objectives that provide it with the means of realizing its ambitions for members and clients by seeking new ways to increase its return to the community.

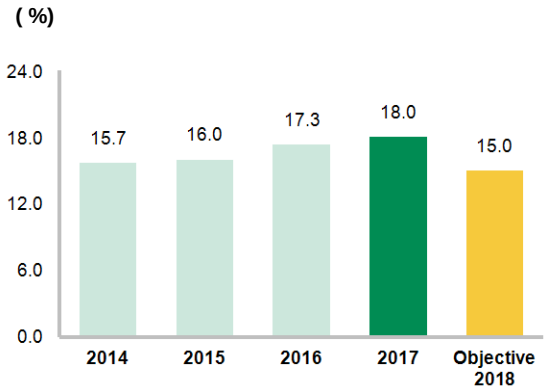
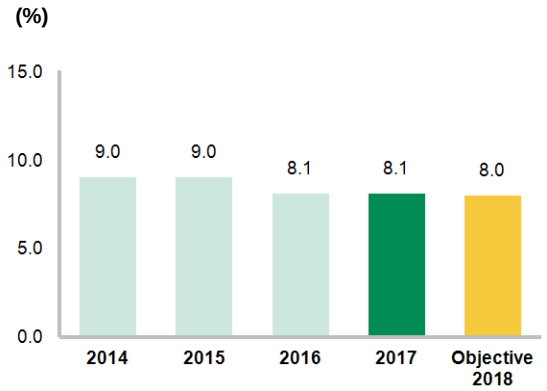
This section shows the progress made toward the objectives stated in 2017 and shows them in relation to the results achieved. Performance in 2018 will be measured using key indicators aligned with Desjardins's new ambitions according to the orientations and strategic priorities. Desjardins Group, through its members and clients, enriches the lives of people and communities in order to be first in people's hearts. Creating wealth and redistributing it to its members and their communities, constantly working in their best interests, involves Desjardins Group's financial performance, as well as other factors.

Overall performance

The trend in Desjardins Group's overall performance over the last few years has been positive. Surplus earnings before member dividends and operating income have grown, and the targets for return on equity and capital were met. For the coming years, senior management is aiming for an equitable return to all members and clients that is consistent with Desjardins Group's financial performance. Additional investments, particularly in innovative information technology platforms, will allow Desjardins to enhance the member and client experience and to improve productivity.

The financial objectives are monitored exclusive of the specific items as defined in the "Basis of presentation of financial information". Readers may refer to Section 2.0 "Review of financial results" for an analysis of Desjardins Group's results before the specific items.

Key indicators[1]	Results achieved in 2017	2018 objectives	Trend
Growth in adjusted surplus earnings before member dividends Desjardins Group monitors growth in surplus earnings to measure value creation for members and clients.	Growth in adjusted surplus earnings before member dividends was 7.1%, exceeding the 4% objective for 2017. The caisse network, included in the Personal and Business Services segment, continued to grow. The Wealth Management and Life and Health Insurance segment posted a solid performance for its investments and growth in its assets under management. However, the Property and Casualty Insurance segment had a higher claims experience for the current year than in 2016, and there were less favourable developments in prior-year claims in 2017 than in 2016.	For 2018, Desjardins Group's objective is to achieve growth of between 5% and 10% in adjusted surplus earnings before member dividends.	
Growth in adjusted operating income Desjardins Group monitors growth in its operating income to measure growth in its operations.	Adjusted operating income increased by 7.5% in 2017, exceeding the 7% objective for 2017. Net interest income was up as a result of growth in the entire portfolio of loans and acceptances outstanding. In addition, this growth stemmed from the increase in net premiums due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.	For 2018, Desjardins Group's objective is to achieve growth of between 7% and 10% in adjusted operating income.	
Growth differential between adjusted operating income and adjusted non-interest expense Desjardins Group ensures that operating income grows faster than non-interest expense for the organization's sustainability and profitability.	The growth differential between adjusted operating income and adjusted non-interest expense was 5.5% in 2017. Growth in operations combined with productivity initiatives had an impact on non-interest expense.	For 2018, Desjardins Group's objective is to achieve a differential of 6%.	
Adjusted productivity index Desjardins Group uses the productivity index as a measure of efficiency.	The index was 72.3% at the end of fiscal 2017. This result, which did not meet the ambitious 70% objective, was mainly due to additional investments in innovative technology platforms. However, Desjardins Group's adjusted productivity index has improved compared to 2016 on account of growth in its operations and productivity initiatives that had an effect on non-interest expense.	For 2018, Desjardins Group has again set its ambitious objective of 70%.	

Key indicators[1]	Results achieved in 2017	2018 objectives	Trend
Tier 1A capital ratio Desjardins Group monitors the Tier 1A capital ratio to maintain its financial strength.	As at December 31, 2017, the Tier 1A capital ratio was 18.0%, exceeding Desjardins Group's15% objective.	For 2018, Desjardins Group is maintaining its objective of exceeding 15%.	
Adjusted return on equity Return on equity is used to measure profitability resulting in value creation for members and clients.	Adjusted return on equity was 8.1% in 2017, in line with Desjardins's 8% objective.	For 2018, Desjardins Group has set an objective of exceeding 8%.	

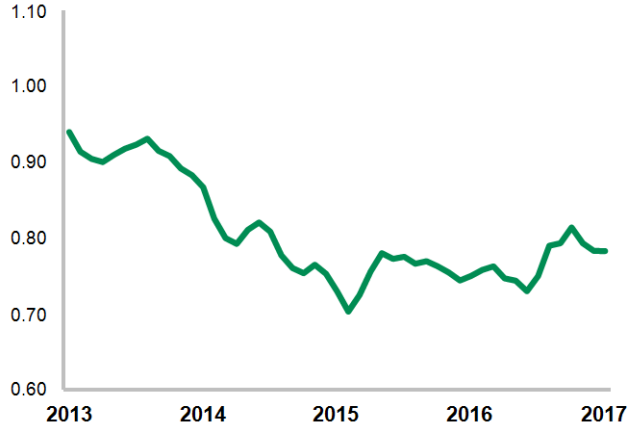
[1] See "Basis of presentation of financial information".

FINANCIAL OUTLOOK

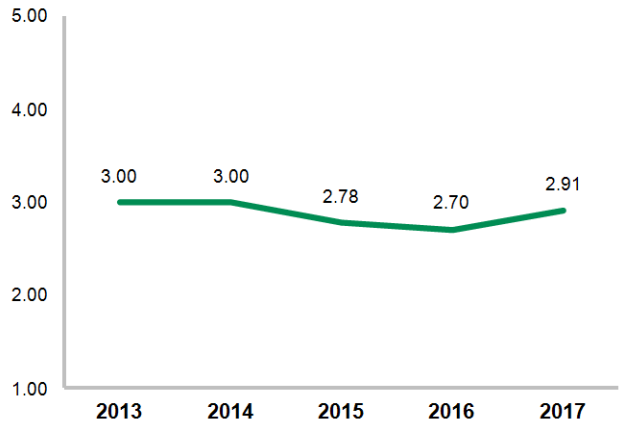
Desjardins Group will continue the year on a solid footing, with a level of capitalization that is higher than the average for the Canadian banking industry as well as increasing profitability in an economic environment that should remain at a satisfactory level over the coming year. Stiff competition in the banking sector will place sustained pressure on net interest income. Rigorous cost control and strict capital management will enable Desjardins Group to make significant investments for the benefit of members and communities and adopt innovative concepts to enhance service delivery, with the constant aim of being first in people's hearts and making it easier to do business with Desjardins.

1.4 Changes in the economy

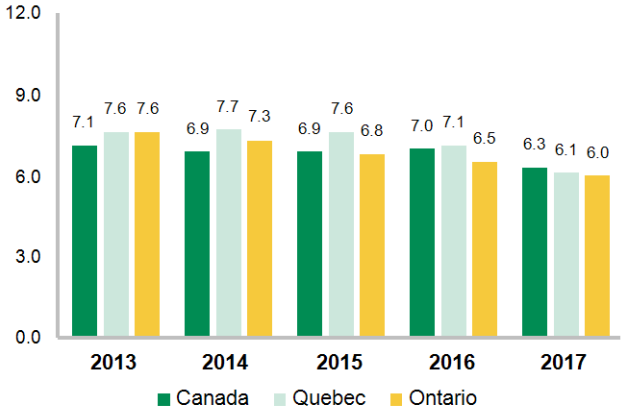
Changes in the Canadian dollar vs. the U.S. dollar (monthly average)
(Canadian dollars/U.S. dollars)



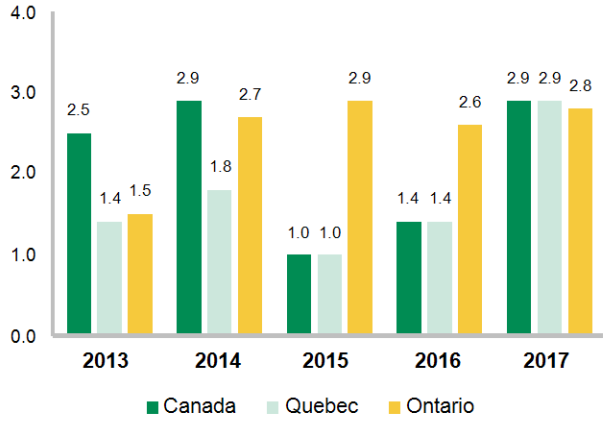
Changes in the prime rate (annual average)
(as a percentage)



Changes in the unemployment rate (annual average)
(as a percentage)



Annual growth in GDP
(as a percentage)



ECONOMIC ENVIRONMENT IN 2017

Global economy

The global economy grew at an accelerating pace in 2017. The gain in real GDP is estimated at 3.6%, compared to 3.1% in 2016. International trade also gathered momentum. The best economic growth was in the advanced countries (2.3% compared to 1.6% in 2016) and the emerging countries (4.4% compared to 4.1%). Real GDP growth in China even picked up slightly, from 6.7% to 6.9%. In Europe there was a marked improvement in the household and business confidence indexes, which was reflected in accelerating real GDP growth in the eurozone. The annual change is estimated at 2.5% in 2017 compared to 1.8% in 2016. The uncertainties surrounding the United Kingdom's withdrawal from the European Union (Brexit) ultimately had an impact on the UK economy in 2017, while Britain's production was relatively resilient in 2016.

The improved economic environment in 2017 was good for the financial markets. The main North American indexes climbed by more than 15%, and the performance of several exchanges overseas was as impressive. In Canada, following a remarkable performance in 2016, the Toronto Stock Exchange posted mixed results in 2017 as the major sectors related to commodities experienced difficulties in the first half of the year. The year nevertheless ended on a more positive note marked by a rebound in commodity prices, allowing the Toronto Stock Exchange to close 2017 at 6% growth. The strength of the economy led the Fed to announce three 0.25% hikes in U.S. key interest rates and to begin gradually reducing its bond holdings. However, low inflation rates in most countries helped keep long-term bond rates very low. The Bank of Canada (BoC) suddenly began monetary tightening, instituting two 0.25% increases to its key interest rate during the summer, which caused interest rates and the Canadian dollar to surge. Following these hikes the BoC nevertheless adopted a more cautious tone, which brought the Canadian dollar back down to just under US$0.80.

United States

Once again, the U.S. economy struggled in the first quarter of 2017. However, the following quarters rendered rather strong real GDP growth of close to 3.0%. Real GDP growth in 2017 has been estimated at 2.3%, a clear improvement over the 1.5% gain recorded for 2016. Even the devastating hurricanes in August and September had only a limited effect on growth, and the reconstruction and rebound in production took hold quickly in their wake. A recovery in the oil sector also supported investment. Despite the concerns engendered by Donald Trump's arrival in the White House, household and business confidence remained strong. The labour market performed well, and the unemployment rate fell to its lowest level since 2000. Salary growth, much like inflation, continued to be relatively modest.

Canada

The Canadian economy got off to a strong start in 2017 with cumulative real GDP growth of 4.0% (annual rate) in the first half of the year. It was the strongest start of the year since 2002. Domestic demand was particularly vigorous, in part due to sustained growth in consumer spending. It should be noted that several favourable factors helped buoy consumer spending in the first half of 2017. The labour market registered good growth. Household confidence improved in an environment characterized by extremely low interest rates. Non-residential business investment also began to recover, following major problems faced in 2015 and 2016 after the drop in oil prices. Average residential investment also grew in the first half of 2017. Lastly, the upward trend in exports continued on the strength of growing global demand. But such a strong expansion could not last, and the second half of 2017 was marked by growth that slowed toward a more sustainable level. Several factors contributed to the slowdown. Temporary problems, in particular in the auto industry, impeded foreign trade in the summer. The slight increase in key interest rates that began in July and September 2017 somewhat discouraged consumer spending, in particular for durable goods. The housing market also began to show signs of slowing in certain regions, with the combined effects of a slight increase in interest rates and the introduction of new measures to drag on the Toronto real estate market. Ultimately, the results for 2017 as a whole should show an increase in real GDP of approximately 2.9%. This is a net improvement from the 1.4% gain recorded for 2016.

Quebec

The Quebec economy grew much faster in 2017. Real GDP rose by approximately 2.9% for the year, posting the best results in 15 years. Economy activity was lifted by household spending, through consumption and the residential sector. Retail sales experienced strong growth due to improved conditions in the labour market. In December 2017, the monthly unemployment rate even fell to 5.0%, its lowest level in 40 years. This low rate was due to job creation and an aging population, which is driving a significant wave of retirements. The residential sector had a strong year. A high volume of sales of existing homes drove up prices by approximately 5% in 2017. Despite this improvement, there have been no signs of overheating in the Montreal market, even if there have been more foreign buyers in the market since a 15% tax was implemented in Vancouver and Toronto. Business investment remained weak and export performance was disappointing, including due to the uncertainties surrounding the renegotiation of the North American Free Trade Agreement (NAFTA).

ECONOMIC OUTLOOK FOR 2018

Global economy

The favourable outlook for the global economy suggests that the bullish trend in the stock exchanges could continue in 2018. Following their remarkable performance in 2017, world exchanges are nevertheless expected to post more modest growth. Commodity prices should still rise somewhat, and the Toronto Stock Exchange is expected to perform well in 2018. The good economic performance, combined with a gradual increase in inflation, should lead the Fed and the BoC to gradually raise their key interest rates over the next few quarters. In this environment, the rates on North American bonds are also expected to trend upwards in 2018, while remaining low in historical terms. Monetary tightening in Canada and a modest increase in oil prices should provoke a slight appreciation of the Canadian dollar.

The accelerating economic activity in the global economy in 2017 should continue in 2018, but the growth is expected to be even more pronounced in the emerging countries. Faster real GDP growth is expected in India and Brazil. The Chinese economy is expected to grow at a slightly slower pace, without straying too far from the recent trend. In the eurozone, economic growth should stabilize as the economy's production over-capacity dwindles. The British economy is expected to slow again as the consequences of the uncertainties surrounding Brexit continue to emerge. Global trade may change in response to the protectionist tendencies of the Trump administration.

United States

In the U.S., the recent momentum in the economy should continue in 2018. Of course economic conditions will depend on the President's actions and benefit from the tax reform bill adopted by Congress at the end of 2017, but vast infrastructure spending programs are not expected. In addition, it is too early to predict whether any trade agreements, such as NAFTA, will be revoked. Confidence remains high enough to ensure good growth in personal consumption and corporate investment. The key interest rates in the U.S. will continue to rise gradually, with three 25-basis-point increases expected in 2018.

Canada

In Canada, economic growth is expected to continue at a satisfactory pace in 2018. On average, real GDP may grow 2.2% during the year, faster than its potential growth rate for 2018, which the BoC pegs at approximately 1.4%. Good performance by the labour market will continue to stimulate consumer spending, and non-residential business investment should continue to recover. Exports are expected to maintain their upward trend due to vigorous global demand. The benefits of the new trade agreement between Canada and the European Union may also become increasingly apparent. That being said, there is considerable uncertainty over the future of Canadian foreign trade due to the NAFTA renegotiations. In theory, residential investment should slow in 2018 with the expected increases in interest rates and the presence of several restrictive measures, including the new rules introduced by the Office of the Superintendent of Financial Institutions (OSFI) Canada in January 2018. Despite it all, the housing market has often surprised market watchers over the last few years by showing great resilience.

Quebec

The outlook for Quebec in 2018 is good, but the economy is expected to grow at a slower pace than last year. Consumer spending is unlikely to grow as fast, since job creation is expected to abate. The government of Quebec, which has generated budget surpluses of $4.6 billion over the last two years, has announced an additional $1.1 billion in cuts to personal income taxes. Beginning in 2018, the cuts will apply retroactively to January 1, 2017. The provincial government also has sufficient flexibility in its budget to accelerate growth public spending. The residential sector is expected to lose some steam due to the cumulative effect of interest rate hikes and stricter mortgage rules. The outcome of the trade negotiations with the U.S. will play a crucial role in business investment and exports. Quebec's real GDP should increase by 2.0% in 2018, but there are downside risks if the talks do not lead to an agreement.

The situation of the markets in which Desjardins Group segments are present is described in their respective analyses in Section 2.3 "Analysis of business segment results".

2.0 Review of financial results

2.1 Impact of the sale of subsidiaries

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, namely Western Financial Group Inc., a financial services company, and Western Life Assurance Company, a life and health insurance company, to Trimont Financial Ltd., a subsidiary of The Wawanesa Mutual Insurance Company, for a total consideration of $722 million. A gain of $249 million, net of expenses and after income taxes, on the sale of these subsidiaries was recognized in the Combined Statements of Income for the year ended December 31, 2017.

It should also be recalled that the sale of Western Financial Insurance Company to Economical Insurance was completed on January 1, 2017.

The table below presents the operating results of these three subsidiaries included in Desjardins Group's financial results in the Property and Casualty Insurance segment.

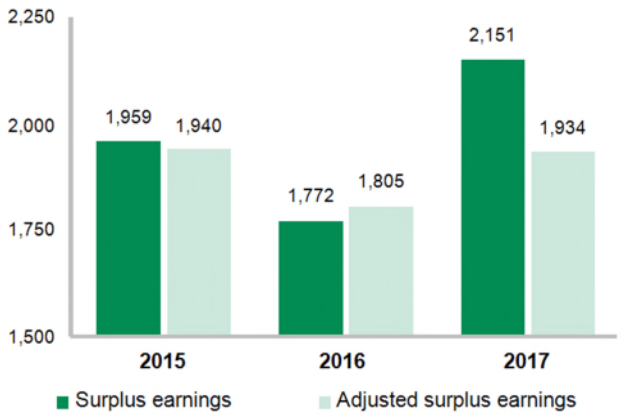
Table 3 – Impact of the sale of subsidiaries
For the years ended December 31

(in millions of dollars)	**2017[1]**	2016	2015
Net interest income	**$ 3**	$ 5	$ 5
Net premiums	**65**	213	172
Other operating income[2]	**97**	197	189
Operating income[2]	**$ 165**	$ 415	$ 366
Investment income[2]	**9**	6	7
Total income	**174**	421	373
Claims, benefits, annuities and changes in insurance contract liabilities	**22**	77	55
Non-interest expense	**124**	295	268
Income taxes on surplus earnings	**9**	16	13
Surplus earnings before member dividends	**$ 19**	$ 33	$ 37

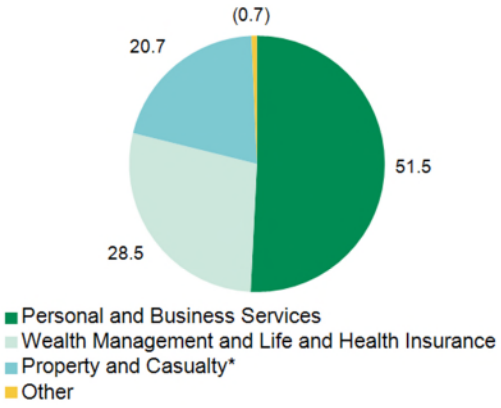
(1) Represents results for the period from January 1, 2017 to June 30, 2017 of Western Financial Group Inc. and Western Life Assurance Company considering that the sale was completed on July 1, 2017.
(2) See "Basis of presentation of financial information".

2.2 Analysis of 2017 results

Surplus earnings before member dividends
(in millions of dollars)



Segment contributions to surplus earnings before member dividends in 2017
(as a percentage)



* Includes a $241 million gain in this segment related to the sale of subsidiaries.

Table 4 – Summary of financial results
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Results			
Net interest income	**$ 4,405**	$ 4,273	$ 4,279
Net premiums	**8,049**	7,168	6,907
Other operating income[2]	**2,959**	2,641	2,694
Operating income[2]	**15,413**	14,082	13,880
Investment income[2]	**1,688**	1,119	1,362
Total income	**17,101**	15,201	15,242
Provision for credit losses	**349**	319	377
Claims, benefits, annuities and changes in insurance contract liabilities	**6,717**	5,446	5,431
Non-interest expense	**7,348**	7,204	6,959
Income taxes on surplus earnings	**536**	460	516
Surplus earnings before member dividends	**$ 2,151**	$ 1,772	$ 1,959
Adjusted surplus earnings before member dividends[2]	**$ 1,934**	$ 1,805	$ 1,940
Contribution to combined surplus earnings by business segment[3]			
Personal and Business Services	**$ 1,108**	$ 1,025	$ 1,071
Wealth Management and Life and Health Insurance	**612**	461	503
Property and Casualty Insurance[4]	**446**	296	360
Other	**(15)**	(10)	25
	$ 2,151	$ 1,772	$ 1,959

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".
(3) The breakdown by line item is presented in Note 33, "Segmented information", to the Combined Financial Statements.
(4) Includes a $241 million gain in this segment related to the sale of subsidiaries.

2017 SURPLUS EARNINGS

For 2017, Desjardins Group continued to grow its operations and reported surplus earnings before member dividends of $2,151 million, a year-over-year increase of $379 million, or 21.4%. Surplus earnings adjusted for specific items totalled $1,934 million, compared to $1,805 million in 2016, for an increase of $129 million, or 7.1%.

By its very nature as a cooperative financial group, Desjardins Group's mission is to improve the economic and social well-being of people and communities, which it continued to strive to achieve in 2017:

- A total of $320 million returned to the community, compared to $259 million in 2016, a 23.6% increase.
  - Member dividends of $202 million for the year ended December 31, 2017, compared to $144 million for the previous year.
  - An amount of $82 million was given to various organizations in the form of sponsorships, donations and bursaries, which is stable compared to 2016.
  - Through the Desjardins Member Advantages program, $36 million was paid out, which is stable compared to 2016.

Segment contributions to surplus earnings

- Personal and Business Services: **Contribution of $1,108 million**, up $83 million, or 8.1% compared to 2016.
  - Growth in caisse network operations.
  - Growth in business volume related to credit cards and point-of-sale financing.
  - Higher income from mergers and acquisitions related to capital markets.
  - The segment contributed 51.5% to surplus earnings.
- Wealth Management and Life and Health Insurance: **Contribution of $612 million**, up $151 million, or 32.8%, compared to 2016.
  - Solid investment performance in 2017.
  - Favourable adjustments to actuarial assumptions in the normal course of business in 2017.
  - Higher income from growth in assets under management.
  - Offset by a less favourable claims experience in 2017.
  - The segment contributed 28.5% to surplus earnings.
- Property and Casualty Insurance, including the gain on the sale of subsidiaries: **Contribution of $446 million**, up $150 million compared to 2016.
  - Surplus earnings adjusted for specific items of $237 million, down $92 million compared to 2016.
  - Higher claims experience for the current year than in 2016, and favourable developments in prior-year claims, which were lower than in 2016.
  - The segment contributed 20.7% to surplus earnings.

- **Return on equity was 9.1%**, compared to 8.0% for 2016.
- **Adjusted return on equity was 8.1%**, the same as in 2016.

OPERATING INCOME

Table 5 – Operating income
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Net interest income	**$ 4,405**	$ 4,273	$ 4,279
Net premiums	**8,049**	7,168	6,907
Other operating income[2] (see Table 8)	**2,959**	2,641	2,694
Total operating income[2]	**$ 15,413**	$ 14,082	$ 13,880

[1] Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
[2] See "Basis of presentation of financial information".

Operating income totalled $15,413 million, up $1,331 million, or 9.5%, compared to 2016. Excluding the gain of $278 million before taxes on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, operating income would have been $15,135 million, up $1,053 million, or 7.5%, compared to 2016.

Net interest income

Net interest income is the difference between interest income earned on assets, such as loans and securities, and the interest expense related to liabilities, such as deposits, borrowings and subordinated notes. It is affected by interest rate fluctuations, funding and matching strategies, as well as the composition of both interest-bearing and non-interest-bearing financial instruments.

For analysis purposes, Table 6 shows the changes in net interest income for the main asset and liability classes. Table 7 details how net interest income was affected by changes in volume and interest rates for the different asset and liability classes.

- **Net interest income of $4,405 million**, up $132 million, or 3.1%, mainly because of growth in the entire average portfolio of loans and acceptances outstanding.

- **Net interest margin of 2.31%** in 2017, as a percentage of average interest-bearing assets, down 7 basis points compared to 2016, mainly on account of fierce competition in the market which continued to put pressure on interest margins.

- **Interest income of $6,246 million**, up $245 million, or 4.1%, essentially due to the following items:
  - Growth in average volume of total interest-bearing assets, mainly loans, which added $344 million to interest income.
  - However, a decline in average return on total interest-bearing assets, mainly loans, which reduced interest income by $99 million.

- **Interest expense of $1,841 million**, up $113 million, or 6.5%, primarily as a result of the following items:
  - Growth in average deposits, offset by a decline in borrowings and subordinated notes, leading to an $81 million increase in interest expense.
  - An increase in the average cost of funding, mainly from deposits, raised this expense by $32 million.

Table 6 – Net interest income on average assets and liabilities

For the years ended December 31

(in millions of dollars and as a percentage)	2017			2016[1]			2015[1]		
	Average balance	**Interest**	**Average rate**	Average balance	Interest	Average rate	Average balance	Interest	Average rate
Assets									
Interest-bearing assets									
Securities, cash and deposits with financial institutions	**$ 22,363**	**$ 323**	**1.44%**	$ 19,977	$ 315	1.58%	$ 19,059	$ 308	1.62%
Loans	**167,944**	**5,923**	**3.53**	159,363	5,686	3.57	151,863	5,765	3.80
Total interest-bearing assets	**190,307**	**6,246**	**3.28**	179,340	6,001	3.35	170,922	6,073	3.55
Other assets	**6,126**	**-**	**-**	6,431	-	-	7,083	-	-
Total assets	**$ 196,433**	**$ 6,246**	**3.18%**	$ 185,771	$ 6,001	3.23%	$ 178,005	$ 6,073	3.41%
Liabilities and equity									
Interest-bearing liabilities									
Deposits	**$ 168,098**	**$ 1,763**	**1.05%**	$ 159,200	$ 1,643	1.03%	$ 151,093	$ 1,665	1.10%
Borrowings and subordinated notes	**1,377**	**78**	**5.66**	1,581	85	5.38	2,434	129	5.30
Total interest-bearing liabilities	**169,475**	**1,841**	**1.09**	160,781	1,728	1.07	153,527	1,794	1.17
Other liabilities	**10,147**	**-**	**-**	9,496	-	-	9,788	-	-
Equity	**16,811**	**-**	**-**	15,494	-	-	14,690	-	-
Total liabilities and equity	**$ 196,433**	**$ 1,841**	**0.94%**	$ 185,771	$ 1,728	0.93%	$ 178,005	$ 1,794	1.01%
Net interest income		**$ 4,405**			$ 4,273			$ 4,279	
As a percentage of average interest-bearing assets			**2.31%**			2.38%			2.50%

[1] Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.

Table 7 – Impact of changes in volumes and rates on net interest income

For the years ended December 31

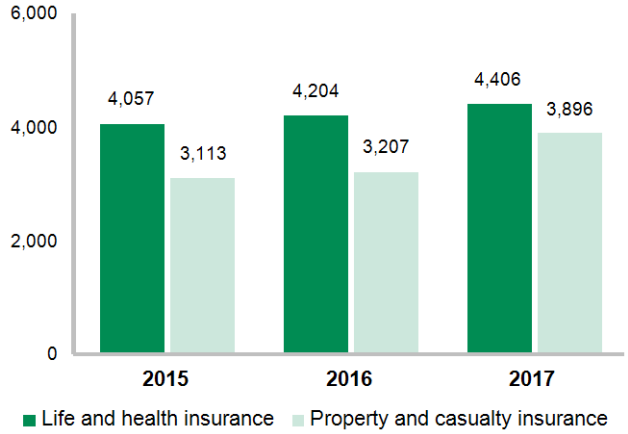
(in millions of dollars and as a percentage)	2017		Increase (decrease)			2016[1]		Increase (decrease)		
	Change in average volume	**Change in average rate**	**Interest**	**Average volume**	**Average rate**	Change in average volume	Change in average rate	Interest	Average volume	Average rate
Assets										
Securities, cash and deposits with financial institutions	**$ 2,386**	**(0.14)%**	**$ 8**	**$ 38**	**$ (30)**	$ 918	(0.04)%	$ 7	$ 15	$ (8)
Loans	**8,581**	**(0.04)**	**237**	**306**	**(69)**	7,500	(0.23)	(79)	285	(364)
Change in interest income			**245**	**344**	**(99)**			(72)	300	(372)
Liabilities										
Deposits	**8,898**	**0.02**	**120**	**92**	**28**	8,107	(0.07)	(22)	89	(111)
Borrowings and subordinated notes	**(204)**	**0.32**	**(7)**	**(11)**	**4**	(853)	0.08	(44)	(45)	1
Change in interest expense			**113**	**81**	**32**			(66)	44	(110)
Change in net interest income			**$ 132**	**$ 263**	**$ (131)**			$ (6)	$ 256	$ (262)

[1] Data for 2016 have been reclassified to conform to the current year's presentation.

Net premiums

Net premiums, comprising life and health insurance, annuity, and property and casualty insurance premiums, rose by $881 million, or 12.3%, to total $8,049 million as at December 31, 2017.

Net premiums [1]
(in millions of dollars)



(1) The difference between total results and the sum of business segment results is due to intersegment transactions.

Wealth Management and Life and Health Insurance segment

- **Net insurance and annuity premiums of $4,406 million**, up $202 million, or 4.8%, due to business growth.
  - Premiums up $202 million, with group insurance accounting for $160 million and individual insurance for $40 million.
  - Annuity premiums stable compared to 2016.

Property and Casualty Insurance segment

- **Net premiums of $3,896 million**, up $689 million, or 21.5%, essentially due to the following items.
  - Increase of $660 million on account of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Increase of $168 million due to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
  - Offset by a decrease in net premiums resulting from the sale of Western Life Assurance Company on July 1, 2017 and Western Financial Insurance Company on January 1, 2017.

Other operating income

Table 8 – Other operating income
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Deposit and payment service charges	**$ 458**	$ 488	$ 489
Lending fees and credit card service revenues	**660**	574	550
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**428**	376	365
Foreign exchange income	**77**	70	88
Other	**249**	27	165
Total other operating income[2]	**$ 2,959**	$ 2,641	$ 2,694

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".

Other operating income stood at $2,959 million for 2017, which is an increase of $318 million, or 12.0%, compared to the previous year. Excluding the gain before taxes of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, other operating income would have been $2,681 million, up $40 million, or 1.5%, compared to 2016.

- Deposit and payment service charges of $458 million, down $30 million, or 6.1%.
  - Lower income from deposits because of changes in pricing.
- Lending fees and credit card service revenues of $660 million, up $86 million, or 15.0%.
  - Growth in business volume from the various payment solutions offered by Card and Payment Services.
- Income from brokerage and investment fund services of $1,087 million, down $19 million, or 1.7%.
  - Decrease in commission income following the sale of Western Financial Group Inc., as presented in the "Impact of the sale of subsidiaries" section under other operating income.
  - Offset by growth in income from assets under management.
- Management and custodial service fees up $52 million, or 13.8%.
  - Growth in fees related to increase of $6.7 billion in assets under management.
- Other operating income of $249 million, up $222 million.
  - Gain before taxes of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company.
  - Offset by an increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.

INVESTMENT INCOME

Table 9 – Investment income
For the years ended December 31

(in millions of dollars)	2017	2016	2015
Net income on securities at fair value through profit or loss	**$ 1,079**	$ 533	$ 809
Net income on available-for-sale securities	**408**	388	318
Net other investment income	**201**	198	235
Total investment income[(1)]	**$ 1,688**	$ 1,119	$ 1,362

(1) See "Basis of presentation of financial information".

Investment income totalled $1,688 million for 2017, an increase of $569 million, or 50.8%, compared to the previous year.

- Net income on securities at fair value through profit or loss up $546 million.
  - Increase primarily due to change in the fair value of assets backing liabilities related to life and health insurance operations.
    - Increase largely offset by the change in actuarial liabilities that in turn led to higher expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
    - Changes for the most part due to fluctuations in the fair value of the portfolio of stocks, bonds and derivative products.

  This increase was partially offset by the following:
  - Decrease in income generated by asset-backed term note (ABTN) operations, which have been substantially settled since January 2017.
  - Decrease in 2017 in the fair value of derivative financial instruments, including those associated with hedging operations for Desjardins Group as a whole.
- Net income on available-for-sale securities up $20 million, or 5.2%, primarily because of higher gains on disposal of investments in 2017.
- Net other investment income of $201 million, stable compared to 2016.

TOTAL INCOME

Total income, comprising net interest income, net premiums, other operating income and investment income, amounted to $17,101 million, an increase of $1,900 million, or 12.5%, compared to 2016.

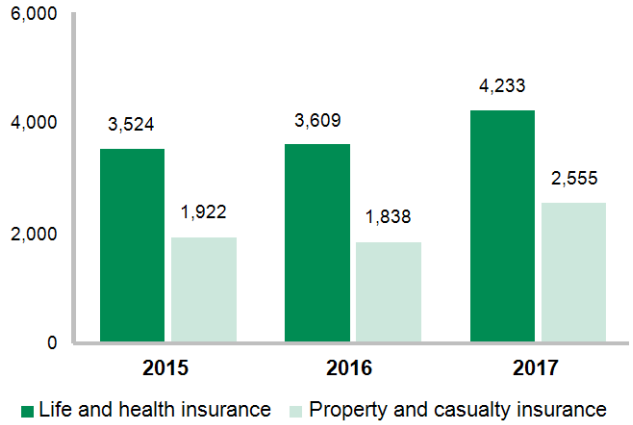
PROVISION FOR CREDIT LOSSES

Desjardins Group's loan portfolio continued to be of high quality in 2017. The provision for credit losses totalled $349 million, up $30 million, or 9.4%. In 2016, there was a recovery of the collective allowance as a result of refining the methodology used in the models for calculating the collective allowance. Favourable developments in portfolio risk curbed the increase, however.

- The provisioning rate was 0.20% as at December 31, 2017, which is comparable to 2016.
- The ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.25% as at December 31, 2017, down from 0.32% a year earlier. Improved economic conditions helped to reduce the volume of gross impaired loans.

CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE CONTRACT LIABILITIES

Claims, benefits, annuities and changes in insurance contract liabilities[1]
(in millions of dollars)



(1) The difference between total results and the sum of business segment results is due to intersegment transactions.

Expenses related to claims, benefits, annuities and changes in insurance contract liabilities totalled $6,717 million, up $1,271 million, or 23.3%, compared to 2016.

Wealth Management and Life and Health Insurance segment

- **Cost of claims of $4,233 million**, up $624 million, or 17.3%. This increase was basically the result of the following:
  - Increase of $425 million in the actuarial liabilities recognized under "Insurance contract liabilities", which includes the effect of an increase in the fair value of matched investments.
  - Favourable effect of adjustments to the actuarial assumptions as well as the less favourable effect of the claims experience included in actuarial liabilities.
  - Increase in benefits related to growth in operations.

Property and Casualty Insurance segment

- **Cost of claims of $2,555 million**, up $717 million, or 39.0%.
  - Increase mainly due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - The P&C insurers' loss ratio was 67.7% for 2017, compared to 60.2% in 2016.
    - Higher ratio partly attributable to less positive developments in 2017 than in 2016 concerning prior-year claims, (15.0%) vs. (20.2%), chiefly automobile insurance claims taken over from State Farm as at January 1, 2015, which were lower than in 2016.
    - Increased ratio also due to higher claims experience for the current year than for 2016, (80.1% vs.75.8%), primarily in automobile insurance in all geographical markets.
  - Offset by less significant impact of catastrophes and major events compared to 2016, when there had been two catastrophes related to hail and the Fort McMurray wildfire in Alberta.

NON-INTEREST EXPENSE

Table 10 – Non-interest expense
For the years ended December 31

(in millions of dollars and as a percentage)	2017	2016 [1]	2015 [1]
Salaries and fringe benefits			
Salaries	**$ 2,808**	$ 2,909	$ 2,830
Fringe benefits	**644**	639	645
	3,452	3,548	3,475
Premises, equipment and furniture, including depreciation	**727**	667	613
Service agreements and outsourcing	**319**	306	331
Communications	**284**	307	299
Other	**2,566**	2,376	2,241
Total non-interest expense	**$ 7,348**	$ 7,204	$ 6,959
Desjardins Group productivity index[2]	**70.8%**	73.8%	70.9%
Adjusted Desjardins Group productivity index[2]	**72.3**	73.4	70.8

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".

Non-interest expense totalled $7,348 million for 2017, up $144 million, or 2.0%, compared to 2016, mainly because of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. Effective cost control following the implementation of productivity initiatives limited the increase in a context of operations growth.

- **Salaries and fringe benefits of $3,452 million**, down $96 million, or 2.7%, compared to 2016, mainly because of the following items:
  - Severance costs incurred in 2016 following changes in Desjardins Group's senior management.
  - Lower personnel expenses as a result of this reorganization.
  - Implementation of productivity initiatives, reflected in a reduction in payroll.
  - This expense item represented 47.0% of total non-interest expense, lower than the 49.3% recorded in 2016.
  - The ratio of fringe benefits to total base compensation was 22.9% in 2017, up compared to 22.0% in 2016, primarily because of the 2016 severance costs included in 2016 salaries.

- **Expenses related to premises, equipment and furniture (including depreciation) of $727 million**, up $60 million, or 9.0%, compared to 2016.
  - The increase resulted mainly from the purchase of computer hardware.

- **Service agreements and outsourcing of $319 million**, up slightly compared to 2016.

- **Communication expenses of $284 million**, down $23 million, or 7.5%, compared to 2016.
  - The decrease resulted from the implementation of productivity initiatives.

- **Other expenses of $2,566 million**, up $190 million, or 8.0%, compared to 2016.
  - Increase due in large part to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increased popularity of the BONUSDOLLARS Rewards Program with Card and Payment Services clients.
  - Business growth, particularly in credit card and point-of-sale financing activities and assets under management.
  - Write-off of intangible assets.
  - Offset by a decrease of $171 million in expenses following the sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 as well as Western Financial Insurance Company on January 1, 2017, as presented in the "Impact of the sale of subsidiaries" section.

- **Productivity index at 70.8% for 2017**, compared to 73.8% in 2016.
- **Adjusted productivity index at 72.3% for 2017**, compared to 73.4% in 2016. The improvement in the 2017 productivity index in 2017 was partly due to an increase in surplus earnings, affected by growth in operations as well as by productivity initiatives that impacted non-interest expense.

INCOME TAXES AND INDIRECT TAXES

Desjardins Group is a cooperative financial group, and each of its entities that operate as a financial services cooperative—namely the caisses, the *Fédération des caisses Desjardins du Québec* and the *Fédération des caisses populaires de l'Ontario Inc.*—is considered a private and independent company for tax purposes, unlike the vast majority of other Canadian financial institutions, which are large public corporations. Each caisse is subject to the private company tax regime and benefited until December 31, 2016, when tax rules allowed it, from certain preferential tax rates under the credit union tax regime. Desjardins entities that are not financial services cooperatives are subject to the large corporation tax regime.

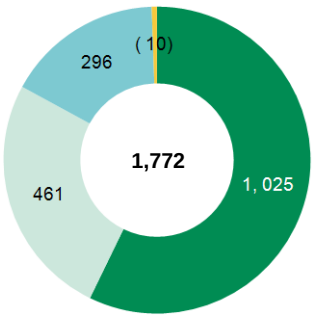
- **Income taxes on surplus earnings before member dividends of $536 million**, up $76 million compared to 2016.
  - Effective tax rate of 19.9% for the year ended December 31, 2017, down compared to 20.6% for 2016. If specific items are excluded, the effective tax rate would have been 21.2%, up slightly compared to 20.7% in 2016.

Note 28, "Income taxes on surplus earnings", to the Combined Financial Statements presents, among other things, a reconciliation of the statutory tax rate and the effective tax rate, expressed in dollars.

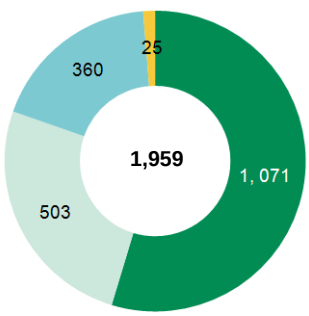
Indirect taxes consist of property and business taxes, payroll and social security taxes, the goods and services tax, and sales taxes. Indirect taxes are included in non-interest expense. For 2017, Desjardins entities paid $1,358 million in indirect taxes, compared to $1,326 million in 2016, mainly due to an increase in the compensation tax.

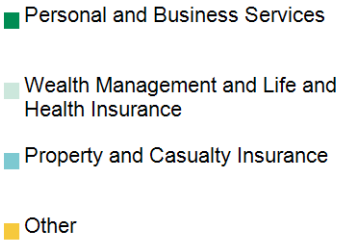
COMPARISON OF 2016 AND 2015

2016 surplus earnings before member dividends
(in millions of dollars)



2015 surplus earnings before member dividends
(in millions of dollars)





For 2016, Desjardins Group posted surplus earnings before member dividends of $1,772 million, compared to $1,959 million for 2015. Surplus earnings adjusted for specific items totalled $1,805 million, for a decrease of $135 million, or 7.0%. Return on equity was 8.0%, compared to 9.1% in 2015, while adjusted return on equity was 8.1% in 2016, compared to 9.0% in 2015.

Segment results

- **Personal and Business Services: Surplus earnings before member dividends of $1,025 million in 2016**, down $46 million compared to 2015, chiefly due to higher non-interest expense in 2016 as a result of:
  - Business growth, particularly in credit card and point-of-sale financing activities.
  - Investments aimed, in particular, at enhancing the service offer to members and clients.

- **Wealth Management and Life and Health Insurance: Net surplus earnings of $461 million in 2016**, down $42 million compared to 2015, essentially due to the following items:
  - Adjustments to actuarial assumptions made in the normal course of business had an unfavourable effect in 2016.
  - Higher gains on the disposal of investments in 2015.
  - Less favourable claims experience in 2016.

  This decrease was partly offset by the following:
  - Solid investment performance in 2016.
  - Limited growth in non-interest expense in 2016 on account of effective cost control in a context of operations growth.

- **Property and Casualty Insurance: Net surplus earnings of $296 million in 2016**, down $64 million compared to 2015, mainly due to the gain arising from the acquisition of State Farm's Canadian operations, recognized in 2015.

Combined results

- **Operating income of $14,082 million in 2016**, up $202 million compared to 2015.
  - Net interest income of $4,273 million in 2016, comparable to the amount in 2015.
  - Net premiums up $261 million in 2016, mainly because of the following:
    - Business growth related to Wealth Management and Life and Health Insurance segment insurance operations.
    - Increase in net premiums as a result of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Other operating income of $2,641 million, down $53 million in 2016, essentially due to the following:
    - Other income down $138 million in 2016 as a result of an increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations and the gain realized at the time of this acquisition in 2015.

