DESJARDINS GROUP MANAGEMENT'S DISCUSSION AND ANALYSIS

TABLE OF CONTENTS

Section 1.0
Desjardins Group
This section gives a brief overview of Desjardins Group and its 2012 financial highlights. It presents the results related to its priority financial objectives and the financial outlook for 2013. It also includes a description of the economic environment in 2012, industry trends and the economic outlook for 2013.

Section 2.0
Review of financial results
This section provides an analysis of Desjardins Group's results for the year ended December 31, 2012. It contains information on Desjardins Group's business segments, including a profile of each segment, a description of the industry, financial highlights of 2012, the segment's strategy and priorities for 2013, and an analysis of financial results, including fourth quarter results and quarterly trends.

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, including capital management, analysis of cash flows 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 future results.

SECTION 5.0
Additional information
This section presents controls and procedures, related party disclosures, material events, critical accounting policies and estimates, future accounting changes and various annual statistics.

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

This Management's Discussion and Analysis (MD&A), dated February 21, 2013, presents the results of the analysis of the key elements of and changes to Desjardins Group's balance sheet for the year ended December 31, 2012, in comparison to previous fiscal years. The MD&A should be read in conjunction with the Audited Combined Financial Statements (the Combined Financial Statements), including the Notes, as at December 31, 2012.

Additional information about Desjardins Group is available on the SEDAR website at **www.sedar.com** (under the *Capital Desjardins inc.* profile), where the Annual Information Forms of *Capital Desjardins inc.*, *Caisse centrale Desjardins* (under the *Caisse centrale Desjardins* profile) and the Federation (under the *Fédération des caisses Desjardins du Québec* profile) can also be found. More information is also available on the Desjardins website at **www.desjardins.com/en/a_propos/investisseurs**; however, none of the information presented on these sites is incorporated by reference into this report.

BASIS OF PRESENTATION OF FINANCIAL INFORMATION

Desjardins Group issues its Combined Financial Statements in accordance with Canadian generally accepted accounting principles (GAAP) and the accounting requirements of the *Autorité des marchés financiers* in Quebec (AMF), which do not differ from GAAP.

The International Financial Reporting Standards (IFRS) constitute GAAP for Desjardins Group. Therefore, Desjardins Group's Combined Financial Statements have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board (IASB). For more information about accounting policies, see the Combined Financial Statements.

This MD&A was prepared in accordance with the Regulation in force on continuous disclosure obligations issued by the Canadian Securities Administrators. 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 and presents both IFRS measures and various non-IFRS financial measures.

Effective December 31, 2012, Desjardins Group used the concept of operating income to analyze its financial results. This information allows for better structuring of financial data and makes it easier to compare operating activities from one period to the next by excluding investment income. 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, net premiums and other operating income such as deposit and payment service charges, lending fees and credit card service revenues and brokerage, investment fund and trust services income, as well as other income. These items, taken individually, correspond to those presented in the Combined Financial Statements.

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. Investment income also includes income from the insurance subsidiaries' matching activities and from derivatives not designated as part of a hedging relationship.

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 prescribed IFRS measures. The non-IFRS measures may be useful to investors to analyze financial performance, among other things. These measures are defined as follows:

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 claims, benefits, annuities and changes in insurance and investment contract liabilities, expressed as a percentage. A lower ratio indicates greater productivity.

Return on equity

Return on equity, which is expressed as a percentage, is equal to surplus earnings before member dividends, excluding the non-controlling interests' share, divided by average equity before non-controlling interests.

Growth in operating income

Growth in operating income is equal to the percentage change in operating income in relation to the corresponding period of the previous year.

Gap between income growth and expense growth

The gap, expressed as a percentage, between income growth and expense growth is equal to the difference between the growth in total income, net of claims, benefits, annuities and changes in insurance and investment contract liabilities, compared to the corresponding period of the previous year, and the growth in non-interest expense from the corresponding period of the previous year.

Average assets – Average loans – Average deposits – Average equity

The average balance for these items is equal to the average of the amounts at the end of the previous five quarters, calculated starting from December 31.

REGULATORY CONTEXT AND CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

REGULATORY CONTEXT

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) that do business in Quebec, including the caisses and the Federation. Other regulations, including those developed by the Office of the Superintendent of Financial Institutions Canada (OSFI), may also govern some operations of Desjardins Group entities, such as those related to insurance or securities brokerage.

Moreover, Desjardins Group complies with the minimum regulatory capital requirements issued by the AMF, which are adapted to reflect the provisions of the Basel II Accord. While 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 practices provided in the regulation to demonstrate its willingness to comply with best practices in financial governance. Desjardins Group's financial and corporate governance are discussed on pages 86 and 87 of this MD&A and pages 183 to 202 of the *2012 Desjardins Group Annual Report*.

It should also be mentioned that Desjardins Bank, National Association, a subsidiary of *Caisse centrale Desjardins* incorporated under U.S. federal laws, is supervised by the Office of the Comptroller of the Currency of the United States (OCC), and that *Caisse centrale Desjardins'*s operations in the U.S., as a bank holding company, are subject to the supervisory and regulatory authority of the Board of Governors of the Federal Reserve System. *Caisse centrale Desjardins* US Branch, the branch of *Caisse centrale Desjardins* operating in the State of Florida and incorporated under the U.S. federal laws, is also supervised by the OCC.

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

Desjardins Group's public communications often include verbal 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 in this MD&A 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 under sections 1.2, "Monitoring of financial objectives", 1.3, "Changes in the economy and the industry", 2.2, "Analysis of business segment results", 3.0, "Balance sheet review", and 5.0, "Additional information". 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, these 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. A number of factors beyond Desjardins Group's control 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, counterparty and issuer, market, foreign exchange, liquidity, operational, insurance, strategic and reputation risk. Additional risk factors include environmental risk, legislative or regulatory developments in Quebec, Canada or globally, such as changes in fiscal and monetary policies; liquidity reporting and regulatory guidance, or interpretations thereof, and amendments to and new interpretations of capital guidelines.

There are also factors linked to changes in economic and financial conditions in Quebec, Canada or globally, including the unemployment rate; the geographic concentration of economic activity; changes in interest rates and exchange rates; trade between Quebec and the United States; the ability of third parties to comply with their obligations to Desjardins Group; consumer spending; credit demand; the effects of increased competition in a market open to globalization; and competition from new entrants and established competitors. There is also fraud, including fraud resulting from the use of new technologies in unprecedented ways against Desjardins Group, its members or its clients; legal or regulatory procedures and lawsuits; consumer saving habits; the effects of possible natural disasters or international conflicts, including terrorism; and new developments.

Furthermore, there are also operational risk factors, such as risk management models with intrinsic limitations, technological issues, service disruptions caused by the Internet or other technological issue, the ability to design new products and services and bring them to market in a timely fashion, the ability to collect complete and accurate information on clients and counterparties, and the ability to perform and integrate strategic acquisitions and alliances. Lastly, there are also changes to the accounting policies Desjardins Group uses to present its balance sheet and operating results, including the uncertainties associated with significant accounting assumptions and estimates, as well as changes to estimates, the impact of applying future accounting changes, the ability to recruit and retain key management personnel, including senior management and management's ability to foresee and manage the risk factors.

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 results. Additional information about these and other factors is found in section 4.0, "Risk management". 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.

Any forward-looking statements contained in this report represent the views of management only as at the date hereof, and are presented for the purpose of assisting members and analysts in understanding 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 verbal or written forward-looking statements that may be made from time to time by or on behalf of Desjardins Group, except as required under applicable securities legislation.

1.0 DESJARDINS GROUP

SECTION 1.1

PROFILE AND STRUCTURE

WHO WE ARE

Desjardins Group is the largest cooperative financial institution in Quebec, with assets of $196.7 billion. We are also the leading cooperative financial group in Canada, bringing together 397 caisses in Quebec and Ontario, the *Fédération des caisses Desjardins du Québec* and its subsidiaries (including *Capital Desjardins inc.*), *Caisse centrale Desjardins,* the *Fédération des caisses populaires de l'Ontario Inc.* and the *Fonds de sécurité Desjardins*. A number of our subsidiaries and components are active across Canada. Our Personal Services and Business and Institutional Services, Wealth Management and Life and Health Insurance, and Property and Casualty Insurance business segments offer a full range of financial products and services adapted to the needs of our members and clients, individuals and businesses alike. As one of the largest employers in the country, Desjardins Group capitalizes on the skills of 44,942 employees and the commitment of 5,268 elected officers.

The tasks of carrying out treasury operations and acting as the official Desjardins representative with the Bank of Canada and the Canadian banking system are assumed by *Caisse centrale Desjardins,* also a cooperative financial institution which is an integral part of Desjardins Group.

MISSION

To contribute to improving the economic and social well-being of people and communities within the compatible limits of its field of activity:

- By continually developing an integrated cooperative network of secure and profitable financial services, owned and administered by the members, as well as a network of complementary financial organizations with competitive returns, controlled by the members.
- By educating people, particularly members, officers and employees, about democracy, economics, solidarity, and individual and collective responsibility.

WHAT MAKES US DIFFERENT

At Desjardins Group we stand out from other Canadian financial institutions because of our cooperative nature. Our mission and strong values reflect our cooperative nature and are championed by our officers, managers and employees. Our mission and our values are echoed in our priorities and help us achieve our vision to promote sustainable prosperity within the communities we serve. Since the inception of the first caisse in 1900 in Lévis, Quebec, Desjardins Group has been a key player in financial education. We believe that the cooperative business model is key to sustainable prosperity and is more relevant than ever.

What guides us in our actions is the desire to be close to our members and clients. Thanks to our varied distribution channels, numerous intermediary networks and personnel who strive to deliver the highest quality of service, we are able to stay close to our members and the communities. In order to best meet our members' increasingly diverse needs, we pay special attention to the number of caisses and our range of service delivery methods. We also seek, in this way, to support and enhance the cooperative nature of the caisses, in terms of democracy, representation, education and training, intercooperation and support for community development.

Another hallmark of Desjardins Group is the active participation of elected officers in the caisses and in the organization's decision-making structure through the regional general meetings and the councils of representatives.

VISION

Desjardins,
the leading cooperative financial group in Canada,
inspires trust around the world
through the commitment of its people,
its financial strength and
its contribution to sustainable prosperity.

STRUCTURE OF DESJARDINS GROUP

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

MEMBERS

REGIONAL GENERAL MEETINGS
COUNCILS OF REPRESENTATIVES
ASSEMBLY OF REPRESENTATIVES

CAISSES
GENERAL MEETING
BOARD OF DIRECTORS
PRESIDENT AND CHIEF EXECUTIVE OFFICER OF DESJARDINS GROUP

MONITORING
Desjardins Group Monitoring Office

DESJARDINS GROUP CORPORATE EXECUTIVE DIVISION

CAISSE NETWORK
- Cooperative Development and Democratic Governance Support
- Cooperative Network Support

DESJARDINS GROUP FUNCTIONS
- Finance and Office of the CFO
- Risk Management
- Technology and Shared Services
- Treasury, Investor Relations and Compliance
- People and Culture
- Communications

BUSINESS SECTORS

Personal Services	Business and Institutional Services	Wealth Management and Life and Health Insurance	Property and Casualty Insurance
Regular, convenience and savings transactions	Regular, convenience and savings transactions	Insurance for individuals and business people	Automobile insurance
Financing	Integrated offer for businesses	Group insurance plans	Motorcycle and recreational vehicle insurance
Card and payment services	Integrated offer for the agricultural and agri-food industries	Savings for individuals and business people	Home insurance
Telephone and Internet access services	Specialized services	Specialized savings	Business insurance
	Capital markets	Group retirement savings	Pet insurance
	Development capital and business ownership transfers	Brokerage and private management	Distribution of financial products
	Payroll services		

HIGHLIGHTS

- Combined surplus earnings before member dividends of $1,591 million, a result comparable to 2011
- A total of $364 million returned to members and the community, which includes the member dividend expense, sponsorships and donations
- Growth of 3.3% in operating income, which totalled $11.3 billion
- Increase in the number of credit cards issued, for a total of more than 5 million cards outstanding
- In-force group insurance premiums hit the $2.0 billion mark
- Productivity index of 71.3%, comparable to the 2011 ratio
- Tier 1 capital ratio of 16.8% as at December 31, 2012
- Annual growth of 3.5% in total assets, which amounted to $196.7 billion as at December 31, 2012
- Residential mortgage loans outstanding up $6.2 billion over the year, to total $85.9 billion
- Quality loan portfolio, with a gross impaired loans ratio of 0.35%
- Increase of 5.0% in savings recruitment, which amounted to $129.6 billion
- Year-over-year growth of $32.1 billion in assets under administration to total $313.1 billion at the end of 2012
- Sales of capital shares of the Federation reached $1 billion during 2012
- US $1.5 billion in medium-term covered bonds issued by *Caisse centrale Desjardins* on the U.S. market
- $800 million in medium-term notes issued by *Caisse centrale Desjardins* on the Canadian market
- Redemption, on June 1, 2012, by *Capital Desjardins inc.* of all its outstanding Series C Senior Notes due in 2017, in the amount of $300 million
- Acquisition of an interest in Maple Group Acquisition Corporation, representing a commitment of $98 million
- Acquisition of several insurance brokers by Western Financial Group Inc.:
  - Hodges & Company Insurance Services Ltd., a British Columbia-based brokerage network specializing in commercial insurance
  - Brown & Ward Insurance Ltd., a leading property and casualty insurance broker in Alberta
  - Roblin Insurance Travel and Realty Agencies Ltd., based in Manitoba
  - BC Yacht Insurance Brokers Inc., a company based in Sidney, British Columbia
  - Orion Insurance Brokers Ltd., with offices in Winnipeg, Manitoba
- On February 4, 2013, Desjardins Group, through Desjardins Financial Corporation Inc., entered into a final agreement, to purchase between 25% and 40% of the outstanding shares of Qtrade Canada Inc.