    This decrease was partly offset by the following:
    - Increase of $69 million in income from brokerage and investment fund services chiefly due to a larger volume of assets under management from the sale of various financial products.
    - Increase of $24 million in lending fees and credit card service revenues as a result of business volume growth.

- **Investment income of $1,119 million in 2016**, down $243 million compared to 2015.
  - Net income on securities at fair value through profit or loss down $276 million in 2016.
    - Decrease mainly due to fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
      - Decrease partly offset by the change in actuarial liabilities that in turn led to a reduction in expenses related to claims, benefits, annuities and changes in insurance contract liabilities. These differences were mostly attributable to changes in the fair value of the bond portfolio.
    - Unfavourable changes in the fair value of derivative financial instruments associated with hedging operations for Desjardins Group as a whole, which were partially offset by the increase in the fair value of derivative financial instruments in the Property and Casualty Insurance segment in 2016.
  - Income from available-for-sale securities up $70 million in 2016.
    - A loss in share value had been recorded in 2015 as a result of strong market volatility.
  - Net other investment income down $37 million in 2016.
    - Smaller gains on the disposal of real estate investments in 2016.

- **Provision for credit losses of $319 million in 2016**, down $58 million compared to 2015.
  - Decrease mainly due to the recovery of the collective allowance as a result, in particular, of refining the methodology used in the models for calculating the allowance, combined with a high-quality loan portfolio.
  - Ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, of 0.32% as at December 31, 2016, down from 0.34% as at December 31, 2015.
  - Provisioning rate of 0.20% as at December 31, 2016, down from 0.24% as at December 31, 2015.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities**, up $15 million in 2016.
  - Wealth Management and Life and Health Insurance segment up $85 million in 2016.
    - Increase of $82 million in 2016 in the actuarial liabilities recognized under "Insurance contract liabilities", which included the effect of a $149 million decrease in the fair value of matched investments.
    - Actuarial liabilities up $33 million due to changes in assumptions made in 2016, whereas a release of $51 million had been recognized in 2015, following changes to the investment portfolio. The $47 million increase in group annuity premiums and the claims experience also contributed to the higher actuarial liabilities.
  - Property and Casualty Insurance segment: expenses down $84 million in 2016.
    - Decrease resulted mainly from more favourable developments in prior-year claims in 2016 than in 2015, primarily in automobile insurance.
    - Offset by a higher claims experience in 2016 than in 2015.
    - Loss ratio for P&C insurers of 60.2% for 2016, compared to 62.1% in 2015.

- **Non-interest expense** up $245 million in 2016, mainly due to the following:
  - Additional investment in innovative technology platforms in 2016.
  - Payment of severance allowances in 2016.
  - Business growth, particularly in credit card, point-of-sale financing and insurance activities.
  - Offset by strict cost control that made it possible to limit the increase in non-interest expense in 2016.

2.3 Analysis of business segment results

Desjardins Group's financial reporting is organized by business segments, which are defined based on the needs of members and clients, the markets in which Desjardins operates, and on its internal management structure. In first quarter 2017, certain changes were made to the business segments to reflect senior management's decisions about the way each segment is managed, as mentioned in the respective business segment sections. Desjardins Group's financial results are divided into the following three business segments: Personal and Business Services; Wealth Management and Life and Health Insurance; and Property and Casualty Insurance. In addition to these three segments, there is also the Other category. This section presents an analysis of results for each of these segments. Prior-period amounts have been restated to conform to these reclassifications.

Intersegment transactions are recognized at the exchange amount, which represents the amount agreed upon by the various legal entities and business units. The terms and conditions of these transactions are comparable to those offered on capital markets.

2.3.1 Personal and Business Services

PROFILE

Personal and Business Services is central to Desjardins Group's operations. Through a comprehensive, integrated line of products and services designed to meet the needs of individuals, businesses, institutions, non-profit organizations and cooperatives, Desjardins Group is a leader in financial services in Quebec and a player on the financial services scene in Ontario as well.

Desjardins's offer includes regular, convenience and savings transactions, card and payment services, financing, specialized services, access to capital markets, development capital, business ownership transfers and advisory services, and through its distribution network, life and health insurance and property and casualty insurance products.

In addition, members and clients know that they can rely on the largest advisory force in Quebec, made up of dedicated professionals who are there for them at every stage in their life or entrepreneurial growth.

To meet the constantly changing needs of its members and clients, Desjardins Group offers its services through the caisse network and the Desjardins Business centres, as well as through complementary distribution networks and specialized teams, by phone, online, via applications for mobile devices, and at ATMs.

The operations of the *Fonds de sécurité Desjardins* and the shared services which the Federation provides to this segment, formerly presented in the Other category, have been recorded in this segment since the first quarter of 2017.

Additional information about the Personal and Business Services segment's principal risks is presented on page 71 of the "Risk management" section of this MD&A.

SERVICES

Regular and convenience transactions consist of activities related to regular and convenience transactions, including transactions carried out at the caisse counter, requests for information and specialty services, such as purchasing foreign exchange, money orders, drafts and safety deposit boxes.

Savings and investment services include activities related to savings operations, such as variable savings, including current accounts, Build-Up savings accounts like the Youth Profit account, term savings and the High-Interest S@vings Account offered exclusively through *AccèsD* Internet and mobile.

The **integrated business offer** features customized solutions to support businesses of all sizes in their expansion plans, whether on Quebec, Canadian or international markets.

Financing services include:
- **Residential mortgages**, for the purchase of land, new or existing homes and for renovations;
- **Consumer loans**, such as loans for the purchase of automobiles and durable goods, personal lines of credit, student loans and Accord D financial solutions;
- **Commercial credit**, which makes it possible to offer financing in the commercial and industrial, agricultural and agri-food, public and institutional sectors, as well as for commercial and multi-residential real estate.

Payment operations include debit, credit and prepaid card payment services for individuals and businesses, merchant payment acceptance services (Monetico), electronic payment services and both domestic and international funds transfers.

AccèsD operations make Desjardins caisse network products and services available at anytime, anywhere in the world, by phone, online and via applications for mobile devices.

Access to **capital markets** operations meet the financing needs of Canadian corporations, institutions and cooperatives, and provide advisory services for mergers and acquisitions, as well as intermediation and execution services on the stock and fixed income securities markets. These services are carried out by seasoned sales and trading teams who are supported by a research team that is renowned in the industry for its excellence.

Activities related to **development capital** facilitate investment, both directly and through funds, in small and medium-sized enterprises (SMEs) and cooperatives in every region of Quebec. Desjardins Capital Management Inc., which manages *Capital régional et coopératif Desjardins*, supports the growth of businesses, especially in business ownership transfers. With the backing of a team of specialists operating throughout Quebec, this segment helps to develop and maintain the highest calibre of entrepreneurship in Quebec by providing entrepreneurs with assistance at every stage of their company's growth.

Specialized services include international services, cash management services, custodial and trust services, as well as payroll and human resources solutions.

2017 ACHIEVEMENTS

- **Android Pay and Apple Pay:** From now on, Desjardins members and clients who use a compatible device can take advantage of two new secure and user-friendly payment methods to pay for purchases with their mobile device: Apple Pay, and Google's Android Pay. Desjardins Group is the first Quebec financial institution to offer such a wide range of mobile services to its members and clients.
- **SPOT transit payment system**: Launch of a pilot project with the *Société de transport de Laval* (STL) on six routes with 163 payment terminals. The aim of the project is to replace cash on buses, a Canadian first. The technology chosen is contactless payment, which is simple, fast and secure.
- **Voice signature** for online credit card applications: Members no longer have to print off the form, sign it and return it by mail to complete an online credit card application. Not only does this reduce the steps involved, it also speeds up application processing and issuing the card.
- Opening of eight **Signature Service** centres, for a total of 11 to date in different regions of Quebec. Their mandate is to provide integrated services to high-net-worth individuals.
- Launch of the **regional development fund**, for an amount of $100 million over three years, with the goal of supporting and expanding projects and initiatives related to Desjardins Group's socio-economic mission.
- Launch of the new **Desjardins Capital SME fund** designed to support the expansion of SMEs in every region of Quebec. The fund could commit up to $500 million in investments over a five-year horizon. Investments could initially range from $100,000 to $10 million per company in the form of equity or subordinated debt.
- Desjardins Group is a **leader in financial business transfers**. In 2017, this translated into a financing volume in excess of $500 million for more than 250 transfers. These interventions have made it possible to keep many jobs and businesses in every region of Quebec and Ontario, as well as ensure entrepreneurial succession.
- Introduction of the **"Click to sign"** functionality to simplify the signing of documents for the opening of a business account.
- Launch of an **investment fund entirely dedicated to the fintech sector** and artificial intelligence applications to finance, for $50 million. Desjardins Group and the *Caisse de dépôt et placement du Québec* are the two founding institutions and will be joined by other institutional partners. The fund expects to begin operations in 2018.

INDUSTRY

The Canadian financial industry did not experience any major disruptions in 2017. It comprises some 85 domestic and foreign banking institutions, as well as 570 savings and loan cooperatives, slightly more than 50% of which belong to Desjardins Group.

In the Canadian banking services industry, the outstanding volume of financing to individuals and businesses was estimated at $2,891.2 billion at year-end 2017, a year-over-year increase of 5.7%, compared to an increase of 5.3% as at December 31, 2016. Credit demand continued to be supported by a favourable economic climate. On-balance sheet and off-balance sheet personal savings was estimated at $4,187.1 billion as at December 31, 2017, for a year-over-year increase of 7.8%, compared to a 9.4% increase a year earlier. The lower rate is in large part due to more modest stock market activity, which reduced growth in off-balance sheet savings, such as investment funds and securities brokerage.

In Quebec, the outstanding volume of financing to individuals and businesses was estimated at $542.2 billion at year-end 2017, a year-over-year increase of 6.4%, compared to an increase of 8.3% as at December 31, 2016. Credit demand lost stream mainly because of the slowdown in business loans. Annual growth in financing to individuals was estimated at 5.8% as at December 31, 2017, reaching a volume of $380.5 billion at that date, compared to a rate of 4.7% a year earlier. Residential mortgages were chiefly responsible for the sustained credit demand from individuals, with a year-over-year growth rate of 5.5% at that date, compared to an increase of 4.0% a year earlier, a trend that can be traced to improved housing market activity. For instance, housing starts and resales of existing homes were up 19.4% and 5.8%, respectively, during 2017, while the average selling price increased by 4.5%. Consumer loans grew at an estimated rate of 7.2% annually as at December 31, 2017, to total $82.7 billion, compared to a 7.3% increase at year-end 2016. Robust retail sales accounted for the stronger demand in personal loans; retail sales were up close to 6% during the same period, whereas sales of new and used automobiles increased by close to 10%.

With regard to financing to businesses in Quebec, the outstanding volume was estimated at $161.7 billion as at December 31, 2017, for an estimated year-over-year increase of 7.7%, compared to growth of 18.2% at year-end 2016. This contraction was largely due to commercial and industrial loans, which posted a year-over-year increase estimated at 7.8% at that date, for a volume of $143.3 billion, compared to a rate of 19.2% a year earlier. Agricultural loans, which are also part of financing to businesses, recorded year-over-year growth estimated at 6.7% as at December 31, 2017, to total $18.4 billion, compared to an 11.0% increase a year earlier.

On-balance sheet and off-balance sheet personal savings in Quebec had an outstanding volume estimated at $791.3 billion as at December 31, 2017, for annual growth of 8.5%, compared to an increase of 9.2% at the end of 2016. Off-balance sheet savings is partly responsible for this slower growth. It posted a year-over-year increase estimated at 10.2% at the same date, to total $549.3 billion, compared to growth of 10.9% recorded a year earlier. Significantly slower growth in stock market activity, especially in Canada, where the S&P/TSX index grew by only 6.0% in 2017, compared to 17.5% in 2016, accounts for the slowdown in off-balance sheet savings products, such as investment funds and securities brokerage. On-balance sheet savings also contributed to this slowdown, with an estimated outstanding volume of $242.0 billion as at December 31, 2017, a year-over-year increase of 4.9%, compared to a 5.6% gain observed at the end of 2016.

The major industry players are deploying business models that target quality and consistency in personal services, or as partners for Quebec-based SMEs. Their strategies are based primarily on client experience, access to services and proactive advice. The fight for market share therefore continues to be very fierce. All players are adopting strategies aimed at intensifying business relations with their clients and getting to know them better. Innovation has become an absolute necessity in this fight for market share in order to satisfy customers.

At the same time, a number of technology giants, like Google, Apple, Facebook and Amazon, are competing directly with traditional financial institutions or entering major partnerships with them.

Desjardins Group is a Quebec leader in financial services to individuals and businesses. In loans to individuals, it had market shares of 36.1% and 22.4%, respectively, in residential mortgages and consumer credit as at December 31, 2017. Card and Payment Services is also the number one card issuer in Quebec, and fourth in Canada, in terms of outstandings, with more than 6.8 million credit cards and 5.9 million debit cards issued in Canada. In on-balance sheet personal savings in Quebec, Desjardins Group once again is included at the top of the list, with a market share of this industry estimated at 41.6% as at December 31, 2017. Finally, with estimated market shares of 19.7% and 39.3% as at December 31, 2017 in commercial and industrial loans and agricultural loans, respectively, Desjardins Group is also a leader.

Additional information about the Personal and Business Services' economic environment can be found in the "Changes in the economy" section of this MD&A.

2018 STRATEGY AND PRIORITIES

The 2018 strategies and priorities of the Personal and Business Services segment are incorporated into Desjardins Group's strategic priorities and are aimed at helping Desjardins to achieve its ambition of being first in people's hearts. The Personal and Business Services segment intends to strengthen its leadership position in financing, savings and, through its distribution network, life and health and P&C insurance products. Capitalizing on the strengths of the entire cooperative group in serving members and clients and increasing their satisfaction will again be Desjardins Group's key priorities in the coming year. To do so, it will facilitate interactions with members and clients across all Desjardins channels, in particular by streamlining its processes.

Reaching ambitious objectives requires the commitment of every manager, employee and officer, as well as a high-calibre, comprehensive and integrated offer that is innovative and easy to access. The segment further intends to underscore the cooperative difference by contributing to lasting prosperity in businesses and communities. Its strategy is based on establishing enduring relationships of closeness and trust with members, clients and partners, and on a sustainable development philosophy. The strategy is built on strong foundations and long-standing commitments in the regions and in various socio-economic communities.

The segment is also continuing to implement its plan to achieve profitable growth in order to remain a major player in the Quebec industry while enhancing its productivity. It seeks to grow while maximizing its synergies with other Desjardins entities and segments.

More specifically, this segment's priorities for 2018 are to:

- Accelerate the shift to a member- and client-focused culture across Desjardins Group.
- Continue the digital transformation of products and services across all distribution channels.
- Facilitate interactions with members and clients throughout Desjardins components and across all channels (mobile, website, call centres, caisses, Desjardins Business centres, online business centres, etc.).
- Offer members and clients proactive support and the expertise of the entire Desjardins Group to help them grow their businesses.
- Ensure a high level of satisfaction among members and clients.

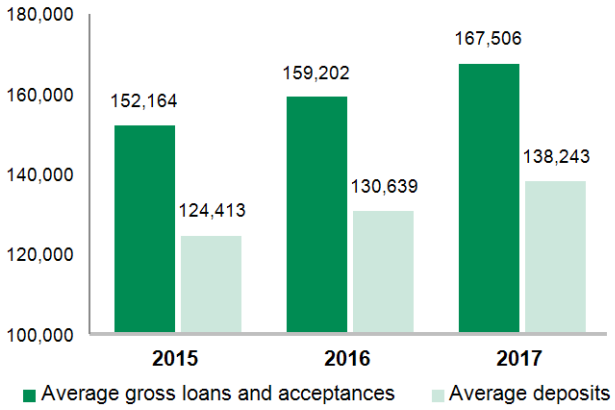
ANALYSIS OF FINANCIAL RESULTS FOR THE PERSONAL AND BUSINESS SERVICES SEGMENT

Table 11 – Personal and Business Services – Segment results
For the years ended December 31

(in millions of dollars and as a percentage)	2017	2016[1]	2015[1]
Net interest income	**$ 3,916**	$ 3,743	$ 3,730
Other operating income[2]	**2,035**	1,940	1,901
Operating income[2]	**5,951**	5,683	5,631
Investment income[2]	**230**	360	386
Total income	**6,181**	6,043	6,017
Provision for credit losses	**345**	318	377
Non-interest expense	**4,365**	4,281	4,215
Income taxes on surplus earnings	**363**	419	354
Surplus earnings before member dividends	**1,108**	1,025	1,071
Member dividends, net of tax recovery	**148**	105	113
Net surplus earnings for the year after member dividends	**$ 960**	$ 920	$ 958
Of which:			
Group's share	**$ 960**	$ 918	$ 957
Non-controlling interests' share	**-**	2	1
Indicators			
Average gross loans and acceptances[2]	**$ 167,506**	$ 159,202	$ 152,164
Average deposits[2]	**138,243**	130,639	124,413
Provisioning rate[2]	**0.21%**	0.20%	0.25%
Gross impaired loans/gross loans and acceptances ratio[2]	**0.25**	0.33	0.34

[1] Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
[2] See "Basis of presentation of financial information".

Average gross loans and acceptances and average deposits
(in millions of dollars)



COMPARISON OF 2017 AND 2016 – PERSONAL AND BUSINESS SERVICES

- **Surplus earnings before member dividends of $1,108 million**, up $83 million, or 8.1%, essentially due to the following items:
  - The caisse network performed well, related to growth in operations.
  - Growth in credit card and point-of-sale financing activities.
  - Higher income from mergers and acquisitions related to capital markets.

- **Operating income of $5,951 million**, up $268 million, or 4.7%.
  - Increase of $173 million in net interest income mainly as a result of year-over-year growth of $8.3 billion in the entire average portfolio of loans and acceptances outstanding. However, fierce competition in the market continued to put pressure on interest margins.
  - Other operating income of $2,035 million, up $95 million, or 4.9%, mainly due to the following:
    - Growth in business volume from the various payment solutions offered by Card and Payment Services.
    - Growth in income from capital markets.
    - Increase in caisse network sales of various Desjardins Group products designed by the subsidiaries, such as investment funds.
    - Offset by lower deposit income on account of changes in pricing.

- **Investment income of $230 million**, down $130 million, or 36.1%, chiefly from the following items:
  - Lower income from derivatives.
  - Larger gains on the disposal of securities in 2016.
  - Offset by an increase in capital market trading income.

- **Total income of $6,181 million**, up $138 million, or 2.3%.

- **Provision for credit losses of $345 million**, up $27 million, or 8.5%. This provision had decreased significantly in 2016 as a result of refining the methodology used in calculating the collective allowance. However, favourable developments in portfolio risk curbed this increase.

- **Non-interest expense of $4,365 million**, up $84 million, or 2.0%.
  - Business growth, especially in credit card and point-of-sale financing activities that had an effect on bonus programs.
  - Offset by the favourable effect of productivity initiatives implemented.

2.3.2 Wealth Management and Life and Health Insurance

PROFILE

The Wealth Management and Life and Health Insurance segment combines different categories of service offers aimed at growing the assets of Desjardins Group members and clients and helping them protect their financial security. These offers are intended for individuals and businesses, while its group insurance and savings plans meet the needs of employees through their company, or individuals who are part of any other group.

The segment designs several lines of individual insurance (life and health) coverage as well as savings and investment products. In addition to its own products and services, it distributes external savings and investment products as well as private wealth management services. The segment also includes asset management for institutional clients.

One of the greatest strengths of the Wealth Management and Life and Health Insurance segment is its vast and diversified Canada-wide distribution network, which mainly includes:
- Employees of the caisse network and Desjardins Business centres.
- Financial security advisers dedicated to caisse members.
- Investment advisers and private managers.
- Exclusive agents and independent partners.
- Actuarial consulting firms and group plan representatives.

To meet members' and clients' needs and preferences, certain product lines are distributed directly via customer care centre, online or through applications for mobile devices. Online services are constantly being finetuned so that they meet clients' changing requirements.

Additional information about the Wealth Management and Life and Health Insurance segment's principal risks is presented on page 71 of the "Risk management" section of this MD&A.

SERVICES

Insurance for individuals includes products and services offered on an individual basis, or to businesses or groups by way of group plans. These life and health insurance coverages provide peace of mind by reducing the financial impacts that could occur due to illness, disability, accident or death.

Savings and investment services include the various investment solutions for individuals and businesses, as well as group retirement savings plans for company employees, or individuals who are part of any other group. The wide array of investment solutions offered means that individuals and businesses can find the one best suited to their needs, whether for preparing for retirement, planning a trip or any other financial goal.

Securities brokerage services include the distribution of all types of investments, including stock market securities. There are two separate brokerage models: the sound, customized services of an investment adviser (full-service brokerage) or online brokerage services for savvy investors who want to trade on their own.

Private wealth management services are set out in a constantly updated and integrated offer intended for wealthy clients. The personalized support of private managers includes a number of aspects, such as financial planning, tax and philanthropy optimization as well as portfolio management.

Lastly, **institutional asset management** services are provided by a group of investment experts specializing in asset management for institutional clients in order to obtain competitive returns and an attractive risk-return trade-off for them.

2017 ACHIEVEMENTS

New offers that stand out by always meeting the changing needs of Desjardins Group members and clients in the best possible way:

- Individual insurance: **New participating life insurance** that provides life insurance coverage together with tax-efficient investments, which can also entitle policyholders to dividend payments.
- Group insurance:
  - An innovative first in Canada: A **program to improve the quality of sleep and employee productivity** with three entry points: raising awareness, screening and diagnosis.
  - With **Epsylio**, Desjardins Group is the first insurer to use artificial intelligence to provide personalized support to clients who do not feel ready to use the Employee Assistance Program 360°.
- Savings and investments:
  - Desjardins Group is launching its own **fixed income and global equities Exchange Traded Funds (ETFs),** aimed at reducing the risk of losses in market downturns and making the most of upswings.
  - **New SocieTerra Canadian Equity Fund**.
  - **Market-linked guaranteed investments**: Desjardins Group ranks first in Canada (33% of the market share) for guaranteed investment products with this highly popular product because of its stock market growth potential while protecting invested capital.
  - **Virtual savings and investment assistant**: An additional tool to be used by investment advisers to support investors who want to trade on their own.
  - **Announcement of the creation of Aviso Wealth**: Desjardins Group has joined forces with the provincial credit union centrals and The CUMIS Group to create one of the largest wealth management companies in Canada. The business combination of their subsidiaries Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. will create Aviso Wealth in the first half of 2018, subject to obtaining the required regulatory approvals and satisfying the usual closing conditions.
- Group retirement savings: **Online innovative educational video clips** provided on a secure site for members of Desjardins group retirement savings plans. This first in the industry incorporates a member's data into the video and the personalized scenario provides even better support to the member in achieving retirement goals.
- Online securities brokerage: **New customizable transactional platform** that is also more agile and robust, and provides active investors with certain unique advantages, including an interface and online help tool in French.
- Desjardins Private Wealth Management: Launch of a **new private fund** with Desjardins Capital Management Inc. to support the growth of businesses across Quebec.

INDUSTRY

The wealth management industry and the life and health insurance industry are complementary because their aim is to provide products and services that will increase the net worth of Canadian households and make sure that their financial future is secure.

The financial assets held by Canadian households in various savings and investment products (wealth management) totalled $4,135 billion at the end of 2016, growing annually at 7.9% on a compound basis over the past five years, and 9.7% in the past year.

All major banking groups as well as life and health insurance and investment fund companies have a wealth management division that designs and distributes diversified financial products and services to meet the investment and financial, tax and estate planning needs of our client bases, including affluent and wealthy clients. These clients have specific needs, and their expectations are high, leading major players in the industry to outdo each other in terms of ingenuity in order to win them over and build their loyalty.

Given such high and complex needs, financial advisers still play a key role in providing relevant information, making sales and maintaining relationships. Nevertheless, the industry is proactively meeting certain clients' desire for self-directed products and diversifying ways to access services by using virtual and mobile interfaces. This will continue to be a major challenge over the next few years and is why an increasing number of competitors are developing digital offers both in Canada and globally.

According to 2016 statistics, there are more than 150 life and health insurance providers doing business in Canada, and 37 are foreign owned. Five of them accounted for 78.9% of the Canadian market, clearly showing a highly consolidated industry. The industry plays a major stabilizing role in capital markets, even in difficult economic conditions, given its strong presence as a regular long-term capital provider to business and government. It has nonetheless grown by 4.2% in the past five years and in 2016, it recorded premium income of more than $106 billion as a result of life insurance, health insurance and annuities.

Desjardins Financial Security Life Assurance Company remains a leader in Quebec and ranks fifth in Canada, with written premiums of $4.3 billion. Based on 2016 figures, 22 million Canadians protect their family's financial security by taking out individual or group life insurance, amounting to insurance in effect of $4.5 trillion. In addition, the Canadian life and health insurance industry paid out $88 billion in benefits.

2018 STRATEGY AND PRIORITIES

The 2018 strategies and priorities of the Wealth Management and Life and Health Insurance segment form part of Desjardins Group's strategic priorities that aim to help Desjardins Group to achieve its ambition of being first in people's hearts. Just like the other Desjardins Group business segments, the Wealth Management and Life and Health Insurance segment intends to build exceptional member and client relationships and ensure the excellence of its services. This segment enjoys a special place within the lives of people, groups and businesses because of its distinctive offering in life insurance, health insurance, savings and investments and securities brokerage. In order to maintain Desjardins Group's leadership role, the segment's priorities for 2018 are to accelerate the shift to a member- and client-focused culture by reducing the irritants reported by members and clients. To this end, the segment intends to optimize its product lines, further automate its processes and accelerate its digital shift. The resulting efficiency gains will enable it to provide constantly better service to members and clients, which is its raison d'être.

Another priority of the Wealth Management and Life and Health Insurance segment is to help actively promote Desjardins Group's cooperative difference. Concretely, it will therefore pursue its financial literacy initiatives with regard to savings and retirement as well as its activities to promote health management and financial security. Additional action would be to maintain its leadership in the area of responsible investing across Canada, thereby promoting the development of a sustainable and responsible economy.

The Wealth Management and Life and Health Insurance segment's third priority is to capitalize on Desjardins Group's strengths as an expansive cooperative group. It will therefore take action to maximize synergies within Desjardins Group, by unleashing, for instance, the full potential of business development, particularly in Ontario, and by expanding its product offer to all Desjardins Group distribution networks and external networks.

To summarize, the top three priorities of the Wealth Management and Life and Health Insurance segment are:

- Build exceptional member and client relationships and ensure the excellence of its services.
- Help actively promote Desjardins Group's cooperative difference.
- Capitalize on Desjardins Group's strengths as an expansive cooperative group.

In order to successfully carry out the combined actions of these three priorities, this segment can rely on a team of employees and distribution partners who are determined to always better meet the needs of members and clients by providing exemplary and distinctive quality service.

ANALYSIS OF FINANCIAL RESULTS FOR THE WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE SEGMENT

Table 12 – Wealth Management and Life and Health Insurance – Segment results

For the years ended December 31

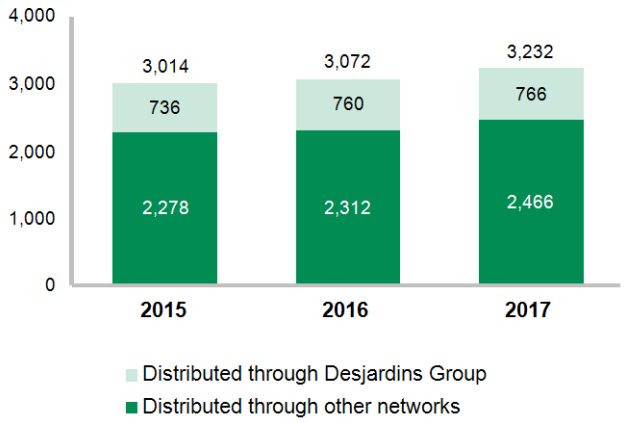
(in millions of dollars)	2017	2016	2015
Net interest income	**$ 1**	$ -	$ -
Net premiums	**4,406**	4,204	4,057
Other operating income[1]	**1,514**	1,386	1,263
Operating income[1]	**5,921**	5,590	5,320
Investment income[1]	**1,406**	795	942
Total income	**7,327**	6,385	6,262
Provision for credit losses	**4**	-	-
Claims, benefits, annuities and changes in insurance contract liabilities	**4,233**	3,609	3,524
Non-interest expense	**2,329**	2,208	2,104
Income taxes on surplus earnings	**149**	107	131
Net surplus earnings for the year	**$ 612**	$ 461	$ 503
Of which:			
Group's share	**$ 610**	$ 440	$ 392
Non-controlling interests' share	**2**	21	111
Indicators			
Net sales of savings products	**$ 8,755**	$ 8,465	$ 7,256
Insurance sales	**523**	471	451
Group insurance premiums	**3,232**	3,072	3,014
Individual insurance premiums	**836**	796	746
Annuity premiums	**338**	336	297
Receipts related to segregated funds	**1,840**	2,811	1,705

[1] See "Basis of presentation of financial information".

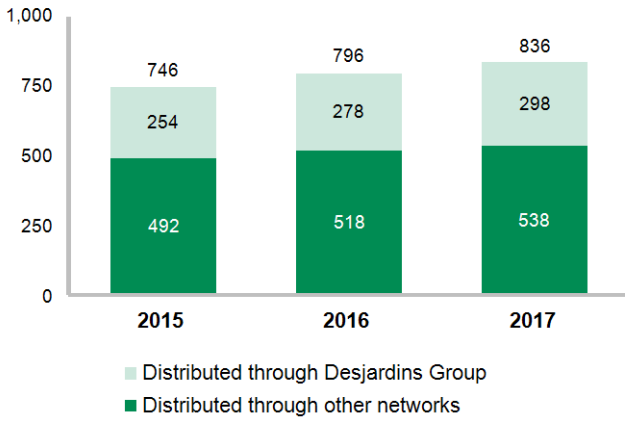
Table 13 – Expenses attributable to policyholders
For the years ended December 31

(in millions of dollars)	2017	2016	2015
Insurance and annuity benefits	**$ 3,037**	$ 2,904	$ 2,889
Change in actuarial liabilities	**984**	559	477
Policyholder dividends, experience refunds and other	**212**	146	158
Total	**$ 4,233**	$ 3,609	$ 3,524

Group insurance premiums by distribution network
(in millions of dollars)



Individual insurance premiums by distribution network
(in millions of dollars)



COMPARISON OF 2017 AND 2016 – WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

- **Net surplus earnings of $612 million,** up $151 million, or 32.8%, mainly as a result of:
  - Solid investment performance.
  - Favourable adjustments to actuarial assumptions made in the normal course of business.
  - Higher income as a result of growth in assets under management.
  - Offset by a less favourable claims experience in 2017.

- **Operating income of $5,921 million,** up $331 million, or 5.9% basically because of:
  - Increase of $202 million in premiums, of which $160 million was from group insurance and $40 million, from individual insurance.
  - Other operating income totalled $1,514 million, up $128 million, or 9.2%.
    - Higher income from growth in assets under management.

- **Investment income of $1,406 million,** up $611 million, or 76.9%.
  - Increase primarily due to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
    - Offset by the change in actuarial liabilities leading to higher expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
    - Differences due for the most part to changes in the fair value of the portfolio of stocks, bonds and derivatives.
  - Higher gains on the sale of investments in 2017.

- **Total income of $7,327 million,** up $942 million, or 14.8%.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of $4,233 million,** up $624 million, or 17.3%.
  - Increase of $425 million in actuarial liabilities under "Insurance contract liabilities", which included the effect of the increase in the fair value of matched investments.
  - Actuarial liabilities also included the favourable effect of the adjustments to actuarial assumptions and the less favourable effect of claims experience.
  - Increased benefits from growth in operations.

- **Non-interest expense of $2,329 million,** up $121 million, or 5.5% chiefly as a result of higher expenses for assets under management, but limited by effective cost control in a context of operations growth.

2.3.3 Property and Casualty Insurance

PROFILE

The Property and Casualty (P&C) Insurance segment offers insurance products providing coverage for Desjardins Group members and clients against disasters. It includes the operations of Desjardins General Insurance Group Inc. and its subsidiaries.

Desjardins General Insurance Group Inc. offers a personal line of automobile and property insurance products across Canada and also provides businesses with insurance products.

Its products are distributed through property and casualty insurance agents in the Desjardins caisse network in Quebec, a number of client care centres (call centres) and Desjardins Business centres, through an exclusive agent network of close to 500 agencies outside Quebec distributing P&C insurance and several other financial products online and via applications for mobile devices.

Desjardins General Insurance Group Inc., which has more than 3,000,000 clients, markets its products to the Canada-wide individual and business market under the Desjardins Insurance and State Farm banners, and to the group market—including members of professional associations and unions, and employers' staff—under The Personal banner. As part of its integration plan for State Farm's Canadian operations, Desjardins Group will switch from the State Farm banner to the Desjardins Insurance banner starting on May 1, 2018 until December 31, 2019. Desjardins General Insurance Group Inc. is also active on the white label market, in particular with well-established Canadian financial institutions.

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, Western Financial Group Inc. and Western Life Assurance Company, while Western Financial Insurance Company was sold on January 1, 2017. Additional information concerning these transactions is presented in the "Impact of the sale of subsidiaries" section on page 30.

Additional information about the Property and Casualty Insurance segment's principal risks is presented on page 71 of the "Risk management" section of this MD&A.

SERVICES

Automobile insurance, including motorcycle and recreational vehicle insurance, offers insurance coverage tailored to clients' specific needs and their vehicle features. Automobile insurance also includes the necessary coverage to obtain financial compensation for bodily injury in provinces where such coverage is not provided by a public plan.

Property insurance offers owners and tenants insurance coverage to protect their physical property, with all-risk insurance coverage and optional coverages for primary and secondary residences.

Business insurance covers the insurance requirements for commercial vehicles, commercial property and public liability for businesses. Service is provided to the following sectors, among others: service firms, retailers and wholesalers, garages, self-employed workers, general or specialized contractors, restaurants, offices, health care professionals, commercial buildings, condominiums and apartment buildings.

2017 ACHIEVEMENTS

- Continued streamlining, modernizing and enhancing the member and client experience:
  - Since clients are of paramount concern to the P&C Insurance segment, **national flood coverage** was introduced in March 2017, thereby enhancing its line of water damage coverage.
  - The P&C Insurance segment continues to develop its mobile offer, which offers more advantages to its insureds with the **Ajusto and Alert programs**, now available in the new Desjardins Insurance Home-Auto, The Personal or State Farm apps. Alert is a brand new Canada-wide program to prevent water damage in home insurance by using a detector placed close to a potential source of leaks. The Ajusto telematics program, which provides personalized feedback on drivers' behind-the-wheel habits, continues to promote improved driving habits since its initial launch in 2013, according to the results of a recent survey of Ajusto users.
  - The P&C Insurance segment continues its **digital transformation**, in particular with quick new quotes for condo owners and tenants, and the deployment of online purchases of Desjardins Insurance auto insurance.
- **Integration of State Farm's Canadian operations** is still on schedule and should for the most part be completed in 2018.
- Continuation of the **program to modernize IT systems** for business insurance for exclusive agents in Ontario, the Atlantic region and the West.

INDUSTRY

The Canadian P&C insurance industry offers insurance coverage for vehicles, personal and commercial property, and public liability. In 2016, direct premiums written on the Canadian market totalled $49 billion, of which individual insurance accounted for 63% and business insurance accounted for 37%. Brokers across Canada hold market shares of 63%, while direct writers have 27%, and exclusive agents hold 11%. In Quebec, direct writers continue to gain significant individual market shares and now account for 64% of the market, compared to 34% for brokers, and 2% for exclusive agents.

The Canadian P&C insurance market is a mature market, with an average annual growth rate of 3.4% over the past five years. Its growth is influenced by the level of premiums, which varies in particular according to changes in the value of insured property and other factors relating to the different business lines. The industry's financial performance depends on the profitability of insurance operations, which is based on the insurance premiums collected less the cost of claims and non-interest expense, as well as on the investment portfolio return.

In this context, underwriting and pricing risk, access to consumers and customer satisfaction still play an important role in not only attracting new clients but also in building the loyalty of the existing client base. Changes in consumer preferences and the growing importance of digital channels as an addition to traditional channels affect customer habits so that most clients tend to use a variety of methods to interact with their insurer.

The entire auto insurance industry in Canada is now facing challenges associated with profitability resulting from a sharp rise in claims, which reflects in particular the cost of new technologies in motor vehicles, the increase in distractions behind the wheel and the U.S. exchange rate because numerous spare parts are built in the U.S. The Desjardins Group P&C Insurance segment is proactive regarding these challenges and has implemented an action plan to optimize its profitability in a changing world given the difficult situation.

In addition, consolidation in the Canadian P&C insurance market continues to increase. In 2016, the top 10 P&C insurers held 69% of the market, up 5% since 2012. The trend toward consolidation in this market continues with large insurers' and distributors' transactions putting additional pressure on their smaller rivals.

The 2017 flood season significantly affected the insurance industry this year. According to the firm Catastrophe Indices and Quantification Inc. (CatIQ), the spring flooding in 2017 caused insured losses of over $223 million in Ontario and Quebec. More than 7,000 claims were filed with Desjardins General Insurance Group Inc. between April and May 2017 in Ontario and Quebec. Desjardins Insurance launched flooding coverage across Canada in March, enhancing its line of water damage coverage and reaffirming that it is a caring P&C insurer.

While the Canadian industry is developing at an unprecedented rate, the various industry players are competing simultaneously on several fronts. The Canadian market will continue to develop quickly as in recent years, driven by technological innovations, changes in expectations and consumer behaviour as well as the advent of new business models. Significant investments are also being made to create new technology infrastructure and data management capabilities. In fact, data analysis will provide important leverage for all sectors and will be facilitated by artificial intelligence. In addition, a number of insurers are working to make their interaction with consumers easier and simpler through multi-channel logic so that they can be contacted in the way consumers prefer (in person, by phone or online). These insurers are starting to position themselves in response to new trends such as Insurtech or the sharing economy, and the Desjardins Group P&C Insurance segment is proactive vis-à-vis these new trends.

Desjardins General Insurance Group Inc. relies on its operational excellence and its key competencies in terms of market access, risk segmentation and claims management to enhance the value it offers to members and clients. As at December 31, 2016, the P&C Insurance segment ranked third in the Canadian property and casualty insurance market, and it was in second place in the individual insurance market.

2018 STRATEGY AND PRIORITIES

The Property and Casualty Insurance segment's 2018 strategies and priorities fall within the scope of Desjardins Group's strategic priorities, and aim to help Desjardins Group attain its goal of being number one in people's hearts. The Property and Casualty Insurance segment will focus its efforts in 2018 on enhancing the member and client experience as well as on the digital shift and transformation and the implementation of the initiatives already under way.

As a result, in 2018, the segment will continue its efforts to be recognized as a leader in Canada in promoting the member and client experience. Enhancing this experience will involve in particular accelerating the streamlining and image process already initiated by optimizing the performance of its value chain and adapting its business practices in the interests of its members and clients.

Moreover, in order to affirm Desjardins Group's cooperative difference, the segment intends to continue to modernize its insurance model to enhance added value interactions by capitalizing on analytics and the digital transformation.

The segment will also continue to build on the strengths of the expansive cooperative group to which it belongs. In Quebec, it intends to pursue growth by maximizing its synergy in conjunction with other Desjardins Group entities and segments and by speeding up the shift to the *Caissassurance* model. Outside Quebec, it will focus on the exclusive agent network by completing the integration of State Farm's Canadian operations in tandem with the other Desjardins Group entities and will ensure that Desjardins's full potential is developed.

In short, the Property and Casualty Insurance segment's key priorities for 2018 are:

- Enhance the member and client experience.
- Continue the digital transformation.
- Effectively perform various ongoing projects.

ANALYSIS OF FINANCIAL RESULTS FOR THE PROPERTY AND CASUALTY INSURANCE SEGMENT

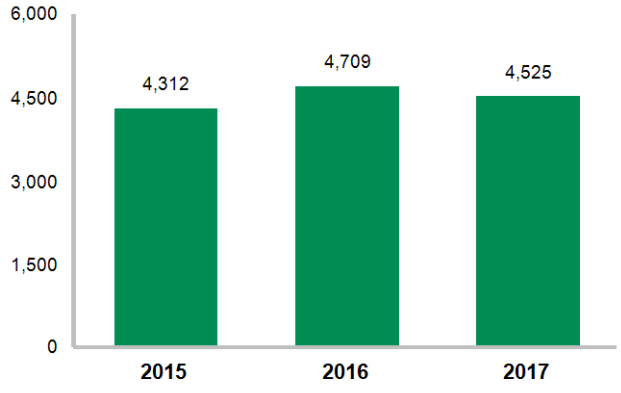
Table 14 – Property and Casualty Insurance – Segment results

For the years ended December 31

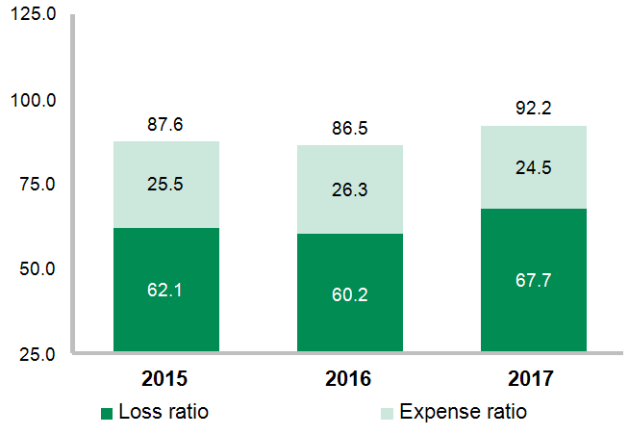
(in millions of dollars and as a percentage)	2017	2016	2015
Net interest income	**$ 1**	$ 1	$ 1
Net premiums	**3,896**	3,207	3,113
Other operating income (loss)[1]	**78**	(55)	104
Operating income[1]	**3,975**	3,153	3,218
Investment income[1]	**214**	206	228
Total income	**4,189**	3,359	3,446
Claims, benefits, annuities and changes in insurance contract liabilities	**2,555**	1,838	1,922
Non-interest expense	**1,099**	1,132	1,070
Income taxes on surplus earnings	**89**	93	94
Net surplus earnings for the year	**$ 446**	$ 296	$ 360
Specific items, net of income taxes			
Gain, net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company[2]	**(241)**	-	-
Gain and expenses related to the acquisition of State Farm's Canadian operations[3]	**32**	33	(22)
Adjusted net surplus earnings for the year[1]	**$ 237**	$ 329	$ 338
Of which:			
Group's share	**$ 405**	$ 245	$ 303
Non-controlling interests' share	**41**	51	57
Indicators			
Gross written premiums[4]	**$ 4,525**	$ 4,709	$ 4,312
Loss ratio[1]	**67.7%**	60.2%	62.1%
Current year loss ratio[1]	**80.1**	75.8	73.7
Loss ratio related to catastrophes and major events[1]	**2.6**	4.6	0.1
Ratio of favourable changes in prior year claims[1]	**(15.0)**	(20.2)	(11.7)
Expense ratio[1]	**24.5**	26.3	25.5
Combined ratio[1]	**92.2**	86.5	87.6

(1) See "Basis of presentation of financial information".
(2) The difference between the data presented in the table of Desjardins Group's adjusted surplus earnings before member dividends is due to intersegment transaction expenses.
(3) The difference between the data presented in the table of Desjardins Group's adjusted surplus earnings before member dividends is due to an amount from the Wealth Management and Life and Health Insurance segment.
(4) Includes life insurance premiums of Western Financial Group Inc.