TABLE 1 – BALANCE SHEET AND RATIOS
As at December 31
(in millions of dollars, as a percentage and as a coefficient)

	2012	2011	2010
Balance sheet			
Assets	$ 196,706	$ 190,137	$ 178,931
Loans	132,576	125,154	118,258
Deposits	129,624	123,403	114,663
Equity	16,041	14,027	12,156
Ratios			
Tier 1 capital ratio(1)	16.8%	17.3%	17.7%
Total capital ratio(1)	19.3%	19.3%	18.7%
Gross impaired loans/gross loans ratio	0.35%	0.41%	0.43%
Gross loans/deposits	1.03	1.02	1.04

(1) See section 3.2, "Capital management".

TABLE 2 – FINANCIAL RESULTS AND RATIOS

For the years ended December 31
(in millions of dollars and as a percentage)

	2012	2011	2010
Results			
Net interest income	$ 3,848	$ 3,921	$ 3,892
Net premiums	5,126	4,851	4,360
Other operating income(1)			
Deposit and payment service charges	499	512	535
Lending fees and credit card service revenues	517	483	451
Brokerage, investment fund and trust services	700	676	656
Other	610	493	240
Operating income(1)	11,300	10,936	10,134
Investment income(1)			
Net income on securities at fair value through profit or loss	674	1,706	984
Net income on available-for-sale securities	268	299	174
Net other investment income	236	264	251
	1,178	2,269	1,409
Total income	12,478	13,205	11,543
Provision for credit losses	241	237	203
Claims, benefits, annuities and changes in insurance and investment contract liabilities	4,397	5,292	4,136
Non-interest expense	5,760	5,623	5,380
Income taxes on surplus earnings	489	471	438
Surplus earnings before member dividends	$ 1,591	$ 1,582	$ 1,386
Contribution to combined surplus earnings by business segment			
Personal Services and Business and Institutional Services	$ 889	$ 987	$ 934
Wealth Management and Life and Health Insurance	241	280	249
Property and Casualty Insurance	205	144	131
Other	256	171	72
	$ 1,591	$ 1,582	$ 1,386
Amount returned to members and the community			
Provision for member dividends	$ 279	$ 320	$ 299
Sponsorships and donations	85	81	80
	$ 364	$ 401	$ 379
Ratios			
Return on equity(1)	10.4%	12.2%	12.2%
Productivity index(1)	71.3	71.1	72.6

(1) See "Basis of presentation of financial information" on page 15.

TABLE 3 – OTHER INFORMATION

As at December 31 and for the years then ended

	2012	2011	2010
Number of members	5.581 million	5.617 million	5.723 million
Number of elected officers	5,268	5,366	5,877
Number of employees	44,942	44,645	42,641
Number of caisses	397	422	451
Number of service centres	897	888	924
Number of automated teller machines	2,508	2,559	2,652
Number of automated transactions	783,648,717	677,329,852	596,344,721
Including transactions made using mobile devices (1)	68,517,593	23,230,629	2,090,008

(1) The transaction service for mobile devices was launched in September 2010.

SECTION 1.2

MONITORING OF FINANCIAL OBJECTIVES

TABLE 4 – PROGRESS REPORT ON 2012 RESULTS
For the year ended December 31
(as a percentage)

	Financial objectives for 2010-2012	Results for 2012	Financial objectives for 2013-2016
Growth and development			
Growth in operating income(1)	Greater than 8%	3.3%	Between 5% and 10%
Profitability and productivity			
Productivity index(1)	Less than 70% in 2012	71.3%	Less than 70% in 2016
Gap between income growth and expense growth(1)	Greater than 2% in 2012	(0.3)	Greater than 2%
Growth in surplus earnings after income taxes	Between 5% and 10%	0.6	Between 5% and 10%
Return on equity(1)	Greater than 9%	10.4	Greater than 8%
Financial stability and risk management			
Tier 1 capital ratio	Greater than 15%	16.8%	Greater than 15%

(1) See "Basis of presentation of financial information" on page 15.

REVIEW OF 2012 FINANCIAL RESULTS

The priority financial objectives for 2010-2012 were established based on the orientations and initiatives that supported Desjardins Group's 2010-2012 Strategic Plan. During this period, Desjardins Group grew its surplus earnings before member dividends from $1,091 million as at December 31, 2009, to close to $1,591 million as at December 31, 2012. This increase in surplus earnings was achieved while implementing various measures that helped Desjardins Group strengthen its financial stability and resilience to a less favourable future economic context.

More specifically in 2012, Desjardins Group posted a higher-than-expected financial performance, with surplus earnings before member dividends of $1,591 million, comparable to the previous year. In spite of strong pressure on its income base resulting from slower economic growth and persistent low interest rates, which had a direct impact on net interest income, Desjardins Group's initiatives made it possible to continue to work at improving productivity. In addition, it made major investments in its information technology transformation program and in continuing various strategic development initiatives.

FINANCIAL OUTLOOK FOR 2013–2016

In January 2013, the Board of Directors adopted Desjardins Group's strategic goals for 2013–2016, which were established to contribute to Desjardins's business development by focusing on service, growth and efficiency as major priorities.

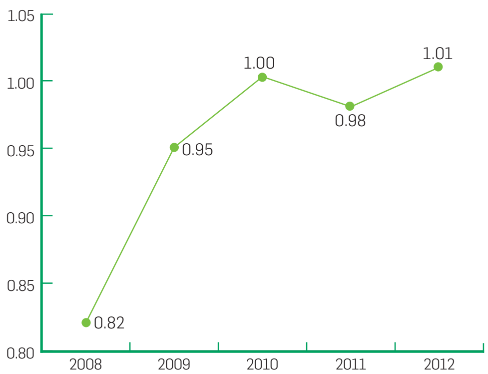
In spite of less favourable forecasts for economic and financial conditions for the next few years, Desjardins Group has maintained most of its financial objectives for the 2013–2016 period, but it lowered its growth in operating income and return on equity objectives slightly. In these still uncertain economic conditions, the current low interest rate environment will last for some time and put pressure on net interest income and, consequently, on Desjardins Group's surplus earnings. Furthermore, significant additional expenses related to pension plans and the harmonizing of sales taxes will put downward pressure on Desjardins's profitability starting in 2013.

Building on its achievements from the 2010–2012 Strategic Plan, Desjardins Group will undertake its strategic initiatives for 2013–2016 on a solid footing so it is better prepared to meet the new Basel III regulatory requirements taking effect on January 1, 2013, which will affect both capitalization and liquidity. Raising productivity remains a top priority for Desjardins Group so that it can hold on to the competitive positioning of its service offer for its members and clients, achieve its profitability and growth targets, and strengthen its capitalization over 2013–2016.

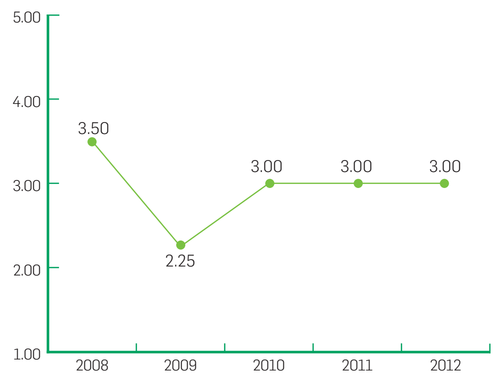
SECTION 1.3

CHANGES IN THE ECONOMY AND THE INDUSTRY

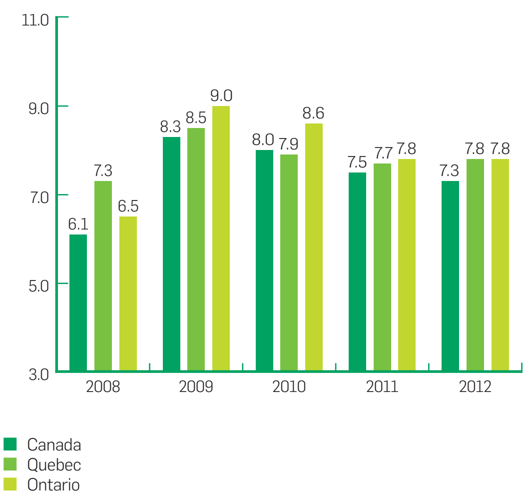
CHANGES IN THE CANADIAN DOLLAR VS. THE U.S. DOLLAR
(Canadian dollars/U.S. dollars)



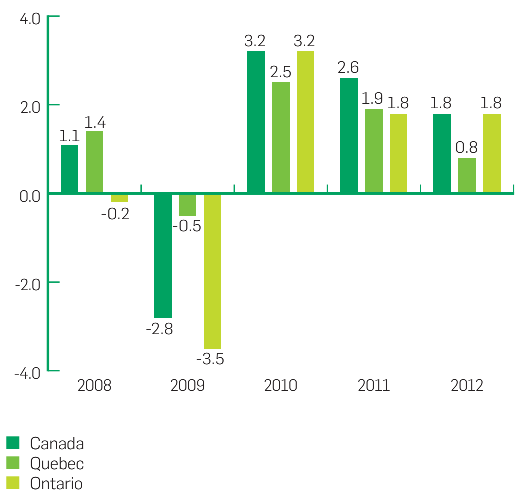
CHANGES IN THE PRIME RATE
(as a percentage)



CHANGES IN THE UNEMPLOYMENT RATE
(as a percentage)



CHANGES IN GDP
(as a percentage)



2012 ECONOMIC ENVIRONMENT

Several obstacles stood in the way of economic recovery in 2012. Growth even slowed down in some parts of the world, especially in the eurozone, where the sovereign debt crisis continues. Encouraging progress has nevertheless been observed in this region. Greece obtained a debt reduction that required considerable effort on the part of its private creditors and a promise to continue applying austerity measures. The European Central Bank was also more active, conducting long-term refinancing operations, reducing its key interest rates and creating a sovereign securities purchase program. European countries have also implemented a Financial Stability Mechanism—a new rescue fund—and continued negotiations aimed at improving the efficiency of the eurozone, which led to planning a banking union.

Many emerging countries suffered from weak demand from industrialized countries. They also had difficulty attracting capital, with investors demonstrating a high aversion to risk. Growth in China stabilized at under 8%, confirming the success of its economic actions. The United States and Japan were among the few countries to see real GDP rise faster in 2012. In the U.S., accelerating growth was supported by the real estate market, which is set to get back on its feet. In Japan, results were boosted by the reconstruction effort that followed the March 2011 earthquake.

In Canada, growth slowed somewhat from 2011 to 2012. Foreign trade continued to be affected by the strength of the Canadian dollar and the weakness of global demand. Quebec and Ontario were directly impacted by these factors, but provincial economies more dependent on natural resources also suffered as a result of weaker commodity prices. The Canadian economy as a whole was affected by government measures aimed at reducing deficits and by more moderate consumption of goods by households. The real estate market also showed signs of losing momentum after several years of rising prices and sustained activity.

INDUSTRY DESCRIPTION AND TRENDS

Despite the tentative economic environment that prevailed in the past year, there were no major changes in the Canadian financial industry. Canada has over 800 savings and loan cooperatives, of which slightly less than half are part of Desjardins Group, as well as some 70 Canadian and foreign banks. Insurance companies are another major industry player. In 2012, more than 300 were in operation across Canada. Although some were present in both property and casualty insurance and life and health insurance, most of them, almost two-thirds, specialized in property and casualty insurance, while the remaining third operated in life and health insurance.

There were a few key players in life and health insurance, with the top three accounting for close to 60% of premiums collected in this industry in Canada. Desjardins Group, through its subsidiary Desjardins Financial Security Life Assurance Company, ranked fifth in this market in 2012. The property and casualty sector is less concentrated, with a higher number of large institutions. The top three companies therefore accounted for only about 30% of the industry. However, consolidation appears to be underway in this sector due to the merger of Intact and AXA at the end of 2011. Through its subsidiary Desjardins General Insurance Group Inc., Desjardins Group ranked eighth in 2012, up from ninth in 2011

Canadian financial institutions stayed on course despite the many concerns preoccupying financial markets in 2012. They had to deal with an uncertain economic climate that did not encourage business and household confidence as well as profit margins under pressure from low interest rates. Despite conditions that could have tested their mettle, such as a slowdown in residential real estate markets and the state of Canadians' personal finances, these financial institutions remained stable. The World Economic Forum has rated the Canadian banking industry the strongest in the world for a fifth consecutive year. While this does not mean it is invincible, it does have certain advantages over other banking systems the world over.

ECONOMIC OUTLOOK FOR 2013

Economic conditions are expected to remain precarious in many parts of the world in 2013, especially in the eurozone. Austerity measures should still hinder growth for the next few quarters. The European Central Bank may intervene again to support the economy and the financial system by lowering key interest rates one last time and by buying sovereign bonds of countries experiencing difficulty. However, as a prerequisite to such intervention, these countries will have to formally request assistance from the European Stability Mechanism. Spain may make this move. Greece could still undermine the markets, and more and more participants are recommending a second debt restructuring, one that would be assumed by the public sector this time.

Elsewhere in the world, the economies of emerging countries should improve as the situation turns around in Europe and the United States. The outcome of the fiscal cliff negotiations at the end of 2012 should reduce U.S. growth by approximately 1% in 2013, and the need to raise the debt ceiling remains a major source of concern. Other factors will offset the government's negative contribution to growth. Consumption will be supported by improving household finances and a lower unemployment rate. In addition, the real estate market should continue its new upward trend. The pace of growth in the U.S. economy as a whole should nevertheless slow down somewhat in 2013. This should prompt the U.S. Federal Reserve to maintain its key interest rates at low levels until the mid-2015 and extend its quantitative easing program until at least fall 2013.

The Canadian economy may benefit from growing global demand and a slight rise in commodity prices. On the other hand, the Canadian dollar is expected to remain above parity with the U.S. dollar, which will continue to harm exports, in particular for manufacturers mainly based in Quebec and Ontario. Most public spending cuts and tax increases seem to be behind us. Consumption will probably continue to keep pace with improvements in the labour market and rising income levels, but caution is still called for, given the already high debt levels. The real estate market should continue to stabilize gradually. Overall, economic growth for 2013 should approach 2% in Canada as well as in Ontario and 1.5% in Quebec. Economic activity will likely not, however, be strong enough to bring inflation back above the Bank of Canada's target range, and so the Bank is not expected to raise key interest rates.