Gross written premiums
(in millions of dollars)



Combined ratio
(as a percentage of net premiums earned)



COMPARISON OF 2017 AND 2016 – PROPERTY AND CASUALTY INSURANCE

- **Surplus earnings of $446 million,** up $150 million, or 50.7%, including a gain of $241 million, net of expenses and after income taxes, on the sale of subsidiaries.

- **Adjusted net surplus earnings of $237 million,** down $92 million, or 28.0%. This decrease was mainly due to a higher claims experience for the current year than in 2016 and less favourable developments in prior-year claims than in 2016.

- **Operating income of $3,975 million,** up $822 million, or 26.1%.

- **Net premiums of $3,896 million,** up $689 million, or 21.5%, primarily as a result of:
  - Increase of $660 million from the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Increase of $168 million due to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
  - Offset by a decrease in net premiums following the sale of Western Life Assurance Company on July 1, 2017 and of Western Financial Insurance Company on January 1, 2017.

- **Other operating income of $78 million,** up $133 million, chiefly because of the gain on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company.
  This increase was partly offset by the following:
  - Decrease in commission income following the sale of Western Financial Group Inc.
  - Larger increase than in 2016 in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.

- **Investment income of $214 million,** up $8 million, or 3.9%, basically as a result of net gains on the disposal of common shares higher than those recorded in 2016.
  This increase was partly offset by the following:
  - Less favourable results on derivative financial instruments than in 2016.
  - Decrease in the fair value of bonds as a result of the increase in interest rates on the market, which was higher than in 2016. The decrease in the value of the bonds was offset by a similar decrease in the cost of claims because of a matching strategy.

- **Total income of $4,189 million,** up $830 million, or 24.7%.

- **Cost of claims totalling $2,555 million,** up $717 million, or 39.0%.
  - Increase mainly due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Loss ratio of P&C insurers at 67.7% for 2017, compared to 60.2% in 2016.
    - Higher loss ratio partly due to a less favourable change than in 2016 concerning prior-year claims, (15.0%) vs (20.2%), mainly automobile insurance claims taken over from State Farm as at January 1, 2015.
    - Increased loss ratio also attributable to the higher claims experience for the current year than in 2016, (80.1% vs 75.8%), primarily in automobile insurance claims in all geographic markets.
  - Offset by catastrophes and major events, which were less significant than in 2016, when there had been two catastrophes caused by hail and the Fort McMurray wildfire in Alberta.

- **Non-interest expense of $1,099 million,** down $33 million, or 2.9%, mainly as a result of:
  - Decline in expenses due to the sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017, as well as the sale of the pet insurance operations of Western Financial Insurance Company on January 1, 2017.
  - Offsetting increase partly due to the effect of the previously mentioned reinsurance treaty on the charges covered by it.

2.3.4 Other category

The Other category includes financial information that is not specific to a business segment. It mainly includes the Federation's treasury activities and those related to financial intermediation between liquidity surpluses and needs of the caisses. This category also includes the results for the support functions provided by the Federation to Desjardins Group as a whole and the operations of Desjardins Capital Inc. It also includes Desjardins Technology Group Inc., which encompasses all of Desjardins Group's IT operations. In addition to various adjustments required to prepare the Combined Financial Statements, intersegment balance eliminations are classified in this category. The operations of the *Fonds de sécurité Desjardins* and the shared services which the Federation provides, formerly presented in the Other category, have been recorded in the Personal and Business Services segment since first quarter 2017.

Desjardins Group does not consider an item-by-item comparative analysis of the operations in this category to be relevant given the integration of various consolidation adjustments and intersegment balance eliminations. Consequently, Desjardins Group presents an analysis of these operations based on their contribution to surplus earnings.

Table 15 – Other category
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Treasury activities	**$ 113**	$ 110	$ 111
Activities related to derivatives associated with hedging activities	**(4)**	(44)	31
Other[2]	**(124)**	(76)	(117)
Net surplus earnings (deficit) for the year	**$ (15)**	$ (10)	$ 25
Of which:			
Group's share	**$ (15)**	$ (12)	$ 22
Non-controlling interests' share	**-**	2	3

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) Includes support function activities, income from asset-backed term notes, various adjustments required to prepare the Combined Financial Statements, and intersegment balance eliminations.

COMPARISON OF 2017 AND 2016 – CONTRIBUTION BY OTHER CATEGORY TO SURPLUS EARNINGS

- **Net deficit of $15 million,** compared to a net deficit of $10 million in 2016.

- **Treasury activities of $113 million**, up slightly from 2016.
  - Growth in trading income.
  - Offset by unfavourable effect of fluctuations in spreads between European and Canadian interest rate curves on the portion of derivative financial instruments used to hedge foreign currency deposits that does not qualify for hedge accounting.

- **Activities related to derivatives associated with hedging activities recorded a deficit of $4 million**, compared to a deficit of $44 million in 2016.
  - Less unfavourable fluctuation in the fair value of swaps in 2017 compared to 2016, because of higher interest rates in 2017.
  - Increased amortization related to the termination of hedges was favourable compared to 2016.

- **Other activities recorded a $124 million deficit**, compared to a $76 million deficit in 2016.
  - Other activities affected, in 2017 and 2016, by expenses related to the continued implementation of Desjardins-wide strategic projects, in particular, to improve systems and processes as well as to create innovative technology platforms, thereby enhancing the member and client experience and improving productivity. In addition, certain technology assets were written off in 2017.
  - Income tax expense in 2016 partially reduced by a tax recovery related to the remuneration of capital stock, which was not the case in 2017. This was offset in the Personal and Business Services segment.
  - Decline in income from asset-backed term notes (ABTN) activities given that substantially all ABTN were settled in January 2017. ABTM activities generated surplus earnings of $10 million in 2016.
  - Offset by severance costs incurred in 2016, following changes in Desjardins Group's senior management.

2.4 Analysis of fourth quarter results and quarterly trends

Table 16 – Results for the previous eight quarters

(unaudited, in millions of dollars and as a percentage)	2017				2016			
	Q4	Q3	Q2	Q1	Q4[1]	Q3[1]	Q2[1]	Q1[1]
Net interest income	**$ 1,125**	$ 1,136	$ 1,087	$ 1,057	$ 1,087	$ 1,071	$ 1,061	$ 1,054
Net premiums	**2,009**	1,982	2,076	1,982	1,834	1,873	1,740	1,721
Other operating income[2]								
Deposit and payment service charges	**107**	109	122	120	123	128	119	118
Lending fees and credit card service revenues	**180**	154	154	172	150	139	136	149
Brokerage and investment fund services	**261**	241	307	278	282	278	286	260
Management and custodial service fees	**117**	104	106	101	102	94	92	88
Foreign exchange income	**22**	16	20	19	12	20	22	16
Other	**(100)**	295	28	26	(42)	(42)	46	65
Operating income[2]	**3,721**	4,037	3,900	3,755	3,548	3,561	3,502	3,471
Investment income (loss)[2]								
Net income (loss) on securities at fair value through profit or loss	**786**	(484)	476	301	(1,242)	385	878	512
Net income on available-for-sale securities	**82**	65	181	80	111	99	99	79
Net other investment income	**36**	57	54	54	49	49	50	50
	904	(362)	711	435	(1,082)	533	1,027	641
Total income	**4,625**	3,675	4,611	4,190	2,466	4,094	4,529	4,112
Provision for credit losses	**89**	92	76	92	55	98	75	91
Claims, benefits, annuities and changes in insurance contract liabilities	**2,042**	1,000	1,922	1,753	(104)	1,727	2,065	1,758
Non-interest expense	**1,938**	1,685	1,878	1,847	1,871	1,706	1,854	1,773
Income taxes on surplus earnings	**127**	140	154	115	135	109	108	108
Surplus earnings before member dividends	**429**	758	581	383	509	454	427	382
Member dividends, net of tax recovery	**49**	44	29	26	42	25	16	22
Net surplus earnings for the period after member dividends	**$ 380**	$ 714	$ 552	$ 357	$ 467	$ 429	$ 411	$ 360
Of which:								
Group's share	**$ 371**	$ 699	$ 538	$ 352	$ 443	$ 419	$ 390	$ 339
Non-controlling interests' share	**9**	15	14	5	24	10	21	21
Contribution to combined surplus earnings by business segment								
Personal and Business Services	**$ 286**	$ 304	$ 272	$ 246	$ 258	$ 284	$ 251	$ 232
Wealth Management and Life and Health Insurance	**159**	121	189	143	114	126	124	97
Property and Casualty Insurance	**48**	318	98	(18)	182	26	49	39
Other	**(64)**	15	22	12	(45)	18	3	14
	$ 429	$ 758	$ 581	$ 383	$ 509	$ 454	$ 427	$ 382
Total assets	**$ 275,095**	$ 276,310	$ 271,983	$ 267,935	$ 258,367	$ 260,157	$ 260,711	$ 255,137
Indicators								
Return on equity[2]	**7.0%**	12.6%	9.9%	6.8%	8.8%	8.3%	7.8%	7.1%
Tier 1A capital ratio	**18.0**	17.8	17.1	17.2	17.3	16.3	15.9	15.8
Total capital ratio	**18.4**	18.2	17.5	17.6	17.9	16.9	16.6	16.9

(1) Prior-period data have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".

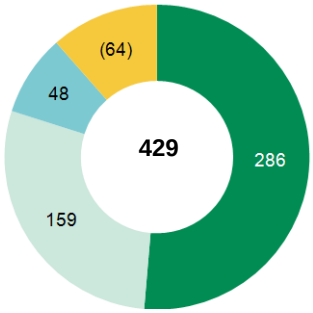
FOURTH QUARTER COMBINED RESULTS

For the fourth quarter ended December 31, 2017, Desjardins Group posted surplus earnings before member dividends of $429 million, down $80 million, or 15.7%, compared to the same period in 2016.

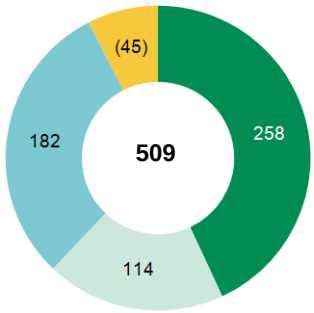
Contribution of segments to surplus earnings

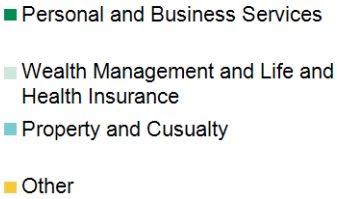
- Personal and Business Services: **Contribution of $286 million**, up $28 million compared to the same period in 2016, mainly as a result of growth in caisse network operations.
- Wealth Management and Life and Health Insurance: **Contribution of $159 million**, up $45 million compared to the same period in 2016, primarily due to favourable adjustments to actuarial assumptions made during the normal course of operations.
- Property and Casualty Insurance: **Contribution of $48 million**, down $134 million compared to the same period in 2016, mainly as a result of the following:
  - Less favourable developments in prior-year claims than in the corresponding quarter of 2016, which had been very favourable.
  - Claims experience for the current year higher than in the corresponding quarter of 2016.
  - Increase in non-interest expense caused largely by the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.

2017 Surplus earnings before member dividends
(in millions of dollars)



2016 Surplus earnings before member dividends
(in millions of dollars)





- **Return on equity of 7.0%, compared to** 8.8% for the fourth quarter of 2016.

- **Operating income of $3,721 million**, up $173 million, or 4.9%.

- **Net interest income of $1,125 million**, up $38 million, or 3.5%, chiefly as a result of the growth of $11.5 billion, or 6.9%, for the year in the entire loans and acceptances portfolio outstanding. However, fiercely competitive market still putting pressure on interest margins.

- **Net premiums of $2,009 million, up $175 million, or 9.5%.**

  - **Wealth Management and Life and Health Insurance:** Net insurance and annuity premium income of $1,088 million, up $10 million, or 0.9%, compared to the same period in 2016.
    - Increase of $51 million in insurance premiums.
      - Growth of $41 million for group insurance and of $10 million for individual insurance.
    - Decrease of $41 million in annuity premiums.

  - **Property and Casualty Insurance:** Net premiums of $983 million, up $167 million, or 20.5%, compared to the same period in 2016.
    - Increase of $168 million as a result of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. The treaty provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
    - Increase due to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.
    - Offset by a decrease in net premiums resulting from the sale of Western Life Assurance Company on July 1, 2017 and of Western Financial Insurance Company on January 1, 2017.

- **Other operating income of $587 million**, down $40 million, or 6.4%, chiefly due to the following:
  - Increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
  - Lower income on account of the subsidiaries sold in 2017, as presented in the "Impact of the sale of subsidiaries" section.
  - Lower income from deposits because of pricing changes.
  - Offset by higher income from assets under management and from growth in credit card and point-of sale financing activities.

- **Investment income of $904 million**, up $1,986 million.
  - Increase mainly due to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
    - Increase offset for the most part by the change in actuarial liabilities that in turn led to an increase in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
    - Differences mostly attributable to changes in the fair value of the portfolio of stocks, bonds and derivatives.
  - Increase in the fair value of bonds in the Property and Casualty Insurance segment as a result of a slight drop in long-term interest rates on markets, while an increase had been recorded in the fourth quarter of 2016.
    - Change in the value of bonds offset by a similar increase in cost of claims because of a matching strategy.
  - Increase in the fair value of derivative financial instruments, including those associated with hedging operations for Desjardins Group as a whole.
  - Offset by lower gains on disposal of investments for the fourth quarter of 2017, than for the corresponding quarter of 2016.

- **Total income of $4,625 million**, up $2,159 million, or 87.6%.

- **Provision for credit losses of $89 million**, up $34 million, or 61.8%.
  - Recovery of the collective allowance in the fourth quarter of 2016 as a result, in particular, of refining the methodology used in the models for calculating the allowance. Desjardins Group's loan portfolio continued to be of high quality.
  - Ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.25% as at December 31, 2017, down from 0.32% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of $2,042 million, up $2,146 million.**

  - **Wealth Management and Life and Health Insurance:** Expenses totalling $1,513 million, up $1,791 million compared to the same period in 2016, mainly as a result of an increase of $1,725 million in actuarial liabilities recognized under "Insurance contract liabilities", which included the effect of an increase in the fair value of matched investments.

  - **Property and Casualty Insurance segment:** Claims expenses totalling $599 million, up $424 million compared to the same period in 2016, mainly due to the following:
    - Less favourable developments in prior-year claims, primarily in auto insurance, than in the corresponding quarter of 2016.
    - Claims experience for the current year higher than in the corresponding quarter of 2016.
    - Effect of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
    - Loss ratio of P&C insurers at 59.9% for the fourth quarter of 2017, compared to 37.8% for the corresponding quarter of 2016.
      - Less favourable developments in prior-year automobile insurance claims than in the corresponding quarter of 2016.
      - Claims experience for the current year unfavourable compared to the fourth quarter of 2016, mainly in automobile and property insurance.

- **Non-interest expense of $1,938 million**, up $67 million, or 3.6%, compared to 2016.
  - Increase caused for the most part by the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations as well as business growth, particularly in credit card and point-of-sale financing activities and assets under management.
  - Increase also due to purchases of computer hardware and the write-off of intangible assets.

  This increase was partly offset by the following:
  - Implementation of productivity initiatives, in particular regarding payroll, which limited the growth in expenses.
  - Decrease in non-interest expense following the sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 as well as of Western Financial Insurance Company on January 1, 2017.

- **Productivity index at 75.0% for the fourth quarter of 2017,** compared to 72.8% for the same period in 2016. Surplus earnings for the fourth quarter of 2017 were based on stable growth in operations combined with a larger increase in non-interest expense, as previously explained. These items caused a drop in the productivity index for the fourth quarter of 2017.

QUARTERLY TRENDS

Quarterly income, expenses and surplus earnings before member dividends are affected by certain trends, including seasonal variations, and by changes in general economic conditions and the capital markets. Desjardins Group's results for the most recent eight quarters were therefore affected by developments in the global, U.S., Canadian and Quebec economies. With expected growth of 2.9% in Canadian real GDP in 2017, compared to 1.4% in 2016, and 2.9% versus 1.4% in Quebec, Desjardins Group's results for the past eight quarters benefited from a growing GDP. Changes in the claims experience and actuarial assumptions may also cause significant variations from quarter to quarter. The past eight quarters were affected as well by the low interest rate environment that continued in 2016 and 2017. However, in the third quarter of 2017, there were two hikes in Canada's key interest rates as a result of monetary tightening.

Combined surplus earnings

- Trend in surplus earnings before member dividends was chiefly affected by the change in claims experience from one quarter to the next and by the contribution of the caisse network, which continues to grow.
- Solid investment performance in the Wealth Management and Life and Health Insurance segment, which contributed to the higher surplus earnings for the second quarter of 2017.
- Fourth quarter of 2017 affected by a higher claims experience for the current year and less favourable developments in prior-year automobile insurance claims.
- 2017 third quarter results affected by a gain of $249 million, net of expenses and after income taxes, on the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.
- Surplus earnings for the fourth quarter of 2016 were affected by very favourable developments in prior-year automobile insurance claims.
- 2016 second and third quarter results affected by the higher claims experience, primarily for automobile insurance, and because of the damage caused by the Fort McMurray wildfire. Claims experience was also higher in property insurance for the third quarter of 2016 because of major events and a catastrophe caused by hail in Alberta.

Combined results

- **Operating income – Upward trend for 2017 quarters, compared to 2016 quarters, except for the fourth quarter of 2017.**
  - Operations growth allowed Desjardins Group to grow operating income, in particular premium income.
  - Increase in net premiums due mainly to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Growth in credit card and point-of-financing activities as well as in income related to assets under management.
  - Increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations in the fourth quarter of 2017, which reduced operating income.
  - Operating income for the third quarter of 2017 affected by the gain on the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.

- **Investment income – Fluctuation mainly as a result of market volatility leading to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.** On account of a matching strategy, these fluctuations were offset by a change in actuarial liabilities, the effect of which was reflected in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.

- **Provision for credit losses – Relatively stable when 2017 and 2016 quarters are compared.**
  - Recovery of the collective allowance in the fourth quarter of 2016, as a result of, among other things, refining the methodology used in the models for calculating the allowance.
  - Ratio for gross impaired loans, as a percentage of the total portfolio of gross loans and acceptances, has been trending slightly down in the past eight quarters. Desjardins Group's loan portfolio has continued to be of high quality.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities – Quarterly fluctuations.**
  - 2017 quarters affected by increased claims resulting from the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Results of the fourth quarter of 2017 affected by the higher claims experience for the current year and the less favourable developments in prior-period automobile insurance claims.
  - Expenses mainly affected by the change in the fair value of investments associated with life and health insurance activities, whose impact was particularly strong in the fourth quarter of 2016 and the third quarter of 2017, and by the change in the loss ratios for property and casualty insurance.
  - Fourth quarter of 2016 affected by favourable developments in prior-year automobile insurance claims and an increase in actuarial liabilities due to changes in assumptions.
  - Results of the second and third quarters of 2016 affected by a higher claims experience, primarily in automobile insurance and because of the damage caused by the Fort McMurray wildfire. The claims experience was also higher in property insurance for the third quarter of 2016 on account of major events and a catastrophe caused by hail in Alberta.

- **Non-interest expense – Upward trend when 2017 and 2016 quarters compared.**
  - Increase primarily attributable to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations with regard to the charges covered by the treaty and to business growth, particularly growth in credit card and point-of-sale financing activities and assets under management.
  - Implementation of productivity initiatives, particularly regarding payroll, which limited the increase in non-interest expense.
  - Sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017, reducing non-interest expense for the third and fourth quarters of 2017.
  - Sale of Western Financial Insurance Company on January 1, 2017, reducing non-interest expense for the 2017 quarters.

Surplus earnings from business segments

- **Surplus earnings before member dividends from the Personal and Business Services segment trending up steadily over the past eight quarters.**
  - Solid performance of caisse network, particularly in the second half of 2017.
  - Net interest income up on account of growth in the entire average portfolio of loans and acceptances outstanding, despite fierce competition in the market, which is still putting pressure on interest margins.
  - Business growth as a result, in particular, of credit card and point-of-sale financing activities.
  - Growth in capital market activities.
  - Fourth quarter 2016 affected by a decline in the provision for losses following recovery of the collective allowance as a result of, among other things, refining the methodology used in the models for calculating the collective allowance.

- **Net surplus earnings of the Wealth Management and Life and Health Insurance segment fluctuating over the past eight quarters.**
  - Income growth related to assets under management during 2017.
  - Higher surplus earnings for fourth quarter 2017, mainly due to favourable adjustments to the actuarial assumptions and partly offset by a deterioration in claims experience.
  - More favourable claims experience for almost all business lines, which affected net surplus earnings positively over the first two quarters of 2017.
  - Solid investment performance, which also contributed to higher surplus earnings in the second quarter of 2017.

- **Net surplus earnings of the Property and Casualty Insurance segment fluctuating over the past eight quarters.**
  - Each of the quarters affected by the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Results for the fourth quarter of 2017 affected by a higher claims experience for the current year and less favourable developments in prior-year automobile insurance claims.
  - Results for the third quarter of 2017 affected by the $241 million gain, net of expenses and after income taxes, related to the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017.
  - Surplus earnings for fourth quarter 2016 affected by very favourable developments in prior-year automobile insurance claims.
  - Results for the second and third quarters of 2016 affected by a higher claims experience, primarily in automobile insurance, and on account of the damage caused by the Fort McMurray wildfire. The claims experience was also higher in property insurance for the third quarter of 2016 due to major events and a catastrophe caused by hail in Alberta.

3.0 Balance sheet review

3.1 Balance sheet management

Table 17 – Combined Balance Sheets
As at December 31

(in millions of dollars and as a percentage)	2017		2016		2015	
Assets						
Cash and deposits with financial institutions	**$ 2,435**	**0.9%**	$ 1,876	0.7%	$ 1,716	0.7%
Securities	**56,588**	**20.6**	53,285	20.6	51,987	21.0
Securities borrowed or purchased under reverse repurchase agreements	**8,674**	**3.2**	7,690	3.0	7,881	3.2
Net loans and acceptances	**177,521**	**64.4**	166,026	64.3	159,881	64.4
Segregated fund net assets	**13,379**	**4.9**	11,965	4.6	9,781	3.9
Derivative financial instruments	**3,206**	**1.2**	3,572	1.4	4,818	1.9
Other assets	**13,292**	**4.8**	13,953	5.4	12,064	4.9
Total assets	**$ 275,095**	**100.0%**	$ 258,367	100.0%	$ 248,128	100.0%
Liabilities and equity						
Deposits	**$ 171,586**	**62.4%**	$ 160,546	62.2%	$ 156,574	63.0%
Commitments related to securities sold short	**9,112**	**3.3**	8,196	3.2	5,464	2.2
Commitments related to securities lent or sold under repurchase agreements	**10,229**	**3.7**	10,323	4.0	10,383	4.2
Derivative financial instruments	**3,094**	**1.1**	2,057	0.8	1,689	0.7
Insurance contract liabilities	**28,272**	**10.3**	27,493	10.6	26,734	10.8
Segregated fund net liabilities	**13,354**	**4.9**	11,957	4.6	9,776	3.9
Other liabilities	**13,287**	**4.8**	13,124	5.1	13,899	5.6
Subordinated notes	**1,388**	**0.5**	1,378	0.5	1,884	0.8
Equity	**24,773**	**9.0**	23,293	9.0	21,725	8.8
Total liabilities and equity	**$ 275,095**	**100.0%**	$ 258,367	100.0%	$ 248,128	100.0%

TOTAL ASSETS

As at December 31, 2017, Desjardins Group's total assets stood at $275.1 billion, up by $16.7 billion, or 6.5%, over the year, compared to growth of $10.2 billion, or 4.1%, for 2016. This growth was largely due to an increase in net loans and acceptances as well as securities, including those borrowed or purchased under reverse repurchase agreements.

CASH AND DEPOSITS WITH FINANCIAL INSTITUTIONS, AND SECURITIES

As at December 31, 2017, Desjardins Group's cash and deposits with financial institutions amounted to $2.4 billion, an increase of $559 million, or 29.8%, over the year, compared to an increase of $160 million, or 9.3%, in 2016. Securities, including those borrowed or purchased under reverse repurchase agreements, totalled $65.3 billion, an increase of $4.3 billion, or 7.0%, over the year, compared to an increase of $1.1 billion, or 1.8%, in 2016. Desjardins Group's market and deposit activities generated the increase.

LOANS AND CLIENTS' LIABILITY UNDER ACCEPTANCES

As at December 31, 2017, Desjardins Group's outstanding loan portfolio, including clients' liability under acceptances, net of the allowance for credit losses, was $177.5 billion, an increase of $11.5 billion, or 6.9%, over the year, compared to growth of $6.1 billion, or 3.8%, during 2016. Among the different credit categories it offers, residential mortgages hold a very important place in its financing activities, accounting for 63.6% of its portfolio at that date and largely responsible for its growth in 2017.

Table 18 – Loans and acceptances
As at December 31

(in millions of dollars and as a percentage)	2017		2016		2015	
Residential mortgages	**$ 113,146**	**63.6%**	$ 106,695	64.1%	$ 102,323	63.8%
Consumer, credit card and other personal loans	**24,044**	**13.5**	22,150	13.3	21,204	13.2
Business and government	**40,769**	**22.9**	37,637	22.6	36,809	23.0
	177,959	**100.0%**	166,482	100.0%	160,336	100.0%
Allowance for credit losses	**(438)**		(456)		(455)	
Total loans and acceptances by borrower category	**$ 177,521**		$ 166,026		$ 159,881	
Loans guaranteed or insured[1]	**$ 46,952**		$ 45,373		$ 44,817	
Loans guaranteed or insured[1] as a percentage of total gross loans and acceptances	**26.4%**		27.3%		28.0%	
Residential mortgages and consumer, credit card and other personal loans as a percentage of total gross loans and acceptances	**77.1**		77.4		77.0	

[1] Loans fully or partially guaranteed or insured by a public or private insurer or a government.

Residential mortgages

Outstanding residential mortgages totalled $113.1 billion, for growth of $6.5 billion, or 6.0%, as at December 31, 2017, compared to an increase of $4.4 billion, or 4.3%, during 2016. Desjardins Group therefore posted sustained growth in this market, mainly because of the strong performance of the housing sector in Quebec and Ontario, in both resales of existing homes and new home construction.

Considering the significant weight of residential mortgages in its total credit portfolio, it is clear that Desjardins Group has always been focused on the needs of its members and clients when they decide to buy a home. It is therefore a very active partner. What is more, its constant drive to innovate over the years has led to the marketing of high quality and very diversified products which, combined with its extensive distribution network, have enabled it to maintain its leadership status in this industry, particularly in Quebec, where its market share was estimated at 36.1% as at December 31, 2017. The reputation it has forged over the years has made it a leading industry player.

Consumer, credit card and other personal loans

As at December 31, 2017, Desjardins Group's outstanding consumer, credit card and other personal loans amounted to $24.0 billion, an increase of $1.9 million, or 8.6%, compared to growth of $946 million, or 4.5%, as at December 31, 2016. Desjardins Group was able to capitalize on stronger credit demand from households as evidenced by an increase in their spending due to a more favourable economic context. The labour market's good performance in Quebec and Ontario, together with a lightening of the tax burden for certain families, gave consumers renewed confidence. This new enthusiasm had a positive effect on their spending, especially for durable goods such as new or used automobiles, furniture, electronic devices and home appliances.

Guaranteed or insured consumer, credit card and other personal loans, including student loans and loans under the Immigrant Investor Program, totalled $3,681 million as at December 31, 2017, compared to $3,726 million a year earlier.

Desjardins Group's market share of consumer, credit card and other personal loans was estimated at 22.4% as at December 31, 2017, stable over the 12-month period.

Business loans

As at December 31, 2017, outstanding business loans totalled $39.0 billion, an increase of $2.9 billion, or 8.1%, compared to growth of $1.4 billion, or 4.0%, as at December 31, 2016. Desjardins Group's business loan portfolio is comprised mainly of commercial and industrial loans, with outstandings of $31.7 billion at year-end 2017, accounting for 81.3% of the portfolio, and with growth of $2.4 billion, or 8.2% over the year. An improved economic climate in Quebec and Ontario encouraged an increase in business spending as well as business credit demand. Over the years, Desjardins has supported many businesses in their investment project by effectively meeting their growing needs. As a result, it has become an invaluable partner for the business community, particularly in Quebec, as can be seen in its market share, estimated at close to 20.0% in commercial and industrial financing in Quebec at the end of 2017.

In the agricultural loan sector, the other component of business loans at Desjardins Group, outstandings totalled $7.3 billion, for an increase of $505 million, or 7.4% as at December 31, 2017, compared to growth of $328 million, or 5.1%, as at December 31, 2016. With an estimated market share of 39.3% as at the same date, Desjardins Group is a leader in this sector across Quebec.

Government loans

Desjardins Group's outstanding government loans, including clients' liability under acceptances, and mainly loans to municipalities, amounted to $1.8 billion as at December 31, 2017, for a year-over-year increase of $215 million, or 13.7%, compared to a decrease of $544 million, or 25.7%, as at December 31, 2016. Given the large volume of these loans in the form of lines of credit, they can vary considerably based on government financing needs.

Credit quality

As at December 31, 2017, Desjardins Group's loan portfolio continued to be of high quality. Outstanding gross impaired loans stood at $442 million, down $90 million, or 16.9%, since the end of 2016, despite a large increase in the portfolio of gross loans and acceptances. In 2016, outstanding gross impaired loans had decreased by $9 million, or 1.7%. The gross impaired loans ratio, as a percentage of the total portfolio of gross loans and acceptances, was 0.25% at the end of 2017, down from 0.32% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans.

Loans guaranteed or insured by governments and other public and parapublic institutions accounted for 26.4% of its total loan portfolio as at December 31, 2017.

Additional information about the quality of Desjardins Group's loan portfolio is presented in section 4.2, "Risk management", on pages 83 to 86 of this MD&A.

DEPOSITS

Table 19 – Deposits

As at December 31

(in millions of dollars and as a percentage)	2017					2016		2015	
	Payable on demand	Payable upon notice	Payable on a fixed date	Total		Total		Total	
Individuals	**$ 46,399**	**$ 3,695**	**$ 50,484**	**$ 100,578**	**58.6%**	$ 96,278	60.0%	$ 91,243	58.2%
Business and government	**24,551**	**452**	**44,099**	**69,102**	**40.3**	62,799	39.1	63,833	40.8
Deposit-taking institutions	**1,407**	**-**	**499**	**1,906**	**1.1**	1,469	0.9	1,498	1.0
Total deposits	**$ 72,357**	**$ 4,147**	**$ 95,082**	**$ 171,586**	**100.0%**	$ 160,546	100.0%	$ 156,574	100.0%

As at December 31, 2017, Desjardins Group's outstanding deposits totalled $171.6 billion, up $11.0 billion, or 6.9%, compared to an increase of $4.0 billion, or 2.5%, as at December 31, 2016. Savings from individuals have always been Desjardins Group's preferred source of financing for its expansion, as can be seen in their weight in its total deposit portfolio, namely 58.6% as at December 31, 2017.

Savings from individuals

As at December 31, 2017, savings from individuals at Desjardins Group totalled $100.6 billion, up $4.3 billion, or 4.5%, since the end of 2016, compared to growth of $5.0 billion, or 5.5%, as at December 31, 2016. These are excellent results that have enabled Desjardins Group to report an estimated market share of 41.6% in Quebec for the year, in a fiercely competitive industry that is highly prized by most financial institutions. Desjardins has therefore maintained its leadership position in this area in Quebec in spite of a historically low interest rate environment. Stock market activity in Canada was less effervescent than in 2016: the S&P/TSX index grew 6.0% in 2017, versus a 17.5% jump the previous year, which reduced investors' appetite for off-balance sheet savings products, such as investment funds and other securities. This climate prompted a good number of investors to shift their savings to safer investment vehicles such as on-balance sheet savings products.

Savings payable on a fixed date amounted to $50.5 billion as at December 31, 2017, for an increase of $491 million, or 1.0%, since the end of 2016, compared to an increase of $569 million, or 1.2%, as at December 31, 2016. This savings category accounted for a large share of Desjardins Group's total portfolio of deposits from individuals as at the end of 2017, namely 50.2%. As evidenced by its relative size, these savings products are very popular with Desjardins Group's members and clients in this market. Savings payable on demand and upon notice, which accounted for 49.8% of deposits made by individuals. They totalled $50.1 billion outstanding as at December 31, 2017, up $3.8 billion, or 8.2%, since December 31, 2016, compared to an increase of $4.5 billion, or 10.7%, as at that date.

Savings from businesses, governments and deposit-taking institutions

As at December 31, 2017, Desjardins Group's outstanding savings from businesses and governments, which represented 40.3% of its deposit liabilities, totalled $69.1 billion, up $6.3 billion, or 10.0%, compared to a decrease of $1.0 billion, or 1.6%, at the end of 2016. This increase was due in particular to the various securities issued on U.S., Canadian and European markets, which supported the growth in Desjardins Group's funding requirements.

Outstanding savings from "Deposit-taking institutions", which accounted for 1.1% of Desjardins Group's deposit liabilities as at December 31, 2017, totalled $1.9 billion at the same date, up $437 million, or 29.7%, compared to a decrease of $29 million, or 1.9%, a year earlier.

Additional information about Desjardins Group's sources of financing can be found on pages 96 to 98, while its liquidity risk management policy is discussed on page 93.

INSURANCE CONTRACT LIABILITIES

As at December 31, 2017, Desjardins Group's insurance contract liabilities were $28.3 billion, up $779 million, or 2.8%, from December 31, 2016, compared to a $759 million, or 2.8%, increase observed a year earlier. This growth is partially due to higher actuarial liabilities as a result of life and health insurance operations, which grew by $854 million.

Note 15, "Insurance contract liabilities", to the Annual Combined Financial Statements provides additional information about these Desjardins Group liabilities.

EQUITY

As at December 31, 2017, equity totalled $24.8 billion, up $1.5 billion, or 6.4%, compared to an increase of $1.6 billion, or 7.2%, a year earlier. Net surplus earnings after member dividends, totalling $2,003 million, were a source of this growth. In addition, the Federation issued F capital shares for proceeds of $244 million, net of certain items, as well as F capital shares having a value of $125 million for the payment of interest when the holder has elected to receive remuneration in F capital shares. The redemption of permanent shares of $275 million and the remuneration on capital stock of $212 million reduced equity.

Note 22, "Capital stock", to the Annual Combined Financial Statements provides additional information about Desjardins Group's capital stock.

3.2 Capital management

Capital management is crucial to the financial management of Desjardins Group. Its goal is to ensure that the capital level and structure of Desjardins Group and its components are consistent with their risk profile, distinctive nature and cooperative objectives. Capital management must also ensure that the capital structure is adequate in terms of protection for members and clients, profitability targets, growth objectives, rating agencies' expectations and regulators' requirements. In addition, it must optimize the allocation of capital and internal capital flow mechanisms, and support growth, development and asset risk management at Desjardins Group.

Desjardins Group advocates prudent management of its capital. Its purpose is to maintain higher regulatory capital ratios than those of the Canadian banking industry and regulatory requirements. Desjardins's prudent capital management is reflected in the quality of the credit ratings assigned by the various rating agencies.

The global financial crisis prompted the industry to place more emphasis on sound capitalization of its operations. Now more than ever, rating agencies and the market favour the best-capitalized institutions. These factors argue in favour of a general increase in the level and quality of capital issued by financial institutions. This is also reflected in the enhanced requirements under Basel III implemented on January 1, 2013. It was against this backdrop that Desjardins Group set its target for Tier 1A and Tier 1 capital at 15%.

Desjardins Group's Integrated Capital Management Framework

Broadly speaking, Desjardins Group's Integrated Capital Management Framework includes the policies and processes required to set targets for its capitalization, to establish strategies to ensure that targets are met, to quickly raise capital, to ensure that the components' performance is appropriately measured, and to optimize internal capital flow and use procedures.

In addition, the Internal Capital Adequacy Assessment Program (ICAAP) enables Desjardins Group to ensure it has an appropriate level of capital to cover all the significant risks to which it is exposed and to implement capital management strategies that take into account changes in its risk profile.

Desjardins Group has developed a stress-testing program aimed at establishing and measuring the effect of various integrated scenarios, i.e. to simulate various economic scenarios and to assess their financial and regulatory repercussions. This process makes it possible to determine if the minimum capital target, as established in the capitalization plan, is adequate in view of the risks to which Desjardins Group is exposed. Additional information on the ICAAP and the stress-testing program is presented in Section 4.2 "Risk management".

Regulatory framework and internal policies

Desjardins Group's capital management is the responsibility of the Federation's Board of Directors. To support it with this task, it has mandated the Management Committee, through the Finance and Risk Management Committee, to ensure that Desjardins Group has a sufficient capital base in light of the organization's strategic objectives and regulatory obligations. The Finance, Treasury and Administration Executive Division is responsible for preparing, on an annual basis, a capitalization plan to forecast capital trends, devise strategies and recommend action plans for achieving capital objectives and targets.

The current situation and the forecasts show that overall, Desjardins Group has a solid capital base that maintains it among the best-capitalized financial institutions.

Desjardins Group's regulatory capital ratios are calculated according to the AMF's guideline on adequacy of capital base standards applicable to financial services cooperatives (the guideline). This guideline takes into account the global regulatory framework for more resilient banks and banking systems (Basel III) issued by the Bank for International Settlements.

The Basel III regulatory framework increases capital requirements. Even though the Basel III regulatory framework provides for a transitional period from 2013 to 2019 to mitigate the impact of the new capitalization rules, the AMF required Desjardins Group to meet the Tier 1A Tier 1 and total capital ratio requirements for 2019 in the first quarter of 2013. The AMF may also set higher target ratios at its discretion when circumstances warrant.

Under this framework, a minimum amount of capital must be maintained on a combined basis by all the Desjardins Group components. Some of these components are subject to separate requirements regarding regulatory capital, liquidity and financing, which are set by regulatory authorities governing banks, insurers and securities, in particular. Desjardins Group oversees and manages the capital requirements of these entities to ensure efficient use of capital and continuous compliance with the applicable regulation.

In this regard, it should be mentioned that the life and health insurance subsidiaries under provincial jurisdiction are subject to the Capital Adequacy Requirements Guideline (CARLI) issued by the AMF. The property and casualty insurance subsidiaries under provincial jurisdiction must comply with the Guideline on Capital Adequacy Requirements issued by the AMF. The property and casualty insurance subsidiaries under federal jurisdiction must comply with the OSFI's Minimum Capital Test (MCT) Guideline for federally regulated property and casualty insurance companies. Developments in these guidelines are presented in the "Changes in the regulatory environment" section on pages 18 to 20 of this MD&A.

For the purpose of calculating capital, Desjardins Financial Corporation Inc., the holding corporation that mainly includes the insurance companies, has been deconsolidated and presented as a partial capital deduction under the rules for significant investments stated in the guideline. Furthermore, Desjardins Financial Corporation Inc. is subject to the AMF's Capital Adequacy Requirements Guideline — Life and Health Insurance.

The table below presents a summary of the target regulatory ratios set by the AMF under Basel III.

Table 20 – Summary of ratios regulated by the AMF under Basel III[(1)(2)]

	Minimum ratio	Capital conservation buffer	Minimum ratio including capital conservation buffer	Supplement applying to D-SIFIs[(3)]	Minimum ratio including capital conservation buffer and supplement applying to D-SIFIs	Capital and leverage ratio as at December 31, 2017
Tier 1A capital ratio	> 4.5%	2.5%	> 7.0%	1.0%	> 8.0%	**18.0%**
Tier 1 capital ratio	> 6.0	2.5	> 8.5	1.0	> 9.5	**18.0**
Total capital ratio	> 8.0	2.5	> 10.5	1.0	> 11.5	**18.4**
Leverage ratio	> 3.0	N/A	> 3.0	N/A	> 3.0	**8.5**

(1) The capital ratios are expressed as a percentage of regulatory capital to risk-weighted assets in accordance with the guideline.
(2) The leverage ratio is calculated according to the guideline and is defined as an independent measure of risk based on the capital measure (namely Tier 1 capital) divided by the exposure measure. The exposure measure includes: 1) on-balance sheet exposures, 2) securities financing transaction exposures, 3) derivative exposures, and 4) other off-balance sheet items.
(3) In June 2013, the AMF determined that Desjardins Group met the criteria for designation as a domestic systemically important financial institution (D-SIFI). Since January 1, 2016, Desjardins Group has therefore been subject, as a D-SIFI, to an additional capital requirement of 1% on its minimum capital ratios.

Regulatory developments

Desjardins Group continues to monitor changes in capital requirements under the global standards developed by the Basel Committee on Banking Supervision (BCBS) and to assess their impact on the capital ratios and the leverage ratio.

On January 14, 2016, the BCBS issued a revised version of the minimum capital requirements for market risk. The objective of the revised framework is to arrange that, for the treatment of market risk, the Standardized Approach and the internal models approach produce credible results regarding the capital base and promote the harmonious implementation of standards in all jurisdictions. On June 29, 2017, the BCBS issued a consultative document entitled "Simplified alternative to the standardised approach to market risk capital requirements" which offers a simplified version of the rules defined in the document issued in January 2016 concerning the Standardized Approach. On December 7, 2017, the BCBS announced that financial institutions would have to start presenting information under the Standardized Approach as of January 1, 2022.

On April 21, 2016, the BCBS issued a document entitled "Interest rate risk in the banking book", intended as an update of the document issued in 2004, "Principles for the management and supervision of interest rate risk", dealing with risk management, the treatment of capital and supervision of interest rate risk in the banking book. Its aim is to ensure that financial institutions have appropriate capital to cover potential losses in the banking book stemming from interest rate fluctuations and thereby limit capital arbitrage between the trading book and the banking book. Application is scheduled as of 2018.

In addition, an update to the AMF's guideline on adequacy of capital base standards for financial services cooperatives took effect on January 1, 2017. It features a change in the treatment of equity investments in investment funds as well as the implementation of a downturn loss given default on residential mortgages, for financial institutions applying the Internal Ratings-Based Approach on loans secured by residential real estate.

On March 29, 2017, the BCBS issued a final document entitled "Regulatory treatment of accounting provisions – interim and transitional arrangements". This document is the result of the application of IFRS 9 effective January 1, 2018, which requires provisioning for expected credit losses rather than incurred losses, as required under the present standard. The BCBS is maintaining the present regulatory treatment of provisions under the Basel Accord framework for a transitional period. Furthermore, on August 21, the OSFI issued a draft for public consultation on the revision of the Capital Adequacy Requirements Guideline to be implemented in the first quarter of 2018. The proposed changes take up the same principles as the BCBS. Authorities may adopt transitional measures in order to gradually take into account any significant future negative effect on regulatory capital as a result of the introduction of the new impairment model based on expected credit losses under IFRS 9. However, on November 29, 2017, the OSFI announced that no transitional measure would be allowed following the adoption of IFRS 9.

On July 6, 2017, the BCBS issued a consultative document entitled "Capital treatment for simple, transparent and comparable short-term securitisations," which sets out additional guidance and requirements allowing financial institutions acting as investors in or as sponsors of simple, transparent and comparable short-term securitizations to determine whether they can benefit from preferential regulatory capital treatment. The AMF has not expressed its intentions with respect to the consultative document.

On October 25, 2017, the BCBS issued a guideline on identification and management of step-in risk, aimed at measuring the risk related to the support that a financial institution could give an unconsolidated entity, should such entity find itself in financial distress, even beyond or in the absence of contractual obligations. The proposed framework does not call for capital requirements to be automatically added to those required under present Basel standards. It is scheduled to come into force in 2020.

On December 7, 2017, the Group of Central Bank Governors and Heads of Supervision, the BCBS's oversight body, endorsed the outstanding Basel III post-crisis regulatory reforms. The reforms are intended to help reduce excessive variability in risk-weighted assets (RWA) and improve the comparability and transparency of financial institutions' capital ratios by:

- enhancing the robustness and risk sensitivity of the standardized approaches for credit risk, credit valuation adjustment (CVA) risk and operational risk;
- constraining the use of the internal model approaches, by placing limits on certain inputs used to calculate capital requirements under the Internal Ratings-Based (IRB) approach for credit risk and by removing the use of the internal model approaches for the CVA risk and for operational risk;
- adjusting the leverage ratio exposure measurement; and
- replacing the existing Basel I output floor with a more robust risk-sensitive floor based on the revised Basel III standardized approaches.

The BCBS has scheduled the implementation of these reforms for January 1, 2022 and the transitional provisions for applying the output floor based on the revised Basel III standardized approach. The AMF may choose to implement more prudent measures and accelerated transitional provisions. In this regard, the OSFI issued a transitional measure on January 12, 2018 allowing the Basel I output floor to be replaced by a revised capital output floor as of the second quarter of 2018.

On December 7, 2017, the BCBS also issued a discussion paper on the regulatory treatment of sovereign exposures. The BCBS is receiving comments on the topic until March 9, 2018.

On November 23, 2017, the AMF issued a notice concerning the deferred implementation, until the first quarter of 2019, of the BCBS's rules related to the standardized approach for counterparty credit risk (SA-CCR) and the revised capital requirements for bank exposure to central counterparties.

The "Changes in the regulatory environment" section presents additional details on regulation as it affects all Desjardins Group operations. In addition, this section contains information on the internal recapitalization (bail-in) file, or the TLAC guideline project.

Compliance with requirements

As at December 31, 2017, the Tier 1A, Tier 1 and total capital ratios of Desjardins Group, calculated in accordance with Basel III requirements, were 18.0%, 18.0% and 18.4%, respectively. The leverage ratio was 8.5%. Desjardins Group therefore has very good capitalization, with a Tier 1A capital ratio above the 15% target.

Desjardins Group and all its components that are subject to minimum regulatory requirements with respect to capitalization were in compliance with said requirements as at December 31, 2017.

Regulatory capital

The following tables present Desjardins Group's main capital components, regulatory capital, capital ratios, and movements in capital over the year.

Table 21 – Main capital components

	Total capital		
	Tier 1 capital		Tier 2 capital
	Tier 1A[1]	Tier 1B[1]	
Eligible items	• Reserves and undistributed surplus earnings • Eligible accumulated other comprehensive income • Federation capital shares • Permanent shares and surplus shares subject to phase-out	• Non-controlling interests[2]	• Eligible collective allowance • Subordinated notes subject to phase-out • Eligible qualifying shares
Regulatory adjustments	• Goodwill • Software • Other intangible assets • Deferred tax assets essentially resulting from loss carryforwards • Shortfall in allowance		
Deductions	• Mainly significant investments in financial institutions[3]		• Investment in preferred shares of a component deconsolidated for regulatory capital purposes • Subordinated financial instrument

[1] The Tier 1A and Tier 1B ratios are the equivalent of the financial institutions' CET1 and AT1 ratios, for financial services cooperatives regulated by the AMF.
[2] The amount of non-controlling interests is determined, in particular, based on the nature of the operations and the capitalization level of the investee.
[3] Represent the portion of investments in the components deconsolidated for regulatory capital purposes (mainly Desjardins Financial Corporation Inc.) that exceeds 10% of capital net of regulatory adjustments. In addition, when the non-deducted balance, plus deferred tax assets net of corresponding deferred tax liabilities, exceeds 15% of the adjusted capital, the surplus is also deducted from this capital. The net non-deducted balance will be subject to risk-weighting at a rate of 250%.

Table 22 – Regulatory capital
As at December 31

(in millions of dollars and as a percentage)	2017	2016
Tier 1A capital		
Federation capital shares[1]	**$ 4,518**	$ 4,142
Permanent shares and surplus shares subject to phase-out	**794**	1,078
Reserves	**16,707**	15,052
Undistributed surplus earnings	**1,336**	1,502
Eligible accumulated other comprehensive income	**410**	392
Non-controlling interests	**-**	-
Deductions[2]	**(2,780)**	(3,446)
Total Tier 1A capital	**20,985**	18,720
Non-controlling interests	**13**	12
Total Tier 1B capital	**13**	12
Total Tier 1 capital	**20,998**	18,732
Tier 2 capital		
Subordinated notes subject to phase-out	**1,032**	1,206
Eligible collective allowance	**257**	252
Other eligible instruments	**25**	25
Non-controlling interests	**-**	-
Deductions	**(876)**	(872)
Total Tier 2 capital	**438**	611
Total regulatory capital (Tiers 1 and 2)	**$ 21,436**	$ 19,343
Ratios and leverage ratio exposure		
Tier 1A capital ratio	**18.0%**	17.3%
Tier 1 capital ratio	**18.0**	17.3
Total capital ratio	**18.4**	17.9
Leverage ratio	**8.5**	8.1
Leverage ratio exposure	**$ 246,832**	$ 230,472

[1] Including capital shares held in a segregated fund.
[2] Deductions from Tier 1A are comprised of regulatory adjustments and significant investments of $651 million and $2,129 million, respectively as at December 31, 2017, and of $687 million and $2,759 million as at December 31, 2016.

In compliance with Basel III requirements, capital instruments that no longer meet the eligibility criteria for capital tiers have been excluded from them effective January 1, 2013, as prescribed. In accordance with the transitional provisions set out in the guideline, instruments that meet certain conditions are being phased out from capital at an annual rate of 10% over a nine-year period that began on January 1, 2013. These instruments include permanent shares and surplus shares issued before September 12, 2010, which total $2.1 billion.

In addition, the subordinated notes issued by Desjardins Capital Inc. are also subject to the 10% amortization. In order to be fully eligible for Tier 2 capital, such notes must meet Non-Viability Contingent Capital (NVCC) requirements. Desjardins Group has not issued any instruments of this type as discussions concerning the application of these regulations by Desjardins Group are still in progress with the AMF.

On December 21, 2017, the Federation filed a new short-form prospectus and obtained a receipt allowing it to issue, in the 12 months following the date of the receipt, F capital shares for a maximum amount of $125 million. This new issue started on January 23, 2018. During 2017, the Federation issued F capital shares for proceeds of $244 million, net of certain items. It also issued F capital shares for an amount of $125 million in order to pay interest where a holder elected to receive remuneration in capital shares.

As at December 31, 2017, the Tier 1A capital ratio was up 71 basis points compared to December 31, 2016. Growth in surplus earnings and reserves was partly offset by an increase in risk-weighted assets. On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, Western Financial Group Inc. and Western Life Assurance Company, which contributed to the increase in the Tier 1A capital ratio.

Table 23 – Change in regulatory capital
As at December 31

(in millions of dollars)	2017	2016
Tier 1A capital		
Balance at beginning of year	**$ 18,720**	$ 17,354
Increase in reserves and undistributed surplus earnings[1]	**1,489**	1,924
Eligible accumulated other comprehensive income	**18**	45
Federation capital shares[2]	**376**	598
Permanent shares and surplus shares subject to phase-out	**(284)**	(393)
Non-controlling interests	**-**	(15)
Deductions	**666**	(793)
Balance at end of year	**20,985**	18,720
Tier 1B capital		
Balance at beginning of year	**12**	17
Non-controlling interests	**1**	(5)
Balance at end of year	**13**	12
Total Tier 1 capital	**20,998**	18,732
Tier 2 capital		
Balance at beginning of year	**611**	1,329
Non-controlling interests	**-**	(2)
Senior notes subject to phase-out	**(174)**	(686)
Eligible collective allowance	**5**	(30)
Deductions	**(4)**	-
Balance at end of year	**438**	611
Total capital	**$ 21,436**	$ 19,343

(1) Amount including the change in defined benefit pension plan liabilities.
(2) Amount net of issuance expenses.

Risk-weighted assets (RWA)

Desjardins Group calculates the risk-weighted assets for credit risk, market risk and operational risk. Since March 2009, Desjardins has been using the Internal Ratings-Based Approach for credit risk related to retail loan portfolios − Personal. Other exposures to credit and market risk are measured according to the Standardized Approach. On June 19, 2017, Desjardins Group received the AMF's authorization to use the Standardized Approach for calculating operational risk as of the second quarter of 2017. In addition, Desjardins Group is subject to a threshold defined under Basel I, where the threshold is determined by the difference between the minimum regulatory capital requirement in accordance with the rules of the last version of the AMF guideline based on Basel I, multiplied by an adjustment factor set by the AMF, and the minimum regulatory capital requirement calculated under Basel III.

As indicated in the table below, risk-weighted assets totalled $116.5 billion as at December 31, 2017. Of this amount, $88.1billion was for credit risk, $2.0 billion for market risk, $11.9 billion for operational risk, and $14.9 billion was for the threshold adjustment. As at December 31, 2016, risk-weighted assets stood at $108.1 billion.

Table 24 – Risk-weighted assets

(in millions of dollars and as a percentage)	Internal Ratings-Based Approach		Standardized Approach		Total as at December 31, 2017				Total as at December 31, 2016
	Exposure [1]	Risk-weighted assets	Exposure [1]	Risk-weighted assets	Exposure [1]	Risk-weighted assets	Capital requirement [2]	Average risk weighting rate	Risk-weighted assets
Credit risk other than counterparty risk									
Sovereign borrowers	$ -	$ -	$ 14,564	$ 28	$ 14,564	$ 28	$ 2	- %	$ 2
Financial institutions	-	-	10,065	2,094	10,065	2,094	168	21	1,668
Businesses	-	-	54,116	43,738	54,116	43,738	3,499	81	40,355
Securitizations	-	-	6	75	6	75	6	1,250	1,138
Equities	-	-	152	241	152	241	19	159	98
SMEs similar to other retail client exposures	-	-	6,981	4,687	6,981	4,687	375	67	4,399
Mortgages	105,681	9,623	411	146	106,092	9,769	782	9	8,271
Other retail client exposures (excluding SMEs)	9,993	3,753	279	222	10,272	3,975	318	39	3,133
Qualifying revolving retail client exposures	37,349	8,833	-	-	37,349	8,833	707	24	7,590
Subtotal - Credit risk other than counterparty risk	153,023	22,209	86,574	51,231	239,597	73,440	5,876	31	66,654
Counterparty risk									
Sovereign borrowers	-	-	8	-	8	-	-	-	-
Financial institutions	-	-	1,713	343	1,713	343	27	20	317
Businesses	-	-	6	5	6	5	-	83	13
Trading portfolio	-	-	1,268	365	1,268	365	29	29	191
Credit valuation adjustment charge	-	-	-	-	-	903	72	-	807
Additional requirements for banking and trading portfolio	-	-	-	-	68	1	-	-	1
Subtotal - Counterparty risk	-	-	2,995	713	3,063	1,617	128	53	1,329
Other assets [3]	-	-	-	-	16,705	11,677	934	70	9,674
Scaling factor [4]	-	1,333	-	-	-	1,333	107	-	1,121
Total credit risk	153,023	23,542	89,569	51,944	259,365	88,067	7,045	34	78,778
Market risk									
Interest rate position risk	-	-	-	1,692	-	1,692	135	-	1,428
Currency risk	-	-	-	151	-	151	12	-	262
Additional requirements for other risks [5]	-	-	-	122	-	122	10	-	120
Total market risk	-	-	-	1,965	-	1,965	157	-	1,810
Operational risk [6]	-	-	-	11,850	-	11,850	948	-	13,315
Total risk-weighted assets before threshold	153,023	23,542	89,569	65,759	259,365	101,882	8,150	-	93,903
Risk-weighted assets (RWA) after the transitional provisions for the credit valuation adjustment charge [7]									
RWA for Tier 1A capital	-	-	-	-	-	101,629	8,129	-	93,612
RWA for Tier 1 capital	-	-	-	-	-	101,674	8,134	-	93,668
RWA for total capital	-	-	-	-	-	101,710	8,137	-	93,716
Transitional threshold adjustment [8]	-	-	-	-	-	14,858	1,189	-	14,532
Total risk-weighted assets	$ 153,023	$ 23,542	$ 89,569	$ 65,759	$ 259,365	$ 116,487	$ 9,318	- %	$ 108,144

(1) Net exposure, after credit risk mitigation (net of specific allowances under the Standardized Approach but not under the Internal Ratings-Based Approach in accordance with the AMF guideline).
(2) The capital requirement represents 8% of risk-weighted assets.
(3) Other assets are measured using a method other than the Standardized Approach or the Internal Ratings-Based Approach. Other assets include the investments portion below a certain threshold in components that are deconsolidated for regulatory capital purposes (mainly Desjardins Financial Corporation Inc.), the investments portion below a certain threshold in associates as well as the portion of other deferred tax assets below a certain threshold. These three items are weighted at 250% and the deducted portion (namely above a certain threshold) is weighted at 0%. This class does not include the credit valuation adjustment (CVA) charge and additional requirements for the banking and trading portfolio, which are disclosed in the counterparty credit risk section.
(4) The scaling factor is a 6.0% calibration of risk-weighted assets measured using the Internal Ratings-Based Approach for credit exposures in accordance with Section 1.3 of the AMF guideline.
(5) Other risks include equities risk, commodities risk and options risk.
(6) Since second quarter 2017, the Standardized Approach has been used to assess operational risk. The Basic Indicator Approach was used in prior periods.
(7) The scaling factors used since January 1, 2014 to account for CVA charge requirements are being phased in to calculate the Tier 1A, Tier 1 and total capital ratios. They were 72%, 77% and 81%, respectively, in 2017 (64%, 71% and 77% in 2016) and will reach 100% for each class of capital by 2019.
(8) As prescribed in Section 1.6 of the AMF guideline. The threshold is presented to take into account risk-weighted assets after the transitional provisions for the CVA charge for Tier 1A capital.

Movements in risk-weighted assets

For credit risk, fluctuations in RWA during 2017 are segmented into two items, namely credit risk other than counterparty risk, and counterparty risk. In credit risk other than counterparty risk, the principal fluctuations were caused by changes in the portfolio's size, which resulted in a $7.4 billion increase in RWA, whereas the improvement in portfolio quality caused a decrease of $408 million. In addition, the updating of models generated a $2.1 billion increase. The change in procedures and policies caused a slight increase of $8 million in RWA, chiefly due to the integration of the downturn loss given default. The sale of two subsidiaries, Western Financial Group Inc. and Western Life Assurance Company, led to a $65 million increase due to the 10% capital threshold procedure applied in calculating RWA, and finally the change in exchange rates accounted for a $217 million decrease. In counterparty risk, the larger size of the portfolio mainly accounted for an increase of $328 million in 2017.

In market risk, a $155 million increase in RWA was observed due to a change in risk levels. A $1.5 billion decrease was also noted in operational risk as a result of fluctuations in the income generated and changes in the calculation methods for regulatory capital.

The threshold adjustment as previously defined increased by $326 million of RWA in 2017, basically as a result of the updating of models and the change in procedures and policies.

Table 25 – Change in risk-weighted assets

As at December 31

(in millions of dollars)	2017			2016		
	Credit risk other than counterparty risk	**Counterparty and issuer risk**	**Total**	Credit risk other than counterparty risk	Counterparty and issuer risk	Total
Credit risk						
Risk-weighted assets at beginning of year	**$ 77,449**	**$ 1,038**	**$ 78,487**	$ 73,303	$ 1,214	$ 74,517
Size of portfolio[1]	**7,431**	**282**	**7,713**	4,255	39	4,294
Quality of portfolio[2]	**(408)**	**(13)**	**(421)**	666	(215)	451
Updating of models[3]	**2,120**	**-**	**2,120**	(577)	-	(577)
Procedures and policies[4]	**8**	**59**	**67**	(123)	-	(123)
Acquisitions and transfers	**65**	**-**	**65**	-	-	-
Change in exchange rates	**(217)**	**-**	**(217)**	(71)	-	(71)
Other	**-**	**-**	**-**	(4)	-	(4)
Total changes in risk-weighted assets	**8,999**	**328**	**9,327**	4,146	(176)	3,970
Risk-weighted assets at end of year	**$ 86,448**	**$ 1,366**	**$ 87,814**	$ 77,449	$ 1,038	$ 78,487

(in millions of dollars)	2017	2016
Market risk		
Risk-weighted assets at beginning of year	**$ 1,810**	$ 2,157
Change in risk levels[5]	**155**	(347)
Updating of models[3]	**-**	-
Procedures and policies[4]	**-**	-
Acquisitions and transfers	**-**	-
Change in exchange rates	**-**	-
Other	**-**	-
Total changes in risk-weighted assets	**155**	(347)
Risk-weighted assets at end of year	**$ 1,965**	$ 1,810
Operational risk		
Risk-weighted assets at beginning of year	**$ 13,315**	$ 13,032
Revenue generated	**126**	283
Procedures and policies[4]	**(1,591)**	-
Acquisitions and transfers	**-**	-
Total changes in risk-weighted assets	**(1,465)**	283
Risk-weighted assets at end of year	**$ 11,850**	$ 13,315
Transitional threshold adjustment		
Risk-weighted assets at beginning of year	**$ 14,532**	$ 18,778
Size of portfolio[1]	**83**	(177)
Quality of portfolio[2]	**456**	(317)
Updating of models[3]	**(2,076)**	519
Procedures and policies[4]	**1,864**	(4,271)
Acquisitions and transfers	**(1)**	-
Change in exchange rates	**-**	-
Other	**-**	-
Total changes in risk-weighted assets	**326**	(4,246)
Risk-weighted assets at end of year	**$ 14,858**	$ 14,532

(1) Increase or decrease in underlying risk exposure.
(2) Change in risk mitigation factors and portfolio quality.
(3) Changes in risk parameters and models.
(4) Regulatory changes and developments in the regulatory capital calculation method.
(5) Change in risk levels and fluctuation in exchange rates, which are not considered to be material.

3.3 Off-balance sheet arrangements

In the normal course of operations, Desjardins Group enters into various off-balance sheet arrangements, including assets under management and under administration on behalf of its members and clients, credit instruments, contractual commitments, financial assets held as collateral and other, as well as structured entities, including securitization.

ASSETS UNDER MANAGEMENT AND UNDER ADMINISTRATION

As at December 31, 2017, Desjardins Group administered, for the account of its members and clients, assets totalling $411.5 billion. This represented an annual decrease of $8.6 billion, or 2.1%, compared to an increase of $16.8 billion, or 4.2%, recorded as at December 31, 2016. The decrease was mainly due to custodial services for institutional securities. Financial assets placed with Desjardins Group as wealth manager amounted to $58.2 billion at the close of 2017, for an increase of $6.7 billion, or 12.9% on an annual basis, compared to an increase of $5.5 billion, or 11.9%, a year earlier. The increase was chiefly due to growth in Desjardins Funds.

Assets under management and under administration by Desjardins Group are comprised essentially of financial assets in the form of investment funds, securities held in custody and assets accumulated by pension funds. They do not belong to Desjardins Group, but to its members and clients and, as a result, they are not recognized on the Combined Balance Sheets. The Wealth Management segment is primarily responsible for the activities related to assets under management and under administration.

Table 26 – Assets under management and under administration

As at December 31

(in millions of dollars)	2017	2016	2015
Assets under management			
Institutions and individuals	**$ 15,263**	$ 12,205	$ 11,595
Investment funds[1]	**42,957**	39,345	34,458
Total assets under management	**$ 58,220**	$ 51,550	$ 46,053
Assets under administration			
Individual and institutional trust and custodial services	**$ 313,517**	$ 326,798	$ 321,401
Investment funds[1]	**98,031**	93,368	81,949
Total assets under administration	**$ 411,548**	$ 420,166	$ 403,350

(1) Including Desjardins Funds and Northwest and Ethical Funds.

CREDIT INSTRUMENTS

In order to meet its members' and clients' financing needs, Desjardins Group enters into various agreements with them for such instruments as credit commitments, indemnification commitments related to securities lending and documentary letters of credit. These products are generally off-balance sheet instruments and may expose Desjardins Group to credit and liquidity risks. These instruments are subject to Desjardins Group's usual risk management rules.

Note 29, "Commitments, guarantees and contingent liabilities", to Desjardins Group's Combined Financial Statements provides more detailed information about these credit instruments.

GUARANTEES

Desjardins Group also enters into various guarantee and indemnification agreements with its members and clients in the normal course of operations. These agreements remain off-balance sheet arrangements and include guarantees, standby letters of credit and credit default swaps. Note 29, "Commitments, guarantees and contingent liabilities", to Desjardins Group's Combined Financial Statements provides information about these off-balance sheet arrangements.

ASSETS PLEDGED AND HELD AS COLLATERAL

In the normal course of business, Desjardins Group holds financial assets as collateral as a result of transactions involving securities borrowed or those purchased under reverse repurchase agreements. Note 29, "Commitments, guarantees and contingent liabilities", to Desjardins Group's Combined Financial Statements provides additional information about assets held as collateral.

STRUCTURED ENTITIES

Desjardins Group enters into various financial transactions with structured entities in the normal course of operations to diversify its sources of financing and manage its capital. Structured entities are usually created for a unique and distinct purpose, and they frequently have limited activities. These entities may be included in Desjardins Group's Combined Balance Sheets if it has control over them. Detailed information concerning significant exposure to structured entities not included in Desjardins Group's Combined Balance Sheets is provided below. Note 13, "Interests in other entities", to the Combined Financial Statements provides more information about structured entities.

Master Asset Vehicle (MAV) trusts

Desjardins Group holds financial interests in MAV trusts, which are structured entities not included in its Combined Balance Sheets. These trusts were created for the specific purpose of aggregating the restructured notes arising from asset-backed commercial paper held by Canadian institutional investors. Substantially all of the asset-backed term notes were settled during the first quarter of 2017.

Securitization of Desjardins Group's financial assets

Desjardins Group participates in the *National Housing Act* (NHA) Mortgage-Backed Securities Program to manage its liquidities and capital. Transactions carried out under this program sometimes require the use of a structured entity, the Canada Housing Trust (CHT), set up by Canada Mortgage and Housing Corporation (CMHC) under the Canada Mortgage Bonds (CMB) Program. Note 8, "Derecognition of financial assets", to the Combined Financial Statements provides more information about the securitization of Desjardins Group's loans.

4.0 Risk management

The shaded areas and tables marked with an asterisk (*) in this section contain information about credit, market and liquidity risks in accordance with IFRS 7, "Financial Instruments: Disclosures". They also contain an analysis of how Desjardins Group assesses its risks as well as a description of its risk management objectives, policies and methods. IFRS 7 provides that risk disclosures may be included in the MD&A. Consequently, the shaded areas and tables marked with an asterisk (*) are an integral part of the Combined Financial Statements, as explained in Note 31, "Financial instrument risk management", to the Combined Financial Statements.

4.1 Risk factors that could impact future results

In addition to the risks presented in Section 4.2 of this MD&A, other risk factors, which are outside of Desjardins Group's control, may impact its future results. Furthermore, as indicated in the caution concerning forward-looking statements, general or specific risks and uncertainties may cause the actual results of Desjardins Group to differ from those in the forward-looking statements. Some of these risk factors are presented below.

Principal risks and emerging risks

Principal risks and emerging risks are risks or risk factors that could have a significant impact on Desjardins Group's financial health and would likely affect its reputation, the volatility of its results, the adequacy of its capitalization or liquidities, in the event they fully materialize. Among these risks, certain so-called emerging risks are sharply growing or developing risk factors. Desjardins Group continues to be proactive in identifying and tracking these risks so that it can take the appropriate management measures when required. For example, the external environment is continuously monitored to identify the risk factors and economic and regulatory events that could impact its operations. In addition, regular exchanges between the Risk Management Executive Division, risk officers and the business segments further define the risk factors of greatest concern.

Principal risks and emerging risks	Description
Cyber threats	The faster pace of virtual business environments and their complexity, whether in banking, insurance or wealth management operations, are increasing the organization's exposure to the risk of cyber threats. For instance, the trend toward interactive and virtual payment methods increases the risk of external fraud involving data integrity, while the instability of transactional platforms for members and clients could lead to a breach of trust, with negative repercussions on business operations. These factors could result in litigation and adversely affect financial results as well as Desjardins Group's reputation. Desjardins remains vigilant and proactive in identifying and managing such risks by adopting cyber defence techniques to safeguard its systems and data in order to protect its members and clients.
Technological developments	Technological development risks are growing because of the increased use of technology by the financial services sector, as well as by other sectors of the economy. The financial services industry is in a state of flux. The business environment has changed very quickly in recent years with the advent of unconventional rivals from the world of technology offering efficient, alternative payment and financing services. These competitors have flexible technology tools and a less restrictive regulatory framework. With the advent of fintech, traditional players from the financial sector have had to position themselves in these new markets and overhaul their operating methods to promote innovation and deploy new solutions. Desjardins Group has been no exception and remains active in managing this strategic risk, among others, by investing in financial technology and by reviewing and diversifying its products, services and distribution channels to meet the needs of its members and clients.

Principal risks and emerging risks	Description
Regulatory developments	Desjardins Group is subject to a complex, varied and changing regulatory environment as well as to increased supervision from regulatory authorities, particularly because of its status as a domestic systemically important financial institution and its operations across Canada and the United States. Regulatory changes and their complexity expose Desjardins to a higher risk of non-compliance and uncertainty regarding the impact of such changes on business practices and financial results. Note in particular the work to update the Quebec *Act respecting financial services cooperatives* and the Quebec *Deposit Insurance Act*, the publication of the OSFI's final version of Guideline B-20, *Residential Mortgage Underwriting Practices and Procedures* (effective January 1, 2018), and the AMF's draft guideline on granting residential mortgages. Also of note is the upcoming compliance with IFRS 17, which has just amended the measurement rules for actuarial liabilities in insurance (scheduled implementation in 2021). The organization has significant resources allocated to monitoring, analyzing and applying the different legal and regulatory requirements related to its operations and cooperative nature.
Household indebtedness and changes in the housing market	An economic slowdown, which is felt more acutely in times of geopolitical uncertainty, could substantially affect households whose debt levels are still high. This economic situation could lead to a decline in the housing market, which is still strong despite some signs of losing steam, and to the expected impact of tighter mortgage granting rules, including a stress test involving interest rates for mortgage financing. Desjardins Group has a large portfolio mainly concentrated in Quebec, making it vulnerable to a decline in the housing market. However, Desjardins has sound practices in granting and managing mortgage financing which should allow it to circumvent this risk.
Low interest rate environment	Interest rates have remained at very low levels since the recovery from the 2008 financial crisis. This low rate environment puts pressure on financial intermediation margins, resulting in lower interest income and fiercer competition for deposits as a number of investors in search of higher returns abandon traditional bank products for high interest savings accounts and investment vehicles. This situation also affects Desjardins Group's insurer and pension plan matching activities while the valuation of liabilities increases and returns on assets decrease. Desjardins Group is still actively involved in its matching strategies and effectively manages these risks. However, the Bank of Canada's key interest rate is trending gradually upward, which together with tighter mortgage rules, could impact households' financial health. Desjardins nevertheless remains alert and is monitoring the credit quality of its loan and credit card portfolio to mitigate this risk.
Geopolitical uncertainties	The geopolitical landscape is changing. The adoption of protectionist measures by the U.S. administration increases global uncertainty, especially for the Canadian economy because of the North American Free Trade Agreement (NAFTA) negotiations and the withdrawal of the U.S. from the Trans-Pacific Partnership Agreement. The European political landscape is also undergoing significant change because of Great Britain's negotiations to withdraw from the European Union (Brexit) or even Catalonia's attempted separation. In addition, the outlook for militarization of international relations with North Korea is fuelling fears of political instability. Aware of the strong global economic integration, Desjardins Group remains vigilant and continues to rely on its robust risk management framework to identify, measure and mitigate risk.

Other risk factors that could impact future results

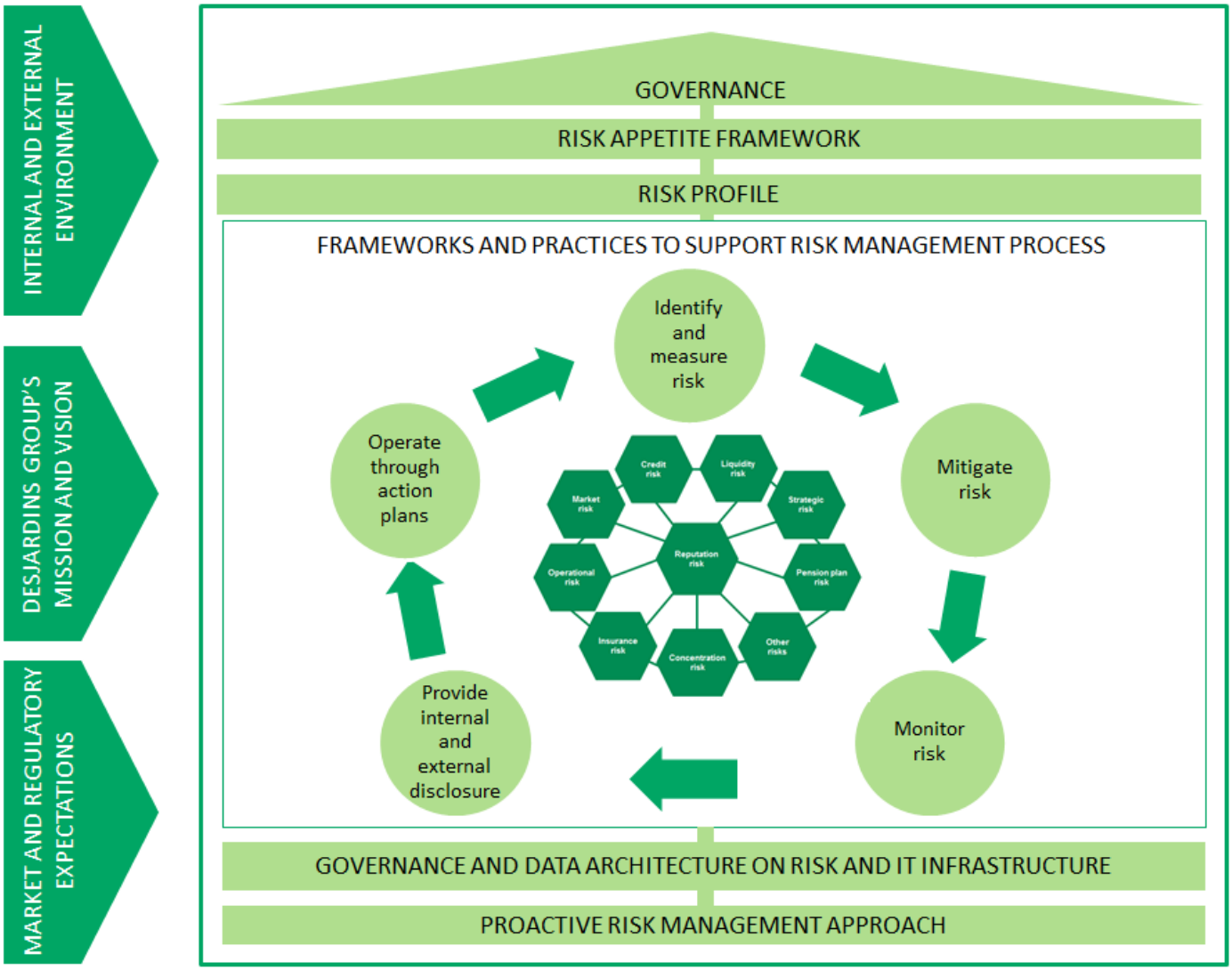
Risk factors	Description
General economic and business conditions in regions in which Desjardins Group operates	General economic and business conditions in the regions in which Desjardins Group operates may significantly affect its revenues and surplus earnings. These conditions include short and long-term interest rates, inflation, debt securities market fluctuations, foreign exchange rates, the volatility of capital markets, tighter liquidity conditions in certain markets, the level of indebtedness, the strength of the economy, consumer spending and saving habits, and the volume of business conducted by Desjardins Group in a given region.
Monetary policies	The monetary policies of the Bank of Canada and the Fed, as well as other interventions in capital markets, have an impact on Desjardins Group's income. The general level of interest rates may impact Desjardins Group's profitability because interest rate fluctuations affect the spread between interest paid on deposits and interest earned on loans, thereby affecting Desjardins Group's net interest income. Furthermore, considering the current level of indebtedness of Canadian households, higher interest rates could have an adverse effect on consumers' ability to service their debt, leading to an increased risk of loan losses for financial institutions. Desjardins Group has no control over changes in monetary policies or capital market conditions, and it therefore cannot forecast or anticipate them systematically.
Accuracy and completeness of information concerning clients and counterparties	Desjardins Group relies on the accuracy and completeness of the information it has on its clients and counterparties. When deciding to authorize a loan or other transactions with clients or counterparties, Desjardins Group may use information provided by them, including financial statements and other financial information. It may also rely on representations made by clients and counterparties regarding the completeness and accuracy of such information, and on auditors' reports regarding the financial statements. The financial position and income of Desjardins Group could be adversely affected if the financial statements on which it relies fail to comply with accounting standards, are misleading or do not present fairly, in all material respects, the financial position, performance and cash flows of its members, clients and counterparties. Desjardins Group trains its employees and implements procedures to mitigate the risks related to the use of inaccurate, incomplete or fraudulent information from its members, clients or counterparties.

Risk factors	Description
Critical accounting estimates and accounting standards	The Combined Financial Statements were prepared in accordance with the IFRS. The accounting policies used by Desjardins Group determine how it reports its financial position and results of operations, and management may be required to make estimates or rely on assumptions about matters that are inherently uncertain. Any change in these estimates and assumptions may have a significant impact on Desjardins Group's financial position and results of operations. Also note the upcoming compliance with IFRS 9, which incorporates a forward-looking perspective in calculating allowances for credit losses (2018 implementation), and IFRS 17, which has just amended the measurement rules for actuarial liabilities in insurance (scheduled implementation in 2021). These new standards may affect the organization's financial results.
New products and services to maintain or increase market share	Strong competitive pressures from Canadian financial institutions and the emergence of new competitors have led Desjardins Group to develop new products and services at a faster pace to maintain or increase its attractiveness as a financial institution with its clients. Developing these new products and services could require large investments by Desjardins or involve risks not identified at the time of their development. Desjardins cannot be certain that the new products and services it offers will result in the anticipated financial benefits.
Geographic concentration	Desjardins Group's operations are heavily concentrated in Quebec. As at December 31, 2017, Desjardins Group's loans to Quebec members and clients therefore accounted for 92.1% of its aggregate loan portfolio. As a result of this significant geographic concentration, its results largely depend on economic conditions in Quebec. Any deterioration in these conditions could adversely impact: • past due loans; • problem assets and foreclosed property; • claims and lawsuits; • the demand for products and services; the value of collateral available for loans, especially mortgages, and by extension, clients' and members' borrowing capacity, the value of assets associated with impaired loans and collateral coverage.
Acquisitions and joint arrangements	Desjardins Group has implemented a rigorous internal control environment for the acquisition and joint arrangement processes. Nevertheless, its financial or strategic objectives could fail to be met because of unexpected factors such as delays in approval of transactions by regulators or their imposing of additional conditions, the inability to apply the strategic plan in its original form, difficulties in integrating or retaining clients, an increase in regulatory costs, unexpected expenses, or changes in the economic and competitive environment. As a result, synergies, higher income, cost savings, increased market share and other expected benefits may not materialize or may be delayed, thereby impacting Desjardins Group's future surplus earnings. The integration of State Farm's Canadian operations within Desjardins Group is progressing satisfactorily, particularly with regard to the consolidation of the functions related to the use of State Farm banners and trademark during a certain period of time after the closing. Similarly, the agreement regarding the rendering of certain transitional services to Desjardins Group by State Farm during the period agreed upon after the closing is working out as scheduled. However, fully achieving the benefits anticipated by Desjardins Group will depend on its ability to capitalize on growth opportunities. Desjardins Group still risks experiencing problems up to the end of the integration and transition process, which could have an unfavourable impact on its operations, financial position, results of operations and cash flows.
Credit ratings	The credit ratings assigned to Desjardins Group by rating agencies are instrumental to its access to sources of wholesale funding and the cost of such funding. These ratings may be revised or withdrawn at any time by the agencies. In addition, a significant downgrade to various ratings could raise Desjardins Group's cost of funding, reduce its access to capital markets, and increase additional obligations required by its counterparties.
Catastrophes and climate change	Catastrophes are events whose unforeseeable nature and severity may have a material impact on Desjardins Group's results. More specifically, the financial results of Desjardins P&C insurance subsidiaries, given the nature of their operations, are more significantly affected by natural disasters. The risks associated with catastrophes and climate change are subject to specific governance within the P&C insurance subsidiaries as well as to mitigation measures, the most important of which is still the catastrophe reinsurance treaty, under which the volatility of financial results can be reduced. Desjardins Group understands the challenge posed by climate change to its P&C insurance operations and is an active participant in various industry initiatives. Moreover, Desjardins and its P&C insurance subsidiaries have set up a management structure to coordinate their activities and promote the rapid deployment of personnel in order to provide the best possible support to their insureds given the sufficiently high frequency of such extreme weather events.
Other factors	Other factors that may have an impact on Desjardins Group's future results include changes in tax laws, unexpected changes in consumer spending and saving habits, the ability to implement Desjardins Group's disaster recovery plan within a reasonable time, the possible impact of international conflicts on operations, and Desjardins Group's ability to anticipate and manage the risks associated with these factors properly despite a disciplined risk management environment. Desjardins Group cautions the reader that factors other than the foregoing could affect future results. Investors and other stakeholders relying on forward-looking statements to make decisions with respect to Desjardins Group should carefully consider these factors as well as other uncertainties, potential events, and industry factors or other items specific to Desjardins Group that could adversely impact its future results.

4.2 Risk management

Integrated risk management framework

Desjardins Group's objective in risk management is to optimize the risk-return trade-off, within set tolerance limits, by developing and applying integrated risk management strategies, frameworks, practices and procedures to all its operations. To this end, Desjardins developed an Integrated Risk Management Framework aimed, among other things, at giving its senior management and the Federation's Board of Directors an appropriate level of confidence and comfort regarding the understanding and management of the full spectrum of risks associated with the achievement of its objectives.



RISK IDENTIFICATION

Desjardins Group considers it important to periodically assess the environment in which it operates and to identify key risks, as well as the aforesaid principal risk factors and emerging risks to which it is exposed. Desjardins Group has a risk log that sets out the main categories and subcategories of risks to which Desjardins Group is exposed and which could affect results. The log is updated at least annually and is used as a basis to make a quantitative and qualitative assessment of risk materiality, to determine Desjardins Group's risk profile and to implement appropriate strategies to mitigate risk.

In the normal course of business, Desjardins Group is exposed to the principal risks shown below, which are covered in specific subsections of this MD&A.

Credit	Market	Liquidity	Operational	Insurance	Strategic	Reputation	Pension plan	Environmental	Legal and regulatory environment

In addition to strategic, operational, liquidity and reputation risks inherent in operations, the top risks of Desjardins Group's business segments are:

- Personal and Business Services: Credit and market risk
- Wealth Management and Life and Health Insurance: Insurance, market and credit risk
- Property and Casualty Insurance: Insurance and market risk

Strict and effective management of these risks is a priority for Desjardins Group, its purpose being to support its major orientations, particularly regarding its financial soundness as well as its sustained and profitable growth, while complying with regulatory requirements. Desjardins Group considers risk an inextricable part of its development and consequently strives to promote a proactive approach in which each of its business segments, employees and managers is responsible for risk management.

RISK MEASUREMENT

Desjardins Group uses both quantitative and qualitative techniques to determine its risk exposure. It ensures that an appropriate selection of measurement tools and mitigation techniques are designed and maintained in order to support its business development.

Models play a central role in assessing risk at Desjardins Group and support decision-making in many situations. They are applied to various aspects of risk management. Quantitative models are used for modelling credit risk measurement parameters. They are also used in market risk measurement, economic capital calculations, asset valuation and pricing. Risks are quantified based on both the current economic context as well as on hypothetical stress-testing situations, which are measured for specific risks on a Desjardins-wide integrated basis.

Desjardins-wide integrated stress testing

Desjardins-wide sensitivity tests and crisis scenarios are used as additional risk analysis tools to measure the potential impact of exceptional but plausible events on profitability and capital levels. Organization-wide crisis scenarios are developed based on the anticipated economic outlook under unfavourable conditions. In accordance with the second pillar of the Basel Capital Accord, the results of these analyses are a key element of Desjardins Group's internal capital adequacy assessment program and can identify potential vulnerabilities in various operations in relation to risk factors. Desjardins-wide stress testing is conducted annually.

Desjardins Group economists develop a series of potential crisis scenarios annually, based on current economic conditions, on the principal risk factors to which the organization is exposed and on emerging risks. These scenarios are then submitted to senior management for approval of an enterprise-wide assessment. More than 20 macroeconomic variables, including GDP, the jobless rate, housing prices, stock indices and inflation, are projected for each of the scenarios and different interest rate curves.

This exercise requires input from various business units and business segments to ensure a global perspective for the analysis as well as consistency among the various estimated impacts. Credit portfolios belonging to the Desjardins caisse network and the Federation are among the large portfolios analyzed. The analysis also covers the two insurance groups, namely Desjardins Financial Security Life Assurance Company and Desjardins General Insurance Group Inc., as well as the Desjardins Group Pension Plan.

The exercise is tied in with Desjardins Group's integrated financial planning, projected over a three-year horizon. The exercise's results are also used to establish capitalization targets and to update risk appetite and tolerance indicators.

During Desjardins-wide stress testing in 2017, the scenarios developed separately considered the possibility of a global economic crisis followed by a real estate decline in Canada, a crisis stemming from U.S. economic policies and increased protectionism and a crisis resulting from a cyber attack affecting international capital markets. The results obtained from the assessment of these scenarios show that Desjardins Group's current capitalization levels would be enough to withstand the economic deterioration considered and that its capital ratios would still exceed regulatory limits and its own risk appetite limits.

The results of the exercise are presented annually to various internal committees consisting of Desjardins Group's directors and senior management, namely the Risk Management Commission, the Desjardins Group Finance and Risk Management Committee, the Desjardins Group Management Committee and the Federation's Board of Directors.

In addition to the crisis scenarios studied during its financial planning, Desjardins Group carries out regulatory stress testing based on AMF prescribed assumptions and according to the frequency set by the AMF, generally every two years.

Governance and model validation

In order to oversee the use of Desjardins Group risk models, activities such as the development, performance monitoring and validation of models for credit risk, market risk, economic capital and stress testing are subject to guidelines that specify the roles and responsibilities of the various parties involved in these activities.