2.0 REVIEW OF FINANCIAL RESULTS

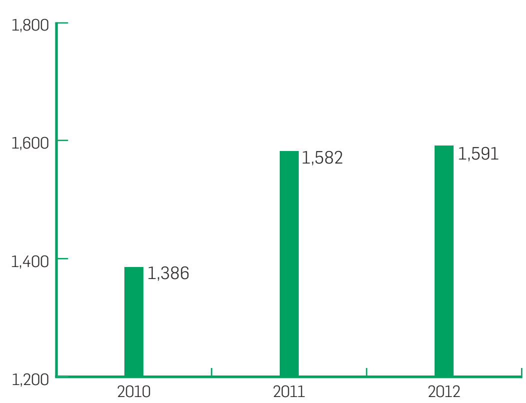
HIGHLIGHTS

- Combined surplus earnings before member dividends of $1,591 million, which is comparable to 2011 results
- A total of $364 million returned to members and the community, which includes member dividends, sponsorships and donations
- Growth of 3.3% in operating income, which totalled $11.3 billion
- Increase in the number of credit cards issued, for a total of more than 5 million cards outstanding
- A $73 million, or 1.9%, decrease in net interest income
- Net premium growth of $275 million, or 5.7%
- In-force group insurance premiums hit the $2.0 billion mark
- A $162 million, or 7.5%, increase in other operating income
- A $1,091 million, or 48.1%, decrease in investment income
- A $895 million, or 16.9%, decrease in expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities
- A $137 million, or 2.4%, increase in non-interest expense
- Productivity index of 71.3%, comparable to the 2011 ratio

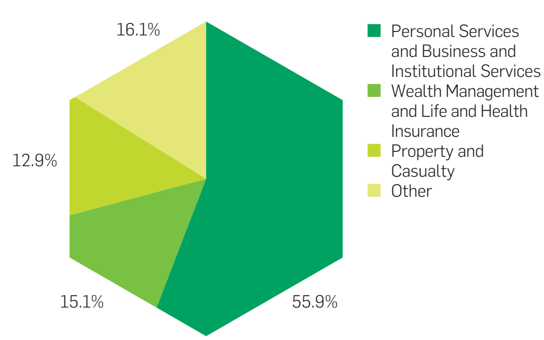
SECTION 2.1

ANALYSIS OF 2012 RESULTS

SURPLUS EARNINGS BEFORE MEMBER DIVIDENDS
(in millions of dollars)



SEGMENT CONTRIBUTIONS TO SURPLUS EARNINGS BEFORE MEMBER DIVIDENDS IN 2012



2012 SURPLUS EARNINGS

For 2012, Desjardins Group reported surplus earnings before member dividends of $1,591 million, which is comparable to 2011 results. Return on equity was 10.4%, compared to 12.2% in 2011. The lower return was due to the increase in equity as a result of the issue of $1.0 billion in capital shares by the Federation and growth in undistributed surplus earnings.

These results include the contribution of $889 million, or 55.9% of surplus earnings, made by the Personal Services and Business and Institutional Services segment. The Wealth Management and Life and Health Insurance segment and the Property and Casualty Insurance segment contributed $241 million and $205 million, respectively, representing 15.1% and 12.9% of surplus earnings. The operations grouped under the Other category made a contribution of $256 million, or 16.1%, of surplus earnings.

Desjardins Group's approach to distributing its surplus earnings is to ensure an appropriate balance between development, capitalization and sustainability. With that in mind, for fiscal 2012, the amount provisioned as a liability for member dividends, calculated based on caisse network surplus earnings, was $305 million, compared to $331 million in 2011. A $26 million downward adjustment was made in the 2012 member dividend expense to take into account the reversal of the amount provisioned in 2011. Between member dividends, donations and sponsorships, the total amount returned to members and the community in 2012 was $364 million, compared to $401 million in 2011.

OPERATING INCOME

Operating income includes net interest income, net premiums and other operating income, as presented in Table 5. Operating income totalled $11,300 million, up $364 million, or 3.3%, compared to 2011.

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 bonds. It is affected by interest rate fluctuations and funding strategies, as well as by 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 main asset and liability classes.

For 2012, net interest income was $3,848 million, down $73 million, or 1.9%, from the previous year. Expressed as a percentage of average assets, this net margin was down 22 basis points. Accordingly, the change in interest rates and its effect on the credit, investment and savings products and maturities selected by members shaved 28 basis points off the average return on loans, while the average cost of deposits decreased 6 points. The negative change in net interest income is explained in Table 7.

Interest income amounted to $5,865 million in 2012, a decrease of $25 million, or 0.4%, compared to the previous year. Overall, the $8.6 billion, or 6.4%, growth in the average volume of total interest bearing assets boosted interest income by $377 million, while the 28-basis-point decrease in the average return on these assets reduced it by $402 million.

As at December 31, 2012, Desjardins Group's loan portfolio outstanding, net of the allowance for credit losses, stood at $132.6 billion, compared to a volume of $125.2 billion as at December 31, 2011, for an increase of $7.4 billion, or 5.9%. All the main loan categories offered by Desjardins contributed to this increase, but its home financing market activities stand out as the biggest contributor. Desjardins Group was able to capitalize on the strong performance of the housing market in Quebec and Ontario during that period. As a result, its mortgage loans outstanding reached a volume of $85.9 billion, up $6.2 billion, or 7.8%, compared to the $5.2 billion, or 7.0%, increase recorded in 2011. In addition, the increase in consumer, credit card and other personal loans since the end of 2011 was $535 million, or 3.0%, resulting in outstanding loans totalling $18.5 billion as at December 31, 2012, compared to growth of $481 million, or 2.7%, the previous year.

Loans to businesses and governments grew by $596 million, or 2.1%, in 2012 to total $28.5 billion, compared to an increase of $1.2 billion, or 4.4%, in 2011.

TABLE 5 – OPERATING INCOME

For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Net interest income	$ 3,848	$ 3,921	$ 3,892
Net premiums	5,126	4,851	4,360
Other operating income (see Table 8)	2,326	2,164	1,882
Total operating income	$ 11,300	$ 10,936	$ 10,134

TABLE 6 – NET INTEREST INCOME ON AVERAGE ASSETS AND LIABILITIES

For the years ended December 31
(in millions of dollars and as a percentage)

	2012			2011		
	Average balance	Interest	Average rate	Average balance	Interest	Average rate
Assets						
Interest-bearing assets						
Securities, cash and deposits with financial institutions	$ 18,112	$ 391	2.16%	$ 17,161	$ 428	2.49%
Loans	125,154	5,474	4.37	117,548	5,462	4.65
Total interest-bearing assets	143,266	5,865	4.09	134,709	5,890	4.37
Other assets	6,773	—	—	5,956	—	—
Total assets	$ 150,039	$ 5,865	3.91%	$ 140,665	$ 5,890	4.19%
Liabilities and equity						
Interest-bearing liabilities						
Deposits	$ 126,604	$ 1,851	1.46%	$ 119,266	$ 1,818	1.52%
Borrowings and subordinated bonds	3,180	166	5.22	2,944	151	5.13
Total interest-bearing liabilities	129,784	2,017	1.55	122,210	1,969	1.61
Other liabilities	8,670	—	—	7,895	—	—
Equity	11,585	—	—	10,560	—	—
Total liabilities and equity	$ 150,039	$ 2,017	1.34%	$ 140,665	$ 1,969	1.40%
Net interest income		$ 3,848			$ 3,921	
As a percentage of average assets			2.57%			2.79%

TABLE 7 – IMPACT OF CHANGES IN VOLUMES AND RATES ON NET INTEREST INCOME

For the year ended December 31
(in millions of dollars and as a percentage)

	2012			Increase (decrease)	
	Change in average volume	Change in average rate	Interest	Average volume	Average rate
Assets					
Securities, cash and deposits with financial institutions	$ 951	(0.33)%	$ (37)	$ 24	$ (61)
Loans	7,606	(0.28)	12	353	(341)
Change in interest income			(25)	377	(402)
Liabilities					
Deposits	7,338	(0.06)	33	112	(79)
Borrowings and subordinated bonds	236	0.09)	15	12	3
Change in interest expense			48	124	(76)
Change in net interest income			$ (73)	$ 253	$ (326)

Interest expense stood at $2,017 million, up $48 million, or 2.4%, over 2011. The $7.6 billion, or 6.2%, growth in average funding from deposits, borrowings and subordinated bonds pushed up interest expense by $124 million, while the 6-basis-point decrease in the average cost of deposits reduced interest expense by $79 million.

At the end of 2012, Desjardins Group's deposits outstanding had increased by $6.2 billion, or 5.0%, to total $129.6 billion. The composition of the deposit portfolio did not change significantly during the year. Savings from its members and clients—individuals, businesses and governments—still make up the main source of financing to support Desjardins's development. It forms a solid base that alone accounted for 98.3% of Desjardins Group's deposit liabilities at the end of 2012, compared to 98.5% in 2011. These savings were up $5.9 billion, or 4.8%, to total $127.4 billion as at December 31, 2012.

To round out its main sources of financing, other types of deposits, such as deposits by deposit-taking institutions and other sources, represented 1.7% of Desjardins Group's deposit liabilities at the end of 2012. These deposits were up $363 million over the year to total $2.2 billion.

NET PREMIUMS

Net premiums, comprising life and health insurance, property and casualty insurance, and annuity premiums, rose $275 million, or 5.7%, to total $5,126 million for the year ended December 31, 2012.

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE SEGMENT

The overall insurance operations of the Wealth Management and Life and Health Insurance segment posted net insurance and annuity premium income of $3,366 million for 2012, compared to $3,261 million for 2011, representing a 3.2% increase. Net insurance premiums were up 5.3% over 2011 to total $3,099 million. They increased by 4.5% in Quebec and 6.1% in the other provinces.

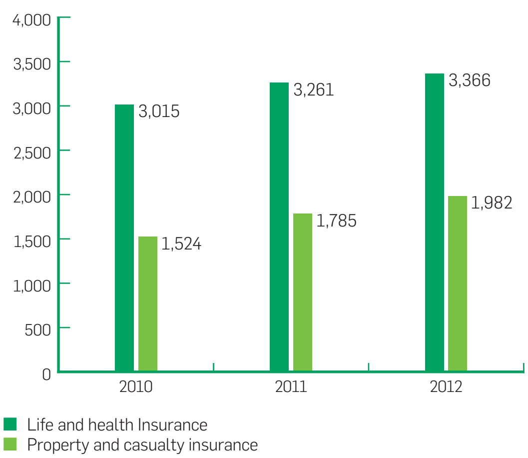
Premium volume for individual insurance was $533 million, a $34 million increase over 2011. Premium volume from the network of financial security advisors assigned to Desjardins caisses increased by 4.3% over the previous year. After remarkable sales growth from the distribution networks in recent years, premiums cashed increased by $23 million, or 7.6%, over 2011. Furthermore, the volume of premiums related to products marketed via direct distribution posted 6.9% growth to stand at $88 million.

Premiums for group insurance purchased by Desjardins Group members increased by 4.6% and group insurance premiums from other client bases were up 5.1%.

PROPERTY AND CASUALTY INSURANCE SEGMENT

The overall operations of the Property and Casualty Insurance segment generated net premium income of $1,982 million in 2012, compared to $1,785 million in 2011, an 11.0% increase stemming from, among other things, the increase in policies issued due to growth initiatives targeting mass market clients and groups both in Quebec and across Canada, the development of white label partnerships, the development of the insurance offer for businesses and higher average premiums in certain activity sectors. Western Financial Group Inc. contributed $109 million to net premium revenue in 2012.

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.

OTHER OPERATING INCOME

TABLE 8 – OTHER OPERATING INCOME
For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Deposit and payment service charges	$ 499	$ 512	$ 535
Lending fees and credit card service revenues	517	483	451
Brokerage, investment fund and trust services	700	676	656
Other	610	493	240
Total other operating income	$ 2,326	$ 2,164	$ 1,882

Other operating income stood at $2,326 million for fiscal 2012, up $162 million, or 7.5%, over 2011.

Income from deposit and payment service charges decreased by $13 million, or 2.5%. Income from lending fees and credit card service revenues, consisting mainly of income from payment solutions offered by Card and Payment Services, totalled $517 million in 2012, up by 7.0%, or $34 million, over 2011, as a result of growth in business volume. Income from brokerage, investment fund and trust services amounted to $700 million, an increase of $24 million, or 3.6%, chiefly due to growth in average assets under management.

Income under the Other category increased by $117 million, or 23.7%, over 2011, to total $610 million. The increase was partly due to higher commission income from the insurance sales generated by Western Financial Group Inc., a subsidiary acquired in the second quarter of 2011.

INVESTMENT INCOME

TABLE 9 – INVESTMENT INCOME
For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Net income on securities at fair value through profit or loss	$ 674	$ 1,706	$ 984
Net income on available-for-sale securities	268	299	174
Net other investment income	236	264	251
Total investment income	$ 1,178	$ 2,269	$ 1,409

Investment income stood at $1,178 million for fiscal 2012, down $1,091 million, or 48.1%, compared to 2011.

Net income on securities at fair value through profit or loss was down $1,032 million, or 60.5%, to $674 million in 2012. The decrease was chiefly due to the reduction in investment income related to life and health insurance operations resulting from the $1,073 million change in the fair value of assets backing liabilities, which was partly offset by changes in actuarial liabilities. This decrease was mitigated by the $162 million favourable change in the fair value of the asset-backed term note (ABTN) portfolios net of hedging positions. Net income on available-for-sale securities and net other investment income decreased as realized gains on disposal of investments were lower in 2012 than the previous year.

TOTAL INCOME

Total income, comprising net interest income, net premiums, other operating income and investment income, amounted to $12,478 million, a decrease of $727 million, or 5.5%, compared to 2011.

PROVISION FOR CREDIT LOSSES

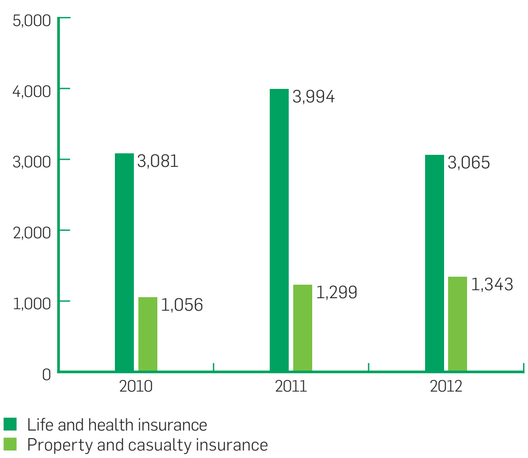
Desjardins Group's loan portfolio continued to be of excellent quality. As at December 31, 2012, gross impaired loans outstanding stood at $466 million, down $54 million since December 31, 2011. The ratio of gross impaired loans, as a percentage of the total gross loan portfolio, was 0.35% as at December 31, 2012, an improvement over the ratio of 0.41% as at December 31, 2011. Desjardins Group's ratio in this regard remains one of the best in the Canadian banking industry.

The provision for credit losses totalled $241 million, up $4 million, or 1.7%, over 2011, mainly as a result of the increase in loans outstanding for credit card financing in 2012, which was offset by adjustments related to changes in the parameters of the provision.

CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE AND INVESTMENT CONTRACT LIABILITIES

CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE AND INVESTMENT 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 and investment contract liabilities decreased $895 million, or 16.9%, to $4,397 million for the year ended December 31, 2012.

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE SEGMENT

The Wealth Management and Life and Health Insurance segment had expenses of $3,065 million, down $929 million, or 23.3%, compared to 2011, mainly as a result of a $987 million decrease in changes in actuarial liabilities included under "Insurance and investment contract liabilities", attributable in particular to the fluctuation in the fair value of investments. Changes in valuation assumptions in the normal course of business pushed expenses up by $60 million, whereas they had decreased by $43 million in 2011. Gains related to underwriting experience in individual insurance narrowed the unfavourable difference created by these changes in assumptions.

PROPERTY AND CASUALTY INSURANCE SEGMENT

Expenses for the Property and Casualty Insurance segment were $1,343 million, compared to $1,299 million in 2011, for an increase of $44 million, or 3.4%. The loss ratio was 69.1% in 2012, compared to 73.1% in 2011.

NON-INTEREST EXPENSE

Non-interest expense totalled $5,760 million compared to $5,623 million in 2011, an increase of $137 million, or 2.4%, essentially reflecting the increase in salaries and fringe benefits as a result of business growth and annual indexing. This increase was offset, however, by a reduction in provisions related to the investment portfolio.

PRODUCTIVITY INDEX

The productivity index, calculated as the ratio of non-interest expense to total income, net of expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities, was 71.3% in 2012, comparable to the index in 2011.

SALARIES AND FRINGE BENEFITS

Salary and fringe benefit expenses rose $100 million, or 3.6%, to $2,882 million in 2012, mainly reflecting growth and salary indexing. This expense item represented 50.0% of Desjardins Group's total non-interest expense, which is comparable to the 2011 percentage. For 2012, salaries amounted to $2,396 million, up 3.2% over $2,321 million in 2011.

The ratio of fringe benefits to total base compensation remained relatively stable, going from 19.9% in 2011 to 20.3% in 2012.

OTHER EXPENSES

For 2012, expenses related to premises, equipment and furniture (including depreciation) totalled $415 million, compared to $428 million in 2011, a decrease of $13 million, or 3.0%. Service agreement and outsourcing fees were down $42 million, or 15.6%, compared to the previous year, to stand at $228 million. This decrease was partly attributable to the synergies resulting from the creation of Desjardins Technology Group Inc. Communications expenses, which include telephone systems, advertising, courier services and stationery costs, rose $24 million, or 9.7%, from 2011 to stand at $271 million in 2012.

Other expense categories totalled $1,964 million, for an increase of $68 million, or 3.6%, compared to 2011. This increase is largely due to the operations of the subsidiaries acquired during 2011 and higher professional fees. Higher expenses related to the BONUSDOLLARS Rewards Program and asset revaluation also contributed to expense growth. However, the reduction in provisions related to the investment portfolio offset the increase in non-interest expense.

NON-INTEREST EXPENSE
(in millions of dollars)

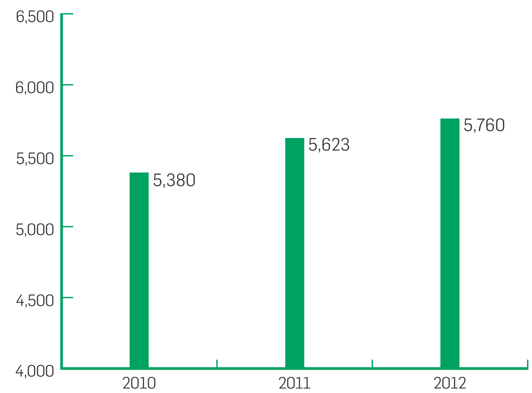


TABLE 10 – NON-INTEREST EXPENSE
For the years ended December 31
(in millions of dollars and as a percentage)

	2012	2011	2010
Salaries and fringe benefits			
Salaries	$ 2,396	$ 2,321	$ 2,173
Fringe benefits	486	461	428
	2,882	2,782	2,601
Premises, equipment and furniture, including depreciation	415	428	425
Service agreements and outsourcing	228	270	363
Communications	271	247	258
Other	1,964	1,896	1,733
Total non-interest expense	$ 5,760	$ 5,623	$ 5,380
Desjardins Group productivity index[(1)]	71.3%	71.1%	72.6%

(1) See "Basis of presentation of financial information" on page 15.

INCOME TAXES AND INDIRECT TAXES

Desjardins Group is a cooperative financial group, and each of its entities that operate as a financial services cooperative—mainly the caisses, *Caisse centrale Desjardins,* the *Fédération des caisses Desjardins du Québec* and the *Fédération des caisses populaires de l'Ontario*—is considered a private and independent company. This distinguishes Desjardins Group from most other financial institutions, which are large public corporations. Each caisse is therefore subject to the tax regulations applicable to private companies. Legislators have adapted these regulations to allow the caisses to accumulate a sufficient general reserve to serve as a capital base for the protection of members' deposits. When the general reserve reaches the legislated limit, the caisse is subject to the same tax rates as a large corporation.

Desjardins entities that are not financial services cooperatives are subject to the tax regulations that apply to large corporations.

Income taxes on surplus earnings include income taxes on the operations of Desjardins Group's various entities.

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 fiscal 2012, the entities of Desjardins Group paid $817 million in indirect taxes.

COMPARISON OF 2011 AND 2010

The following analysis presents a comparison between the results for the years ended December 31, 2011 and 2010.

For 2011, Desjardins Group posted surplus earnings before member dividends of $1,582 million, a $196 million, or 14.1%, increase over 2010. Return on equity was 12.2%, the same as in 2010.

These results reflected the significant contribution of the Personal Services and Business and Institutional Services segment, which totalled $987 million, or 62.4%, for the year ended December 31, 2011. For that same year, the Wealth Management and Life and Health Insurance segment and the Property and Casualty Insurance segment contributed $280 million and $144 million respectively, 17.7% and 9.1% of overall surplus earnings. For the operations grouped under the Other category, the contribution was $171 million, or 10.8%.

In 2011, operating income, comprising net interest income, net premiums and other operating income, amounted to $10,936 million, up $802 million, or 7.9%, compared to 2010. Net interest income remained relatively stable compared to 2010, reaching $3,921 million. Net premiums grew by 11.3% to total $4,851 million, due in particular to insurance premium growth in both life and health insurance and property and casualty insurance. Finally, other operating income amounted to $2,164 million, an increase of $282 million, or 15.0%, due mainly to the $90 million contribution from the consolidation of the operations of Western Financial Group Inc., a company acquired during 2011.

Investment income totalled $2,269 million in 2011, an increase of $860 million, or 61.0%, compared to 2010, primarily because of the $715 million growth in investment income associated with life and health insurance operations resulting from the change in the fair value of assets backing liabilities, which was partly offset by changes in actuarial liabilities

Desjardins Group's loan portfolio continued to be of excellent quality in 2011. As at December 31, 2011, gross impaired loans outstanding stood at $520 million, up $8 million since December 31, 2010.

As at December 31, 2011, expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities were up $1,156 million, or 27.9%, to $5,292 million. This growth mainly resulted from the increase in actuarial liabilities included under "Insurance and investment contract liabilities", including the increase in the fair value of investments, growth in the automobile insurance portfolio in Ontario, and Hurricane Irene, which affected primarily Quebec and the Maritimes during the third quarter of 2011.

Non-interest expense was $5,623 million in 2011, up $243 million, or 4.5%, compared to 2010, essentially due to an $85 million investment in modernizing IT systems, the consolidation of the operations of Western Financial Group Inc., for an amount of $122 million, and annual growth in salaries and fringe benefits, plus indexing.

SECTION 2.2

ANALYSIS OF BUSINESS SEGMENT RESULTS

Desjardins Group's financial reporting is organized by operations, which are defined based on the needs of its members and clients, and by the markets in which it operates, thereby reflecting its internal management structure. Desjardins Group's financial results are therefore divided into the following three business segments: Personal Services and Business and Institutional Services; Wealth Management and Life and Health Insurance; and Property and Casualty Insurance. This section presents the profile, activities, industry, 2012 financial highlights, 2013 strategy and priorities, and an analysis of results for each segment. In addition to these three segments, there is also the Other category.

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.

SECTION 2.2.1

PERSONAL SERVICES AND BUSINESS AND INSTITUTIONAL SERVICES

PERSONAL SERVICES

PROFILE

Personal Services offers a range of products and services to members and clients through the caisse network, including regular and convenience transactions, variable and term savings, financing, and payment and credit cards.

It also makes its products and services available through complementary distribution networks and mortgage representatives, by phone, online, via mobile applications, and at ATMs.

ACTIVITIES

Regular, convenience and savings activities include transactions carried out at the caisse counter, requests for information and specialty services (drafts, safety deposit boxes, etc.). They also include variable savings (chequing accounts, regular savings accounts, etc.) and term savings.

Financing activities include the following:

- **Residential mortgage loans**: for the purchase of new or existing homes and for renovations
- **Consumer loans**: such as loans for the purchase of automobiles and durable goods, advances to credit card holders, personal lines of credit and student loans

The activities of **Card and Payment Services** include card payment services for individuals and businesses, merchant payment services, financing solutions (Accord D) and point-of-sale financing for automobiles and durable goods.

AccèsD Services activities involve making products and services available at any time, anywhere in the world, by phone, online and via mobile applications.

INDUSTRY

The Canadian banking services industry represents an outstanding volume of $1,683 billion in financing and $1,113 billion in on-balance sheet savings, both variable- and fixed-rate.

The already widespread competition has only intensified in the industry, particularly in the mortgage market. The key success factors for thriving in the current low interest rate environment are service quality, productivity, and tailoring products to the specific needs of individual client segments.

The year was characterized by regulators' constant concerns over the fragile state of the economy and consumer debt levels. Key rates in Canada have not budged since September 2010, and even if the Bank of Canada intends to eventually raise rates, they will likely remain where they are for now, given the current economic climate in Canada. As a result, the Bank of Canada is not expected to start raising its key rates until early 2014.

It should also be mentioned that for the fourth time in as many years, the federal government has changed mortgage lending rules. The following are some of the changes that took effect in 2012:

- The maximum amortization period for mortgages insured by Canada Mortgage and Housing Corporation was reduced from 30 to 25 years.
- The maximum insurable loan amount for mortgage loan refinancings was reduced from 85% to 80% of home value .

Finally, the OSFI and the AMF have issued guidelines intended to limit borrower indebtedness and the risk of persistence of outstanding balances.

The purpose of these new measures is to prevent the real estate market from overheating and to combat over-indebtedness.

2012 FINANCIAL HIGHLIGHTS

- Desjardins is Quebec's leader in residential mortgages and consumer loans, including point-of-sale financing, with market shares of 35.8% and 22.9% respectively.
- Desjardins.com is a pioneer and leader in online services in Quebec, holding the title of most visited financial website in Quebec and one of the most visited in Canada. Desjardins Group has 2.3 million individual members who use AccèsD Internet.
- Desjardins is the number one credit and debit card issuer in Quebec. Personal Services has more than 5.1 million credit card holders and 5.6 million debit card holders in Canada.
- Residential mortgage loans grew by $6.3 billion, helping Desjardins keep its Quebec market share at 35.8%.
- On-balance sheet savings grew by $2.3 billion in Quebec, helping Desjardins keep its Quebec market share at 42.7%.

2013 STRATEGY AND PRIORITIES

The Personal Services sector intends to strengthen its lead in financing, savings and transactional services, while increasing satisfaction among Desjardins Group members and clients. This strategy will centre on offering high-quality and innovative products and services with respect to financing, savings, payments, regular transactions and convenience services, and remaining highly accessible.

In 2013, this sector will focus on the following priorities:

- Increase membership numbers, business volumes and member satisfaction by tailoring solutions to client needs
- Constantly strive to make the financing offer more competitive while maintaining growth
- Bolster growth in the payments sector to hold on to market share
- Continue to leverage technology and recruit resources to support development outside Quebec
- Develop automated services to make it simpler and easier for members and clients to access Desjardins products and services
- Optimize physical and virtual distribution
- Focus more on financial literacy activities, particularly with respect to responsible use of credit

BUSINESS AND INSTITUTIONAL SERVICES

PROFILE

Business and Institutional Services offers Desjardins members and clients a comprehensive, integrated line of products and services designed to meet the needs of businesses of all sizes, as well as institutions and cooperatives, through the caisses in Quebec and Ontario, their business centres and the major accounts team. Its offering includes regular and convenience transactions, securities investments, financing, specialized services, access to capital markets, development capital, business ownership transfers and advisory services.

It also makes its products and services available through complementary distribution networks, by phone, online, through mobile applications and at ATMs.

ACTIVITIES

In addition to regular, convenience, savings and loan activities, this sector supports businesses of all sizes through every stage of their growth in the Quebec, Canadian and international markets.

Credit activities targeting **medium-sized businesses** include Desjardins products and services in the following areas: commercial and industrial sectors, commercial real estate, the public sector, franchises and business ownership transfers.

This sector also provides a full range of products and services to meet the specific needs of businesses operating in the **agricultural and agri-food industries.**

Specialized services include asset custody and trust services, payroll and human resources solutions, international services, banking services and the Immigrant Investor Program.