The validation team, which is independent from the units responsible for developing models and the end-user units, is in charge of running the appropriate validation program based on the model's importance. For the most important models, the program consists of a series of points to be validated for evaluating the model on design methodology, including assumptions, reliability and data quality. The program also includes the automatic replication of certain results obtained by the modelling team and the review of some aspects affecting implementation of the model. In addition, for models used to calculate regulatory capital, validation aims to assess compliance with applicable regulatory requirements. For models of lesser importance, the program has a smaller number of validation points. The validation team is also responsible for determining the importance level of each of Desjardins Group's risk assessment models. A model's importance level often dictates how often the model will be validated during its lifetime. Even though the governance structure overseeing design and performance monitoring activities mitigates the risk that inadequate models are deployed and used, independent validation is the main measure mitigating this risk.

RISK DISCLOSURE

A risk disclosure report is prepared quarterly and presented to the Desjardins Group Management Committee, the Risk Management Commission and the Federation's Board of Directors. These reports provide relevant information on changes in the principal risks identified as well as on the capital position, particularly capital adequacy in relation to Desjardins Group's risk profile. These reports are regularly updated to include the latest risk management developments.

RISK APPETITE

As a significant component of the Integrated Risk Management Framework, risk appetite makes it possible to determine the risk type and level that Desjardins is prepared to assume in pursuing its business, financial and strategic objectives. Risk appetite forms an integral part of strategic planning, which makes it possible to guide risk-taking in order to ensure Desjardins Group's stability and sustainability in the case of unfavourable future events that could affect reputation, the volatility of profitability, capital adequacy or liquidities. As a result, risk appetite provides a basis for integrated risk by promoting a better understanding of the effect of principal risks and emerging risks on Desjardins Group's actual results.

The risk appetite framework reflects Desjardins Group's risk-taking philosophy, mission and values and is based on:

- taking necessary risks to enrich the lives of people and communities, contributing to the development of a sustainable and responsible economy and managing such risks conscientiously;
- protecting Desjardins Group's reputation with its members, clients, communities, regulatory authorities and other stakeholders, while respecting its cooperative values;
- understanding the risks arising from Desjardins Group's operations and engaging in only new activities for which the risks are defined, assessed and understood;
- modernizing Desjardins Group's technologies to adapt to the needs of members, clients and employees in order to simplify their experience;
- thanks to adequate profitability in light of risk exposure, ensuring Desjardins Group's sustainability to be able to give back to members and communities and to meet its commitments;
- maintaining financial stability within the market by preserving a capitalization level that meets market expectations and complies with regulatory requirements;
- managing liquidities and refinancing activities in order to guard against liquidity risk;
- avoiding excessively large risk concentrations;
- adequately managing operational and regulatory risks.

The risk appetite framework also provides a system of qualitative and quantitative risk indicators that are monitored on a regular basis to ensure that Desjardins Group's risk profile remains within the risk appetite limits set by senior management and the Board of Directors. Desjardins Group's risk profile is analyzed quarterly by the Risk Management Executive Division and presented to senior management and the Board of Directors. In the event a level or limit for a risk appetite indicator is exceeded, a mechanism to implement an action plan is deployed and information is transmitted to the appropriate bodies. The Board of Directors is responsible for approving the risk appetite framework and ensuring that Desjardins Group's financial and strategic objectives are in line with its risk appetite.

The risk appetite framework is reviewed regularly and submitted to the Federation's Board of Directors for approval. The Desjardins Group Risk Management Executive Division relays the main guidelines for risk appetite to the business segments and components, and supports them in implementing these concepts by ensuring consistency in all the indicators, targets, levels and limits with the Desjardins Group framework.

PROACTIVE RISK MANAGEMENT APPROACH

A proactive risk management approach is one of the cornerstones of Desjardins Group's Integrated Risk Management Framework. It represents all the practices and behaviours of individuals and groups within the organization that condition the collective ability to identify, understand and openly discuss risks and handle present and future risks. First and foremost, the Board of Directors, senior management and the Risk Management Executive Division set the tone by promoting risk-taking behaviour in line with Desjardins Group's risk management frameworks and its risk appetite. A proactive risk management approach promotes open and transparent communication between Desjardins Group's risk management function and its other support functions, business segments and components, while promoting an appropriate risk-return trade-off.

Ethical conduct and integrity are firmly entrenched in Desjardins Group's proactive risk management approach, which relies on the *Desjardins Code of Professional Conduct.* The code sets out the values and principles that Desjardins Group has espoused in order to maintain a high level of integrity.

Other methods used to support the proactive risk management approach and to promote accountability for risk include:
- defining and communicating risk management roles and responsibilities to all line levels in terms of an operations management approach based on the Three Lines of Defence model;
- alignment of strategic decisions and compensation processes with risk-taking;
- the dissemination of risk management frameworks;
- the organizing of risk management training and education sessions, bearing in mind the type of risk discussed and the role of the various parties involved.

Risk management and the Integrated Risk Management Framework are based on the following guidelines that provide in particular for:
- the accountability of Desjardins Group's business segments and other functions with regard to the risks inherent to their operations;
- the independence of the risk management function in relation to business segments;
- implementation at every level of the organization in order to obtain a comprehensive vision of risk exposure;
- a procedure aimed at ensuring that risk matters are disclosed and flagged accurately and transparently to senior management in a timely manner;
- the existence and presence of a complete and rigorous process to determine the appropriate capital level based on the risks assumed;
- consideration of risk management in the formulation of strategic plans and business strategies and in the resulting decisions;
- thorough risk assessment prior to launching new products or initiating transactions with a strong financial impact.

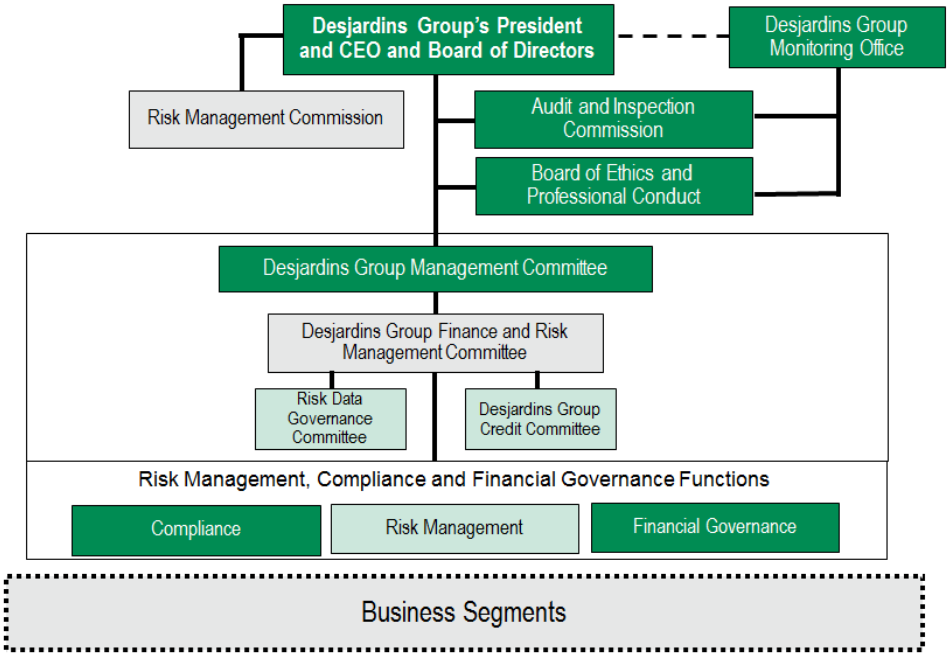
Compensation in relation to risk management

Desjardins Group has established strict governance with regard to total compensation. The Board of Directors is responsible for the annual changes in the total compensation of senior executives, members of the Management Committee and all employees. In this regard, it establishes an annual salary review, sets the objectives and measures the results of the general incentive plan. Acting as a subcommittee of the Board of Directors, the Human Resources Commission periodically reviews Desjardins Group's position with regard to total compensation so that it can remain competitive.

Incentive plans for senior executives, which are consistent with risk-taking at Desjardins Group, provide, as a general rule, for the medium to long-term deferral of a significant portion of members' annual bonus. The amounts thus deferred can vary annually depending on Desjardins Group's results. This formula encourages key stakeholders to have a long-term vision of Desjardins Group's development, which is beneficial for the organization's members and clients.

RISK MANAGEMENT GOVERNANCE

The Integrated Risk Management Framework is based on a solid risk governance structure and reflects Desjardins Group's organizational structure as shown below.



The **Federation's Board of Directors** is responsible for guiding, planning, coordinating and monitoring all of Desjardins Group's operations, and in such capacity, it participates actively in overseeing the major risks to which Desjardins Group is exposed. It is in particular responsible for adopting the overall directions and strategies proposed by senior management as well as risk management policies aimed at ensuring sound and prudent management of operations. The Board is supported in this regard by the Risk Management Commission, the Audit and Inspection Commission, the Board of Ethics and Professional Conduct and the Desjardins Group Management Committee. Further information about these bodies is found in the Corporate Governance section of the 2017 Desjardins Group Annual Report.

The **Desjardins Group Management Committee** must, in particular, make recommendations to the Board of Directors concerning risk management policies and strategies and ensure that they are implemented effectively and efficiently. The Management Committee can rely on the Finance and Risk Management Committee, made up of the heads of Desjardins Group's strategic functions and Desjardins experts.

The **Desjardins Group Finance and Risk Management Committee** is responsible for analyzing the key elements of the risk appetite framework and, where needed, for making recommendations to the Desjardins Group Management Committee, ensuring that the on- or off-balance sheet principal risks to which Desjardins Group is or will be exposed directly or through one or more of its subsidiaries have been identified and measured, and assessing the potential impact of identified risks on business strategies. This committee is supported by the Desjardins Group Credit Committee and by the Risk Data Governance Committee, which provides guidance and exercises authority in establishing and monitoring risk data governance in accordance with Desjardins Group's needs and regulatory requirements. In addition, it prioritizes the actions to improve risk data quality. The Desjardins Group Credit Committee is also supported by a risk supervision function in charge of ensuring the integrated governance of risk segmentation models and tools as well as regulatory models.

Operations management approach based on the Three Lines of Defence model

Risk management governance and the Integrated Risk Management Framework are also based on the Three Lines of Defence model. The Three Lines of Defence encompass complementary responsibilities that are coordinated to support sound risk-taking. In this regard, the roles and responsibilities relating to operations management and their risks must be clearly identified.

3rd Line of Defence	
Desjardins Group Monitoring Office	Responsible for conducting a periodic, independent and objective assessment of the First and Second Lines of Defence.
2nd Line of Defence	
Risk management,compliance and control functions	Responsible for providing risk management support to the First Line of Defence: develop frameworks and tools, mentor and train the First Line of Defence and ensure the orientations proposed are applied.
1st Line of Defence	
Process owner **(Business Segments and support functions)**	Accountable for the performance of the process, and works with agents and the team to ensure the consistent development of the process in line with member's needs and Desjardins Group's strategic vision.
Agent	Responsible for the performance of his area in order to attain the targets set by the owner and ensure the proper conduct of operations.

1st Line of Defence

The first line of defence is more specifically accountable for the overall performance of the activities assigned to it in the process and for managing the resulting risks. Its responsibility is therefore to:

- identify, measure, monitor and mitigate the risks arising from the activities assigned to it in the process;
- identify and analyze the controls in place and issue a conclusion on their adequacy and quality;
- design and set up controls, and then implement and monitor them;
- identify the changes that could affect the risk level of the activities assigned to it in the process and measure the impact;
- identify, design and monitor indicators that permit managing the risks of the activities assigned to it in the process;
- produce a risk profile for the processes assigned to it and report thereon;
- participate in critical review activities performed by the second and third lines of defence and take corrective action, if required;
- comply with regulatory requirements for risk data, risk disclosure and the governance framework, taking this into account during the budgetary and strategic planning process and when designing and carrying out new initiatives.

2nd Line of Defence

The **Risk Management Executive Division** is a strategic function whose main purpose is to partner with the business segments and Desjardins as a whole in their development by identifying, measuring and managing risks while ensuring Desjardins's sustainability. In partnership with the business segments, the Desjardins Group risk management function is responsible for recommending and establishing risk management frameworks, and setting up the appropriate risk management infrastructure, processes and practices to target all major Desjardins-wide risks.

The second line of defence can rely on the work performed by specialized programs for targeted risk assessment, which are also part of this line of defence. Although each specialized program has a separate mandate based on its expertise, they all help to regulate and properly manage certain issues inherent to Desjardins Group's operations. These expert programs are financial governance, business continuity, risk data quality and governance, compliance, technology risk, outsourcing and financial crime.

3rd Line of Defence

The **Desjardins Group Monitoring Office** is an independent and objective advisory and assurance body that assists Desjardins Group's officers in carrying out their governance responsibilities. It also oversees and advises management with respect to its duty to manage in a sound and prudent manner. In so doing, it contributes to improving Desjardins Group's overall performance and maintaining the confidence of its members, the public and the regulatory bodies. The Desjardins Group Monitoring Office includes the internal audit services of Desjardins Group components.

Basel capital accord

Basel III is an international capital adequacy tool designed to align regulatory capital requirements more closely with risk exposure and to further the continuous development of the risk assessment capabilities of financial institutions.

The Basel III framework is essentially based on three pillars: the first pillar sets out the requirements for risk-weighted regulatory capital; the second pillar deals with the supervisory review process; and the third pillar stipulates financial disclosure requirements.

In compliance with the guideline on adequacy of capital base standards, which was adapted to reflect the provisions of Basel III, Desjardins Group uses the Internal Ratings-Based Approach, subject to conditions, for credit risk related to the retail loan portfolios − Personal. Other exposures to credit, market and operational risk are currently measured according to the Standardized Approach. These provisions are used to calculate Desjardins Group's capital ratios, among other things.

In accordance with the AMF guideline on adequacy of capital base standards, Desjardins Group has also set up an internal capital adequacy assessment program (ICAAP). This program is a sound management practice recognized in the industry and is the key element of the second pillar of the Basel Accord. It allows a financial institution to provide for an appropriate level of capital to cover all major risks to which it is exposed, and to implement capital management strategies that follow the changes in its risk profile.

Desjardins Group's ICAAP is under the responsibility of the Risk Management Executive Division. Capital adequacy is assessed by verifying whether available capital is sufficient to cover the capital required. The units responsible oversee the overall adequacy of Desjardins Group's available capital based on both internal measures of economic capital and the regulatory capital requirements under the first pillar. The results of stress testing exercises are also considered in the capital adequacy assessment.

The internal measure of capital used by Desjardins Group is economic capital, namely the amount of capital that an institution must maintain, in addition to expected losses, to remain solvent over a certain horizon and at a high confidence level. For Desjardins Group, economic capital is assessed over a one-year horizon. A confidence level is selected to meet the objective of maintaining attractive credit ratings. In order to assess Desjardins Group's overall capital adequacy in relation to its risk profile, all significant risks identified through the risk logging process are assessed using internal methodologies to measure economic capital. It should be pointed out that all economic capital methodologies are validated independently to ensure that modelling input and assumptions used allow the assessed risk to be measured appropriately.

In the course of its operations, Desjardins Group is exposed to various risks. The table below provides its risk profile by business segment. Economic capital is broken down to illustrate the relative size of the risks associated with the various business segments. The distribution of risk-weighted assets shows Desjardins Group's exposure to credit risk, market risk and operational risk for the purposes of regulatory capital measurement.

Table 27 – Economic capital and risk-weighted assets[1] by business segment and by risk type
As at December 31, 2017

(in millions of dollars and as a percentage)

Desjardins Group

Economic capital	
Banking activities	
Credit risk	27.3%
Market risk	1.6
Operational risk	6.6
Other risks[2]	21.1
Total banking activities	56.6
Insurance activities	37.1
Risk related to goodwill and other intangible assets[3]	6.3

Risk-weighted assets	
Credit risk	$ 87,814
Market risk	1,965
Operational risk	11,850
Threshold adjustment	14,858

Business segment	Personal and Business Services	Wealth Management and Life and Health Insurance	Property and Casualty Insurance	Other
Balance sheet[4]	Assets $ 211,447	Assets $ 42,005	Assets $ 13,138	Assets $ 8,505
Economic capital	Proportion of total for Desjardins Group 41.8%	Proportion of total for Desjardins Group 30.0%	Proportion of total for Desjardins Group 16.5%	Proportion of total for Desjardins Group 11.7%
	Banking activities	Banking activities	Banking activities	Banking activities
	Credit risk 60.7	Credit risk 0.7	Credit risk -	Credit risk 14.1
	Market risk 1.9	Market risk -	Market risk -	Market risk 8.4
	Operational risk 15.2	Operational risk 2.7	Operational risk -	Operational risk 1.2
	Other risks[5] 21.4	Other risks[5] 3.8	Other risks[5] -	Other risks[5] 61.5
	Total banking activities 99.2	Total banking activities 7.1	Total banking activities -	Total banking activities 85.3
	Insurance activities[6] -	Insurance activities[6] 87.2	Insurance activities[6] 88.8	Insurance activities[6] -
	Risk related to goodwill and other intangible assets[3] 0.8	Risk related to goodwill and other intangible assets[3] 5.7	Risk related to goodwill and other intangible assets[3] 11.2	Risk related to goodwill and other intangible assets[3] 14.7
Risk-weighted assets	Credit risk $ 75,542	Credit risk $ 5,263	Credit risk $ 2,437	Credit risk $ 4,572
	Market risk 1,265	Market risk 10	Market risk -	Market risk 690
	Operational risk 8,885	Operational risk 719	Operational risk -	Operational risk 2,246
Risk profile	Desjardins Group is exposed to credit risk, market risk, operational risk and other risks, including in particular defined benefit plan risk, liquidity risk, interest rate risk, strategic risk, reputation risk and insurance risk.			

[1] The amount of risk-weighted assets is the risk-weighted asset amount used to calculate the Tier 1A capital ratio.
[2] Includes defined benefit plan risk, liquidity risk, interest rate risk, strategic risk, reputation risk and the diversification effect.
[3] The economic capital amount for the risk related to goodwill and other intangible assets is the carrying amount of these assets. It is considered that in a worst-case scenario for economic capital, the value of these assets would become nil.
[4] The different adjustments required to prepare the Combined Financial Statements as well as intersegment balance eliminations are classified in the asset amount of the Other category.
[5] Includes liquidity risk, interest rate risk, strategic risk and reputation risk. The risk related to other credit assets and deferred tax assets, defined benefit plan risk and the diversification effect are not allocated to business segments.
[6] For insurance operations, economic capital is the amount of capital equal to each insurance subsidiary's internal target ratio. Such economic capital covers all risks.

Again this year, numerous efforts were made throughout Desjardins Group to reinforce the implementation of sound risk management practices and to align regulatory capital requirements more closely with risk exposure. Desjardins Group is continuing to invest in improving its tools and systems and aligning them with sound practices in the industry for the principal types of risk. In recent years, the Bank for International Settlements has issued new requirements (Basel III) for the global regulation of capital standards. These new rules, in effect since January 1, 2013, have increased not only capital requirements but also risk management requirements. In addition to the changes made to the level and definition of eligible capital and the measurement of risk-weighted assets, Basel III has, under the second pillar, introduced new liquidity requirements and raised expectations for a number of management practices. Disclosure standards, which fall under the third pillar, have also been enhanced. These new requirements under the third pillar will become effective for Desjardins Group on December 31, 2018. Desjardins Group will continue its development by integrating these new regulatory requirements into its Integrated Risk Management Framework.

Additional information about capital management is presented in Section 3.2, "Capital management".

Credit risk

Credit risk is the risk of losses resulting from a borrower's, guarantor's, issuer's or counterparty's failure to honour its contractual obligations, whether or not such obligations appear on the Combined Balance Sheets.

Desjardins Group is exposed to credit risk first through its direct personal, business and government loans, which accounted for 64.5% of assets on the Combined Balance Sheets as at December 31, 2017, comparable to the ratio recorded a year earlier. It is also exposed through various other commitments, including letters of credit and transactions involving derivative financial instruments as well as securities transactions.

CREDIT RISK MANAGEMENT

Desjardins Group upholds its goal of providing efficient service to all its members and clients. To this end, it has developed distribution channels specialized by product and customer base. The various units and components making up these channels are considered centres of expertise and are accountable for their performance in their respective markets, including credit risk management. In this regard, they have specific frameworks to support them, powers of approval, and the corresponding management and monitoring tools. To provide assistance in this area to these units and components, Desjardins Group has set up centralized structures and procedures to ensure that its Integrated Risk Management Framework allows for effective management that remains sound and prudent.

The Risk Management Executive Division has been structured so that it can effectively manage credit risk and provide credit approval, support, quantification and monitoring, and report on credit matters.

Framework

A set of policies, guidelines, rules, practices and standards govern all aspects of credit risk management at Desjardins Group. This framework defines the responsibilities and powers of the parties involved, the limits imposed by risk tolerance, the rules governing the assignment and administration of files, and the disclosure rules for Desjardins Group's exposure to credit risks.

All these frameworks govern Desjardins's credit risk management and control activities.

Assessment of credit and counterparty risk

The AMF has authorized two credit risk assessment approaches to be included in calculating regulatory capital, namely the Standardized Approach and the Internal Ratings-Based Approach. RWA calculations are used to measure Desjardins Group's credit risk, as well as market risk and operational risk. Desjardins has adopted the Internal Ratings-Based Approach for credit risk related to loan portfolios of retail clients – Personal. In order to apply this method, Desjardins Group had to make internal estimates to calculate the probability of default (PD), loss given default (LGD) and exposure at default (EAD) on loan products. Other credit risk exposures are measured using the Standardized Approach.

For purposes of measuring credit and counterparty risk, Desjardins Group calculates EAD by exposure category and by counterparty category.

Credit and counterparty risk exposure are classified according to the following categories:

- Used exposure is the amount of funds invested or advanced to a member or client.
- Unused exposure is the amount of credit in loans or margins that has been authorized, but not yet used after credit conversion factors (CCF) have been applied.
- Repo-style transactions are contractual transactions between two parties, including a retrocession commitment at a pre-set price. Repo-style transactions include repurchase agreement transactions, reverse repurchase agreement transactions, and lending and borrowing of securities that are not outstanding with a central counterparty as well as these same transactions carried out with a non-qualifying central counterparty.
- Over-the-counter (OTC) derivative instruments refer to all OTC derivative financial instruments with different underlying instruments.
- Off-balance sheet exposures include guarantees, commitments, derivatives and other contractual agreements of which the total notional principal amount may not be recognized on the balance sheet.
- The net exposure is calculated after using credit risk mitigation (CRM) techniques, including collateral, guarantees and credit derivatives.

As at December 31, 2017, the EAD was $264.4 billion before using CRM techniques, and $242.6 billion after using CRM techniques. The complete results of the credit risk assessment, depending on the type of risk exposure, asset class and the calculation method used (the Standardized Approach or the Internal Ratings-Based Approach (Basel III), as required by the AMF), are found in the table below.

Table 28 – Risk exposure by asset class (Exposure at default [EAD])[1]*

As at December 31

(in millions of dollars)	2017 Used exposure	Unused exposure	Repo-style transactions	OTC derivatives	Off-balance sheet exposure	Total	Net exposure[2]
Standardized Approach							
Sovereign borrowers	**$ 13,745**	**$ 678**	**$ 16**	**$ 8**	**$ 141**	**$ 14,588**	**$ 14,572**
Financial institutions	**7,475**	**2,478**	**483**	**3,287**	**524**	**14,247**	**11,778**
Businesses	**49,094**	**4,823**	**283**	**2**	**639**	**54,841**	**54,122**
SMEs similar to other retail client exposures	**6,822**	**188**	**-**	**-**	**34**	**7,044**	**6,981**
Mortgages	**411**	**-**	**-**	**-**	**-**	**411**	**411**
Other retail client exposures (excluding SMEs)	**1,438**	**67**	**-**	**-**	**-**	**1,505**	**279**
Securitization	**6**	**-**	**-**	**-**	**-**	**6**	**6**
Equities	**152**	**-**	**-**	**-**	**-**	**152**	**152**
Trading portfolio	**-**	**-**	**17,840**	**750**	**-**	**18,590**	**1,268**
Internal Ratings-Based approach							
Mortgages	**93,067**	**12,614**	**-**	**-**	**-**	**105,681**	**105,681**
Revolving retail client exposures	**11,239**	**26,110**	**-**	**-**	**-**	**37,349**	**37,349**
Other retail client exposures	**9,577**	**395**	**-**	**-**	**21**	**9,993**	**9,993**
Total	**$ 193,026**	**$ 47,353**	**$ 18,622**	**$ 4,047**	**$ 1,359**	**$ 264,407**	**$ 242,592**

(in millions of dollars)	2016 Used exposure	Unused exposure	Repo-style transactions	OTC derivatives	Off-balance sheet exposure	Total	Net exposure[2]
Standardized Approach							
Sovereign borrowers	$ 14,321	$ 457	$ 861	$ 2	$ 89	$ 15,730	$ 14,909
Financial institutions	4,849	2,618	957	3,786	781	12,991	9,260
Businesses	45,398	4,498	517	-	935	51,348	50,135
SMEs similar to other retail client exposures	6,922	56	-	-	42	7,020	6,951
Mortgages	143	-	-	-	-	143	143
Other retail client exposures (excluding SMEs)	1,521	17	-	-	-	1,538	247
Securitization	807	-	-	-	-	807	807
Equities	98	-	-	-	-	98	98
Trading portfolio	-	-	14,563	844	-	15,407	915
Internal Ratings-Based approach							
Mortgages	88,199	8,500	-	-	-	96,699	96,699
Revolving retail client exposures	10,682	23,920	-	-	-	34,602	34,602
Other retail client exposures	8,332	326	-	-	18	8,676	8,676
Total	$ 181,272	$ 40,392	$ 16,898	$ 4,632	$ 1,865	$ 245,059	$ 223,442

(1) The definition of exposure classes related to regulatory capital requirements differs from the accounting classification.
(2) After using credit risk mitigation (CRM) techniques, including collateral, guarantees and credit derivatives.

The following table presents exposure at default for portfolios of businesses, sovereign borrowers and financial institutions by industry using the Standardized Approach. The different industries are based on the North American Industry Classification System.

Table 29 – Exposure at default - Businesses, sovereign borrowers and financial institutions by industry*
As at December 31

	2017						
(in millions of dollars)	Used exposure	Unused exposure	Repo-style transactions	OTC derivatives	Off-balance sheet exposure	Total	Net exposure[1]
Agriculture	$ 6,492	$ 144	$ -	$ -	$ 12	$ 6,648	$ 6,640
Mining, oil and gas	308	460	-	-	52	820	819
Utilities	13,306	1,404	16	-	174	14,900	14,877
Construction	2,066	583	-	-	78	2,727	2,678
Manufacturing	2,601	597	-	-	96	3,294	3,280
Wholesale trade	1,256	192	-	-	45	1,493	1,484
Retail trade	2,592	328	-	-	8	2,928	2,910
Transportation	1,090	463	-	-	53	1,606	1,600
Information industry	333	345	-	-	-	678	677
Finance and insurance	7,345	1,053	766	3,297	683	13,144	10,247
Real estate	23,863	623	-	-	42	24,528	24,466
Professional services	445	133	-	-	14	592	586
Management of companies	817	224	-	-	18	1,059	982
Administrative services	206	15	-	-	7	228	219
Education	1,621	926	-	-	4	2,551	2,550
Health care	2,716	216	-	-	1	2,933	2,926
Arts and entertainment	729	41	-	-	3	773	772
Accommodation	1,020	33	-	-	2	1,055	1,046
Other services	635	34	-	-	7	676	669
Other businesses	873	165	-	-	5	1,043	1,044
Total business loans	$ 70,314	$ 7,979	$ 782	$ 3,297	$ 1,304	$ 83,676	$ 80,472

	2016						
(in millions of dollars)	Used exposure	Unused exposure	Repo-style transactions	OTC derivatives	Off-balance sheet exposure	Total	Net exposure[1]
Agriculture	$ 5,768	$ 105	$ -	$ -	$ 11	$ 5,884	$ 5,872
Mining, oil and gas	312	457	-	-	3	772	771
Utilities	15,159	1,121	838	-	144	17,262	16,446
Construction	1,956	432	-	-	84	2,472	2,421
Manufacturing	2,476	538	-	-	88	3,102	3,092
Wholesale trade	1,094	169	-	-	34	1,297	1,283
Retail trade	2,283	695	-	-	9	2,987	2,974
Transportation	1,041	289	-	-	48	1,378	1,376
Information industry	368	308	-	-	19	695	694
Finance and insurance	3,905	1,084	1,497	3,788	1,232	11,506	6,845
Real estate	21,475	746	-	-	34	22,255	22,183
Professional services	401	97	-	-	17	515	510
Management of companies	784	139	-	-	17	940	865
Administrative services	278	2	-	-	5	285	275
Education	1,185	959	-	-	3	2,147	2,147
Health care	2,577	151	-	-	1	2,729	2,724
Arts and entertainment	638	46	-	-	4	688	687
Accommodation	915	14	-	-	1	930	921
Other services	658	128	-	-	5	791	784
Other businesses	1,295	93	-	-	46	1,434	1,434
Total business loans	$ 64,568	$ 7,573	$ 2,335	$ 3,788	$ 1,805	$ 80,069	$ 74,304

[1] After using credit risk mitigation (CRM) techniques, including collateral, guarantees and credit derivatives.

Credit granting

The Risk Management Executive Division assigns approval limits to the various units and components, including the caisse network. The units and components are primarily responsible for approving the files originating from them. However, the Risk Management Executive Division approves any commitments exceeding the approval limits assigned to them. Its approval responsibilities and the depth of the analyses required depend on product features as well as the complexity and extent of transaction risk.

The Risk Management Executive Division also sets commitment limits, namely the maximum commitment that can be granted to a borrower and the related entities. Where required, risk-sharing arrangements can be used, mainly with other caisses or certain Desjardins Group components. Risk-sharing arrangements can also be made with other financial institutions through banking syndicates.

Retail loans

Retail loan portfolios consist of residential mortgages, personal loans and lines of credit, point-of-sale financing and credit card loans. The Internal Ratings-Based Approach for credit risk is currently used for most of these portfolios.

Under the Internal Ratings-Based Approach, credit risk is measured according to three parameters: Probability of default (PD), loss given default (LGD) and exposure at default (EAD).

PD is the likelihood of a borrower defaulting on its obligations within a one-year time horizon. Behavioural scoring models, estimated using logistic regressions, produce risk levels monthly. The predictive features of these models include in particular borrower and account-specific features such as account age, loan size and delinquency. These models allow proactive management of the portfolio credit risk. However, for regulatory purposes, the PD from scoring models is:

- calibrated by groups of products according to the following drivers: residential mortgages, loans and lines of credit, point-of-sale financing and credit cards;
- adjusted slightly upward (prudential margins) to compensate for the historical volatility of PD.

LGD measures the size of the possible economic loss in the event of the borrower's default. It is expressed as a percentage of EAD. LGD estimates reflect average economic losses by collateral or guarantee type input into an internal history. Economic losses include direct and indirect management costs as well as any recoveries adjusted for the delay between the time of default and the time of the transaction. LGD is adjusted upward to take into account the possible effects of an economic slowdown.

EAD is an estimate of the amount outstanding for a given exposure at the time of default. For on-balance sheet exposures, EAD is equal to the balance at the time of observation. For off-balance sheet exposures, EAD includes an estimate of the additional drawdowns that may occur between the time of observation and the default. Estimates of such possible additional drawdowns reflect the internal history of the average drawdown on revolving credit products between the observation date and the time of default. Finally, EAD of off-balance sheet exposures is adjusted upward to take into account the possible effects of an economic slowdown.

In general, credit decisions concerning retail customers are based on risk ratings generated using predictive credit scoring models. Credit adjudication and portfolio management methodologies are designed to ensure consistent granting of credit and early identification of problem loans. Desjardins Group's automated risk rating system evaluates the creditworthiness of each member and client on a monthly basis. This process ensures the quick, valid identification and management of problem loans.

Table 30 presents PD tranches in relation to risk levels.

Table 30 – Probabilities of default of retail clients by risk level*

Risk levels	PD tranches
Excellent	0.00% - 0.14%
Very low	0.15% - 0.49%
Low	0.50% - 2.49%
Average	2.50% - 9.99%
High	10.00% - 99.99%
Default	100.00%

Monitoring performance of credit risk assessment models using the Internal Ratings-Based Approach

For portfolios assessed using the Internal Ratings-Based Approach, the Risk Management Executive Division is responsible for the design, development and performance monitoring of models, in accordance with various guidelines on the subject.

Credit risk assessment models are developed and tested by specialized teams supported by the business units and related credit risk management units concerned by the model.

The performance of credit risk parameters is analyzed on an ongoing basis through back testing. This testing is performed on out-of-time and out-of-sample inputs and aims to assess parameter robustness and adequacy. If necessary, i.e. where a statistically significant overage is observed, prudential upward adjustments are made to reflect an unexpected trend in a segment in particular. These adjustments, allowing a more adequate risk assessment related to the transactions and borrowers, are validated and approved by the units responsible.

More specifically for PD, such back testing takes the form of various statistical tests to assess the following criteria:

- model's discriminating power;
- calibration of the model;
- stability of model results.

Independent validations are also performed on credit risk assessment models. The most critical aspects to be validated are factors allowing appropriate risk classification by level, the adequate quantification of exposures and the use of assessment techniques taking external factors into consideration, such as economic conditions and the credit situation, and lastly, alignment with internal policies and regulatory provisions.

The model approval procedure and reporting are regulated by different bodies depending on the type and size of the approval in question. As a result, new models and significant changes to existing models are approved by the next higher committee than the one that is informed of the annual model performance monitoring results and authorizes any resulting recommendations.

The table below shows the quality of the retail loan portfolio by asset class using the Internal Ratings-Based Approach.

Table 31 – Exposure to credit risk of retail loan portfolios[(1)]*

As at December 31

	2017				2016
	EAD				
(in millions of dollars)	Exposures related to residential mortgage loans	Qualifying revolving retail client exposures	Other retail client exposures	Total	Total
Excellent	$ 36,776	$ 14,122	$ 1,076	$ 51,974	$ 54,855
Very low	27,814	13,246	1,267	42,327	30,757
Low	35,669	7,386	3,626	46,681	43,426
Average	4,183	1,291	3,603	9,077	7,776
High	882	1,187	345	2,414	2,518
Default	357	117	76	550	645
Total	$ 105,681	$ 37,349	$ 9,993	$ 153,023	$ 139,977

(1) Exposures depend on the regulatory scope, which excludes insurance operations.

The table below presents the quality of the retail loan portfolio subject to the Standardized Approach by risk tranche.

Table 32 – Exposures to retail clients by risk tranche[(1)]*

As at December 31

	2017							2016
	Risk tranches							
(in millions of dollars)	0%	20%	35%	50%	75%	100%	Other	Total	Total
Residential mortgages	$ -	$ -	$ 408	$ -	$ -	$ 3	$ -	$ 411	$ 143
Other retail client exposures (except for SMEs)	-	-	-	-	1,456	49	1	1,506	1,538
Total	$ -	$ -	$ 408	$ -	$ 1,456	$ 52	$ 1	$ 1,917	$ 1,681

(1) Exposures depend on the regulatory scope, which excludes insurance operations.

Loans to businesses, sovereign borrowers and financial institutions

These loans include retail loans, loans to sovereign borrowers and public bodies, loans to the housing sector and loans to other businesses. Work is in progress to switch these portfolios to the Internal Ratings-Based Approach.

The following table presents the credit quality of the portfolio of loans and acceptances to businesses, sovereign borrowers and financial institutions by risk tranche.

Table 33 – Exposures to businesses, sovereign borrowers and financial institutions by risk tranche[(1)]*
As at December 31

	2017								2016
	Risk tranches								
(in millions of dollars)	0%	20%	35%	50%	75%	100%	Other	Total	Total
Sovereign borrowers	$ 938	$ -	$ -	$ -	$ -	$ 2	$ -	$ 940	$ 729
Financial institutions	-	5,746	-	15	-	390	3	6,154	5,734
Businesses	-	-	-	566	-	52,341	707	53,614	49,235
SMEs similar to other retail client exposures	-	-	-	-	5,354	1,506	113	6,973	7,051
Total	$ 938	$ 5,746	$ -	$ 581	$ 5,354	$ 54,239	$ 823	$ 67,681	$ 62,749

(1) Exposures depend on the regulatory scope, which excludes insurance operations.

Retail clients, small residential rental properties and small commercial rental properties

Credit scoring systems based on proven statistics are used to assess the risk of credit activities involving these client bases.

These systems were designed using the behavioural history of borrowers with a profile or characteristics similar to those of the applicant in order to estimate the transaction risk.

Such systems are used for initial approval as well as for the monthly reassessment of borrowers' risk level. Ongoing updates allow for proactive management of the portfolios' credit risk.

The performance of these systems is periodically analyzed and adjustments are made regularly to measure transaction and borrower risk as adequately as possible. The units responsible for developing scoring systems and the underlying models ensure that adequate controls are set up to monitor their stability and performance.

Other segments

The granting of credit is based on the detailed analysis of a file. Each borrower's financial, market and management characteristics are analyzed using a credit risk assessment model designed from internal and external historical data, taking into account the size of the business, the special characteristics of the main industry in which the borrower operates, and the performance of comparable businesses.

In order to determine the model to be used, a segment is assigned to each borrower based on the borrower's main industry and some other features. A quantitative analysis based on financial data is supplemented by an assessment of qualitative factors by the person in charge of the file. Once this analysis is finished, each borrower is assigned a credit risk rating representing the borrower's risk level.

The use of scoring results has been expanded to other risk management and governance activities such as establishing analysis requirements and the required decision-making level, determining the different types of follow-up activities, as well as assessing and disclosing portfolio risk quality.

Credit risk mitigation

The terms and conditions of credit risk mitigation are set out in the credit policies, rules and practices established by the Risk Management Executive Division.

When a loan is granted to a member or client, Desjardins Group may obtain collateral to mitigate the borrower's credit risk. Such collateral normally takes the form of assets such as capital assets, receivables, inventory, investments, government securities or equities.

For some portfolios, programs offered by various organizations, in particular Canada Mortgage and Housing Corporation (CMHC) and *La Financière agricole du Québec*, are used in addition to customary collateral. As at December 31, 2017, guaranteed or insured loans represented 26.4% of Desjardins Group's total gross loans, compared to 27.3% at the end of 2016.

Frameworks adapted to each type of collateral contain the requirements for appraising collateral, its legal validity and follow-up. The type of collateral as well as the value of the assets encumbered by such collateral are established on the basis of a credit risk assessment of the transaction and the borrower, depending in particular on the borrower's PD. Such an assessment is required whenever any new loan is granted in accordance with Desjardins Group's frameworks. When an outside professional, such as a chartered appraiser or an environmental assessment firm, is required to determine the value of the collateral, the selection of the professional and the mandate must comply with the necessary requirements in the frameworks. Considering that the collateral is used to recover all or part of the unpaid balance of a loan in the event of the borrower's default to make payment, the quality, the legal validity and the ease with which the collateral can be realized are determining factors in obtaining a loan.

In order to ensure that the value of the collateral remains adequate, it must be periodically updated. The frequency of reappraisals depends in particular on the risk level, the type of collateral or certain triggering events such as a deterioration in the borrower's financial position or the sale of an asset held as collateral. The decision-making level is responsible for approving the updated value of the collateral, if applicable.

Loan debt relief

In managing loan portfolios, Desjardins Group may, for financial or legal reasons, change the original terms and conditions of a loan granted to a borrower experiencing financial difficulty and therefore prevented from discharging his obligations. Such changes may include an interest rate adjustment, the deferral or extension of principal and interest payments or the waiver of a tranche of the principal or interest.

Loans with debt relief totalled $242 million as at December 31, 2017, compared to $144 million at the end of 2016. Of these loans, $77 million were classified as gross impaired loans as at December 31, 2017, compared to $75 million as at December 31, 2016.

File monitoring and management of higher risk files

Credit practices govern the monitoring of loans. Files are reassessed on a regular basis. Requirements regarding review frequency and depth increase with a higher PD or the size of potential losses on receivables. The officer in charge of the file monitors high risk loans using various intervention methods. A positioning, which must be authorized by the appropriate decision-making level, is required to be performed for files with irregularities or increased risk as well as for files in default.

The unit in charge of the financing is primarily responsible for monitoring files and for managing higher risks. However, certain tasks or files may be outsourced to the Federation's intervention units specializing in turnarounds or recovery. Supervision reports produced and submitted periodically to the appropriate bodies make it possible to monitor the position of high-risk borrowers as well as changes in the corrective measures put in place. In addition, a report accounting for credit activities, covering changes in credit quality and financial issues, is submitted quarterly to the management of the component concerned.

Default situations

A borrower or counterparty is considered to be in default in certain situations defined by the frameworks. Such situations include in particular any past due payment of more than 90 days, unauthorized overlimits of over 90 days, forced restructuring, bankruptcies or insolvencies, or any other reason which would lead one to believe that a borrower will be unable to repay his debt in full unless the appropriate action is taken. A borrower ceases to be considered in default once certain conditions have been met.

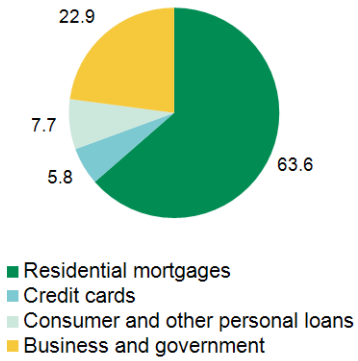
Monitoring of portfolio and reporting

The Risk Management Executive Division oversees the management of all risks to which the organization is exposed, including credit risks. The operating methods require ongoing monitoring of the credit risks to which Desjardins Group is exposed, as well as periodic reporting on portfolio quality to the appropriate bodies.

BREAKDOWN AND QUALITY OF LOAN PORTFOLIO

The following chart presents the distribution of loans and acceptances by borrower category. Over half of the portfolio consists of residential mortgages, for which, statistically, the loss rate is lower.

Breakdown of loans and acceptances
As at December 31, 2017
(as a percentage)



Loans by borrower category and by industry are presented in the table below. As at December 31, 2017, the main sectors of the business loan portfolio were real estate, agriculture and retail trade, which accounted for 51.2% of the business loan portfolio amounting to $37.1 billion. The main industries are the same as they were as at December 31, 2016.

Table 34 – Loans by borrower category and by industry

As at December 31

(in millions of dollars)	2017		2016[1]		2015[1]	
	Gross loans	**Gross impaired loans**	Gross loans	Gross impaired loans	Gross loans	Gross impaired loans
Residential mortgages	**$113,146**	**$ 141**	$ 106,695	$ 174	$ 102,323	$ 182
Consumer, credit card and other personal loans	**24,044**	**89**	22,150	102	21,204	99
Public bodies[2]	**3,621**	**-**	2,925	-	3,729	-
Business						
Agriculture	**7,988**	**24**	7,506	37	6,584	36
Mining, oil and gas	**306**	**1**	321	1	451	-
Utilities	**410**	**6**	518	-	360	-
Construction	**2,168**	**35**	2,109	45	2,034	37
Manufacturing	**2,750**	**38**	2,640	41	2,479	45
Wholesale trade	**1,261**	**5**	1,118	7	1,014	12
Retail trade	**2,933**	**22**	2,737	22	2,263	17
Transportation	**1,277**	**9**	1,307	10	1,164	10
Information industry	**344**	**6**	387	7	328	11
Finance and insurance	**753**	**-**	649	1	720	-
Real estate	**8,099**	**10**	7,195	13	6,103	13
Professional services	**614**	**4**	550	5	425	4
Management of companies	**927**	**1**	907	2	896	2
Administrative services	**255**	**4**	231	6	227	3
Education	**183**	**-**	324	2	163	-
Health care	**2,511**	**17**	2,306	13	1,945	18
Arts and entertainment	**722**	**4**	733	7	647	13
Accommodation	**1,267**	**16**	1,217	26	1,078	27
Other services	**803**	**8**	887	11	694	9
Other businesses	**1,546**	**2**	1,059	-	3,129	3
Total business loans	**$ 37,117**	**$ 212**	$ 34,701	$ 256	$ 32,704	$ 260
Total loans	**$177,928**	**$ 442**	$ 166,471	$ 532	$ 159,960	$ 541

(1) As a result of a change in methodology, the amounts for 2016 and 2015 have been restated.
(2) Including loans to governments.