Activities to provide access to **capital markets** meet the financing needs of large Quebec-based corporations, Canadian cooperatives and businesses operating in industries such as mining, metals and energy, and provide advisory services for business mergers and acquisitions, as well as intermediation and execution activities on the stock and bond markets. These services are provided by seasoned sales and trading teams who are supported by a research team that is renowned in the industry for its excellence.

Through its **development capital and business ownership transfer** activities, the sector invests, both directly and through funds, in Quebec cooperatives and SMEs with promising projects and guides them through every stage of their growth. Through the assets it manages, Desjardins Venture Capital Inc. supports the growth of 363 businesses, cooperatives and funds all across Quebec.

INDUSTRY

The Business and Institutional Services sector operates in a constantly changing and competitive economic environment. Certain risks and concerns, particularly those related to the global economy, have influenced the economic climate in Canada. Activity on the Canadian debt and equity market fluctuated widely throughout the year. The Canadian stock market underperformed compared to other world stock markets. Canadian key rates also remained unchanged.

Nonetheless, commercial and industrial loans showed some vigour, with 7.7% growth, as a result of an increase in non-capital expenditure by businesses. In agricultural loans, Quebec recorded 4.2% growth. With a 24.2% market share of the Quebec business loan market, estimated to be worth some $85 billion, Desjardins Group is a leader in the entrepreneurial sector.

The competition among commercial lenders continued to be fierce in 2012. Since the end of the financial crisis, there has been a general easing in the credit conditions offered to Canadian businesses.

The business segment of the financial services industry has remained concerned with customer satisfaction. Customers have become more and more demanding, especially since the financial crisis, and expect close, high-quality relationships with their financial institutions, competitively priced products and services, and easier access to credit.

The industry is also investing considerable effort in technology in order to better meet the needs of customers. A number of players have been investing heavily in their online products and services, particularly those directly related to savings and loan transactions and specialized services. In addition, online tools are being introduced for businesses to improve the management of their own operations and thereby increase their productivity.

2012 FINANCIAL HIGHLIGHTS

- Net interest income from activities designed to access equity markets and loans to medium-sized businesses increased by $19 million compared to 2011.
- *Caisse centrale Desjardins*'s average outstandings rose 13.5% to $6.3 billion as at December 31, 2012:
  - Income from mergers and acquisitions was up 20.0% compared to 2011.
  - Net growth in agricultural sector outstandings totalled $5.5 billion as at December 31, 2012, or an increase of 1.9% compared to the same date in 2011.
- Assets under management at Desjardins Venture Capital Inc. grew to $1.4 billion at the end of 2012, compared to $1.2 billion at the end of 2011.

2013 STRATEGY AND PRIORITIES

The Business and Institutional Services sector aims to contribute to the sustainable economic growth of the businesses and communities it serves. Its strategy is based on establishing relationships of trust with its members, clients and partners, and on a sustainable development philosophy. The strategy is supported by strong foundations in the regions and long-standing commitments in the socio-economic community.

The sector's priorities in 2013 are to deliver superior services to its members and clients, to achieve sustained growth, particularly in certain high-potential markets, and continue its efforts to enhance efficiency.

More specifically, this sector will aim to:

- Post the strongest growth in the industry for medium-sized business financing
- Maximize its business ownership transfer offering, particularly through better support to entrepreneurs (buyers and sellers)
- Maintain strong leadership in financing for target segments by:
  - Enhancing support to small and very small businesses, and developing business with specific agricultural client bases
  - Providing cooperatives with the best offer on the market
- Develop the international product and service offering for Canadian businesses
- Create value for its members and clients and build sustainable and flexible relationships with them
- Continue efforts to boost efficiency, particularly through continued investments in technology and process optimization

ANALYSIS OF FINANCIAL RESULTS FOR THE PERSONAL SERVICES AND BUSINESS AND INSTITUTIONAL SERVICES SEGMENT

TABLE 11 – PERSONAL SERVICES AND BUSINESS AND INSTITUTIONAL SERVICES – SEGMENT RESULTS

For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Net interest income	$ 3,690	$ 3,715	$ 3,679
Other operating income	1,676	1,631	1,445
Operating income	5,366	5,346	5,124
Investment income	58	107	108
Total income	5,424	5,453	5,232
Provision for credit losses	241	236	204
Non-interest expense	3,990	3,883	3,779
Income taxes on surplus earnings	304	347	315
Surplus earnings before member dividends	$ 889	$ 987	$ 934
Provision for member dividends, net of tax recovery	206	230	218
Net surplus earnings for the year after member dividends	$ 683	$ 757	$ 716
Of which:			
Group's share	$ 682	$ 756	$ 714
Non-controlling interests' share	1	1	2

COMPARISON OF 2012 AND 2011

For 2012, the Personal Services and Business and Institutional Services segment recorded surplus earnings before member dividends of $889 million, down $98 million, or 9.9%, compared to 2011.

Operating income was impacted by a $25 million, or 0.7%, decrease in net interest income, mainly due to the continuing low interest rate environment and strong competition in mortgage lending. The $6.3 billion increase in residential mortgages outstanding and in other consumer and business loans offset the reduction in net interest income compared to 2011. Other operating income was up $45 million compared to 2011, primarily because of growth in credit card and point-of-sale financing activities, as well as an increase in caisse network sales of Desjardins products designed by the subsidiaries. The increase in other operating income was mitigated, however, by the reduction in deposit and payment service charges in the caisse network.

Investment income was down $49 million compared to 2011, mainly because of a lower return on surplus liquidities and investments in the caisse network as a result of the continuing low interest rate environment and a drop in trading income due to capital market volatility. However, this reduction was offset by the disposal of an investment, which generated a $21 million gain.

The segment's total income was $5,424 million in 2012, a slight decrease of 0.5% compared to 2011.

The provision for credit losses was comparable to 2011, in spite of an increase in the loan portfolio outstanding, chiefly as a result of adjustments related to changes in the parameters of the provision.

Non-interest expense was up $107 million, or 2.8%, over 2011 as a result of the increase in salaries and fringe benefits related to business growth and annual indexing. Growth in operations and the BONUSDOLLARS Rewards Program also led to higher other expenses.

SECTION 2.2.2

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

PROFILE

The Wealth Management and Life and Health Insurance segment offers a complete range of products and services tailored to the changing wealth management and financial security needs of individuals, groups, businesses and cooperatives, either as members of the Desjardins caisse network or clients of complementary distribution networks.

Wealth Management includes investment fund and guaranteed investment manufacturing and distribution activities, group retirement savings activities as well as full-service and direct (online) securities brokerage. It also includes private management services and trust services.

The insurance operations of Desjardins Financial Security Life Assurance Company generate premiums of over $3.1 billion through its diversified range of life and health insurance products for individuals. This entity also offers life, health and disability coverage to employers and their employees.

Wealth Management and Life and Health Insurance products and services are distributed by advisors and financial planners in the Desjardins caisse network, while those of the Private Management sector are distributed by life insurance representatives, life and health insurance and employee benefit agents and brokers, and securities brokers. Some products lines are also distributed directly online and through client care centres.

ACTIVITIES

Insurance activities for individuals and business people offer these clients insurance products that protect their quality of life, their health, their families and their loved ones, and also help them face life's unforeseen events.

Group insurance plan activities meet the needs of businesses, cooperatives and organizations of all sizes with solutions that are tailored to their specifications by group plan implementation and administration experts.

Savings activities for individuals and business people feature a comprehensive range of financial security products to help clients with projects such as preparing for retirement, planning trips and financing their children's education.

Specialized savings activities include specialized savings and investment products, such as investment funds and other investment solutions as well as market-linked guaranteed investments to meet the needs of caisse members and clients of various complementary networks.

Group retirement savings activities are geared to the needs of business members and other clients in the area of employee retirement savings plans.

Brokerage and private management activities include full-service and online brokerage for members and clients, private management and management of investment companies of large business families with complex needs.

INDUSTRY

In 2011, the wealth management industry represented outstandings of approximately $1,841 billion, measured in terms of the assets of the managed products and the fee accounts held by Canadian households. These assets experienced average annual growth of 1.8% in the past five years. This modest growth was due to the current stock market volatility and low interest rate environment.

Major fund companies and banking and life and health insurance financial groups all have a wealth management division that designs and distributes diversified products and services to meet the investment, financial, tax and estate planning needs of the affluent client segments. Changes in the socio-demographic profile of the Canadian population, tending toward a higher concentration of wealth in these segments, have led the major players to outdo each other with respect to their product and service offer in order to win over and retain demanding clients with varied needs.

Advisors, whether "mobile" or working in an establishment still play a key role in providing advice, making sales and maintaining relationships. However, the industry has been proactive about meeting certain clients' desire for autonomy by diversifying the means of access to services and making the most of virtual interfaces.

In 2011, the Canadian life and health insurance industry recorded premiums of $81.0 billion through a broad range of products, providing 27 million insured persons in Canada with financial security products, and representing the equivalent of $3.8 trillion in life insurance coverage for the entire country. Benefits paid by the industry in 2011 totalled $63.6 billion. The top five Canadian life and health insurers accounted for 75.0% of the market in 2011, which shows that the industry is highly consolidated. In 2012, the industry once again had to deal with low long-term interest rates and a difficult economic environment. In spite of this, it has grown 4.6% in the past five years across Canada, and 3.7% during the same period in Quebec.

Life and health insurance products are distributed to consumers in a traditional manner, namely through advisory relationships and personal meetings, 86.0% of the time. Remaining sales are made through various channels, including at branches of credit institutions, online, via call centres and at travel agencies.

2012 FINANCIAL HIGHLIGHTS

- Continued implementation of the accelerated growth plan for the life and health insurance segment, with savings assets outside Quebec growing 4.7% in 2012 to $5.2 billion, and group and business insurance generating almost half of the premiums outside Quebec
- Increase of 5.1% in insurance premium volume
- Increase of 15.2% in group and business insurance sales for groups of more than 1,000 employees
- Increase of 11.1% in individual insurance sales, of which almost one-third was generated outside Quebec
- Increase of 5.9% in group insurance sales
- Assets under management in the group retirement savings sector exceeded $5.0 billion, up 9.5% compared to 2011
- Off-balance sheet savings: 14.7% market share in Quebec, showing Desjardins Group's continued growth in Quebec
- On-balance sheet savings: Desjardins Group maintained its position with a 42.7% market share
- Increase of 178% in net sales of Desjardins Funds in the caisse network
- Increase of 103.1% in net sales of market-linked guaranteed investments in the caisse network
- The new Chorus II portfolios, launched at the end of 2011, passed the $2.0 billion mark in outstandings
- Assets under management in the Private Management sector exceeded the $3.0 billion mark
- Increase of 10.2% in sales for the Private Management sector
- Increase of 5.7% in Desjardins Securities Inc.'s assets under management

2013 STRATEGY AND PRIORITIES

The Wealth Management and Life and Health Insurance segment reiterates its priority to ensure the profitable growth of its operations which aims at positioning it as a leader in wealth management for mass-affluent individuals and entrepreneurs in Quebec through a unique offer combining investments, insurance and advisory services. It intends to maintain its leadership position in life and health insurance in both the group and individual markets through accelerated development across Canada.

This priority is based on strategies improving service offers to better meet the expectations of each client segment. It is therefore intended to provide higher quality, distinctive service and to increase the satisfaction of caisse members and clients. Growth in the Wealth Management and Life and Health Insurance segment will come from a better use of its distribution advantages, which will fully benefit from all the possibilities provided by Desjardins Group, the marketing of new targeted offers as well as acquisition and partnership opportunities in designated priority areas. By setting up streamlined and automated operational processes, this segment will reduce its unit costs and benefit from gains in efficiency as a result.

Its priorities for 2013 are described below.

Wealth Management:

- Offer caisse members an enhanced client experience by applying an integrated financial planning and advisory service approach tailored specifically to the expectations of prioritized client bases
- Continue to develop the savings and investment product offer so it is adapted to the specific needs of each client segment by taking its diversified distribution networks into consideration
- Improve the characteristics of this offer and the related virtual functionalities
- Review the business and technology architecture of investment operations to improve the quality of service and achieve efficiency gains

Life and Health Insurance:

- Review the key processes to improve its individual and group insurance service offer to better meet the specific expectations of members and clients, and as a result increase their satisfaction
- Accelerate growth across Canada by optimizing the potential of each distribution network and capitalizing on competitive service offers and solid business partnerships

ANALYSIS OF SEGMENT FINANCIAL RESULTS

TABLE 12 – WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE – SEGMENT RESULTS

For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Net interest income	$ 3	$ 4	$ 3
Net premiums	3,366	3,261	3,015
Other operating income	880	830	954
Operating income	4,249	4,095	3,972
Investment income	734	1,807	885
Total income	4,983	5,902	4,857
Provision for credit losses	—	—	(1)
Claims, benefits, annuities and changes in insurance and investment contract liabilities	3,065	3,994	3,081
Non-interest expense	1,615	1,560	1,456
Income taxes on surplus earnings	62	68	72
Surplus earnings before member dividends	$ 241	$ 280	$ 249
Provision for member dividends, net of tax recovery	—	7	6
Net surplus earnings for the year after member dividends	$ 241	$ 273	$ 243
Of which:			
Group's share	$ 192	$ 257	$ 247
Non-controlling interests' share	49	16	(4)

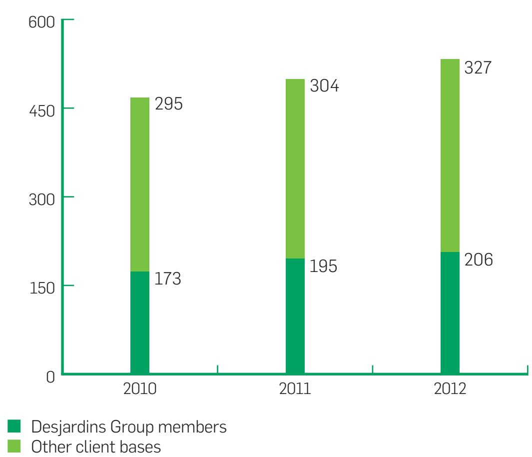
TABLE 13 – EXPENSES ATTRIBUTABLE TO POLICYHOLDERS

For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Insurance and annuity benefits	$ 2,436	$ 2,378	$ 2,214
Changes in actuarial liabilities	508	1,495	754
Interests of policyholders, refunds and other	121	121	113
Total	$ 3,065	$ 3,994	$ 3,081

GROUP INSURANCE PREMIUMS BY DISTRIBUTION NETWORK
(in millions of dollars)

INDIVIDUAL INSURANCE PREMIUMS BY DISTRIBUTION NETWORK
(in millions of dollars)



COMPARISON OF 2012 AND 2011

For 2012, surplus earnings before member dividends were $241 million, down $39 million, or 13.9%, compared to 2011, essentially due to life and health insurance operations.