Loans by geographic distribution are presented in the table below. Desjardins Group's operations are highly concentrated in Quebec. Therefore, as at December 31, 2017, the loans granted by Desjardins to members and clients in Quebec accounted for 92.1% of the total loan portfolio, compared to 92.8% as at December 31, 2016.

Table 35 – Loans by geographic distribution

As at December 31

(in millions of dollars)	2017		2016		2015	
	Gross loans	**Gross impaired loans**	Gross loans	Gross impaired loans	Gross loans	Gross impaired loans
Canada						
Quebec	**$ 163,921**	**$ 389**	$ 154,551	$ 480	$ 151,435	$ 481
Other Canadian provinces	**13,667**	**50**	11,587	51	8,190	58
Total – Canada	**$ 177,588**	**$ 439**	$ 166,138	$ 531	$ 159,625	$ 539
Other countries	**340**	**3**	333	1	335	2
Total	**$ 177,928**	**$ 442**	$ 166,471	$ 532	$ 159,960	$ 541

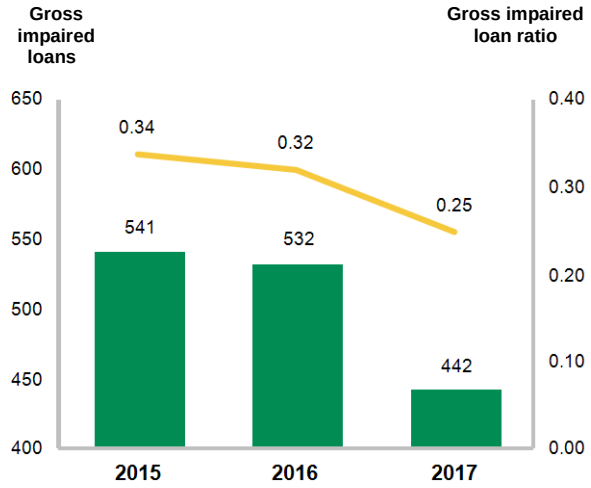
The chart below presents gross impaired loans. As at December 31, 2017, gross impaired loans outstanding stood at $442 million, down $90 million since December 31, 2016. The ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.25% at the end of 2017, down from the ratio of 0.32% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans. Desjardins Group's loan portfolio continues to be of high quality.

Individual allowances for credit losses, which totalled $104 million as at December 31, 2017, made it possible to obtain a total coverage ratio of 23.5% of the gross impaired loan portfolio, compared to a ratio of 22.7% at the end of 2016.

The collective allowance stood at $334 million as at December 31, 2017, which was down slightly from $335 million recorded at the end of 2016. In addition, an allowance for risk related to off-balance sheet arrangements of $49 million was recognized as at December 31, 2017 under "Other liabilities – Other" on the Combined Balance Sheets, down $7 million compared to the amount posted as at December 31, 2016. The collective allowance reflects the best estimate of the allowance for credit losses that have not yet been designated individually as impaired loans.

The methods for measuring the collective allowance and individual allowances, as well as the method for determining an impaired loan, are described in Section 5.3, "Critical accounting policies and estimates – Impairment of financial assets", of this MD&A.

Gross impaired loans
(in millions of dollars and as a percentage)



Tables 36 and 37 present the gross impaired loans by Desjardins Group borrower category and the change in the gross impaired loan balance.

Table 36 – Gross impaired loans by borrower category
As at December 31

(in millions of dollars and as a percentage)	2017					2016		2015	
	Gross loans and acceptances	**Gross impaired loans**		**Individual allowances for credit losses**	**Net impaired loans**	Gross impaired loans	Net impaired loans	Gross impaired loans	Net impaired loans
Residential mortgages	**$ 113,146**	**$ 141**	**0.12%**	**$ 19**	**$ 122**	$ 174	$ 155	$ 182	$ 164
Consumer, credit card and other personal loans	**24,044**	**89**	**0.37**	**12**	**77**	102	87	99	81
Business and government	**40,769**	**212**	**0.52**	**73**	**139**	256	169	260	175
Total	**$ 177,959**	**$ 442**		**$ 104**	**$ 338**	$ 532	$ 411	$ 541	$ 420
As a percentage of gross loans and acceptances[1]			**0.25%**		**0.19%**	0.32%	0.25%	0.34%	0.26%

[1] See "Basis of presentation of financial information".

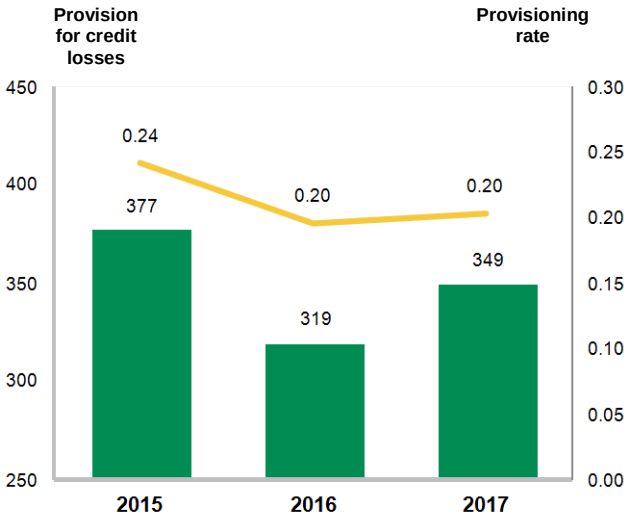
Table 37 – Change in gross impaired loan balance
As at December 31

(in millions of dollars)	2017	2016	2015
Gross impaired loans at the beginning of the year	**$ 532**	$ 541	$ 511
Gross impaired loans since the last year	**901**	1,023	989
Loans returned to unimpaired status	**(668)**	(697)	(606)
Write-offs and recoveries	**(374)**	(367)	(364)
Other changes	**51**	32	11
Gross impaired loans at the end of the year	**$ 442**	$ 532	$ 541

Provision for credit losses

Desjardins Group's provision for credit losses totalled $349 million for 2017, up $30 million compared to 2016. A recovery of the collective allowance resulted in 2016 owing to refinements of the methodology used in models for calculating this allowance. Favourable developments in the risk related to this portfolio nevertheless mitigated the increase. The provisioning rate was 0.20% at the end of 2017, unchanged from what it was as at December 31, 2016.

Provision for credit losses
(in millions of dollars and as a percentage)



Counterparty and issuer risk

Counterparty and issuer risk is a credit risk relative to different types of securities, derivative financial instrument and securities lending transactions.

The Risk Management Executive Division sets the maximum exposure for each counterparty and issuer based on quantitative and qualitative criteria. In addition, limits are set for certain financial instruments. The amounts are then allocated to different components based on their needs.

To properly manage its risk exposure, Desjardins Group assigns a credit rating to each counterparty and issuer, based on the ratings of four external credit rating agencies (DBRS, Moody's, Standard & Poor's and Fitch). The four credit rating agencies meet the eligibility criteria of the Basel Accord and are authorized by the AMF and OSFI. Desjardins uses this credit rating to establish exposure limits and to calculate capital requirements using the Standardized Approach. In addition, to help establish exposure limits, the credit rating may also take internal models into account, depending on the category of the counterparty or issuer. These limits cannot exceed a certain percentage of Tier 1A capital, based on the category of the counterparties and issuers.

A large proportion of Desjardins Group's risk exposure is to the different levels of government in Canada, Quebec public and parapublic entities and major Canadian banks. For most of these counterparties and issuers, the credit rating is A- or higher. In addition, Desjardins Group's exposure to U.S. and European financial institutions is low, and its exposure to sovereign debt is concentrated in Canada and the United States.

In its derivative financial instrument and securities lending transactions, which include repurchase agreements, reverse repurchase agreements and securities borrowing and lending, Desjardins Group is exposed to counterparty credit risk.

Desjardins Group uses derivative financial instruments primarily for asset and liability management purposes. Derivative financial instruments are contracts whose value is based on an underlying asset, such as interest rates, exchange rates or financial indices. The vast majority of Desjardins Group's derivative financial instruments are traded over the counter with a counterparty and include forward exchange contracts, currency swaps, interest rate swaps, credit default swaps, total return swaps, forward rate agreements, and currency, interest rate and stock index options. Other instruments are exchange-traded contracts, consisting mainly of futures and swaps traded through a clearing house. They are standard contracts executed on established stock exchanges or well-capitalized clearing houses for which the counterparty risk is very low.

The credit risk associated with derivative financial instruments traded over the counter refers to the risk that a counterparty will fail to honour its contractual obligations toward Desjardins Group at a time when the fair value of the instrument is positive for Desjardins. This risk normally represents a small fraction of the notional amount. It is quantified using two measurements, namely replacement cost and the credit risk equivalent. Replacement cost refers to the current replacement cost of all contracts with a positive fair value. Credit risk equivalent is equal to the sum of this replacement cost and the potential credit exposure. Desjardins Group also limits counterparty risk exposure by entering into master agreements called International Swaps and Derivatives Association (ISDA) agreements, which define the terms and conditions for the transactions. These agreements provide for netting to determine the net exposure in the event of default. In addition, a Credit Support Annex can be added to the master agreement in order to request the counterparties to pay or secure the current market value of the positions when such value exceeds a certain threshold, which has been set at zero for its main counterparties. The value of these different measures and the impact of the master netting agreements is presented in Note 19, "Derivative financial instruments and hedging activities", to the Combined Financial Statements.

Desjardins Group also limits its risk by doing business with counterparties that have a high credit rating. Note 19, "Derivative financial instruments and hedging activities", to the Combined Financial Statements presents derivative financial instruments by credit risk rating and type of counterparty. Based on replacement cost, this note indicates that substantially all of Desjardins Group's counterparties have credit ratings ranging from AAA to A-. Furthermore, by purchasing hedges through credit derivatives, such as credit default swaps and total return swaps, Desjardins Group can transfer credit risk to a counterparty or hedge itself against various types of risk.

Securities lending transactions are regulated by Investment Industry Regulatory Organization of Canada participation agreements. Desjardins Group also uses netting agreements with its counterparties to mitigate its credit risk exposure and requires a percentage of collateralization (a pledge) on these transactions.

Desjardins Group accepts from its counterparties only financial collateral that complies with the eligibility criteria set out in its policies. These criteria allow for the timely realization of collateral, if necessary, in the event of default. The types of collateral received and pledged by Desjardins Group are mainly cash and government securities.

Additional information about credit risk is presented in Note 5, "Offsetting financial assets and liabilities", Note 19, "Derivative financial instruments and hedging activities", and Note 29, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

Market risk

Market risk refers to the risk of changes in the fair value of financial instruments resulting from fluctuations in the parameters affecting this value, in particular, interest rates, exchange rates, credit spreads and their volatility.

Desjardins Group is exposed to market risk through its trading activities, which result primarily from short-term transactions conducted with the intention of profiting from current price movements or to provide arbitrage revenue. Desjardins Group is also exposed to market risk through its non-trading activities, which group together mainly asset/liability management transactions in the course of its traditional banking activities as well as investment portfolios related to its insurance operations. Desjardins Group and its components have adopted policies that set out the principles, limits and procedures to use in managing market risk.

GOVERNANCE

Desjardins Group's components are primarily structured into different legal entities to deliver products and services that can be distributed to Desjardins Group members and clients. These legal entities manage financial instruments exposed to market risk and are subject to different regulatory environments such as the banking, securities brokerage, wealth management, life and health insurance and property and casualty insurance industries. The board of directors of these entities delegate to various committees the responsibility of setting up systems and procedures to establish measures adapted to their operations and regulatory environments. These measures, together with the appropriate follow-up procedures, are incorporated into their respective policies and guidelines. The function of the Risk Management Executive Division is to monitor these measures and ensure compliance with the said policies. The main measures used and their follow-up processes are described below.

Link between market risk and the Combined Balance Sheets

Table 38 presents the link between the main Combined Balance Sheet data and the positions included in its trading activities and non-trading activities. The principal market risks associated with non-trading activities are also indicated in the table.

Table 38 – Link between market risk and the Combined Balance Sheets
As at December 31, 2017

(in millions of dollars)	Combined Balance Sheets	Exposed to market risk: Trading activities[1]	Exposed to market risk: Non trading activities[2]	Not exposed to market risk	Principal risks associated with non-trading activities
Assets					
Cash and deposits with financial institutions	$ 2,435	$ -	$ 2,435	$ -	Interest rate
Securities					
Securities at fair value through profit or loss	31,654	13,112	18,542	-	Interest rate
Available-for-sale securities	24,934	-	24,934	-	Interest rate, FX, price
Securities borrowed or purchased under reverse repurchase agreements	8,674	8,320	354	-	Interest rate
Net loans and acceptances	177,521	-	177,521	-	Interest rate
Segregated fund net assets	13,379	-	13,379	-	Interest rate, price
Derivative financial instruments	3,206	248	2,958	-	Interest rate, FX, price
Other assets	13,292	-	-	13,292	
Total assets	$ 275,095	$ 21,680	$ 240,123	$ 13,292	
Liabilities and equity					
Deposits	$ 171,586	$ -	$ 171,586	$ -	Interest rate
Commitments related to securities sold short	9,112	9,112	-	-	Interest rate
Commitments related to securities lent or sold under repurchase agreements	10,229	9,566	663	-	Interest rate
Derivative financial instruments	3,094	296	2,798	-	Interest rate, FX, price
Insurance contract liabilities	28,272	-	28,272	-	Interest rate
Segregated fund net liabilities	13,354	-	13,354	-	Interest rate, price
Other liabilities	13,287	-	2,624	10,663	Interest rate
Subordinated notes	1,388	-	1,388	-	Interest rate
Total equity	24,773	-	-	24,773	
Total liabilities and equity	$ 275,095	$ 18,974	$ 220,685	$ 35,436	

Table 38 – Link between market risk and the Combined Balance Sheets (continued)

As at December 31, 2016

(in millions of dollars)	Combined Balance Sheets	Exposed to market risk: Trading activities[1]	Exposed to market risk: Non trading activities[2]	Not exposed to market risk	Principal risks associated with non-trading activities
Assets					
Cash and deposits with financial institutions	$ 1,876	$ -	$ 1,876	$ -	Interest rate
Securities					
Securities at fair value through profit or loss	31,005	12,131	18,874	-	Interest rate
Available-for-sale securities	22,280	-	22,280	-	Interest rate, FX, price
Securities borrowed or purchased under reverse repurchase agreements	7,690	7,134	556	-	Interest rate
Net loans and acceptances	166,026	-	166,026	-	Interest rate
Segregated fund net assets	11,965	-	11,965	-	Interest rate, price
Derivative financial instruments	3,572	192	3,380	-	Interest rate, FX, price
Other assets	13,953	-	-	13,953	
Total assets	$ 258,367	$ 19,457	$ 224,957	$ 13,953	
Liabilities and equity					
Deposits	$ 160,546	$ -	$ 160,546	$ -	Interest rate
Commitments related to securities sold short	8,196	8,196	-	-	Interest rate
Commitments related to securities lent or sold under repurchase agreements	10,323	8,293	2,030	-	Interest rate
Derivative financial instruments	2,057	160	1,897	-	Interest rate, FX, price
Insurance contract liabilities	27,493	-	27,493	-	Interest rate
Segregated fund net liabilities	11,957	-	11,957	-	Interest rate, price
Other liabilities	13,124	-	2,267	10,857	Interest rate
Subordinated notes	1,378	-	1,378	-	Interest rate
Equity	23,293	-	-	23,293	
Total liabilities and equity	$ 258,367	$ 16,649	$ 207,568	$ 34,150	

[1] Trading activity positions for which the risk measure is VaR and SVaR.
[2] Positions mainly related to non-trading banking activities and insurance activities.

MANAGEMENT OF MARKET RISK RELATED TO TRADING ACTIVITIES – VALUE AT RISK

The market risk of trading portfolios is managed on a daily basis under a specific policy. This policy specifies the risk factors that must be measured and the limit for each of these factors as well as the total. Tolerance limits are also provided for various stress testing. Compliance with these limits is monitored daily and a market risk dashboard is produced on a daily basis and sent to senior management. Any limit exceeded is immediately analyzed and the appropriate action is taken.

The main tool used to measure this risk is "Value at Risk" (VaR). VaR is an estimate of the potential loss over a certain time interval at a given confidence level. A Monte Carlo VaR is calculated daily on the trading portfolios, using a 99% confidence level and a holding horizon of one day. It is therefore reasonable to expect a loss exceeding the VaR figure once every 100 days. The calculation of VaR is based on historical data for a one-year interval.

In addition to aggregate VaR, Desjardins Group also calculates an aggregate stressed VaR (SVaR). It is calculated in the same way as aggregate VaR, except for the use of historical data. Therefore, instead of using the interval of the past year, the aggregate SVaR takes into account the historical data for a crisis period of one year from September 2008.

Table 39 presents the aggregate VaR and the aggregate SVaR for Desjardins Group's trading activities by risk category as well as the diversification effect. Equity price risk, foreign exchange risk, interest rate risk and specific interest rate risk are the four risk categories to which Desjardins Group is exposed. These risk factors are taken into account in measuring the market risk of the trading portfolio. They are reflected in the VaR table presented below. The definition of a trading portfolio meets the various criteria defined in the Basel Capital Accord.

Table 39 – VaR by risk category (trading portfolio)*

(in millions of dollars)	As at December 31, 2017	For the year ended December 31, 2017			As at December 31, 2016	For the year ended December 31, 2016		
		Average	High	Low		Average	High	Low
Equities	**$ 0.5**	**$ 0.3**	**$ 1.6**	**$ 0.1**	$ 0.3	$ 0.2	$ 2.4	$ -
Foreign exchange	**0.4**	**0.3**	**1.8**	**-**	0.1	0.3	1.9	0.1
Interest rate	**2.1**	**3.0**	**5.1**	**1.8**	3.0	3.2	5.2	1.7
Specific interest rate risk[1]	**4.3**	**5.2**	**8.2**	**2.5**	3.0	4.6	7.3	2.3
Diversification effect[2]	**(5.1)**	**(5.7)**	**N/A[3]**	**N/A[3]**	(3.4)	(5.0)	N/A[3]	N/A[3]
Aggregate VaR	**$ 2.2**	**$ 3.1**	**$ 5.1**	**$ 2.0**	$ 3.0	$ 3.3	$ 5.2	$ 1.7
Aggregate SVaR	**$ 11.1**	**$ 11.9**	**$ 19.7**	**$ 8.2**	$ 8.7	$ 9.1	$ 13.3	$ 4.2

(1) Specific risk is the risk directly related to the issuer of a financial security, independent of market events. A portfolio approach is used to distinguish the specific risk from the general market risk. This approach consists of creating a sub-portfolio that contains the positions involving the specific risk of the issuer, such as provinces, municipalities and companies, and a sub-portfolio that contains the positions considered to be without issuer risk, such as governments in the local currency.
(2) Refers to the risk reduction related to diversification, namely the difference between the sum of the VaR of the various market risks and the aggregate VaR.
(3) The highs and lows of the various market risk categories can refer to different dates.

The average of the trading portfolio's aggregate VaR was $3.1 million for 2017, down $0.2 million compared to 2016, mainly as a result of a decrease in the average of the interest rate VaR. As for the average of the aggregate SVaR, it was $11.9 million for 2017, up $2.8 million compared to 2016. It should be noted that there was no change in the model or assumption in the past fiscal year.

Aggregate VaR and aggregate SVaR are appropriate measures for a trading portfolio but they must be interpreted by taking into account certain limits, in particular the following ones:

- these measures do not allow future losses to be predicted if the actual market fluctuations differ markedly from those used to do the calculations;
- these measures are used to determine the potential losses for a one-day holding period, and not the losses on positions that cannot be liquidated or hedged during this one-day period;
- these measures do not provide information on potential losses beyond the selected confidence level of 99%.

Given these limits, the process of monitoring trading activities using VaR is supplemented by stress testing and by establishing limits in this regard.

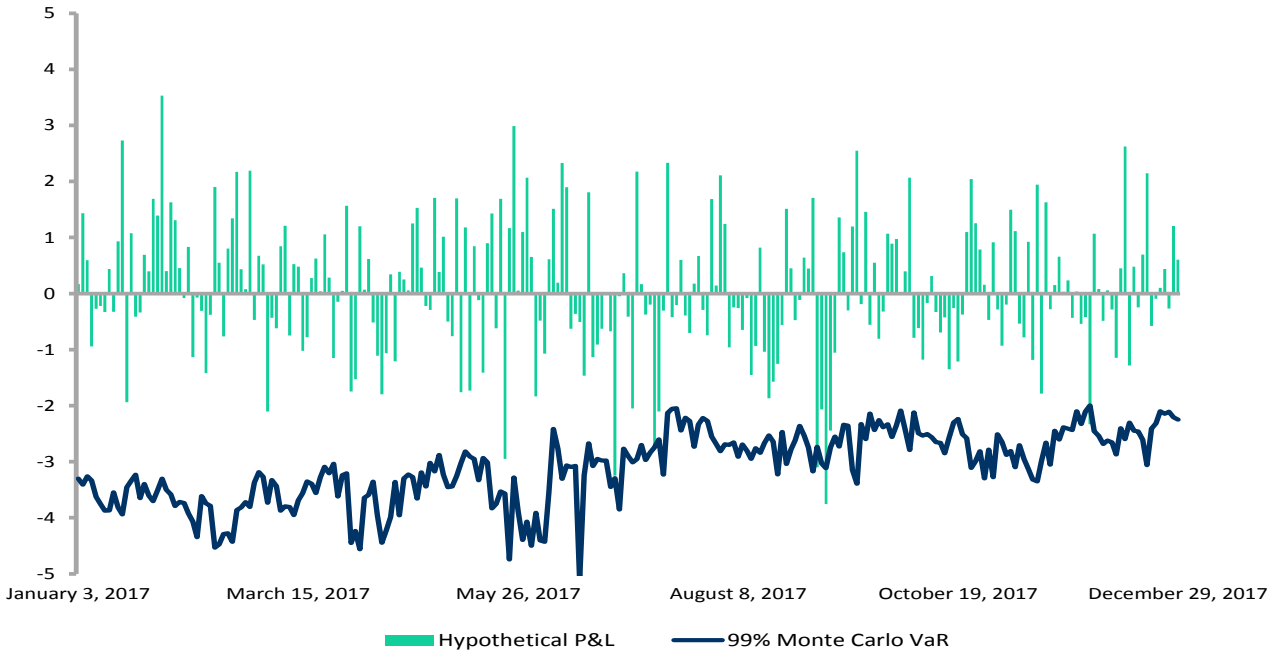
Back testing

Back testing, which is a daily comparison of the VaR with the profits and losses (P&L) on portfolios, is conducted to validate the VaR model used by ensuring that hypothetical results correspond statistically to those of the VaR model. In addition, an independent modelling validation unit works on the model every year.

Desjardins Group performs back testing daily, applying a hypothetical P&L to its trading portfolios. The hypothetical P&L is calculated by determining the difference in value resulting from changes in market conditions between two consecutive days. The portfolio mix between these two days remains static.

The following chart presents changes in VaR for trading activities as well as hypothetical P&L related to these activities for 2017. Hypothetical P&L was exceeded four times during the year. Three overages of $0.04 million, $0.4 million and $0.6 million of hypothetical P&L were observed on July 11, September 1 and September 6, respectively. These overages were due in particular to exposure to a reduction in the Canadian government's 30-year interest rate. Another overage of $0.3 million of hypothetical P&L was observed on November 30 as a result of interest rate fluctuations. In spite of these overages, the VaR model remains adequate.

VaR compared to hypothetical P&L for trading activities
(in millions of dollars)



Stress testing

Certain events that are considered highly unlikely and that may have a significant impact on trading portfolios may occur from time to time. These events are at the tail-end of the distribution and are the result of extreme situations. Use of a stress-testing program is required to assess the impact of these potential situations.

The stress-testing program used for trading portfolios includes historical, hypothetical and sensitivity scenarios based, for instance, on events such as 9/11 or the 2008 credit crisis. Using such stress testing, changes can be monitored in the market value of positions held depending on various scenarios. Most stress-testing is predictive. For a given stress test, shocks are applied to certain risk factors (interest rates, exchange rates, commodities) and the effects of these shocks are passed on to all the risk factors taking historical correlations into account. The running of each stress test is considered to be independent of the others. In addition, certain stress testing is subject to limit tracking. Stress-testing results are analyzed and reported daily using a dashboard, together with VaR calculations, in order to detect vulnerability to such events. The stress-testing program is reviewed periodically to ensure that it is kept current.

STRUCTURAL INTEREST RATE RISK MANAGEMENT

Desjardins Group is exposed to structural interest rate risk, which represents the potential impact of interest rate fluctuations on net interest income and the economic value of equity. This risk is the main component of market risk for Desjardins Group's traditional banking activities other than trading, such as accepting deposits and granting loans, as well as for its securities portfolios used for long-term investment purposes and as liquidity reserves.

Interest rate sensitivity is based on the earlier of the repricing or the maturity date of the assets, liabilities and derivative financial instruments used to manage structural interest rate risk. The situation presented reflects the position only on the date indicated and can change significantly in subsequent years depending on the preferences of Desjardins Group members and clients, and the application of policies on structural interest rate risk management.

Some Combined Balance Sheet items are considered non-interest-rate-sensitive instruments, including investments in equities, non-performing loans, non-interest-bearing deposits, non-maturity deposits with an interest rate not referenced to a specific rate (such as the prime rate), and equity. As dictated in its policies, Desjardins Group's management practices are based on prudent assumptions with respect to the maturity profile used in its models to determine the interest rate sensitivity of such instruments.

In addition to the total sensitivity gap, the main structural interest rate risk factors are:
- the trend in interest rate level and volatility;
- the changes in the shape of the interest rate curve;
- member and client behaviour in their choice of products;
- the financial intermediation margin;
- the optionality of the various financial products offered.

In order to mitigate risk factors, sound and prudent management is applied to optimize net interest income while minimizing the negative incidence of interest rate movements. The established policies describe the principles, limits and procedures that apply to structural interest rate risk management. Simulations are used to measure the effect of different variables on changes in net interest income and the economic value of equity. These policies specify the structural interest rate risk factors, the risk measures selected, the risk tolerance levels and the management limits as well as the procedures in the event that limits are exceeded. Structural interest rate risk is assessed at the required frequency according to portfolio volatility (daily, monthly and quarterly).

The assumptions used in the simulations are based on an analysis of historical data and on the effects of various interest rate environments on changes in such data. These assumptions concern changes in the structure of assets and liabilities, including modelling for non-maturity deposits and equity, in member and client behaviour, and in pricing. Desjardins Group's asset and liability management committee (the Asset/Liability Committee) is responsible for analyzing and approving the global matching strategy on a monthly basis while respecting the parameters defined in structural interest rate risk management policies.

Table 40 presents the potential impact before income taxes, with regard to structural interest rate risk management associated with banking activities, of a sudden and sustained 100 basis point increase or decrease in interest rates on net interest income and the economic value of equity for Desjardins Group. The impact related to insurance activities is presented in Note 1 of this table.

Table 40 – Interest rate sensitivity (before income taxes)[1]*

As at December 31

(in millions of dollars)	2017		2016	
	Net interest income[2]	**Economic value of equity[3]**	Net interest income[2]	Economic value of equity[3]
Impact of a 100-basis-point increase in interest rates	**$ (11)**	**$ 60**	$ (47)	$ 4
Impact of a 100-basis-point decrease in interest rates [4]	**(27)**	**(79)**	(21)	77

(1) Interest rate sensitivity related to insurance activities is not reflected in the amounts above. For these activities, a 100-basis-point increase in interest rates would result in a $226 million decrease in the economic value of equity before taxes as at December 31, 2017, and a $205 million decrease as at December 31, 2016. A 100-basis-point decrease in interest rates would result in an increase of $205 million in the economic value of equity before taxes as at December 31, 2017, and of $177 million as at December 31, 2016. Additional information is provided in the " Interest rate risk management" section of Note 15, " Insurance contract liabilities", to the Combined Financial Statements.

(2) Represents the interest rate sensitivity of net interest income for the next 12 months.

(3) Represents the sensitivity of the present value of assets, liabilities and off-balance sheet instruments.

(4) The results of the impact of a decrease in interest rates take into consideration the use of a floor to avoid negative interest rates.

FOREIGN EXCHANGE RISK MANAGEMENT

Foreign exchange risk arises when the actual or expected value of assets denominated in a foreign currency is higher or lower than that of liabilities denominated in the same currency.

In certain specific situations, Desjardins Group and its components may become exposed to foreign exchange risk, particularly with respect to the U.S. dollar and the euro. This exposure mainly arises from their intermediation activities with members and clients, and their financing and investment activities. A Desjardins Group policy on market risk has set foreign exchange risk exposure limits, which are monitored by the Risk Management Executive Division. To ensure that this risk is properly controlled, Desjardins Group and its components also use, among other things, derivative financial instruments such as forward exchange contracts and currency swaps. Desjardins Group's residual exposure to this risk is low because it reduces its foreign exchange risk by using derivative financial instruments.

PRICE RISK MANAGEMENT

In its non-trading activities, Desjardins Group is exposed to price risk, related mainly to components that operate in insurance and their investment portfolios. *Price risk is the risk of potential loss resulting from a change in the market value of assets (shares, commodities, real estate properties, index-based assets) but not resulting from a change in interest rates or foreign exchange rates, or in the credit quality of a counterparty.*

Management of price risk related to real estate activities

The insurance components may be exposed to changes in the real estate market through the properties they own, whose market value may fluctuate. They manage this risk using policies that set out diversification limits such as geographic limits and limits for real estate property categories. Each real estate investment is subject to an annual professional appraisal to determine its market value in accordance with the standards prescribed by regulatory authorities.

Management of price risk related to stock markets

The insurance components may also be exposed to price risk related to stock markets, particularly through the equity securities and derivative financial instruments they hold as well as the minimum guarantees provided under segregated fund contracts, whose value is affected by market fluctuations. They manage this risk using the different limits set in policies and a hedging program to mitigate the effect of market volatility. For additional information, see Note 15, "Insurance contract liabilities", to the Combined Financial Statements.

Liquidity risk

Liquidity risk refers to Desjardins Group's capacity to raise the necessary funds (by increasing liabilities or converting assets) to meet a financial obligation, whether or not it appears on the Combined Balance Sheets.

Desjardins Group manages liquidity risk in order to ensure that it has timely and cost-effective access to the funds needed to meet its financial obligations as they become due, in both routine and crisis situations. Managing this risk involves maintaining a sufficient level of liquid securities, ensuring stable and diversified sources of financing, monitoring indicators and having a contingency plan in the event of a liquidity crisis.

Liquidity risk management is a key component of the overall risk management strategy. Desjardins Group and its components have established policies describing the principles, limits, risk appetite thresholds as well as the procedures that apply to liquidity risk management. These policies are reviewed on a regular basis to ensure that they are appropriate for the operating environment and prevailing market conditions. They are also updated to reflect regulatory requirements and sound liquidity risk management practices. Given that the insurance companies are subject to specific regulatory requirements, they manage their liquidity risks based on their own needs while following Desjardins Group guidelines. The securities held by these components are not taken into account in the valuation of Desjardins Group's liquidity reserves, since they cannot be used by Desjardins Group's Treasury to generate liquidity for other components.

Desjardins Group's Treasury ensures stable and diversified sources of institutional funding by type, source and maturity. It uses a wide range of financial products and borrowing programs on various markets for its funding needs. Through these operations, the funding needs of Desjardins Group components can be satisfied under conditions comparable to those offered on capital markets.

Furthermore, Desjardins Group issues covered bonds and securitizes CHMC-insured loans in the course of its normal operations. Desjardins Group is also eligible for the Bank of Canada's various intervention programs and loan facilities for Emergency Lending Assistance advances.

The implementation of Basel III strengthens international minimum liquidity requirements through the application of a liquidity coverage ratio (LCR), a net stable funding ratio (NSFR) and the use of Net Cumulative Cash Flow (NCCF). Under its liquidity risk management policy, Desjardins Group already produces these two ratios as well as the NCCF, and reports them on a regular basis to the AMF. The effective date of the regulatory requirements concerning the NSFR has been postponed to January 1, 2019, and Desjardins Group intends to comply with the NSFR requirements once they become effective.

Applying the calculation rules established by the Basel Committee on Banking Supervision and incorporated in the AMF's Liquidity Adequacy Guideline, Desjardins Group's average LCR was 121.4% for the quarter ended December 31, 2017, compared to 119.9% for the previous quarter. The AMF requires that the ratio be greater than or equal to 100% in the absence of stressed conditions. This ratio is proactively managed by Desjardins Group's Treasury, and an appropriate level of high-quality liquid assets is maintained for adequate coverage of the theoretical cash outflows associated with the standardized crisis scenario within the Basel III framework. Desjardins Group's main sources of theoretical cash outflows are a potential serious run on deposits by members of Desjardins caisses and a sudden drying-up of the short-term institutional funding sources used on a day-to-day basis by Desjardins Group.

Liquidity risk measurement and monitoring

Desjardins Group determines its liquidity needs by reviewing its current operations and evaluating its future forecasts for balance sheet growth and institutional funding conditions. Various analyses are used to determine the actual liquidity levels of assets and the stability of liabilities based on observed behaviours or contractual maturities. Maintaining liquidity reserves of high-quality assets is required to offset potential cash outflows following a disruption in capital markets, or events that would restrict its access to funding or result in a serious run on deposits.

The minimum liquid asset levels to be maintained by Desjardins Group are specifically prescribed by policies. Daily management of these securities and the reserve level to be maintained is centralized at Desjardins Group Treasury and is subject to monitoring by the Risk Management function under the supervision of the Finance and Risk Management Committee. Securities eligible for liquidity reserves must meet high security and negotiability criteria and provide assurance of their adequacy in the event of a severe liquidity crisis. The securities held are largely Canadian government securities.

In addition to complying with regulatory ratios, a Desjardins-wide stress testing program has been set up. This program incorporates the concepts put forward by the Basel Committee on Banking Supervision in "Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring". The scenarios, based on a downgrade of Desjardins Group combined with a shock on capital markets, make it possible to:

- measure the extent, over a one-year period, of potential cash outflows in a crisis situation;
- implement liquidity ratios and levels to be maintained across Desjardins Group;
- assess the potential marginal cost of such events, depending on the type, severity and level of the crisis.

The calculations are performed daily to ensure compliance with the liquidity levels to be maintained based on the acute stress scenarios.

Liquid assets

Table 41 presents a summary of Desjardins Group's liquid assets, which do not include assets held by the insurance subsidiaries because these assets are committed to covering insurance liabilities and not the liquidity needs of Desjardins Group's other components. Liquid assets constitute Desjardins Group's primary liquidity reserve for all its operations. Encumbered liquid assets mainly include liquid assets that are pledged as collateral or cannot be used as a result of regulatory requirements or internal policies.

Table 41 – Liquid assets[1]

As at December 31, 2017

(in millions of dollars)	Liquid assets held by Desjardins Group	Securities held as collateral - Securities financing and derivatives trading	Total liquid assets	Encumbered liquid assets	Unencumbered liquid assets
Cash and deposits with financial institutions	**$ 1,453**	**$ -**	**$ 1,453**	**$ -**	**$ 1,453**
Securities					
Issued or guaranteed by Canada, provinces and municipal corporations in Canada, school or public corporations in Canada, and foreign public administrations	**27,112**	**8,644**	**35,756**	**19,773**	**15,983**
Other securities in Canada	**3,441**	**82**	**3,523**	**49**	**3,474**
Issued or guaranteed by foreign issuers	**58**	**-**	**58**	**-**	**58**
Loans					
Insured residential mortgage-backed securities	**6,733**	**-**	**6,733**	**1,240**	**5,493**
Total	**$ 38,797**	**$ 8,726**	**$ 47,523**	**$ 21,062**	**$ 26,461**

As at December 31, 2016

(in millions of dollars)	Liquid assets held by Desjardins Group	Securities held as collateral - Securities financing and derivatives trading	Total liquid assets	Encumbered liquid assets	Unencumbered liquid assets
Cash and deposits with financial institutions	$ 1,532	$ -	$ 1,532	$ -	$ 1,532
Securities					
Issued or guaranteed by Canada, provinces and municipal corporations in Canada, school or public corporations in Canada, and foreign public administrations	25,986	8,544	34,530	18,899	15,631
Other securities in Canada	1,381	21	1,402	9	1,393
Issued or guaranteed by foreign issuers	46	-	46	-	46
Loans					
Insured residential mortgage-backed securities	4,018	-	4,018	1,254	2,764
Total	$ 32,963	$ 8,565	$ 41,528	$ 20,162	$ 21,366

(1) Excluding assets held by insurance subsidiaries.

Table 42 – Unencumbered liquid assets by entity[1]

As at December, 31

(in millions of dollars)	2017	2016[2]
Federation	**$ 7,556**	$ 8,286
Caisse network	**14,456**	10,098
Desjardins Securities[2]	**1,217**	676
Other entities	**3,232**	2,306
Total	**$ 26,461**	$ 21,366

(1) Excluding assets held by insurance subsidiaries. Substantially all unencumbered liquid assets presented in this table are issued in Canadian dollars.
(2) Does not take into consideration amounts payable and receivable related to the settlement of securities lending and borrowing transactions.

Liquidity risk indicators

The purpose of monitoring liquidity indicators daily is to quickly identify a lack of liquidity, whether potential or real, within Desjardins Group and on capital markets. Warning levels subject to an escalation process are established for each of these indicators. If one or more indicators trigger a warning level, the Desjardins Group Finance and Risk Management Committee is immediately alerted. This committee would also act as a crisis committee should the contingency plan be put into action.

This plan lists the sources of liquidity available in exceptional situations. In addition, it lays down the decision-making and information process based on the severity level of a potential crisis. The aim of the plan is to allow quick and effective intervention in order to minimize disruptions caused by sudden changes in member and client behaviour and potential disruptions in capital markets or economic conditions. Furthermore, in the event of a crisis extensive enough to question Desjardins Group's creditworthiness, a living will has been prepared to enable the crisis committee to draw on a broader range of liquidity sources to deal with the situation.

Encumbered assets

In the normal course of its operations, Desjardins Group pledges securities, loans and other assets as collateral, mainly with regard to financing operations, participation in clearing and payments systems and operations related to provisions for claims and adjustment expenses. Table 43 presents, for all assets on the Combined Balance Sheets and securities held as collateral, those that are encumbered as well as those that may be pledged as collateral as part of financing or other transactions.

Table 43 – Encumbered assets

As at December 31, 2017

				Breakdown of total assets			
				Encumbered assets		Unencumbered assets	
(in millions of dollars)	Combined Balance Sheet assets	Securities held as collateral	Total assets	Pledged as collateral	Other[1]	Available as collateral	Other[2]
Cash and deposits with financial institutions	$ 2,435	$ -	$ 2,435	$ -	$ 42	$ 1,499	$ 894
Securities	56,588	2,255	58,843	21,371	2,614	11,494	23,364
Securities borrowed or purchased under reverse repurchase agreements	8,674	-	8,674	-	-	8,532	142
Net loans and acceptances	177,521	-	177,521	19,477	-	67,526	90,518
Segregated fund net assets	13,379	-	13,379	-	-	-	13,379
Other assets	16,498	-	16,498	-	-	-	16,498
Total	**$ 275,095**	**$ 2,255**	**$ 277,350**	**$ 40,848**	**$ 2,656**	**$ 89,051**	**$ 144,795**

As at December 31, 2016

				Breakdown of total assets			
				Encumbered assets		Unencumbered assets	
(in millions of dollars)	Combined Balance Sheet assets	Securities held as collateral	Total assets	Pledged as collateral	Other[1]	Available as collateral	Other[2]
Cash and deposits with financial institutions	$ 1,876	$ -	$ 1,876	$ -	$ 33	$ 1,528	$ 315
Securities	53,285	1,332	54,617	18,544	4,182	10,199	21,692
Securities borrowed or purchased under reverse repurchase agreements	7,690	-	7,690	-	-	7,509	181
Net loans and acceptances	166,026	-	166,026	19,117	-	75,227	71,682
Segregated fund net assets	11,965	-	11,965	-	-	-	11,965
Other assets	17,525	-	17,525	-	-	-	17,525
Total	$ 258,367	$ 1,332	$ 259,699	$ 37,661	$ 4,215	$ 94,463	$ 123,360

(1) Assets that cannot be used for legal or other reasons, such as ABTN.
(2) "Other" unencumbered assets include those of the insurance companies as well as assets that in management's opinion would not be immediately available for collateral or financing purposes in their current form.

Liquidity coverage ratio

The Basel Committee on Banking Supervision has developed a liquidity coverage ratio (LCR) to promote the short-term resilience of the liquidity risk profile of financial institutions. The LCR is the ratio of a stock of unencumbered high-quality liquid assets (HQLA) to net cash outflows over the next 30 days in the event of an acute liquidity stress scenario.

Under the AMF's Liquidity Adequacy Guideline, HQLA eligible for the purpose of calculating the LCR consist of assets that can be converted quickly into cash at little or no loss of value on capital markets. For Desjardins Group, such high-quality liquid assets are comprised essentially of cash and highly rated securities issued or guaranteed by various levels of government. The AMF Guideline also prescribes weightings for cash inflows and outflows.

The table below presents quantitative information regarding the LCR, based on the model recommended for disclosure requirements by the Basel Committee on Banking Supervision.

Table 44 – Liquidity coverage ratio[1]

(in millions of dollars and as a percentage)	For the quarter ended December 31, 2017		For the quarter ended September 30, 2017
	Total non-weighted value[2] **(average**[4]**)**	**Total weighted value**[3] **(average**[4]**)**	Total weighted value[3] (average[4])
High-quality liquid assets			
Total high-quality liquid assets	**N/A**	**$ 22,342**	$ 22,366
Cash outflows			
Retail deposits and small business deposits, including:	**$ 67,626**	**$ 4,458**	$ 4,377
Stable deposits	**32,923**	**988**	1,001
Less stable deposits	**34,703**	**3,470**	3,376
Unsecured wholesale funding, including:	**21,890**	**12,947**	13,658
Operational deposits (all counterparties) and deposits in cooperative bank networks	**4,559**	**1,053**	1,139
Non-operational deposits (all counterparties)	**9,220**	**3,783**	3,699
Unsecured debt	**8,111**	**8,111**	8,820
Secured wholesale funding	**N/A**	**-**	-
Additional requirements, including:	**11,528**	**3,105**	2,808
Outflows related to exposures on derivatives and other collateral required	**1,614**	**1,496**	1,411
Outflows related to funding loss on debt products	**206**	**206**	-
Credit and liquidity facilities	**9,708**	**1,403**	1,397
Other contractual funding liabilities	**918**	**93**	30
Other contingent funding liabilities	**64,217**	**1,720**	1,658
Total cash outflows	**N/A**	**$ 22,323**	$ 22,531
Cash inflows			
Secured loans (e.g. reverse repurchase agreements)	**$ 4,274**	**$ 79**	$ 129
Inflows related to completely effective exposures	**3,025**	**1,515**	1,514
Other cash inflows	**2,324**	**2,324**	2,232
Total cash inflows	**$ 9,623**	**$ 3,918**	$ 3,875

	Total adjusted value[5]	Total adjusted value[5]
Total high-quality liquid assets	**$ 22,342**	$ 22,366
Total net cash outflows	**18,405**	18,656
Liquidity coverage ratio	**121.4%**	119.9%

(1) Excluding the insurance subsidiaries.
(2) The non-weighted values of cash inflows and outflows represent unpaid balances either maturing or falling due and payable within 30 days.
(3) Weighted values are calculated after the "haircuts" prescribed for high quality liquid assets and the rates prescribed for cash inflows and outflows have been applied.
(4) The ratio is presented based on the average of daily data for the quarter.
(5) The total adjusted value takes into account, if applicable, the caps prescribed by the AMF for high-quality liquid assets and cash inflows.