Operating income for 2012 was impacted by the $155 million increase in net insurance premiums and annuity premiums declined by $50 million compared to 2011. Other operating income grew by $50 million compared to the previous year mainly as a result of the growth in average assets under management related to the distribution of various products.

Investment income was down $1,073 million largely as a result of the lower investment income associated with life and health insurance operations attributable to the change in the fair value of assets backing liabilities, which was offset for the most part by changes in actuarial liabilities.

The segment's total income was $4,983 million, down $919 million, or 15.6%, compared to 2011.

Expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities were down $929 million, or 23.3%, from 2011, mainly as a result of a $987 million decline in actuarial liabilities included under "Insurance and investment contract liabilities", including the previously mentioned fluctuation in the fair value of investments. Changes in assumptions for the valuation of actuarial liabilities, made in the normal course of business, pushed up actuarial liabilities by $60 million. These changes had caused actuarial liabilities to go down by $43 million in 2011. In 2012, the adjustments concerned mainly the assumptions related to the contract cancellation rate, certain actuarial valuation methods and models for segregated funds, the mortality rate, operating expenses and return on investments. In 2011, adjustments to assumptions concerned mainly those related to return on investments, the use of certain actuarial valuation methods and models for segregated funds, and the contract cancellation rate. However, gains generated by favourable underwriting experience in individual insurance narrowed the unfavourable difference created by such changes in assumptions.

Non-interest expense was up $55 million, or 3.5%, mainly due to higher salaries and fringe benefits resulting from business growth and the acquisition of MGI Financial Inc. in October 2011, which generated additional expenses of $24 million.

SECTION 2.2.3

PROPERTY AND CASUALTY INSURANCE SEGMENT

PROFILE

The Property and Casualty Insurance segment offers insurance products allowing members and clients to protect themselves against disasters. It includes the operations of Desjardins General Insurance Group Inc. and those of Western Financial Group Inc.

Desjardins General Insurance Group Inc. directly offers the general public and members of partner groups across Canada a line of home and automobile insurance products and provides businesses in the Quebec market with insurance products

Desjardins General Insurance Group's products are distributed through property and casualty (P&C) insurance agents in the Desjardins caisse network, a number of client care centres (call centres) and business centres, through an exclusive agent network in the field, online and via mobile applications.

Western Financial Group Inc. operates an extensive insurance product distribution network serving more than 600,000 clients in western Canada. Its P&C insurance products are distributed to individuals and businesses through a network of brokers, as well as directly to the general public under the Western Direct Insurance brand. Western Financial Group Inc. also distributes its own life insurance products, pet insurance and certain banking products.

Desjardins General Insurance Group Inc., which has more than 2.1 million policies in force, markets its products to the Canada-wide individual market under the Desjardins General Insurance Group Inc. banner, and to the group market—including members of professional associations and unions, and the employers' staff—under the banner of The Personal.

The Property and Casualty Insurance segment is also active on the white label market, notably with a well-established Canadian financial institution, as well as with Western Financial Group Inc., for the direct insurance offer launched in certain target urban markets under the Western Direct Insurance brand.

ACTIVITIES

Automobile insurance operations, including motorcycle and recreational vehicle insurance, offer 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 under a public plan.

Property insurance operations aim to offer owners and tenants insurance coverage for primary and secondary residences to protect their physical property. In addition, with all-risk insurance coverage and optional coverage, they can obtain comprehensive protection tailored to their actual needs.

Business insurance operations meet the insurance requirements for commercial vehicles, commercial property and public liability for businesses in Quebec. Desjardins General Insurance Group Inc. serves the following sectors: service firms, retailers and wholesalers, garages, self-employed workers, general or specialized contractors, restaurants, commercial buildings, condominiums and apartment buildings.

Pet insurance operations cover the healthcare needs of domestic dogs and cats. Western Financial Group Inc. has the necessary licences to write this kind of insurance in all provinces and territories of Canada.

Financial product distribution operations comprise a network of independent brokers representing some 120 points of sale in British Columbia, Alberta, Saskatchewan and Manitoba. This network offers primarily P&C insurance products such as automobile, property, farm, business and liability insurance.

Other operations of Western Financial Group Inc. include certain life insurance products and banking solutions.

INDUSTRY

The Canadian P&C insurance industry offers insurance coverage for vehicles, personal and commercial property, and public liability. In 2011, the total amount of direct premiums written was $43.0 billion, of which 62.1% was individual insurance and 37.9% was business insurance. For Canada as a whole, brokers have a market share of 65.6%, while direct writers have 23.7% of the market, and exclusive agents, hold 10.7%. In Quebec, direct writers have gained significant market share since their arrival and now hold 43.7% of the market, compared to 55.4% for brokers and 0.9% for exclusive agents.

The Canadian P&C insurance market is mature and cyclical, with an average annual growth rate of 4.1% and an average return of 9.3% 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 the loss experience in the different business lines. The industry's financial performance is dependent on the profitability of insurance operations, which is based on the insurance premiums collected less claims and operating expenses, as well as on the investment portfolio return.

The Ontario market accounts for close to 50% of the gross premiums written in the Canadian industry, and automobile insurance is highly regulated in this province. The end of the hard market cycle and a sharp decline in the number of clients served in the Ontario market have slowed down the growth of insurers since early 2012. The latest reforms of the Ontario system were introduced in September 2010 and were aimed at addressing rising claims costs while improving the settlement process to better meet clients' needs. The positive effects of these reforms continued to be felt in 2012, with the stabilizing of rate hikes and settlement costs. In spite of this, high rates especially in the Toronto area, remain a political issue. Fraud is also still a major concern in Ontario, and insurers, the government and regulators are joining forces to find long-term solutions.

In 2011, the top 10 P&C insurers in Canada represented 63.0% of the market, up six percentage points since 2007, while the top five insurers represented 41.0% of the market, compared to 36.0% in 2007. Consolidation of the Canadian P&C insurance market continues in the aftermath of a few large insurers' transactions, which have given them an important advantage by increasing their influence within the industry and thereby putting additional pressure on the competition.

2012 FINANCIAL HIGHLIGHTS

- Increase in net premiums of $197 million, or 11.0%, compared to 2011, to total $1,982 million in 2012
- Contribution of $263 million to total income in 2012 by Western Financial Group Inc.
- Surplus earnings of $205 million, up 42.4% compared to the previous year, resulting in return on equity of 16.1%
- Loss ratio of 69.1% for the segment, compared to 73.1% in 2011

2013 STRATEGY AND PRIORITIES

The Property and Casualty Insurance segment will be actively involved in pursuing Desjardins Group's top priority—member and client satisfaction. Various initiatives will be launched to transform clients into true "promoters" of Desjardins so that Desjardins Group and the Property and Casualty Insurance segment are recognized for the highest quality and satisfaction standards.

This segment will also continue to implement its profitable growth plan to remain a leading industry player in Quebec and to confirm Desjardins Group's position as a preferred insurer in Ontario, in addition to boosting its development in western Canada. In Quebec, the segment intends to achieve above-market growth by fully leveraging its membership in Desjardins Group and building on its culture of growth, while preserving sound profitability. It would also like to accelerate development in its business insurance sector. In Ontario, it will continue to make Desjardins Group more widely known, which would include a gradual return to the Toronto area. In western Canada, Western Financial Group Inc. will build on its expansion plan through brokerage acquisitions and will increase the visibility of its brand in its market.

The segment also relies on a model and strategy aligned with the market dynamic. It would like to maintain its edge in risk segmentation and continue optimizing its claims management. It also intends to continue adjusting to changing distribution channels based on market imperatives, while continuing to leverage its expertise in direct distribution.

This segment's priorities for 2013 are indicated below.

Desjardins General Insurance Group Inc.

- Continue to strive to improve client satisfaction by simplifying and enhancing the client experience, an area in which it continually aims to stand out
- Continue its expansion through acquisitions and strategic partnerships, as well as through organic growth, by increasing access to the market
- Optimize its systems and fine-tune its procedures to enhance performance and maintain above-market profitability

Western Financial Group Inc.

- Continue its strong expansion through acquisitions and organic growth to become an important player in the consolidation of the P&C insurance industry's distribution network, and remain the largest network of brokers in western Canada
- Implement joint development initiatives with Desjardins Group components to strengthen Desjardins Group's presence in western Canada

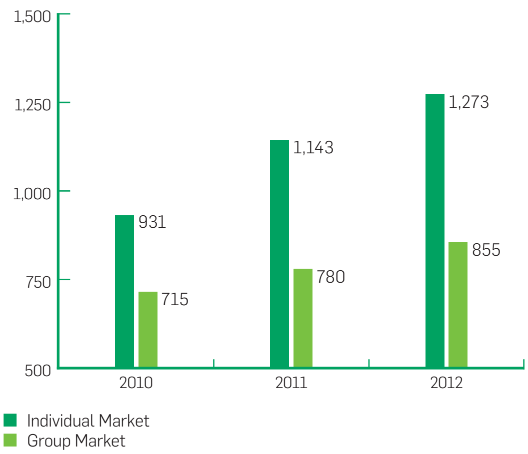
ANALYSIS OF SEGMENT FINANCIAL RESULTS

TABLE 14 – PROPERTY AND CASUALTY INSURANCE – SEGMENT RESULTS

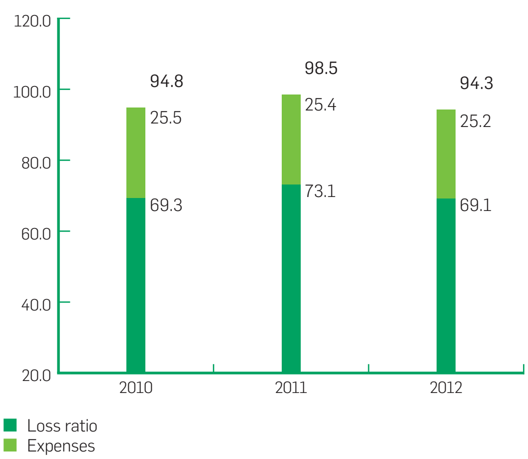
For the years ended December 31
(in millions of dollars)

	2012	2011	2010
Net interest income	$ 11	$ 11	$ —
Net premiums	1,982	1,785	1,524
Other operating income	133	87	1
Operating income	2,126	1,883	1,525
Investment income	142	165	107
Total income	2,268	2,048	1,632
Provision for credit losses	—	1	—
Claims, benefits, annuities and changes in insurance and investment contract liabilities	1,343	1,299	1,056
Non-interest expense	661	550	389
Income taxes on surplus earnings	59	54	56
Net surplus earnings for the year	$ 205	$ 144	$ 131
Of which:			
Group's share	$ 184	$ 127	$ 118
Non-controlling interests' share	21	17	13

GROSS PREMIUMS WRITTEN
(in millions of dollars)



COMBINED RATIO
(as a percentage of net premiums earned)



COMPARISON OF 2012 AND 2011

For 2012, the segment's net surplus earnings amounted to $205 million, an increase of $61 million, or 42.4%, compared to 2011, mainly as result of an improved loss ratio in 2012 for automobile insurance and business insurance. Overall, the loss ratio stood at 69.1% in 2012, down 4.0 points from the previous year.

Operating income was impacted by higher net premiums as a result of the increase in policies issued following multiple growth initiatives. All segments and regions contributed to this increase. Other operating income was up $46 million, essentially because of the higher commission income from Western Financial Group Inc.

Investment income was down $23 million from the previous year as a result of the lower increase in the value of investments in 2012 than in 2011. This decline was nevertheless mitigated by the realized gains on disposals of investments made for the most part in the first quarter.

The segment's total income was $2,268 million, for an increase of $220 million, or 10.7%, compared to 2011.

The loss ratio improved from 73.1% in 2011 to 69.1% in 2012 due to the decrease in the cost of claims in Ontario and to the fact that the decrease in the discount rate in 2012 was not as sharp as in 2011.

Non-interest expense was up $111 million, or 20.2%, for an amount of $74 million, mainly as a result of the consolidation of the operations of Western Financial Group Inc., a company acquired in the second quarter of 2011. The increase in non-interest expense was also due to higher salaries and fringe benefits, as well as higher IT expenses incurred to support business growth.

SECTION 2.2.4

OTHER CATEGORY

The Other category includes financial information that is not specific to any particular business segment. It mainly includes treasury activities related to *Caisse centrale Desjardins's* operations and financial intermediation between liquidity surpluses and needs of the caisses. This category also includes the support functions of the Federation, the operations of *Capital Desjardins inc.* and *Fonds de sécurité Desjardins*, as well as the operating results related to asset-backed term notes (ABTNs) held by Desjardins Group. It also includes Desjardins Technology Group Inc., which encompasses all of Desjardins Group's IT operations. In addition to various adjustments necessary to prepare the Combined Financial Statements, the intersegment balance eliminations are classified in this category.

Desjardins Group does not consider an item-by-item comparative analysis of 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 before member dividends.

CONTRIBUTION TO SURPLUS EARNINGS

Net surplus earnings for the year before member dividends arising from operations combined under the Other category totalled $256 million in 2012, compared to $171 million in 2011.

2012

Net surplus earnings for the year before member dividends of $256 million were mainly due to the $159 million increase in the fair value of the ABTN portfolio, net of hedging positions, to treasury activities, and to the decrease in the provisions related to the investment portfolio.

2011

Net surplus earnings for the year before member dividends of $171 million were notably the result of treasury activities, the favourable net impact of changes in the fair value of derivatives used in hedging operations and the increase in the fair value of ABTN portfolios and related items, which were offset by the large amounts invested to modernize IT systems.

SECTION 2.3

ANALYSIS OF FOURTH QUARTER RESULTS

TABLE 15 – QUARTERLY RESULTS FOR THE PREVIOUS EIGHT QUARTERS
(unaudited, in millions of dollars and as a percentage)

	2012				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Net interest income	$ 948	$ 967	$ 969	$ 964	$ 1,006	$ 969	$ 979	$ 967
Net premiums	1,325	1,278	1,295	1,228	1,221	1,233	1,238	1,159
Other operating income								
Deposit and payment service charges	124	127	125	123	128	132	128	124
Lending fees and credit card service revenues	137	125	127	128	129	120	116	118
Brokerage, investment fund and trust services	185	164	170	181	168	162	170	176
Other	145	166	150	149	169	133	93	98
Operating income	2,864	2,827	2,836	2,773	2,821	2,749	2,724	2,642
Investment income								
Net income (loss) on securities at fair value through profit or loss	65	285	411	(87)	548	796	386	(24)
Net income on available-for-sale securities	45	56	52	115	71	118	49	61
Net other investment income	66	56	57	57	71	63	72	58
Investment income	176	397	520	85	690	977	507	95
Total income	3,040	3,224	3,356	2,858	3,511	3,726	3,231	2,737
Provision for credit losses	47	50	62	82	54	56	83	44
Claims, benefits, annuities and changes in insurance and investment contract liabilities	991	1,235	1,425	746	1,444	1,750	1,277	821
Non-interest expense	1,576	1,360	1,348	1,476	1,477	1,325	1,415	1,406
Income taxes on surplus earnings	101	136	119	133	109	150	103	109
Surplus earnings before member dividends	325	443	402	421	427	445	353	357
Provision for member dividends, net of tax recovery	65	54	49	38	90	43	50	47
Surplus earnings for the year after member dividends	$ 260	$ 389	$ 353	$ 383	$ 337	$ 402	$ 303	$ 310
Of which:								
Group's share	$ 219	$ 378	$ 341	$ 372	$ 315	$ 396	$ 299	$ 304
Non-controlling interests' share	41	11	12	11	22	6	4	6
Total assets	$ 196,706	$ 199,680	$ 193,987	$ 196,409	$ 190,137	$ 189,683	$ 188,024	$ 184,383
Return on equity	7.3%	11.6%	11.1%	12.1%	11.9%	13.5%	11.5%	12.0%
Tier 1 capital ratio	16.8	16.5	16.1	16.0	17.3	17.0	17.2	17.6
Total capital ratio	19.3	19.0	18.8	19.2	19.3	18.3	18.6	19.1

FOURTH QUARTER RESULTS

For the fourth quarter of 2012, Desjardins Group posted surplus earnings before member dividends of $325 million, down $102 million, or 23.9%, compared to the corresponding quarter in 2011.

These results reflect the contribution of the Personal Services and Business and Institutional Services segment, which totalled $262 million. The Wealth Management and Life and Health Insurance segment and the Property and Casualty Insurance segment contributed $44 million and $63 million, respectively. The Other category reduced surplus earnings of $44 million.

Return on equity for the quarter was 7.3%, compared to 11.9% for the fourth quarter of 2011. The decline was due to the significant growth in equity as a result of $1.0 billion in capital shares issued by the Federation and growth in undistributed surplus earnings.

OPERATING INCOME

Net interest income for the fourth quarter of 2012 decreased to $948 million, compared to $1,006 million for the same period in the previous year. Despite the increase of $7.4 billion, or 5.9%, in all outstanding loans during the year, the combination of low interest rates and fierce market competition led to this decline.

Growth in business insurance operations pushed up net premiums by 8.5% to $1,325 million.

The overall insurance operations of the Wealth Management and Life and Health Insurance segment posted net insurance and annuity premiums of $862 million for the fourth quarter of 2012, compared to $792 million for the same period in 2011, representing an 8.8% increase. Net insurance premiums were up 7.6% over 2011 to total $803 million.

Premium volume for individual insurance was $140 million, an $11 million increase compared to the same quarter in 2011. Premium volume from the network of life insurance representatives assigned to Desjardins caisses increased by 7.0%, compared to the corresponding quarter in the previous year. After remarkable sales growth from the distribution networks in recent years, premiums cashed for the fourth quarter of 2012 increased by $7.6 million, or 9.9%, compared to the same quarter in 2011. In addition, the premium volume for products marketed via direct distribution posted a 4.6% growth to total $25 million.

Premiums for group insurance purchased by Desjardins Group members increased by 3.6% and premiums for insurance from other client bases were up 8.8%.

The overall activities of the Property and Casualty Insurance segment generated net premiums of $521 million in the fourth quarter of 2012, compared to $478 million for the same period in 2011, a 9.0% increase, resulting primarily from the increase in policies issued due to spinoffs from growth initiatives targeting mass market clients and groups both in Quebec and across Canada, the development of white label partnerships, the business insurance offer and higher average premiums in certain business sectors. Western Financial Group Inc. contributed $27 million to net premiums in 2012.

Operating income stood at $591 million, down $3 million from the corresponding quarter in 2011.

INVESTMENT INCOME

Investment income was down $514 million from 2011, mainly due to the decrease in investment income associated with life and health insurance operations resulting from changes in the fair value of assets backing liabilities, which were largely offset by changes in actuarial liabilities.

TOTAL INCOME

Total income for the fourth quarter of 2012 was $3,040 million, down $471 million, or 13.4%, from the corresponding quarter in 2011.

PROVISION FOR CREDIT LOSSES

The provision for credit losses totalled $47 million for the fourth quarter of 2012, down $7 million, or 13.0%, from the corresponding period in 2011.

CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE AND INVESTMENT CONTRACT LIABILITIES

Expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities totalled $991 million, for a decrease of 31.4% compared to the same period in the previous year. The Wealth Management and Life and Health Insurance segment had expenses of $671 million, down $455 million, or 40.4%, from those recorded for the same quarter in 2011. This decline resulted mainly from a $987 million decrease in changes in actuarial liabilities included under "Insurance and investment contract liabilities", attributable in particular to the fluctuation in the fair value of investments. Changes in valuation assumptions made in the normal course of business pushed up expenses by $77 million, while they had decreased by $43 million in 2011. Gains related to underwriting experience in individual insurance narrowed the unfavourable difference created by the changes in assumptions.

The expenses of the Property and Casualty Insurance segment totalled $324 million, compared to $319 million in 2011, for an increase of $5 million, or 1.6%. Furthermore, the loss ratio was 64.8% for the fourth quarter of 2012, compared to 67.6% for the corresponding period in 2011.

NON-INTEREST EXPENSE

Non-interest expense was up $99 million, or 6.7%, compared to the fourth quarter of 2011, to total $1,576 million. This increase was mainly due to the annual increase in salaries and fringe benefits, and to the increase in expenses resulting directly from the growth in operations and the revaluation of assets.

The productivity index, calculated as the ratio of non-interest expense to total income, net of expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities, was 76.9% for the fourth quarter, compared to 71.4% for the same quarter a year earlier. The growth in non-interest expense, combined with lower income as a result of the poorer performance of investments in the fourth quarter of 2012, versus the same period in 2011, accounted for the index deterioration.

SEGMENT RESULTS FOR THE FOURTH QUARTER

PERSONAL SERVICES AND BUSINESS AND INSTITUTIONAL SERVICES

The Personal Services and Business and Institutional Services segment recorded surplus earnings before member dividends of $262 million for the fourth quarter of 2012, down $28 million, or 9.7%, from the same period in 2011.

Operating income totalled $1,396 million in the fourth quarter of 2012, compared to $1,379 million for the corresponding period in the previous year. It was affected by a slight decrease in net interest income, and especially by the combination of continuing low interest rates and fierce competition in mortgage lending. However, the increase in outstanding residential mortgages and business loans mitigated the impact. Other operating income was up $33 million compared to the same period in the previous year as a result of the growth in credit card and point-of-sale financing activities and an increase in caisse network sales of Desjardins products designed by the subsidiaries.

Investment income decreased by $16 million compared to the same period a year earlier, mainly due to a lower return on liquidities and investments in the caisse network as a result of the continuing low interest rate environment.

Total income for the segment was $1,405 million, up slightly compared to the fourth quarter of 2011.

The provision for credit losses stood at $47 million for the fourth quarter of 2012, down $7 million, or 13.0%, from the corresponding period in 2011, despite growth in the outstanding loan portfolio. This decline was due mainly to the adjustments related to changes in the parameters of the provision.

Non-interest expense was up $47 million, or 4.9%, compared to the same period in 2011, reflecting the increase in salaries and fringe benefits arising from business growth and annual indexing. The increase in other expenses resulted directly from growth in operations and the BONUSDOLLARS Rewards Program.

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

The Wealth Management and Life and Health Insurance segment recorded net surplus earnings of $44 million for the fourth quarter of 2012, down $61 million, or 58.1%, compared to the same quarter in 2011. This decrease was essentially the result of life and health insurance operations, whose contribution to surplus earnings for the quarter was reduced by changes in valuation assumptions. In 2011, annual updates of these assumptions had had the opposite effect on surplus earnings. This factor was partially offset by an improvement in underwriting experience and a gain on investment transactions.

Operating income was impacted by a $56 million increase in net insurance premiums and a $14 million increase in net annuity premiums compared to 2011.

Investment income was down $568 million compared to 2011, mainly because of the decrease in investment income associated with life and health insurance operations resulting from changes in the fair value of assets backing liabilities, which were largely offset by changes in actuarial liabilities.

The segment's total income was $1,148 million, for a decrease of $498 million, or 30.3%, compared to 2011.

Expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities stood at $671 million, down $455 million, or 40.4%, compared to the same period in 2011. This change essentially results from a decrease of $496 million in the actuarial liabilities included under "Insurance and investment contract liabilities", attributable in particular to the fluctuation in the fair value of investments.

Non-interest expense was up $24 million, or 5.9%, to $429 million for the fourth quarter of 2012.

PROPERTY AND CASUALTY INSURANCE

For the fourth quarter of 2012, this segment's net surplus earnings totalled $63 million, up $21 million, or 50.0%, compared to 2011, mainly as a result of the more favourable loss ratio in 2012. The loss ratio stood at 64.8% for this quarter, down 2.8 points from 2011.

Operating income was impacted by the $43 million increase in net premiums generated by the increase in policies issued. This increase is due to the same reasons as those given for 2012. Other operating income increased by $5 million, chiefly because of the growth in the commission income of Western Financial Group Inc.

Investment income was down $6 million compared to the same period in 2011, essentially as a result of the lower interest rates on the market in 2011, which led to an increase in the value of bonds in 2011, compared to 2012.

Total income for the segment was $586 million for the fourth quarter of 2012, for a $39 million, or 7.1%, increase over the same period in 2011.

The loss ratio decreased from 67.6% in the fourth quarter of 2011 to 64.8% in the corresponding quarter of 2012. The lower loss ratio was primarily due to the reduction in the provisions related to pyrrhotite claims, while an increase in these provisions had been recorded in the fourth quarter of 2011. Finally, as was the case for all of 2012, the discount rate had a favourable impact on the fourth quarter of 2012 compared to the corresponding quarter in 2011.

Non-interest expense rose $12 million, or 7.1%, mainly as a result of the increase in salaries and fringe benefits, IT costs, and advertising expenses incurred to support and stimulate business growth, as well as a $4 million increase related to the operations of Western Financial Group Inc.

OTHER CATEGORY

CONTRIBUTION TO SURPLUS EARNINGS

The deficit for the period of the operations combined in the Other category totalled $44 million, compared with a deficit of $10 million for the corresponding period in 2011.

FOURTH QUARTER 2012

The deficit of $44 million for the period was especially attributable to fringe benefits and the revaluation of assets, which were offset by the increase of $37 million in the fair value of the ABTN portfolio, net of hedging positions.

FOURTH QUARTER 2011

The deficit of $10 million for the period were mainly due to the large amounts invested to modernize IT systems and the unfavourable net impact related to changes in the fair value of derivatives used in hedging operations, which were offset by treasury activities.

QUARTERLY TRENDS

Quarterly income, expenses and surplus earnings before member dividends fluctuate based on certain trends, including seasonal variations and changes in the general economic and market conditions. Table 15 presents the results for the past eight quarters.

Low market interest rates in recent quarters exerted pressure on net interest income, causing it to stagnate even though loans outstanding increased throughout the year. Since the third quarter of 2011, Desjardins Group has posted lower investment income associated with its life and health insurance operations, a decrease that was largely offset, however, by a decline in insurance contract liabilities.

Net premiums have grown steadily since the first quarter of 2011, partly as a result of the various acquisitions made by the insurance segments and business development initiatives.

The provision for credit losses has decreased since the first quarter of 2012 despite the continuous increase in loans outstanding, which reflects the good quality of the loans.

Expenses related to claims, benefits, annuities and changes in insurance and investment contract liabilities experienced quarterly fluctuations as a result of changes in the fair value of investments associated with life and health insurance operations, which reflects market volatility. These changes are also attributable to the lower frequency of claims in the Property and Casualty Insurance segment resulting from more favourable weather conditions.

In step with business growth, non-interest expense has been on the rise since the beginning of 2011. However, summer periods are characterized by a decrease in salary expense due to less intense capital market activity.

Since the second quarter of 2011, the results of Western Financial Group Inc. have been integrated with those of Desjardins Group.