SOURCES OF FINANCING

Core funding, which includes capital, long-term liabilities and a diversified deposit portfolio, is the foundation upon which Desjardins Group's liquidity position depends. The solid base of deposits from individuals combined with wholesale funding, diversified in terms of the programs used as well as the staggering of contractual maturities, allows Desjardins Group to maintain high regulatory liquidity ratios while ensuring their stability. Total deposits, including wholesale funding, presented on the Combined Balance Sheets amounted to $171.6 billion as at December 31, 2017, up $11.0 billion since December 31, 2016. Additional information on deposits is found in Section 3.1 "Balance sheet management" of this MD&A.

Financing programs and strategies

As Desjardins Group's treasurer, the Federation meets the needs of the organization's members and clients. Its first priority is to implement appropriate strategies to identify, measure and manage risks, which strategies are regulated by policies. In 2017, the Federation succeeded in maintaining a liquidity level sufficient to meet Desjardins Group's needs through its strict treasury policy, solid institutional financing and the contribution of the caisse network. Short-term wholesale financing is used to finance very liquid assets while long-term wholesale financing is mainly used to finance less liquid assets and to support reserves of liquid assets.

In order to secure long-term financing at the lowest cost on the market, the Federation maintains an active presence in the federally-guaranteed mortgage loan securitization market under the *National Housing Act* (NHA) Mortgage-Backed Securities Program. In addition, to ensure stable financing, it diversifies its sources from institutional markets. It therefore regularly resorts to the capital markets when conditions are favourable, and makes public and private issues of term notes on Canadian, U.S. and European markets as required.

The main programs currently used by the Federation are:

Table 45 – Main financing programs
As at December 31, 2017

Financing program	Maximum authorized amount
Medium-term notes (Canadian)	**$7 billion**
Covered bonds (multi-currency)	**$10 billion**[1]
Short-term notes (European)	**€3 billion**
Short-term notes (U.S.)	**US$15 billion**
Medium-term notes (multi-currency)	**€7 billion**

[1] This maximum authorized amount covers the Federation's Structured Covered Bond Program and its Legislative Covered Bond Program.

The following table presents the remaining term to maturity of wholesale funding.

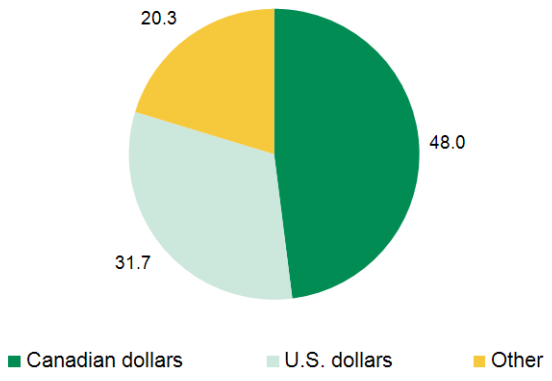
Table 46 – Remaining contractual term to maturity of wholesale funding
As at December 31

(in millions of dollars)	2017								2016
	Less than 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Total – Less than one year	1 to 2 years	Over 2 years	Total	Total
Bearer discount notes	**$ 2,011**	**$ 757**	**$ 17**	**$ 17**	**$ 2,802**	**$ -**	**$ -**	**$ 2,802**	$ 1,908
Commercial paper	**3,856**	**2,614**	**1,101**	**1,705**	**9,276**	**-**	**-**	**9,276**	5,842
Medium-term notes	**2,764**	**-**	**-**	**1,249**	**4,013**	**688**	**6,329**	**11,030**	10,938
Mortgage securitization	**-**	**383**	**556**	**814**	**1,753**	**1,626**	**5,751**	**9,130**	7,975
Covered bonds	**-**	**-**	**-**	**-**	**-**	**3,012**	**1,505**	**4,517**	6,255
Subordinated notes	**-**	**-**	**-**	**-**	**-**	**-**	**1,388**	**1,388**	1,378
Total	**$ 8,631**	**$ 3,754**	**$ 1,674**	**$ 3,785**	**$ 17,844**	**$ 5,326**	**$ 14,973**	**$ 38,143**	$ 34,296
Including:									
Secured	**$ -**	**$ 383**	**$ 556**	**$ 814**	**$ 1,753**	**$ 4,638**	**$ 8,644**	**$ 15,035**	$ 15,608
Unsecured	**8,631**	**3,371**	**1,118**	**2,971**	**16,091**	**688**	**6,329**	**23,108**	18,688

Desjardins Group's total wholesale funding presented in the table above was carried out by the Federation, except for the subordinated notes, which were issued by Desjardins Capital Inc. Total wholesale funding was up $3.8 billion compared to December 31, 2016, mainly because of an increase in commercial paper.

In addition, Desjardins Group diversifies its financing sources in order to limit its dependence on a single currency. The chart "Wholesale funding by currency" presents a breakdown of borrowings on the markets and subordinated notes by currency. These funds are obtained primarily through short- and medium-term notes, mortgage securitization, covered bonds and subordinated notes.

Wholesale funding by currency
As at December 31, 2017
(as a percentage)



In 2017, the Federation also participated in new issues under the NHA Mortgage-Backed Securities Program for a total amount of $2.4 billion. During the same period, it also completed two issues under its Canadian medium-term note program for a total amount of $1.9 billion and an issue of US$300 million under its multi-currency medium-term note program. Also note that on October 31, 2017, the Federation launched a new issue of US$1.5 billion under its multi-currency medium-term note program.

Outstanding notes issued under the Federation's medium-term financing programs amounted to $24.7 billion as at December 31, 2017, compared to $25.2 billion a year earlier. The outstanding notes for these issues are presented under "Deposits – Business and government" in the Combined Balance Sheets. Desjardins Capital Inc.'s senior notes outstanding totalled $1.4 billion as at December 31, 2017, unchanged from a year earlier. Furthermore, to round out its financing and increase its capital base, in 2017, Desjardins Group, through the Federation, issued F capital shares for proceeds of $244 million, net of certain items, as well as F capital shares having a value of $125 million for the payment of interest when the holder has elected to receive remuneration in F capital shares.

Overall, these transactions made it possible to adequately meet the liquidity needs of Desjardins Group, to better diversify its sources of financing and to further extend their average term.

CREDIT RATINGS OF SECURITIES ISSUED

Desjardins Group's credit ratings affect its ability to access sources of funding on capital markets, as well as the conditions of such funding. They are also a factor considered in certain Desjardins Group transactions involving counterparties.

Rating agencies assign credit ratings and related ratings outlooks based on their own proprietary methodology, which includes a number of analytical criteria, including factors that are not under Desjardins Group's control. The rating agencies evaluate Desjardins Group primarily on a combined basis and recognize its capitalization, its consistent financial performance, its significant market shares in Quebec and the quality of its assets. Consequently, the credit ratings of the Federation, a reporting issuer, and of Desjardins Capital Inc., a venture issuer, are backed by Desjardins Group's financial strength.

During 2017, the credit ratings and outlooks for the securities issued by Desjardins Group remained unchanged and were affirmed by the rating agencies Moody's, Standard & Poor's (S&P), DBRS and Fitch.

In addition, on May 10, 2017, Moody's lowered the long-term debt ratings of the six major Canadian banks by a notch, pointing out in particular that an increase in private sector debt could affect the asset quality and profitability of Canadian banks. In its press release, Moody's nevertheless affirmed the credit ratings of Desjardins Group since it considers Desjardins's operations less exposed to the risks it mentioned.

The ratings outlooks for Desjardins Group from S&P and Fitch are stable, but DBRS's and Moody's outlooks for Desjardins Group and several major Canadian banks have remained negative since May 20, 2015 and June 11, 2014, respectively. However, Moody's ratings outlook for Desjardins Capital Inc. remains stable. DBRS and Moody's justified their decision to assign a negative ratings outlook for Desjardins Group as well as for several major Canadian banks due to uncertainty about continued government support to systemically important financial institutions on account of the "bail-in" regime proposed by the Canadian government.

The Federation and Desjardins Capital Inc. have first-class credit ratings that are among the best of the major Canadian and international banking institutions.

Table 47 – Credit ratings of securities issued

	DBRS	STANDARD & POOR'S	MOODY'S	FITCH
Fédération des caisses Desjardins du Québec				
Short-term	**R-1 (high)**	**A-1**	**P-1**	**F1+**
Medium- and long-term, senior	**AA**	**A+**	**Aa2**	**AA-**
Desjardins Capital Inc.				
Medium- and long-term, senior	**AA (low)**	**A**	**A2**	**A+**

Desjardins Group regularly monitors the additional level of obligations its counterparties would require in the event of a credit rating downgrade for the Federation and Desjardins Capital Inc. This monitoring enables Desjardins Group to assess the impact of such a downgrade on its funding capabilities and its ability to perform transactions in the normal course of its operations as well as ensure that it has the additional liquid assets and collateral necessary to meet its obligations. Currently, Desjardins Group is not obliged to provide additional collateral in the event of its credit rating being lowered three notches by one or several credit rating agencies.

CONTRACTUAL MATURITIES OF ON-BALANCE SHEET ITEMS AND OFF-BALANCE SHEET COMMITMENTS

Table 48 presents assets and liabilities recorded on the Combined Balance Sheets and off-balance sheet commitments at their carrying amount and classified according to their residual contractual maturities. The classification of maturities is an information source with regard to liquidity and financing risk, but it differs from the analysis performed by Desjardins Group to determine the expected maturity of the items for liquidity risk management purposes. Many factors other than contractual maturity are taken into consideration to measure expected future cash flows and liquidity risk.

The value of the credit commitments presented in this table represents the maximum amount of additional credit that Desjardins Group could be required to grant if the commitments were fully used. The value of guarantees and standby letters of credit correspond to the maximum cash outflows that Desjardins Group could be required to make in the event of complete default of the parties to the guarantees, without taking any possible recovery into account. These commitments and guarantees do not necessarily represent future liquidity needs, because a large portion of these instruments will expire or be cancelled without giving rise to any cash outflows.

The table below will henceforth present contractual maturities of on-balance sheet items and off-balance sheet commitments in accordance with the EDTF's recommendations for comparison purposes with other financial institutions. Note 15, "Insurance contract liabilities", provides additional information on the contractual maturities of actuarial liabilities and provisions for claims and adjustment expenses.

Table 48 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments*
As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Assets										
Cash and deposits with financial institutions	$ 2,038	$ 378	$ -	$ -	$ -	$ -	$ -	$ -	$ 19	$ 2,435
Securities										
Securities at fair value through profit or loss[1]	45	541	1,152	835	2,112	2,195	7,181	15,881	1,712	31,654
Available-for-sale securities[1]	2,361	625	948	520	1,576	2,291	10,481	2,854	3,278	24,934
Securities borrowed or purchased under reverse repurchase agreements	8,279	257	123	15	-	-	-	-	-	8,674
Loans										
Residential mortgages[2]	1,793	2,580	6,467	7,356	6,417	20,878	58,935	1,645	7,075	113,146
Consumer, credit card and other personal loans[2]	70	100	221	239	304	1,264	5,007	7,116	9,723	24,044
Business and governments[2]	9,360	3,852	4,166	3,807	3,894	3,014	5,749	2,019	4,877	40,738
Allowance for credit losses	-	-	-	-	-	-	-	-	(438)	(438)
Segregated fund net assets	-	-	-	-	-	-	-	-	13,379	13,379
Clients' liability under acceptances	31	-	-	-	-	-	-	-	-	31
Premiums receivable	170	62	13	3	-	-	-	-	1,847	2,095
Derivative financial instruments	100	115	172	153	158	652	1,723	133	-	3,206
Amounts receivable from clients, brokers and financial institutions	1,518	3	-	-	-	(8)	-	-	41	1,554
Reinsurance assets	35	71	72	63	60	213	423	1,038	227	2,202
Investment property	-	-	-	-	-	-	-	-	832	832
Property, plant and equipment	-	-	-	-	-	-	-	-	1,411	1,411
Goodwill	-	-	-	-	-	-	-	-	121	121
Intangible assets	-	-	-	-	-	-	-	-	466	466
Deferred tax assets	-	-	-	-	-	-	-	-	992	992
Other assets	540	57	163	3	5	8	21	-	1,941	2,738
Assets of the disposal group held to be transferred	-	-	-	-	-	-	-	-	881	881
Total assets	$ 26,340	$ 8,641	$ 13,497	$ 12,994	$ 14,526	$ 30,507	$ 89,520	$ 30,686	$ 48,384	$ 275,095

See page 102 for footnotes.

Table 48 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Liabilities and equity										
Deposits										
Individuals[3]	$ 5,288	$ 2,916	$ 5,291	$ 4,671	$ 5,225	$ 12,145	$ 14,424	$ 565	$ 50,053	$ 100,578
Business and governments[3]	11,096	4,047	2,110	2,126	2,727	6,523	13,507	1,878	25,088	69,102
Deposit-taking institutions[3]	482	2	3	-	1	4	7	-	1,407	1,906
Acceptances	31	-	-	-	-	-	-	-	-	31
Commitments related to securities sold short[4]	155	595	114	108	21	1,366	2,225	4,526	2	9,112
Commitments related to securities lent or sold under repurchase agreements	10,229	-	-	-	-	-	-	-	-	10,229
Derivative financial instruments	151	117	176	126	146	431	1,809	138	-	3,094
Amounts payable to clients, brokers and financial institutions	2,628	1	-	-	-	-	-	-	1,618	4,247
Insurance contract liabilities	411	730	893	831	763	1,879	4,113	16,378	2,274	28,272
Segregated fund net liabilities	-	-	-	-	-	-	-	-	13,354	13,354
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	2,624	2,624
Deferred tax liabilities	-	-	-	-	-	-	-	-	155	155
Other liabilities	1,944	518	771	80	61	168	177	747	1,102	5,568
Liabilities of the disposal group held to be transferred	-	-	-	-	-	-	-	-	662	662
Subordinated notes	-	-	-	-	-	-	898	490	-	1,388
Total equity	-	-	-	-	-	-	-	-	24,773	24,773
Total liabilities and equity	$ 32,415	$ 8,926	$ 9,358	$ 7,942	$ 8,944	$ 22,516	$ 37,160	$ 24,722	$ 123,112	$ 275,095
Off-balance sheet commitments										
Credit commitments[5]	$ 3,568	$ 110	$ 149	$ 225	$ 337	$ 2,957	$ 7,031	$ 243	$ 83,850	$ 98,470
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	2,024	2,024
Commitments under lease contracts	8	16	23	23	22	82	185	287	-	646
Documentary letters of credit	1	2	2	-	2	-	-	-	-	7
Guarantees and standby letters of credit	64	128	134	268	289	15	20	84	1	1,003
Credit default swaps	-	-	-	-	-	-	540	-	-	540

See page 102 for footnotes.

Table 48 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2016[6]

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Assets										
Cash and deposits with financial institutions	$ 1,615	$ 241	$ 3	$ -	$ -	$ -	$ -	$ -	$ 17	$ 1,876
Securities										
Securities at fair value through profit or loss[1]	818	317	1,094	577	1,263	2,564	7,410	15,566	1,396	31,005
Available-for-sale securities[1]	358	321	601	153	410	5,115	8,726	3,494	3,102	22,280
Securities borrowed or purchased under reverse repurchase agreements	7,626	64	-	-	-	-	-	-	-	7,690
Loans										
Residential mortgages[2]	2,075	2,527	5,685	5,792	4,599	20,412	56,485	1,912	7,208	106,695
Consumer, credit card and other personal loans[2]	77	86	191	203	285	1,306	4,629	6,239	9,134	22,150
Business and governments[2]	8,083	3,669	4,228	3,937	4,272	2,374	4,419	1,900	4,744	37,626
Allowance for credit losses	-	-	-	-	-	-	-	-	(456)	(456)
Segregated fund net assets	-	-	-	-	-	-	-	-	11,965	11,965
Clients' liability under acceptances	7	4	-	-	-	-	-	-	-	11
Premiums receivable	165	60	12	2	-	-	-	-	1,718	1,957
Derivative financial instruments	73	696	154	408	414	620	1,186	21	-	3,572
Amounts receivable from clients, brokers and financial institutions	1,895	4	3	-	-	-	-	-	630	2,532
Reinsurance assets	39	78	72	60	56	190	454	1,072	561	2,582
Investment property	-	-	-	-	-	-	-	-	823	823
Property, plant and equipment	-	-	-	-	-	-	-	-	1,435	1,435
Goodwill	-	-	-	-	-	-	-	-	471	471
Intangible assets	-	-	-	-	-	-	-	-	690	690
Deferred tax assets	-	-	-	-	-	-	-	-	874	874
Other assets	626	78	93	20	12	14	32	11	1,703	2,589
Total assets	$ 23,457	$ 8,145	$ 12,136	$ 11,152	$ 11,311	$ 32,595	$ 83,341	$ 30,215	$ 46,015	$ 258,367

See page 102 for footnotes.

Table 48 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2016[6]

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Liabilities and equity										
Deposits										
Individuals[3]	$ 5,686	$ 2,534	$ 5,077	$ 4,025	$ 4,516	$ 12,374	$ 15,176	$ 592	$ 46,298	$ 96,278
Business and governments[3]	7,032	6,129	1,132	3,391	1,720	6,862	12,994	1,239	22,300	62,799
Deposit-taking institutions[3]	109	-	1	-	-	8	6	-	1,345	1,469
Acceptances	7	4	-	-	-	-	-	-	-	11
Commitments related to securities sold short[4]	418	62	315	92	-	1,012	2,208	4,089	-	8,196
Commitments related to securities lent or sold under repurchase agreements	10,323	-	-	-	-	-	-	-	-	10,323
Derivative financial instruments	56	87	118	134	136	502	983	41	-	2,057
Amounts payable to clients, brokers and financial institutions	2,399	4	-	-	-	-	-	-	2,256	4,659
Insurance contract liabilities	406	717	873	783	792	1,917	4,292	15,581	2,132	27,493
Segregated fund net liabilities	-	-	-	-	-	-	-	-	11,957	11,957
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	2,256	2,256
Deferred tax liabilities	-	-	-	-	-	-	-	-	179	179
Other liabilities	1,283	658	800	95	90	232	246	50	2,565	6,019
Subordinated notes	-	-	-	-	-	-	1,378	-	-	1,378
Total equity	-	-	-	-	-	-	-	-	23,293	23,293
Total liabilities and equity	$ 27,719	$ 10,195	$ 8,316	$ 8,520	$ 7,254	$ 22,907	$ 37,283	$ 21,592	$ 114,581	$ 258,367
Off-balance sheet commitments										
Credit commitments[5]	$ 3,591	$ 340	$ 388	$ 816	$ 236	$ 2,438	$ 6,165	$ 256	$ 76,981	$ 91,211
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	1,772	1,772
Commitments under lease contracts	8	16	24	24	24	77	167	174	-	514
Documentary letters of credit	5	9	6	2	3	-	-	-	-	25
Guarantees and standby letters of credit	82	157	210	157	242	44	12	76	2	982
Credit default swaps	-	-	-	-	-	-	644	-	-	644

(1) Equity securities are classified under "No stated maturity".
(2) Amounts repayable on demand and impaired loans are classified under "No stated maturity".
(3) Deposits payable on demand or after notice are considered as having "No stated maturity".
(4) Amounts are presented by remaining contractual maturity of the underlying security.
(5) Includes personal lines of credit, lines of credit secured by real or immovable property and credit card lines for which the amounts committed are unconditionally revocable at any time at Desjardins Group's discretion.
(6) Data for 2016 have been reclassified to conform to the current year's presentation.

Operational risk

Operational risk is the risk of inadequacy or failure attributable to processes, people, internal systems or external events and resulting in losses, failure to achieve objectives or a negative impact on reputation.

Operational risk is inherent to all of Desjardins Group's activities, including management and control activities in other risk areas (credit, market, liquidity, etc.) as well as outsourced activities. This risk may lead to losses mainly resulting from theft, fraud, damage to tangible assets, non-compliance with legislation or regulations, systems failures, unauthorized access to computer systems, cyber threats, or problems or errors in process management. To maintain this risk at an acceptable level, an operational risk management framework has been developed and deployed throughout the organization. The framework includes the usual practices for sound management of operations and is based on the three lines of defence model, clearly defining the roles and responsibilities in risk and operations management.

OPERATIONAL RISK MANAGEMENT FRAMEWORK

The purpose of the operational risk management framework is to identify, measure, mitigate and monitor operational risk as well as make interventions and disclosures for operational risk in accordance with operational risk appetite and the frameworks adopted by the Board of Directors. It is supported by guidelines setting out operational risk management foundations. At the same time, the operational risk management framework connects with the other areas of risk.

The operational risk management framework is reviewed annually to ensure its adequacy and its relevance based on Desjardins Group's risk profile and developments in industry practices.

GOVERNANCE

Risk management governance emphasizes accountability and effective risk oversight. Operational risk is governed by a set of policies, directives and rules. These frameworks are reviewed periodically to ensure consistency with the Integrated Risk Management Framework approved by the Board of Directors.

Reporting is done on a regular basis to the committees that provide risk management oversight so that their members can assess Desjardins Group's operational risk exposure.

Approaches to identifying, measuring and monitoring operational risk

With respect to the operational risk management framework, the following table illustrates the tools and methods used to identify, measure and monitor operational risk.

	Description
Risk identification and measurement	A standard inventory of operational risks to which Desjardins Group is exposed has been prepared and is used as the basis for determining the most significant operational risks and evaluating the effectiveness of the mitigation measures in place to reduce them. The risk and control assessments, carried out on a periodic basis, can be related to projects, products, systems, processes and activities, as well as to strategic initiatives and important new products. Consideration of internal and external events (losses, audit findings, etc.) is an integral part of these assessments. When the results indicate operational risk exposures that exceed the established tolerance level, action plans are prepared to reduce exposure to an acceptable level.
Collection of data on operational losses	The collection of internal data on operational losses is carried out to list and quantify losses according to predetermined thresholds. Operational losses are indexed in a database. Through analysis, causes are better understood, trends are determined, and corrective measures are taken when necessary. In addition, external operational risk events in the industry are monitored to detect potential or emerging risks and increase risk management at Desjardins Group, if need be. The main trends identified through analysis of operational losses are reported to the various committees on a regular basis. During 2017, operational losses were consistent with the limits set for risk appetite by senior management and the Board of Directors. Contingent liabilities, including the impact of litigation, are presented in Note 29, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.
Key risk indicators	To monitor their risk profile and track developments in it, the business segments and support functions establish operational risk indicators to help them proactively monitor any increase in their exposure to the most significant risks and act accordingly when the tolerance level is reached.

	Description
Specialized risk assessment programs	Complementing the operational risk management framework are certain programs that are the responsibility of specialized groups. These programs supervise specific risks and track them using their oversight process. They are as follows: - financial disclosure risk management; - technology risk management; - business continuity risk management; - outsourcing risk management; - risk management related to financial crime; - regulatory risk management; - risk management related to governance and data quality.
Risk-sharing insurance programs	Desjardins Group has developed insurance programs to give itself additional protection against material operational losses. These programs offer protection based on the business segment's needs, the institution's risk tolerance, as well as emerging risks on the market.
Calculation of capital exposed to operational risk	Since second quarter 2017, Desjardins Group has used the Standardized Approach to calculate its operational risk in the form of regulatory capital exposed to operational risk.

Insurance risk

Insurance risk refers to the risk that events may turn out differently from the assumptions used when designing, pricing or measuring actuarial reserves for insurance products, and that profitability of these products may be affected.

Desjardins Group is exposed to insurance risk in the course of its life and health and property and casualty insurance operations.

Insurance risk for the life and health insurance subsidiaries is composed of the following elements:
- mortality risk: Potential loss resulting from an increase in the mortality rate of insureds;
- longevity risk: Potential loss resulting from an increase in the life expectancy of insureds;
- morbidity/disability risk: Potential loss resulting from a decline in the state of health of insureds;
- policyholder behaviour risk: Potential loss resulting from unfavourable policyholder behaviour in keeping their policy in force or exercising any options specified in policies;
- expense risk: Potential loss resulting from an increase in the level of expenses.

Insurance risk for the property and casualty insurance subsidiaries is composed of the following elements:
- underwriting risk: Potential loss resulting from an increase in the frequency or severity of losses (e.g., fire, theft, water damage, vandalism) covered by the insurance products offered, which mainly cover physical damage to property, bodily injury as well as liability of insureds (civil, legal, etc.);
- catastrophe risk: Potential loss resulting from an increase in the frequency or severity of catastrophes covered by insurance policies;
- reserve risk: Potential loss resulting from inadequate provisions or actuarial reserves.

Identifying, assessing and mitigating the risks associated with new insurance products and changes made to existing ones are part of a thorough product approval process. All risks at the insurance subsidiaries, including insurance risk, are managed in accordance with their Integrated Risk Management Policy, in line with Desjardins Group's Integrated Risk Management Framework. The process of logging risks under this policy makes it possible to identify all risks likely to affect the subsidiary concerned that should be the subject of governance and a framework, as well as to maintain a register of all such risks and assess them using the appropriate method.

The subsidiaries are accountable for the risk they generate, including insurance risk. Each one has its own specific governance structure. Insurance risk is governed by several policies that clearly set out the roles and responsibilities of the different parties concerned so that they can comply with the various regulatory guidelines. The subsidiaries also have a robust infrastructure that includes the appropriate tools for ensuring the availability, integrity, completeness and aggregation of all the data necessary for sound insurance risk management.

Insurance risk arises from potential errors in projections concerning the many factors used to set premiums, including future returns on investments, underwriting experience in terms of claims experience, mortality and morbidity, and administrative expenses. These projections are essentially based on actuarial hypotheses that must be consistent with the standards of practice in effect in Canada. The insurance subsidiaries also adopt strict pricing standards and policies and perform spot checks to compare their projections with actual results. Insurance product design and pricing are reviewed on a regular basis. Some product pricing may be adjusted depending on the accuracy of projections.

In addition, the subsidiaries limit their losses through reinsurance treaties that vary based on the nature of the activities, and also through additional reinsurance protection with respect to large-scale catastrophic events.

To reduce reinsurance risk, the insurance subsidiaries do business with many reinsurers that meet financial strength criteria, most of which are governed by the same regulatory authorities as the subsidiaries. Such reinsurance treaties do not release the subsidiaries from their obligations toward their policyholders but do mitigate the risks to which they are exposed.

The subsidiaries comply with the standards for sound management practices established by the regulatory bodies that govern them and test their financial soundness using unfavourable scenarios and measure the effect of such scenarios on their capitalization ratio. These tests include stress testing, including the standardized acute stress scenarios required from time to time by regulators, as well as dynamic capital adequacy testing. Test results showed that capital was adequate in each case.

Each insurance sector subsidiary provides independent reports and assessments of its exposure to different risks to its Board of Directors as well as to the appropriate levels at Desjardins Group. They report in particular on changes in material risks and the effectiveness of the procedures in place to mitigate them, the results of risk analyses, and the main assumptions and findings from the stress testing.

The activities specific to the insurance subsidiaries expose them, in addition to insurance risk, to other types of risk, notably the risks identified in Note 15, "Insurance contract liabilities", to the Combined Financial Statements, as well as other risk factors identified in Section 4.1 "Risk factors that could impact future results".

Strategic risk

Strategic risk refers to the risk of loss attributable to an inability to adapt to a changing environment because of failure to act, an inappropriate strategic choice or the inability to effectively implement strategies.

It is first up to senior management and the Board of Directors to address, define and monitor developments in the strategic orientations of Desjardins Group according to its risk appetite and the consultation processes specific to Desjardins. Events that could compromise the achievement of Desjardins Group's strategic objectives are systematically and periodically monitored by Desjardins Group's officers and senior management. Business segments and support functions identify and periodically assess events and risks that could prevent the achievement of strategic objectives, and report thereon to the appropriate bodies.

Organizational development plans are assessed in light of the organization's risk appetite framework to ensure that such initiatives are in line with the organization's strategic plan. Furthermore, this plan is updated annually to take market developments into account, in particular major trends in the industry and action taken by competitors.

Reputation risk

Reputation risk is the risk that a negative perception by the stakeholders, whether or not justified, of Desjardins Group's practices, actions or lack of action could have an unfavourable impact on its income and equity, and the trust that it inspires.

A reputation is of critical importance, and reputation risk cannot be managed separately from other risks. Therefore, managing reputation risk in all its business segments is a constant concern for Desjardins Group. In this regard, Desjardins Group seeks to ensure that all employees are constantly aware of the potential repercussions of their actions on Desjardins's reputation and image. Desjardins Group considers it essential to foster a proactive approach to risk management in which integrity and ethical conduct are fundamental values.

Desjardins Group has defined a management framework, and roles and responsibilities with regard to reputation risk. This framework is in addition to various processes already in place to identify, measure and govern this risk, such as the previously mentioned operational risk management initiatives, the regulatory compliance program, ethical requirements, and reputation risk assessment as part of new initiatives and the introduction of new products. All these aspects aim to promote sound reputation risk management. All officers and employees are required to perform their duties in accordance with these principles and Desjardins Group's values.

Pension plan risk

Pension plan risk is the risk of loss resulting from pension plan commitments made by Desjardins Group for the benefit of its employees. This risk basically arises from rate, price, foreign exchange and longevity risks.

The organization's main pension plan is the Desjardins Group Pension Plan (DGPP). The Federation, through its Board of Directors, is the sponsor of the DGPP and, as such, acts as the representative for all Desjardins Group employers. The Desjardins Group Retirement Committee, which is composed of members of the Board of Directors of the Federation and representatives of active participants and retirees, is the administrator of the DGPP. It is responsible for managing pension fund assets and administering the benefits promised by the plan. It sees to it that the rules specified in the plan are applied and ensures legal compliance as well as sound governance of the plan. In this regard, it has developed policies and an internal by-law as required under the *Supplemental Pension Plans Act*.

To properly manage DGPP risks, the Desjardins Group Retirement Committee has set up a Risk Management Advisory Committee. This committee, under the responsibility of the Desjardins Group Retirement Committee, is tasked with analyzing the main risks associated with management of DGPP operations. In this regard, it examines the integrated risk profile and the asset allocation strategy every year. It also issues opinions on new investments which are submitted to the Investment Committee. In addition, a risk management dashboard for the DGPP, made up of risk indicators identified in the profile, is updated quarterly.

Environmental risk

Environmental risk is the risk of financial, operational or reputational loss for Desjardins Group as a result of the impact of environmental issues, whether they occur through Desjardins Group's credit or investment activities or its operations.

In addition to the potential financial losses that could be incurred through poor management of environmental risk, there is increased credit risk through the impairment of assets pledged as security. Given the nature of their operations, Desjardins Group's property and casualty insurance subsidiaries are particularly exposed to catastrophes and climate change, which are defined in Section 4.1 "Risk factors that could impact future results". In addition, business relations with entities whose operations could involve social or environmental issues could lead to reputation risk.

Environmental risk is an integral part of Desjardins Group's Integrated Risk Management Framework. In December 2017, Desjardins Group announced the introduction of four management practices aimed at strengthening environmental risk mitigation in the short term and making reduction of Desjardins's carbon footprint a reality:

- Offsetting greenhouse gas emissions generated by its activities.
- For its own investments, focusing its direct energy infrastructure investments on renewable energy. The Desjardins Group Pension Plan has made the same commitment.
- For its own investments, reducing its carbon footprint by 25% by 2020 with regard to its portfolios invested in public markets compared to the benchmark indexes.
- Integrating Environmental, Social and Governance (ESG) factors into its business decisions (financing, investment, placement and insurance). Tools are being developed to support teams in phasing in this positioning, as the objective is to be consistent across the organization.

Given that sustainable development is considered a strategic risk for Desjardins, it has equipped itself with an oversight policy for all its activities and has incorporated orientations to support the development of a sustainable and responsible economy in its Strategic Plan and its performance management, particularly by setting targets for reducing its carbon footprint and gradually integrating these targets into its performance objectives. It is also continuing the innovative development of products and services, focused on sustainable development, for its members and clients. The related reporting is filed annually in its social and cooperative responsibility report based on Global Reporting Initiative (GRI) indicators. Furthermore, in accordance with the GRI-G4, Desjardins Group consulted a number of stakeholders about its sustainable development priorities. These stakeholders included employees, member officers (including members of the Youth Advisory Committee), caisse general managers and Desjardins Business centre managers, representatives of the business community, civil society organizations, representatives of public authorities, members of senior management and members of the Board of Directors. Desjardins Group also periodically updates its analysis of climate change risk to its operations and annually makes disclosures of its strategy and risk management related to climate change to the CDP (formerly known as the Carbon Disclosure Project). In 2017, Desjardins received a B rating from CDP, above the industry average of C, which clearly demonstrates that its actions are producing results.

Legal and regulatory environment risk

Legal and regulatory environment risk refers to the risk arising from Desjardins Group's non-compliance with the laws, regulations, standards and practices in effect wherever Desjardins Group operates, as well as its various internal codes of conduct and its contractual commitments, which could lead in particular to financial losses, penalties, harm to its reputation, legal recourse or heightened monitoring by regulators.

Legal and regulatory environment risk entails, *inter alia*, effectively preventing and handling possible disputes and claims that may lead in particular to judgments or decisions by a court of law or regulatory body that could result in financial penalties or sanctions. Present and future judicial decisions and legislative activity could increase Desjardins Group's exposure to new types of litigation. In addition, some lawsuits against Desjardins Group may be very complex and be based on legal theories that are new or have never been verified. The outcome of such lawsuits may be difficult to predict or estimate until the proceedings have reached an advanced stage, which may take several years. Class action lawsuits or multi-party litigation may feature an additional risk of judgments with substantial monetary, non-monetary or punitive damages. Plaintiffs who bring a class action or other lawsuit sometimes claim very large amounts and it is impossible to determine Desjardins Group's liability, if any, for some time. Legal liability or an important regulatory measure could have an adverse effect on the current activities of Desjardins Group, its results of operations and its financial position, in addition to damaging its reputation. Even if Desjardins Group won its court case or was no longer the subject of measures imposed by regulatory bodies, these situations could harm its reputation and have an adverse impact on its financial position, due in particular to the costs associated with such proceedings, and its brand image.

The financial services industry is one of the most strictly regulated and monitored sectors. In recent years, the regulations governing the industry have expanded significantly in response to numerous socio-economic phenomena such as the development of new, increasingly complex financial products, the continuing volatility in the securities industry, financial fraud, the fight against money laundering and terrorist financing, and the fight against tax evasion, to mention but a few. In addition to federal (Canada and the U.S.) and provincial government requirements, the regulatory environment also includes organizations such as the AMF, the Canadian Securities Administrators, the OSFI, the Financial Transactions and Reports Analysis Centre of Canada, the Mutual Fund Dealers Association of Canada, and the Investment Industry Regulatory Organization of Canada. Complying with important legislative and regulatory provisions, such as those for the protection of personal information, laws and regulations governing insurance, the *Foreign Account Tax Compliance Act*, the Standard for Automatic Exchange of Financial Account Information in Tax Matters, the *Dodd-Frank Wall Street Reform and Consumer Protection Act* and the Basel accords, requires considerable technical, human and financial resources and also affects the way Desjardins Group manages its current operations and implements its business strategies.

As an independent supervisory function, the Office of the Chief Compliance Officer of Desjardins Group fosters a proactive approach to compliance by fully integrating compliance into the organization's current operations. It is responsible for developing, updating and maintaining the compliance management framework, which is based on the identification and monitoring of regulatory obligations and the functional units subject to them. Regulatory developments and their impact on operations are therefore monitored and evaluated on an ongoing basis by the compliance function in cooperation with the Office of the Chief Legal Officer, and strategies are implemented as required to mitigate them. The compliance function provides support to managers in charge of business segments and support functions so that they can effectively manage their risks, by developing an appropriate framework and documentation, acting in an advisory capacity, setting up training programs and conducting periodic inspections of operations. The Desjardins Group Monitoring Office provides an independent assessment of the effectiveness of the compliance management framework. Lastly, Desjardins Group has set up a formal reporting process related to compliance for its senior management and various decision-making bodies. In addition, to maintain its reputation for integrity as well as the confidence of its members and clients, the market and the general public, Desjardins Group has developed a code of professional conduct applicable to all its officers and employees and to all its components. This overall management of compliance provides reasonable assurance that Desjardins Group's operations are carried out in compliance with applicable regulations. Despite all these efforts, Desjardins Group may not be able to predict the exact impact of regulatory developments and appropriately implement strategies to respond. It could then sustain an adverse impact on its financial performance, its operations and its reputation. For further information, refer to the "Regulatory environment" section of this MD&A.

On October 5, 2017, the Quebec Minister of Finance tabled Bill 141, *An Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions* (the Bill). The Bill, once it takes effect, will have significant impacts on all institutions and intermediaries operating in Quebec's financial sector. For further information, see page 18 in the "Changes in the regulatory environment" section, which presents changes in the regulations applicable to Desjardins Group.

4.3 Additional information related to certain risk exposures

The tables below provide more details about more complex financial instruments that carry a higher risk.

Table 49 – Asset-backed securities

As at December 31

(in millions of dollars)	2017		2016	
	Notional amounts	**Fair value**	Notional amounts	Fair value
Commercial mortgage-backed securities[1]	**$ -**	**$ -**	$ 15	$ 15
Financial asset-backed and mortgage-backed securities[2]	**146**	**148**	170	174

(1) These securities are presented in the Combined Balance Sheets under "Securities at fair value through profit or loss".

(2) None of the securities held is directly backed by subprime residential mortgage loans. These securities are presented in the Combined Balance Sheets under "Securities at fair value through profit or loss" and under "Available-for-sale securities".

Table 50 – Derivative financial instruments

As at December 31

(in millions of dollars)	2017			2016		
	Notional amounts	**Positive value**	**Negative value**	Notional amounts	Positive value	Negative value
Credit default swaps[1]	**$ 616**	**$ 13**	**$ 2**	$ 644	$ 10	$ -
Total return swaps[2]	**86**	**-**	**1**	66	-	-

(1) Credit default swaps are presented in the Combined Balance Sheets as derivative financial instruments.

(2) These amounts do not include any amounts realized as part of securitization activities. Total return swaps are presented in the Combined Balance Sheets as derivative financial instruments.

Table 51 – Leveraged finance loans and subprime loans

As at December 31

(in millions of dollars)	2017	2016
Leveraged finance loans[1]	**$ 149**	$ 179
Alt-A mortgage loans[2]	**19**	23
Subprime residential mortgage loans[3]	**1**	2

(1) Leveraged finance loans are defined as loans to large corporations and finance companies whose credit rating is between BB+ and D, and whose level of indebtedness is very high compared to other companies in the same industry.

(2) Alt-A mortgages are defined as loans to borrowers with non-standard income documentation. These loans are presented in the Combined Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

(3) These loans are defined as loans to borrowers with a high credit risk profile. Subprime residential mortgages are recorded in the Combined Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

5.0 Additional information

5.1 Controls and procedures

Desjardins Group is not a reporting issuer, on a combined basis, under National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings* (NI 52-109) issued by the Canadian Securities Administrators (CSA). However, it has chosen to apply the provisions of this National Instrument to demonstrate its willingness to comply with best practices in financial governance.

During fiscal 2017, Desjardins Group carried out work so that it could provide certification as at December 31, 2017 of the design and effectiveness of its disclosure controls and procedures, as well as of its internal control over financial reporting.

DISCLOSURE CONTROLS AND PROCEDURES

In accordance with the CSA guidance in National Instrument 52-109, the President and CEO as well as the Executive Vice-President, Finance, Treasury and Administration and Chief Financial Officer (CFO) designed, or caused to be designed, disclosure controls and procedures, which are supported in particular by a process for periodic certification of financial disclosures in annual and interim filings. All information collected as part of the financial governance process is reviewed on a quarterly and annual basis by the members of the Desjardins Group Disclosure Committee and of the Audit and Inspection Commission, who play a lead role in overseeing and assessing the adequacy of disclosure controls and procedures.

As at December 31, 2017, Desjardins Group management assessed the design and effectiveness of its disclosure controls and procedures. Based on the results of this assessment, the President and CEO, and the CFO concluded that disclosure controls and procedures were adequately designed and effective. These controls and procedures are designed to provide reasonable assurance that the information presented in annual, interim or other reports filed or transmitted under securities legislation is recorded, processed, summarized and reported within the time periods prescribed by such legislation. These controls and procedures are also designed to warrant that such information is assembled and disclosed to the management of Desjardins Group, including its signing officers, in accordance with what is appropriate to make timely decisions regarding disclosure.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Desjardins Group management caused an adequate internal control over financial reporting process to be designed and has maintained it. This process is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of combined financial statements for external purposes in accordance with IFRS.

The design and effectiveness of internal control over financial reporting were assessed in accordance with the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control − Integrated Framework (2013) for financial controls and in accordance with the Control Objectives for Information and Related Technologies (COBIT) framework for IT general controls.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements on a timely basis. Management's assessment of the controls provides only reasonable, not absolute, assurance that all the problems related to control which could give rise to material misstatements have been detected.

The assessment of the design and effectiveness of internal control over financial reporting was performed by Desjardins Group management under the supervision of the President and CEO, and of the CFO. Based on the results of this assessment, these senior officers concluded that as at December 31, 2017, internal control over financing reporting was adequately designed and effective, and did not contain any material weakness.

There are two Desjardins Group components subject to NI 52-109 requirements, namely the Federation and Desjardins Capital Inc.

Under the supervision of the certifying officers, the respective management of the Federation and Desjardins Capital Inc. therefore assessed the design and effectiveness of disclosure controls and procedures and of internal control over financial reporting. These controls provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

CHANGE IN INTERNAL CONTROL OVER FINANCIAL REPORTING

During the year ended December 31, 2017, Desjardins Group did not make any changes to its internal control over financial reporting that had materially affected, or may materially affect, its operations.

Various other aspects of corporate governance are examined in more detail in the "Corporate governance" section of the 2017 Desjardins Group Annual Report.

5.2 Related party disclosures

In the normal course of business, Desjardins Group offers financial services to related parties, including its associates and other related companies, and enters into agreements for operating services with them. It also pays its key management personnel compensation under normal market conditions.

Furthermore, Desjardins Group provides its financial products and services, under normal market conditions, to its directors, its key management personnel and the persons related to them.

Desjardins Group has set up a process to obtain assurance that all transactions with its officers and the persons related to them have been carried out as arm's-length transactions and in compliance with the legislative framework for its various components.

Additional information about related party transactions is presented in Note 34, "Related party disclosures", to the Annual Combined Financial Statements.

5.3 Critical accounting policies and estimates

A description of the accounting policies used by Desjardins Group is essential to understanding the Combined Financial Statements as at December 31, 2017. The significant accounting policies are described in Note 2, "Basis of presentation and significant accounting policies", to the Combined Financial Statements. Some of these policies are of particular importance in presenting Desjardins Group's financial position and operating results because they require management to make judgments as well as estimates and assumptions that may affect the reported amounts of some assets, liabilities, income and expenses, as well as related information. The significant accounting policies that required management to make difficult, subjective or complex judgments, often involving uncertainties, are discussed below.

STRUCTURED ENTITIES

A structured entity is consolidated when it is controlled by a Desjardins Group entity. Management must make significant judgments when it assesses the various elements and all related facts and circumstances as a whole to determine whether control exists, especially in the case of structured entities.

A structured entity is an entity that has been designed so that voting rights or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: restricted activities, a narrow and well-defined objective, insufficient equity to permit it to finance its activities without subordinated financial support, or financing in the form of multiple contractually linked instruments issued to investors.

Additional information about structured entities is presented in Note 13, "Interests in other entities", to the Combined Financial Statements.

DETERMINATION OF THE FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument 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.

The fair value measurement of financial instruments is determined using a three-level hierarchy, reflecting the importance of the inputs used for the measurements. Level 1 denotes measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities, while level 2 designates valuation techniques based primarily on observable market data. Level 3 concerns valuation techniques not based primarily on observable market data.

There is little subjectivity in the determination of the fair value of financial instruments, especially securities and commitments related to securities sold short, obtained from quoted prices on active markets. This fair value is based on the quoted price within the bid-ask spread that is most representative of fair value in the circumstances.

If there are no quoted prices on active markets, fair value is determined using models that maximize the use of observable inputs and minimize the use of unobservable inputs. In such cases, fair value estimates are established using valuation techniques such as cash flow discounting, comparisons with similar financial instruments, option pricing models and other techniques commonly used by market participants, if these techniques have been demonstrated to provide reliable estimates. Valuation techniques rely on assumptions concerning the amount and timing of estimated future cash flows and discount rates that are mainly based on observable data, such as interest rate yield curves, exchange rates, credit curves and volatility factors. When one or several material inputs are not observable on the market, fair value is determined mainly based on internal inputs and estimates that take into account the characteristics specific to the financial instrument and any factor relevant to the measurement. For complex financial instruments, significant judgment is used in determining the valuation technique to be used and in selecting inputs and adjustments associated with this technique. Due to the need to use estimates and make judgments when applying many valuation techniques, fair value estimates for identical or similar assets may differ between entities. Fair value reflects market conditions on a given date and may not be representative of future fair values. It should not be considered as being realizable in the event of immediate settlement of these instruments.

Loans

The fair value of loans is determined by discounting expected contractual cash flows using market interest rates charged for similar new loans at the reporting date and takes estimated prepayments into account. Changes in interest rates and in the creditworthiness of borrowers are the main causes of changes in the fair value of loans held by Desjardins Group, which result in a favourable or unfavourable difference compared to their carrying amount. The fair value of impaired loans is assumed to be equal to their carrying amount.

Deposits

The fair value of fixed-rate deposits is determined by discounting expected cash flows using market interest rates currently being offered for deposits with substantially the same term and takes estimated prepayments into account. The fair value of deposits with floating-rate features or with no stated maturity is assumed to be equal to their carrying amount.

Subordinated notes

The fair value of subordinated notes is based on brokers' quotes.

Derivative financial instruments

The fair value of derivative financial instruments is determined using pricing models that incorporate current market prices and the contractual prices of the underlying instruments, the time value of money, interest rate yield curves, credit curves and volatility factors. The fair value of derivative financial instruments is presented without taking into account the impact of legally enforceable master netting agreements. However, Desjardins Group adjusts the measurement of these instruments based on credit risk, and such adjustments reflect the financial ability of the counterparties to the contracts and the creditworthiness of Desjardins Group, as well as credit risk mitigation measures such as legally enforceable master netting agreements.

Financial instruments whose fair value equals their carrying amount

The carrying amount of certain financial instruments that mature in the next 12 months is a reasonable approximation of their fair value. These financial instruments include the following items: "Cash and deposits with financial institutions", "Securities borrowed or purchased under reverse repurchase agreements", "Clients' liability under acceptances", "Premiums receivable", "Amounts receivable from clients, brokers and financial institutions", some items included in "Other assets – Other", "Acceptances", "Commitments related to securities lent or sold under repurchase agreements", "Amounts payable to clients, brokers and financial institutions" and some items included in "Other liabilities – Other".

Additional information on the fair value of financial instruments is presented in Note 4, "Fair value of financial instruments", to the Combined Financial Statements.

DERECOGNITION OF FINANCIAL ASSETS

A financial asset is derecognized from the Combined Balance Sheets when the contractual rights to the cash flows from the asset expire, when the contractual rights to receive these cash flows are retained but Desjardins Group has the obligation to pay them to a third party under certain conditions, or when Desjardins Group transfers the contractual rights to receive the cash flows and substantially all the risks and rewards of ownership of the asset have been transferred.

When substantially all the risks and rewards of ownership of the transferred financial asset are retained by Desjardins Group, such asset is not derecognized from the Combined Balance Sheets and a financial liability is recognized, when appropriate.

When substantially all the risks and rewards related to a financial asset are neither transferred nor retained, Desjardins Group derecognizes the financial asset over which it does not retain control and recognizes an asset or a liability representing the rights and obligations created or retained in the asset transfer. If control of the financial asset is retained, Desjardins Group continues to recognize the asset in the Combined Balance Sheets to the extent of its continuing involvement in said asset.

When a financial asset is derecognized in its entirety, a gain or a loss is recognized in the Combined Statements of Income for an amount equal to the difference between the carrying amount of the asset and the value of the consideration received.

Management must use its judgment to determine whether the contractual rights to the cash flows have expired, have been transferred or have been retained with an obligation to pay them to a third party. With respect to the transfer of substantially all the risks and rewards of ownership of the assets, management evaluates Desjardins Group's exposure before and after the transfer as well as the changes in the amount and timing of the net cash flows of the transferred asset. Lastly, management must make judgments to determine whether it controls the financial asset and to measure retained rights.

Additional information about the derecognition of financial assets is presented in Note 8, "Derecognition of financial assets", to the Combined Financial Statements.

IMPAIRMENT OF FINANCIAL ASSETS

At the reporting date, Desjardins Group assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Allowance for credit losses

Objective evidence of impairment results from a loss event that occurred after a loan was granted but before the reporting date, and that has an impact on the estimated future cash flows of the loan.

The impairment of a loan or a group of loans is determined by estimating the recoverable amount of these financial assets. The allowance is equal to the difference between this amount and the carrying amount. To determine the estimated recoverable amount of a loan, Desjardins Group discounts the estimated future cash flows at the effective interest rate inherent to the loan. When the amounts and timing of future cash flows cannot be estimated with reasonable reliability, the estimated recoverable amount is determined using the fair value of the collateral underlying the loan, net of expected costs of realization, or the observable market price for the loan. The collateral may vary depending on the type of loan.

The allowance for credit losses represents management's best estimate for loan impairment at the reporting date. As part of its evaluation, management must make judgments to determine the data, assumptions and estimates to be used, including determining when a loan is considered impaired and the amount that could be recovered. Changing these estimates and assumptions would have an impact on the allowance for credit losses and the provision for credit losses for the year.

The allowance for credit losses related to impaired loans is measured either individually or collectively for loans that are not individually material, while the allowance for credit losses is measured collectively for unimpaired loans.

For individual allowances, Desjardins Group first reviews its loan portfolios on a loan-by-loan basis to assess credit risk and determine if there is any objective evidence of impairment for which a loss should be recognized in the Combined Statements of Income. Loan portfolios for which there is no objective evidence of impairment are included in groups of financial assets having similar credit risk characteristics and are subject to a collective allowance.

For certain impaired loan portfolios comprised of a large number of homogeneous balances that are not individually material, Desjardins Group establishes a collective allowance for these impaired loans based on the portfolio's historical net loss rate.

The method used by Desjardins Group to determine the collective allowance takes into account the risk parameters of the various loan portfolios, in particular through the integration of sophisticated credit risk models. These collective allowance models take into account certain factors such as the probabilities of default (loss frequency), loss given default (extent of losses) and gross exposures at default. These parameters, which are based on historical losses, are determined according to the category and risk rating of each loan. The measurement of the collective allowance relies heavily on management's judgment and depends on management's assessment of current credit quality trends for business segments, the impact of changes in its credit policies and economic conditions.

Additional information about loans and the allowance for credit losses is presented in Note 7, "Loans and allowance for credit losses", to the Combined Financial Statements.

Available-for-sale securities

Securities classified in the "Available-for-sale" category are examined at the reporting date to determine whether there is any objective evidence that they are impaired. In measuring the impairment loss, Desjardins Group takes into account many factors specific to each investment and all the factors that could indicate such a loss. Factors considered include, but are not limited to, a significant or prolonged decline in fair value, significant financial difficulties of the issuer, a breach of contract, the increasing probability that the issuer will enter bankruptcy or a restructuring and the disappearance of an active market for the financial asset in question. Management also uses judgment to determine when to recognize an impairment loss.

Desjardins Group individually assesses debt securities classified as "Available-for-sale", including preferred shares with characteristics and behaviour similar to those of debt instruments, to determine whether there is any objective evidence of impairment. For equity securities classified in the "Available-for-sale" category, the objective evidence would also include a "significant" or "prolonged" decline in fair value below cost.

Additional information about the recognition of available-for-sale securities and fair value measurement is presented in Note 3, "Carrying amount of financial instruments", Note 4, "Fair value of financial instruments", and Note 6, "Securities", to the Combined Financial Statements.

IMPAIRMENT OF NON-FINANCIAL ASSETS

Desjardins Group assesses at the reporting date whether there is evidence that an asset may be impaired. An impairment loss is recognized when the carrying amount of the asset exceeds its recoverable amount.

The recoverable amount represents the higher of the fair value less costs of disposal and the value in use. Fair value represents the best estimate of the amount that could be obtained from the sale of the asset in an arm's-length transaction between knowledgeable and willing parties. The value in use is calculated using the most appropriate method, generally by discounting recoverable future cash flows.

Estimating the recoverable amount of a non-financial asset to determine whether it is impaired also requires that management make estimates and assumptions, and any change in these estimates and assumptions could impact the determination of the recoverable amount of non-financial assets and, therefore, the outcome of the impairment test. The main estimates and assumptions used in calculating the recoverable amount are future cash flows estimated based on internal financial forecasts, expected future earnings, the growth rate and the discount rate.

Goodwill and intangible assets with indefinite useful lives

Goodwill and intangible assets with indefinite useful lives are tested for impairment once a year and when there is possible evidence of impairment.

The impairment test for goodwill and intangible assets with indefinite useful lives is performed based on the recoverable amount of the asset or each cash-generating unit (CGU) (or each group of CGUs) to which goodwill or the intangible asset with an indefinite useful life applies. Significant judgments must be made to estimate the data taken into account in the model used to determine the recoverable amount of each intangible asset with an indefinite useful life or each CGU.

When the recoverable amount of the asset or the CGU is less than the carrying amount, an impairment loss is recognized in the Combined Statements of Income for the year and is first recorded as a reduction of the intangible asset with an indefinite useful life or, in the case of a CGU, as a reduction of the goodwill allocated to the CGU (or group of CGUs) and then as a reduction of the other identifiable assets of the CGU (or group of CGUs) pro rata on the basis of their carrying amount in the unit. The allocation of an impairment loss to the assets of a CGU (or group of CGUs) must however not result in their carrying amount being lower than the highest of the following amounts: fair value of the assets less costs to sell, their value in use, and zero. Goodwill impairment losses cannot be reversed.

Note 11, "Goodwill and intangible assets", to the Combined Financial Statements provides further information about the impairment of non-financial assets.

INSURANCE CONTRACT LIABILITIES

Life and health insurance contract liabilities

Life and health insurance contract liabilities consist of actuarial liabilities, benefits payable, provisions for claims not reported, provisions for dividends and experience refunds as well as policyholder deposits.

Actuarial liabilities represent the amounts which, together with estimated future premiums and net investment income, will provide for all the life and health insurance subsidiaries' commitments regarding estimated future benefits, policyholder dividends and related expenses. The appointed actuary of each life and health insurance subsidiary is required to determine the actuarial liabilities needed to meet its future commitments. The actuarial liabilities of these subsidiaries are determined using the Canadian Asset Liability Method (CALM), in accordance with Canadian accepted actuarial practices, and they are equal to the value in the Combined Balance Sheets of the assets that back them.

Property and casualty insurance contract liabilities

Property and casualty insurance contract liabilities consist of unearned premiums, provisions for claims and adjustment expenses.

Unearned premiums represent the portion of premiums remaining to be earned at the reporting date.

The provisions for claims and adjustment expenses related to the insurance policies of the property and casualty insurance subsidiaries are estimated using actuarial techniques that consider best estimate assumptions, taking into account currently known data, which are regularly reviewed and updated. Any resulting adjustment is recognized in the Combined Statements of Income for the year in which the revision occurs. The provision for claims and adjustment expenses is reported on a discounted basis using the rate of return of the underlying assets, with a margin for adverse deviations.

Note 15, "Insurance contract liabilities", to the Combined Financial Statements provides information about accounting for the various life and health and property and casualty insurance contract liabilities, the main assumptions used and the impact on profit or loss of changes to assumptions.

PROVISIONS

Provisions are liabilities of uncertain timing or amount. A provision is recognized when Desjardins Group has an obligation (legal or constructive) as a result of a past event, the settlement of which should result in an outflow of resources embodying economic benefits, and when a reliable estimate can be made of the amount of the obligation. The amount of the obligation is discounted where the effect of the time value of money is material.

Provisions are based on management's best estimate of the amounts required to settle the obligation on the reporting date, taking into account the relevant risks and uncertainties. As these estimates are forward-looking in nature, management must use its judgment to forecast the timing and amount of future cash flows. Actual results may differ significantly from these forecasts.

CONTINGENT LIABILITIES

In the normal course of its operations, Desjardins Group is involved in various litigation and legal proceedings.

Additional information about contingent liabilities is presented in Note 29, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

INCOME TAXES ON SURPLUS EARNINGS

The income tax expense on surplus earnings recognized in the Combined Statements of Income comprises the current and deferred tax expense on operating surplus earnings as well as the income tax consequences of remuneration on capital stock and dividends when certain conditions are met. The total income tax expense includes the income tax expense on surplus earnings recognized in the Combined Statements of Income as well as current and deferred taxes on items recognized outside profit or loss directly in the Combined Statements of Comprehensive Income or the Combined Statements of Changes in Equity.

The total income tax expense is based on the expected tax treatment of the transactions. To determine the current and deferred portions of income taxes on surplus earnings, management must make judgments to establish assumptions concerning the dates on which deferred income tax assets and liabilities will be reversed. Significant judgment must be used to interpret the relevant tax legislation in order to determine the income tax expense. If Desjardins Group's interpretation differs from that of taxation authorities or if the reversal dates do not correspond to the forecasted dates, the provision for income taxes on surplus earnings may increase or decrease in subsequent years.

Note 28, "Income taxes on surplus earnings", to the Combined Financial Statements provides additional information on income taxes on surplus earnings.

MEMBER DIVIDENDS

The board of directors of each caisse recommends for approval the surplus earnings distribution plan at the annual general meeting of members, which is held in the four months following year-end. The amount of member dividends to be paid is part of this plan. Member dividends are estimated based on, among other things, the surplus earnings recorded for the year by the caisses, taking into consideration the financial framework for the appropriation of surplus earnings in relation to the Desjardins Group Capitalization Plan, which sets capitalization targets. The difference between the amount of member dividends actually paid following general meetings held by the caisses and the estimated amount of the provision is charged to combined profit or loss for the year in which the payments are made.

The allocation basis of member dividends depends on the interest recorded on loans and deposits, the average outstanding amount of Desjardins investment funds, guaranteed market-linked investments, Accord D loans obtained by the member through the caisse, and the various service charges collected from the member depending on the services used. The caisses can pay out member dividends when legal and regulatory requirements have been met. The provision for member dividends is mainly allocated to the Personal and Business Services segment.

EMPLOYEE BENEFITS

Desjardins Group offers the majority of its employees a defined benefit pension plan and a defined benefit supplemental pension plan. It also offers a post-retirement benefit plan that provides medical, dental and life insurance to retiring employees and their dependents.

Group pension plans are plans whose risks are shared by entities under common control. The main group pension plan offered, the Desjardins Group Pension Plan (DGPP), is a funded defined benefit group plan. Participants and employers share the risks and costs related to the DGPP, including any deficit, on a pro rata basis of 35% and 65%, respectively.

For the DGPP, benefits are determined on the basis of the number of years of membership and take into consideration the average salary of the employee's five most highly paid years, for years of service accumulated before 2013, and the eight most highly paid years, for years of service accumulated subsequently. Benefits are indexed annually using the Consumer Price Index, up to a maximum of 3% for years of service accumulated before 2013, and of 1% for a period of 10 years starting at age 65 for years of service accumulated after 2013.

Defined benefit pension plans are plans for which Desjardins Group has formally committed to a level of benefits and therefore assumes actuarial and, when the plans are funded, investment risks. Since the terms of the pension plans are such that future changes in salary levels will have an impact on the amount of future benefits, the cost of the benefits and the value of the defined benefit plan obligation are in general actuarially determined using various assumptions. Although management believes that the assumptions used in the actuarial valuation process are reasonable, there remains a degree of risk and uncertainty that may cause future actual results to differ materially from these assumptions, which could give rise to actuarial gains or losses.

Actuarial calculations are made based on management's best estimate assumptions primarily concerning the plan obligation discount rate, and also, but to a lesser extent, salary increases, the retirement age of employees, the mortality rate, the rate of increase in pension benefits and the participants' future contributions that will be used to make up the deficit. The participants' estimated discounted contributions required to make up the deficit reduce the defined benefit plan obligation. A complete actuarial valuation is performed each year by a qualified actuary. The discount rates used have been determined by reference to the rates of high quality corporate bonds whose terms are consistent with those of the plans' cash flows.

The terms of the post-retirement benefit plans are such that changes in salary levels or healthcare costs will have an impact on the amount of future benefits. The cost of these benefits is accrued over a part of the service lives of employees using accounting policies similar to those used for defined benefit pension plans.

Note 16, "Net defined benefit plan liabilities", to the Combined Financial Statements provides further information on accounting for defined benefit plans and on the sensitivity of the key assumptions.

5.4 Future accounting changes

Accounting standards and amendments issued by the IASB but not yet effective as at December 31, 2017 are presented below. Regulatory authorities have stated that early adoption of these standards and amendments will not be permitted, unless they indicate otherwise.

IFRS 15, "REVENUE FROM CONTRACTS WITH CUSTOMERS"

In May 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers", which introduces a single, comprehensive revenue recognition model for all contracts with customers other than those within the scope of other standards, such as financial instruments, insurance contracts and leases. The majority of Desjardins Group's revenues will not be affected by the adoption of this standard. IFRS 15 supersedes IAS 18, "Revenue" and related interpretations. The core principle of this standard is that revenue recognition should depict the transfer of goods or services in an amount that reflects the consideration received or expected to be received in exchange for these goods or services.

In April 2016, the IASB issued amendments to IFRS 15 to further clarify revenue recognition and transition provisions with respect to the initial application.

Desjardins Group will have to adopt IFRS 15 retrospectively as at January 1, 2018. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 15 will be recognized in the opening Combined Balance Sheets. Desjardins Group decided not to restate comparative periods upon adopting the provisions of IFRS 15. Consequently, the retrospective impact of applying IFRS 15 will be recognized in the Combined Balance Sheets as at January 1, 2018, which is the effective date of the new standard.

Desjardins Group estimates that adopting IFRS 15 should result in a decrease in the "Equity – Group's share" of approximately $35 million, net of taxes, as at January 1, 2018.

IFRS 9, "FINANCIAL INSTRUMENTS"

In July 2014, the IASB issued the complete and final version of IFRS 9, "Financial Instruments", which will replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 includes the requirements for the classification and measurement of financial assets and liabilities and the impairment of financial assets, as well as general requirements for hedge accounting. Concurrently with the issuance of IFRS 9, IFRS 7, "Financial Instruments: Disclosures", was amended to enhance the required qualitative and quantitative disclosures, which will have to be provided for the years beginning on or after January 1, 2018.

Desjardins Group will have to adopt IFRS 9 retrospectively as at January 1, 2018. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 9 will be recognized in the opening Combined Balance Sheets. Desjardins Group decided not to restate comparative periods upon adopting the provisions of IFRS 9. Consequently, the retrospective impact of applying IFRS 9 will be recognized in the Combined Balance Sheets as at January 1, 2018, which is the effective date of the new standard on financial instruments.

Desjardins Group estimates that adopting IFRS 9 should result in a decrease in "Equity – Group's share" of approximately $175 million, net of taxes, as at January 1, 2018 and in a decrease of approximately 16 basis points in regulatory capital ratios. This impact is mainly due to the increase in the allowance for credit losses resulting from the application of the new financial asset impairment model. Desjardins Group continues to refine its processes relating to the new impairment model in preparation for reporting its financial information for the first quarter of 2018.

Governance and project management

The adoption of IFRS 9 is a major initiative for Desjardins Group, which developed an organization-wide project based on a formal governance structure including various committees comprised of key members from the Finance Executive Division and Office of the CFO as well as Risk Management, and a structured implementation plan. This plan is divided into three main components, corresponding to the three sections of the new standard on financial instruments:

- classification and measurement;
- impairment;
- hedge accounting.

A multidisciplinary team made up of stakeholders from various sectors, such as risk management, including modelling, accounting standardization and information technology, has been assigned to the project and focuses on the following items for each of the above-mentioned components: changes in disclosure and financial reporting as well as in systems, controls and procedures, communications and training. Reports on the progress of the project as well as the main orientations implemented have been presented to the Audit and Inspection Commission, the Risk Management Commission and senior management.

The progress of each of the components of the implementation plan is monitored, and the project continues to advance according to schedule.

Following is a summary of the new IFRS 9 concepts and the progress of the work for each of the above-mentioned components.

Classification and measurement

IFRS 9 sets out a new classification and measurement model for financial assets to determine whether a financial asset should be classified as at amortized cost, at fair value through profit or loss or at fair value through other comprehensive income. This model is based on the contractual cash flow characteristics of the financial asset and the business model under which the financial asset is held.

The classification of debt instruments giving rise to cash flows that are solely payments of principal and interest will be determined, at initial recognition, based on the business model for managing these financial assets:

- Financial assets held within a business model whose objective is to collect contractual cash flows will be classified as at amortized cost.
- Financial assets held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets will be classified as at fair value through other comprehensive income.
- Financial assets managed either for trading purposes or on a fair value basis will be classified as at fair value through profit or loss.

In all cases, if a debt instrument does not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest, the financial asset will be classified as at fair value through profit or loss.

Lastly, Desjardins Group may make, at initial recognition, an irrevocable election to classify a debt instrument as at fair value through profit or loss if such designation eliminates or significantly reduces a measurement or recognition inconsistency for the financial asset and if regulatory requirements are met.

Equity instruments will be classified as at fair value through profit or loss unless, at initial recognition, an irrevocable election is made, on an instrument-by-instrument basis, to classify them as at fair value through other comprehensive income. If such election is made, gains and losses will be recognized in other comprehensive income with no subsequent reclassification to profit or loss.

Certain financial assets that will be reclassified upon adopting IFRS 9 will be designated for purposes of applying the overlay approach. For more details, see IFRS 4, "Insurance Contracts", below.

Derivative financial instruments will continue to be recognized at fair value through profit or loss.

For the classification and measurement of financial liabilities, the new standard essentially carries forward the current requirements of IAS 39, without any significant difference, except for financial liabilities designated as at fair value through profit or loss, for which the change in fair value related to a change in the issuing entity's own credit risk will have to be recognized in other comprehensive income. Since Desjardins Group does not hold any financial liabilities designated as at fair value through profit or loss at the transition date, the new standard will have no impact on the classification and measurement of financial liabilities.

Impairment

Overall comparison of the IFRS 9 and the IAS 39 impairment models

IFRS 9 introduces a new single financial asset impairment model requiring the recognition of expected credit losses instead of incurred losses, as the impairment model under IAS 39 requires. Under the current standard, loss allowances are recognized solely when there is objective evidence of impairment (identified on an individual or collective basis), which is when a loss event occurred after initial recognition, but before the reporting date, and this has an impact on the estimated cash flows from the financial asset. Under IFRS 9, credit losses will be recognized before a loss event occurs, which should result in faster recognition of credit losses than is actually the case with the current model.

The impairment model under IFRS 9 is therefore more forward-looking in nature than the impairment model under IAS 39. Under IFRS 9, assessing changes in credit risk since initial recognition and estimating expected credit losses must take into account the relevant information available at the reporting date, including information about past events and current conditions, as well as reasonable and supportable forward-looking information about economic conditions and future events.

Scope

The impairment model applies to all financial assets as well as loan commitments and financial guarantee contracts, except financial instruments measured or designated as at fair value through profit or loss and those designated as at fair value through other comprehensive income.

General expected credit loss impairment model

The general expected credit loss impairment model comprises three different stages:

- Stage 1: For financial instruments that have not had a significant increase in credit risk since initial recognition and are not considered as credit-impaired financial assets, a loss allowance amounting to 12-month expected credit losses is recognized.
- Stage 2: For financial instruments that have had a significant increase in credit risk since initial recognition but are not considered as credit-impaired financial assets, a loss allowance amounting to the lifetime expected credit losses is recognized.
- Stage 3: For financial assets considered as credit-impaired, a loss allowance amounting to the lifetime expected credit losses continues to be recognized.

The credit-impaired financial asset definition under IFRS 9 will correspond to the internal default definition used for credit risk management purposes, which takes relevant qualitative factors into consideration. Under IAS 39, loans are considered impaired financial assets when they meet the criteria for classification as "impaired loans" set out in Note 2, "Basis of presentation and significant accounting policies" to the Combined Financial Statements. Consequently, the concept of credit-impaired financial asset will differ from the concept currently used under IAS 39.

Financial instruments may, over their life, move from one general impairment model stage to another based on the improvement or deterioration of their credit risk. Instruments will always be classified in the various stages of the general impairment model based on the change in credit risk between the reporting date and the initial recognition date of the financial instrument.

Expected life

The expected life of most financial instruments is equal to the maximum contractual term during which Desjardins Group is exposed to a credit risk, including extension options that may be exercised solely by the borrower. The exception to this rule concerns revolving credit exposures, which consist of personal and business lines of credit and credit card loans. The life of these instruments is estimated as being the period, as of the reporting date, over which there is exposure to credit risk without mitigation of the expected credit losses through normal credit risk management measures.

Determination of significant increases in credit risk

To determine whether, at the reporting date, credit risk has significantly increased since initial recognition, Desjardins Group must base its assessment on the change in default risk over the expected life of the financial instrument in accordance with the requirements of IFRS 9, which will require a high degree of judgment.

In order to determine whether there has been a significant increase in credit risk since initial recognition, Desjardins Group will compare the probability of default (PD) on the financial instrument at the reporting date with the PD at the date of initial recognition, also taking into consideration reasonable and supportable information that is indicative of significant increases in credit risk since initial recognition, including information about future economic conditions, to the extent that such information affects the assessment of the instrument's PD. In order to determine the PD of an instrument, PD assessment models for calculating regulatory capital according to the Internal Ratings-Based Approach will be used, but will be adjusted to comply with IFRS 9. The criteria used to determine a significant increase in credit risk will be mainly based on a relative change combined with an absolute change in the PD and will vary depending on the type of client base.

Desjardins Group has also elected not to rebut the presumption that the credit risk has increased significantly when payments on loans are more than 30 days past due. This would be the latest date on which a financial instrument will be deemed to have experienced a significant increase in credit risk.

Measurement of loss allowances for expected credit losses

Loss allowances for expected credit losses will reflect an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, which will take into consideration reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Loss allowances for expected credit losses will be measured on a collective or individual basis. For financial instruments included in stage 1 and stage 2 of the general impairment model, the loss allowance for expected credit losses will be measured on a collective basis. For financial assets included in stage 3, the loss allowance for expected credit losses will be measured on an individual or collective basis.

Loss allowances for expected credit losses measured on a collective basis will be based mainly on the parameters used to calculate regulatory capital under the Internal Ratings-Based Approach, namely PD, LGD and EAD, as defined under "Credit risk" in Section 4.2, "Risk management". However, these parameters will be adjusted to comply with IFRS 9.

The following table presents the main differences between the parameters used to calculate regulatory capital and those used to calculate loss allowances for expected credit losses under IFRS 9.

	Regulatory capital	IFRS 9
PD	• Estimated using a long-term average for a full economic cycle. • Projected over the next 12 months. • Definition of default associated with an instrument for which payments have been past due for over 90 days, plus certain other criteria.	• Estimated at a point in time for the next 12 months or for the lifetime of the instrument. • Based on past experience, current conditions and relevant forward-looking information. • Will correspond to the definition of default used for regulatory capital purposes.
LGD	• Based on losses that would be expected during an economic downturn. • Subject to certain regulatory floors. • Takes into account all direct and indirect recovery costs . • Discounted to account for the recovery period until default using the discount rate required for regulatory capital purposes.	• Based on past experience, current conditions and relevant forward-looking information. • Excessive conservatism and floors are excluded. • Takes into account only direct recovery costs. • Discounted to account for the recovery period until default using the initial effective interest rate.
EAD	• Corresponds to drawn amounts plus expected use of undrawn amounts before default. • Amount may not be lower than the balance of drawn amounts.	• Based on the expected balance of amounts in default projected over the next 12 months or the lifetime of the instrument based on forward-looking expectations.
Discounting	• No discounting between the date of default and the reporting date.	• Discounted from the date of default to the reporting date using the initial effective interest rate.

Three different economic scenarios prepared by Desjardins Group economists, namely, a base case scenario and two alternative scenarios (bull and bear) to be probability-weighted, will be incorporated into the calculation process for the loss allowance for expected credit losses. The main variables for future economic conditions to be used for establishing the loss allowance for expected credit losses include, in particular, gross domestic product (GDP), unemployment rate, the Consumer Price Index, housing prices and the corporate financing spread. Significant judgment will be required in using forward-looking information and the necessary estimates. Given the forward-looking nature of the IFRS 9 impairment model, Desjardins Group expects that the loss allowance for expected credit losses established according to this standard may be more volatile than that established according to the current model.

The technology solution retained for calculating expected credit losses, which was implemented in fiscal 2017, will track financial asset classification included in each of the stages under the new expected credit loss (ECL) model, handle the impact of expected economic variables and incorporate risk parameters and certain credit risk modelling processes.

In fiscal 2017, Desjardins Group also finalized the development and validation of the impairment model for purposes of calculating expected credit losses, and calculations were simulated. In addition, internal documentation relating to accounting policies, internal controls and procedures were updated, and business and financial reporting processes were modified. Changes were also made to the existing governance process with respect to the allowance for credit losses under IAS 39, in particular by revising the role of the Governance Committee – Collective Allowance, composed of officers from the Finance Executive Division and Office of the CFO as well as Risk Management and Economic Studies and in charge of approving work related to the determination of collective allowances and evaluating the relevance of the amounts to be included in the Combined Financial Statements.

Documents issued by regulatory authorities

In December 2015, the BCBS issued the final version of *Guidance on credit risk and accounting for expected credit losses*, which sets out supervisory guidance on sound credit risk practices associated with the implementation and ongoing application of expected credit loss accounting frameworks. In September 2016, the AMF issued a notice relating to the application of IFRS 9. This notice states that the AMF adheres to the principles and guidance published by the BCBS and expects financial services cooperatives, such as Desjardins Group, to comply with them. Desjardins is taking into consideration this guidance in the implementation and ongoing application of the expected credit loss impairment model under IFRS 9.

Documents regarding the regulatory treatment of accounting provisions were also issued. More information about these documents is found in Section 3.2, "Capital management".

Hedge accounting

IFRS 9 sets out a new hedge accounting model to align hedge accounting more closely with risk management activities.

However, as permitted by IFRS 9, Desjardins Group decided to continue applying the hedge accounting requirements of IAS 39 instead of adopting the provisions of IFRS 9. Nevertheless, the new disclosures resulting from amendments to IFRS 7, "Financial Instruments: Disclosures", will have to be provided.

IFRS 4, "INSURANCE CONTRACTS"

In September 2016, the IASB issued amendments to IFRS 4, "Insurance Contracts", which are designed to address the concerns of insurers and their representative bodies about the different effective dates of IFRS 9, "Financial Instruments", which is January 1, 2018, and of new IFRS 17, "Insurance Contracts".

The amendments permit, but do not require, an entity that issues insurance contracts to elect to use one of two options in connection with adopting IFRS 9: deferring the initial application date of IFRS 9 to January 1, 2021 or applying the overlay approach.

Desjardins Group elected to apply the overlay approach, which is the only option proposed by these amendments that it may apply, to financial assets that are eligible and designated in accordance with certain specific criteria. The overlay approach involves reclassifying between net surplus earnings and other comprehensive income, for designated financial assets, the difference between the amount reported in the Combined Statements of Income under IFRS 9 and the amount that would have been reported in the Combined Statements of Income if Desjardins Group had continued to apply IAS 39 in such a way that net surplus earnings related to designated financial instruments reported in the Combined Statements of Income correspond to the amount that would have been reported if Desjardins Group had continued to apply IAS 39.

Desjardins Group will have to adopt the amendments to IFRS 4 as at January 1, 2018, which is the date of initial application of IFRS 9. According to the transition approach used for adopting IFRS 9, the retrospective impact of the overlay approach will be recognized in the Combined Balance Sheets as at January 1, 2018, and comparative periods will not be restated.

For financial assets reclassified from the "Available for sale" category under IAS 39 to financial assets "Classified as at fair value through profit or loss" under IFRS 9 that have been designated for purposes of applying the overlay approach, Desjardins Group estimates that adopting the amendments to IFRS 4 should result in a reclassification of approximately $405 million, after taxes, from "Undistributed surplus earnings" to "Accumulated other comprehensive income" as at January 1, 2018.

IFRS 16, "LEASES"

In January 2016, the IASB issued IFRS 16, "Leases", to replace the current standard IAS 17, "Leases". IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 introduces a single recognition model for the lessee that requires recognizing lease assets and liabilities for most leases on the balance sheet, thereby eliminating the current distinction between operating and finance leases. For the lessor, the distinction between operating and finance leases remains similar.

Desjardins Group is currently assessing the impact of adopting IFRS 16, which will be effective for annual periods beginning on or after January 1, 2019.

IFRS 17, "INSURANCE CONTRACTS"

In May 2017, the IASB issued IFRS 17, "Insurance Contracts", which will replace the current standard, IFRS 4, "Insurance Contracts". IFRS 17 sets out the recognition, measurement, presentation and disclosure requirements applicable to all insurance contracts.

IFRS 17 requires that insurance contract liabilities be measured using a general model based on current value. This general model uses assumptions as at the reporting date to estimate the amount, timing and uncertainty of future cash flows and takes into account market interest rates and the impact of insurance contract holder options and guarantees.

In addition, under IFRS 17, profits on the sale of insurance policies will no longer be recognized upon initial recognition, but will instead be deferred as a separate liability and recognized in profit or loss over the contract term as services are provided.

Desjardins Group is currently assessing the impact of adopting IFRS 17, which will be effective for annual periods beginning on or after January 1, 2021.

5.5 Five-year statistical review

Table 52 – Combined Balance Sheets
For the years ended December 31

(in millions of dollars)	2017	2016	2015	2014	2013
ASSETS					
Cash and deposits with financial institutions	**$ 2,435**	$ 1,876	$ 1,716	$ 1,781	$ 1,320
Securities					
Securities at fair value through profit or loss	**31,654**	31,005	28,715	24,845	23,536
Available-for-sale securities	**24,934**	22,280	23,272	19,890	19,041
	56,588	53,285	51,987	44,735	42,577
Securities borrowed or purchased under reverse repurchase agreements	**8,674**	7,690	7,881	9,959	7,710
Loans					
Residential mortgages	**113,146**	106,695	102,323	97,512	91,389
Consumer, credit card and other personal loans	**24,044**	22,150	21,204	20,495	19,549
Business and government	**40,738**	37,626	36,433	32,903	30,013
	177,928	166,471	159,960	150,910	140,951
Allowance for credit losses	**(438)**	(456)	(455)	(456)	(418)
	177,490	166,015	159,505	150,454	140,533
Segregated fund net assets	**13,379**	11,965	9,781	8,695	7,252
Other assets					
Clients' liability under acceptances	**31**	11	376	858	985
Premiums receivable	**2,095**	1,957	1,662	1,127	1,123
Derivative financial instruments	**3,206**	3,572	4,818	3,133	2,322
Amounts receivable from clients, brokers and financial institutions	**1,554**	2,532	2,033	1,742	1,891
Reinsurance assets	**2,202**	2,582	1,964	785	648
Investment property	**832**	823	683	571	475
Property, plant and equipment	**1,411**	1,435	1,451	1,374	1,322
Goodwill	**121**	471	472	472	456
Intangible assets	**466**	690	661	569	507
Deferred tax assets	**992**	874	784	1,043	810
Other	**2,738**	2,589	2,354	2,089	2,074
Assets of the disposal group held to be transferred	**881**	-	-	-	-
	16,529	17,536	17,258	13,763	12,613
TOTAL ASSETS	**$ 275,095**	$ 258,367	$ 248,128	$ 229,387	$ 212,005

Table 52 – Combined Balance Sheets (continued)
For the years ended December 31

(in millions of dollars)	2017	2016	2015	2014	2013
LIABILITIES AND EQUITY					
LIABILITIES					
Deposits					
Individuals	**$ 100,578**	$ 96,278	$ 91,243	$ 88,463	$ 86,730
Business and government	**69,102**	62,799	63,833	56,516	49,792
Deposit-taking institutions	**1,906**	1,469	1,498	1,345	224
	171,586	160,546	156,574	146,324	136,746
Other liabilities					
Acceptances	**31**	11	376	858	985
Commitments related to securities sold short	**9,112**	8,196	5,464	6,304	7,754
Commitments related to securities lent or sold under repurchase agreements	**10,229**	10,323	10,383	13,072	9,579
Derivative financial instruments	**3,094**	2,057	1,689	1,675	1,719
Amounts payable to clients, brokers and financial institutions	**4,247**	4,659	4,713	3,713	3,752
Insurance contract liabilities	**28,272**	27,493	26,734	19,435	17,070
Segregated fund net liabilities	**13,354**	11,957	9,776	8,706	7,260
Defined benefit plan liabilities	**2,624**	2,256	2,428	2,700	1,825
Deferred tax liabilities	**155**	179	163	329	303
Other	**5,568**	6,019	6,219	4,814	4,717
Liabilities of the disposal group held to be transferred	**662**	-	-	-	-
	77,348	73,150	67,945	61,606	54,964
Subordinated notes	**1,388**	1,378	1,884	2,564	3,063
TOTAL LIABILITIES	**250,322**	235,074	226,403	210,494	194,773
EQUITY					
Capital stock	**5,361**	5,292	5,158	4,777	3,881
Share capital	**90**	88	86	85	82
Undistributed surplus earnings	**1,360**	1,529	1,793	1,468	1,400
Accumulated other comprehensive income	**445**	514	589	615	420
Reserves	**16,707**	15,052	12,864	11,476	11,005
Equity – Group's share	**23,963**	22,475	20,490	18,421	16,788
Non-controlling interests' share	**810**	818	1,235	472	444
TOTAL EQUITY	**24,773**	23,293	21,725	18,893	17,232
TOTAL LIABILITIES AND EQUITY	**$ 275,095**	$ 258,367	$ 248,128	$ 229,387	$ 212,005

Table 53 – Combined Statements of Income
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]	2014[1]	2013[1]
Interest income					
Loans	**$ 5,923**	$ 5,686	$ 5,765	$ 5,563	$ 5,456
Securities	**323**	315	308	335	313
	6,246	6,001	6,073	5,898	5,769
Interest expense					
Deposits	**1,763**	1,643	1,665	1,753	1,708
Subordinated notes and other	**78**	85	129	137	157
	1,841	1,728	1,794	1,890	1,865
Net interest income	**4,405**	4,273	4,279	4,008	3,904
Net premiums	**8,049**	7,168	6,907	5,916	5,558
Other income					
Deposit and payment service charges	**458**	488	489	498	498
Lending fees and credit card service revenues	**660**	574	550	530	481
Brokerage and investment fund services	**1,087**	1,106	1,037	970	855
Management and custodial service fees	**428**	376	365	348	300
Net income (loss) on securities at fair value through profit or loss	**1,079**	533	809	2,005	(667)
Net income on available-for-sale securities	**408**	388	318	343	221
Net other investment income	**201**	198	235	233	229
Foreign exchange income	**77**	70	88	84	61
Other	**249**	27	165	265	273
	4,647	3,760	4,056	5,276	2,251
Total income	**17,101**	15,201	15,242	15,200	11,713
Provision for credit losses	**349**	319	377	351	277
Claims, benefits, annuities and changes in insurance contract liabilities	**6,717**	5,446	5,431	6,303	3,259
Non-interest expense					
Salaries and fringe benefits	**3,452**	3,548	3,475	3,200	3,125
Premises, equipment and furniture, including depreciation	**727**	667	613	598	570
Service agreements and outsourcing	**319**	306	331	256	232
Communications	**284**	307	299	283	287
Other	**2,566**	2,376	2,241	2,182	1,994
	7,348	7,204	6,959	6,519	6,208
Operating surplus earnings	**2,687**	2,232	2,475	2,027	1,969
Income taxes on surplus earnings	**536**	460	516	434	439
Surplus earnings before member dividends	**2,151**	1,772	1,959	1,593	1,530
Member dividends	**202**	144	154	217	171
Tax recovery on member dividends	**(54)**	(39)	(41)	(57)	(45)
Net surplus earnings for the year after member dividends	**$ 2,003**	$ 1,667	$ 1,846	$ 1,433	$ 1,404
Of which:					
Group's share	**$ 1,960**	$ 1,591	$ 1,674	$ 1,376	$ 1,384
Non-controlling interests' share	**43**	76	172	57	20

[1] Prior-period data have been reclassified to conform to the current year's presentation.

Table 54 – Selected financial measures
For the years ended December 31

(in millions of dollars and as a percentage)	2017	2016[1]	2015[1]	2014[1]	2013[1]
Tier 1A capital ratio	**18.0%**	17.3%	16.0%	15.7%	15.7%
Tier 1 capital ratio	**18.0**	17.3	16.0	15.8	15.7
Total capital ratio	**18.4**	17.9	17.2	17.9	18.4
Leverage ratio[2]	**8.5**	8.1	7.8	N/A	N/A
Return on equity[3]	**9.1**	8.0	9.1	8.7	9.4
Productivity index[3]	**70.8**	73.8	70.9	73.3	73.4
Gross impaired loans / gross loans and acceptances ratio[3]	**0.25**	0.32	0.34	0.34	0.32
Average assets[3]	**$ 269,938**	$ 256,500	$ 246,694	$ 222,542	$ 205,051
Average net loans and acceptances[3]	**171,361**	162,630	155,449	146,542	137,266
Average deposits[3]	**169,219**	160,176	152,140	141,833	133,518

[1] Prior-year data have been reclassified to conform to the current year's presentation.
[2] Effective since January 1, 2015.
[3] See "Basis of presentation of financial information".