3.0 BALANCE SHEET REVIEW

HIGHLIGHTS

- Annual growth of 3.5% in total assets, which amounted to $196.7 billion as at December 31, 2012
- Residential mortgages outstanding up $6.2 billion over the year, to total $85.9 billion
- Quality loan portfolio, with a gross impaired loans ratio of 0.35%
- Increase of 5.0% in savings recruitment, which amounted to $129.6 billion
- Year-over-year growth of $32.1 billion in assets under administration to total $313.1 billion at the end of 2012
- Sales of capital shares of the Federation reached $1.0 billion during 2012
- Issuance of US$1.5 billion in medium-term covered bonds by *Caisse centrale Desjardins* on the U.S. market
- Issuance of $800 million in medium-term notes by *Caisse centrale Desjardins* on the Canadian market
- Tier 1 capital ratio of 16.8% as at December 31, 2012
- Redemption, on June 1, 2012, by *Capital Desjardins inc.* of all its outstanding Series C Senior Notes due in 2017, in the amount of $300 million
- Acquisition of an interest in Maple Group Acquisition Corporation, representing a commitment of $98 million
- Acquisition by Western Financial Group Inc. of several insurance brokers:
  - Hodges & Company Insurance Services Ltd., a British Columbia-based brokerage network specializing in commercial insurance
  - Brown & Ward Insurance Ltd., a leading property and casualty insurance broker in Alberta
  - Roblin Insurance Travel and Realty Agencies Ltd., based in Manitoba
  - BC Yacht Insurance Brokers Inc., a company based in Sidney, British Columbia
  - Orion Insurance Brokers Ltd., with offices in Winnipeg, Manitoba

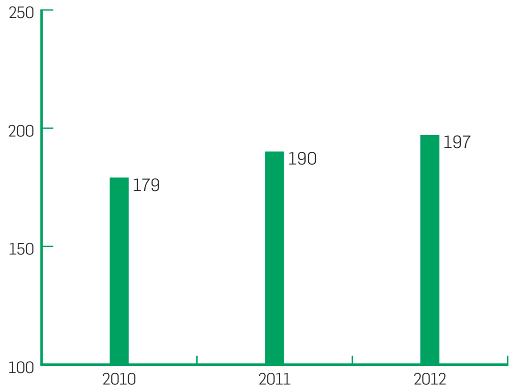
SECTION 3.1

BALANCE SHEET MANAGEMENT

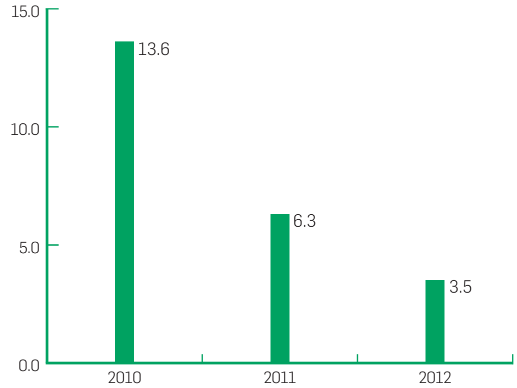
TABLE 16 – COMBINED BALANCE SHEETS
As at December 31
(in millions of dollars and as a percentage)

	2012		2011		2010	
Assets						
Cash and deposits with financial institutions	$ 1,669	0.8%	$ 1,356	0.7%	$ 1,621	0.9%
Securities	40,312	20.5	41,205	21.7	37,420	20.9
Securities borrowed or purchased under reverse repurchase agreements	4,377	2.2	4,959	2.6	7,034	3.9
Loans	132,576	67.4	125,154	65.8	118,258	66.1
Segregated fund assets	6,132	3.1	5,427	2.9	4,774	2.7
Other assets	11,640	6.0	12,036	6.3	9,824	5.5
Total assets	$ 196,706	100.0%	$ 190,137	100.0%	$ 178,931	100.0%
Liabilities and equity						
Deposits	$ 129,624	65.9%	$ 123,403	64.9%	$ 114,663	64.1%
Other liabilities	47,960	24.4	49,357	25.9	49,307	27.5
Subordinated bonds	3,081	1.6	3,350	1.8	2,805	1.6
Equity	16,041	8.1	14,027	7.4	12,156	6.8
Total liabilities and equity	$ 196,706	100.0%	$ 190,137	100.0%	$ 178,931	100.0%

TOTAL ASSETS
(in billions of dollars)



ASSET GROWTH
(as a percentage)



TOTAL ASSETS

As at December 31, 2012, Desjardins Group's total assets stood at $196.7 billion, up $6.6 billion, or 3.5%, from a year earlier, compared to an increase of $11.2 billion, or 6.3%, during 2011. In spite of slower economic growth, Desjardins Group's expansion continued, in large part due to strong credit demand, especially in the residential mortgage sector.

Desjardins Group also stood out in personal, business and government savings recruitment in 2012. Its deposit liabilities, which totalled $129.6 billion as at December 31, 2012, experienced growth that was just as sustained as in 2011 for an increase of $6.2 billion, or 5.0% over the year. In addition, off-balance sheet savings from members and clients, namely savings accumulated in the form of investments in investment funds and other securities, recorded faster growth in 2012, notably because of improvements in the stock market.

CASH AND DEPOSITS WITH FINANCIAL INSTITUTIONS, AND SECURITIES

Cash and deposits with financial institutions, and securities, including securities borrowed or purchased under reverse repurchase agreements, decreased by $1.2 billion, or 2.4%, since year-end 2011, to total $46.4 billion as at December 31, 2012. Securities other than those borrowed or purchased under reverse repurchase agreements amounted to $40.3 billion as at December 31, 2012, down $893 million, or 2.2%. Securities borrowed or purchased under reverse repurchase agreements followed the same trend and declined by $582 million, or 11.7%, during the same period, to $4.4 billion.

LOANS

FINANCING ACTIVITIES

As at December 31, 2012, Desjardins Group's outstanding loan portfolio, net of the allowance for credit losses, was up $7.4 billion, or 5.9%, over the year, to total $132.6 billion, compared to an increase of $6.9 billion, or 5.8%, during 2011. This faster growth is largely due to mortgage financing.

In light of the main borrower categories presented in Table 17, financing, which comprises residential mortgages, consumer loans, credit card advances and other personal loans, formed the largest credit category in Desjardins Group's loan portfolio as at December 31, 2012, representing 78.5%. Loans outstanding in this category were $104.5 billion as at that date, for a year-over-year increase of $6.8 billion, or 6.9%, compared to a growth of $5.7 billion, or 6.2%, during 2011. The improvement in Desjardins Group's results in this market is attributable to residential mortgages.

Moreover, Desjardins Group was also very active in business and government financing. As at December 31, 2012, its outstanding loans in this sector amounted to $28.5 billion, a year-over-year increase of $596 million, or 2.1%, compared to a growth of $1.2 billion, or 4.4%, during 2011.

TABLE 17 – LOANS BY BORROWER CATEGORY

As at December 31
(in millions of dollars and as a percentage)

	2012		2011		2010[1]	
Residential mortgages	$ 85,931	64.6%	$ 79,686	63.4%	$ 74,466	62.7%
Consumer, credit card and other personal loans	18,520	13.9	17,985	14.3	17,504	14.7
Business	26,869	20.2	25,998	20.7	24,776	20.9
Government	1,675	1.3	1,950	1.6	2,001	1.7
	132,995	100.0%	125,619	100.0%	118,747	100.0%
Allowance for credit losses	(419)		(465)		(489)	
Total loans by borrower category	$ 132,576		$ 125,154		$ 118,258	
Loans guaranteed by governments and other public and parapublic institutions included above[1]	$ 40,415		$ 36,362		$ 31,423	
Loans guaranteed by government and other public or parapublic institutions as a percentage of total gross loans	30.4%		28.9%		26.5%	
Residential mortgages and consumer, credit card and other personal loans as a percentage of total gross loans	78.5		77.7		77.4	

(1) 2010 data restated to conform with the presentation of 2012 and 2011.

RESIDENTIAL MORTGAGES

The outstanding residential mortgage portfolio was up $6.2 billion, or 7.8%, over the year, to $85.9 billion as at December 31, 2012, compared to an increase of $5.2 billion, or 7.0%, during 2011. This increase is mainly attributable to the quality and diversity of Desjardins Group's mortgage products and its extensive distribution network. It should be noted that Desjardins Group is still the leading residential mortgage lender in Quebec, with a market share estimated at 35.8% as at December 31, 2012.

CONSUMER, CREDIT CARD AND OTHER PERSONAL LOANS

As at December 31, 2012, the outstanding consumer, credit card and other personal loan portfolio posted a year-over-year increase of $535 million, or 3.0%, to total $18.5 billion, compared to a growth of $481 million, or 2.7%, during 2011. Desjardins Group's sustained growth can be attributed to gains made by Card and Payment Services in automobile financing. Desjardins Group's share of this market in Quebec was estimated at 22.9%.

Government-guaranteed loans in this portfolio included student loans and loans related to the Immigrant Investor Program and totalled $3.8 billion as at December 31, 2012, compared to $3.6 billion a year earlier.

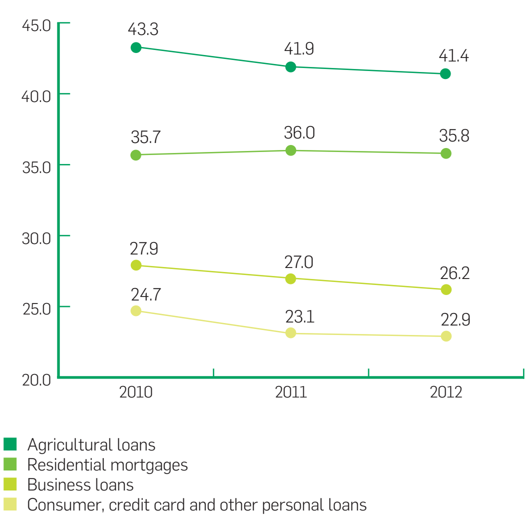
BUSINESS LOANS

At year-end 2012, business loans, which mainly comprise commercial and industrial loans, totalled $26.9 billion, an increase of $871 million, or 3.4%, over the year, due to strong capital spending by businesses, which is supported by low-cost financing and improvements in business profitability. Desjardins Group's share of the Quebec business loan market was estimated at 26.2% at year-end 2012.

As at December 31, 2012, Desjardins Group's outstanding agricultural loans, which are included in the business loan portfolio, amounted to $5.5 billion, for an increase of $105 million, or 2.0%, over the year, compared to an increase of $183 million, or 3.5%, during 2011. Desjardins Group's Quebec market share of agricultural loans was estimated at 41.4% at year-end 2012, which means that it remains a leader in this sector.

QUEBEC MARKET SHARE FINANCING ACTIVITIES

(as a percentage)



GOVERNMENT LOANS

As at December 31, 2012, Desjardins Group's portfolio of outstanding loans to governments, in particular municipalities, stood at $1.7 billion, down $275 million, or 14.1%, from 2011, while it decreased by $51 million, or 2.5%, during 2011. It should be noted that a large proportion of Desjardins Group's credit outstandings in this area are in the form of lines of credit that fluctuate significantly, due to the nature of government financing needs, such as at the municipal level.

CREDIT QUALITY

Desjardins Group's loan portfolio continues to be of excellent quality. Its outstanding gross impaired loans totalled $466 million as at December 31, 2012, down from $520 million at year-end 2011. The gross impaired loans ratio, as a percentage of the total gross loan portfolio, stood at 0.35% as at December 31, 2012, which constitutes an improvement compared to the ratio of 0.41% at the same date a year earlier. Desjardins Group continues to have one of the best gross impaired loans ratios in the Canadian banking industry.

Additional information about the quality of Desjardins Group's credit portfolio is presented in section 4.1, "Risk management", on pages 72 and 73 of this MD&A.

DEPOSITS

COMPOSITION OF THE DEPOSIT PORTFOLIO
(as at December 31, 2012)

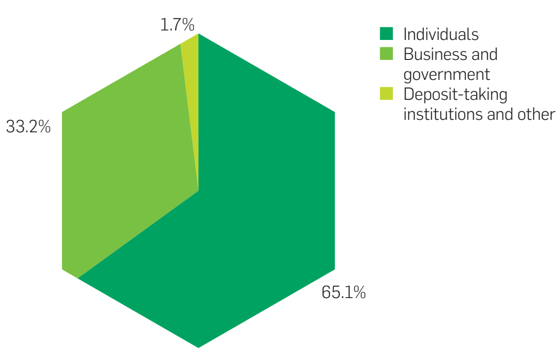


TABLE 18 – DEPOSITS
As at December 31
(in millions of dollars and as a percentage)

	2012					2011[1]		2010[1]	
	Payable on demand	Payable upon notice	Payable on a fixed date	Total	Total	Total	Total	Total	Total
Individuals	$ 26,674	$ 3,990	$ 53,751	$ 84,415	65.1%	$ 82,486	66.8%	$ 78,747	68.7%
Business and government	14,999	311	27,723	43,033	33.2	39,104	31.7	33,686	29.4
Deposit-taking institutions and other	46	—	2,130	2,176	1.7	1,813	1.5	2,230	1.9
Total deposits	$ 41,719	$ 4,301	$ 83,604	$ 129,624	100.0%	$ 123,403	100.0%	$ 114,663	100.0%

(1) 2011 and 2010 data restated to conform with the presentation of 2012.

SAVINGS RECRUITMENT ACTIVITIES

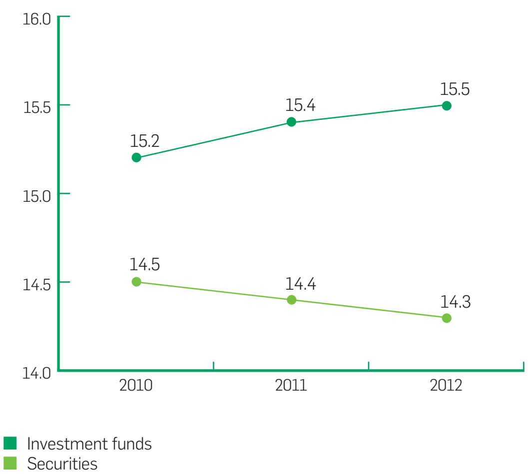
As at December 31, 2012, Desjardins Group's outstanding deposits totalled $129.6 billion, up $6.2 billion, or 5.0%, over the year, compared to an increase of $8.7 billion, or 7.6%, during 2011. This increase was mainly the result of deposit recruitment from individuals, businesses and governments.

The composition of Desjardins Group's deposit portfolio changed very little in 2012. Savings from its members and clients—individuals, businesses and governments—still made up its main source of financing. As at December 31, 2012, it alone accounted for 98.3% of its deposit liabilities, compared to 98.5% at year-end 2011. Deposits by individuals, which stood at $84.4 billion at the end of 2012, were up $1.9 billion, or 2.3%, over the year, versus an increase of $3.7 billion, or 4.7%, during 2011.

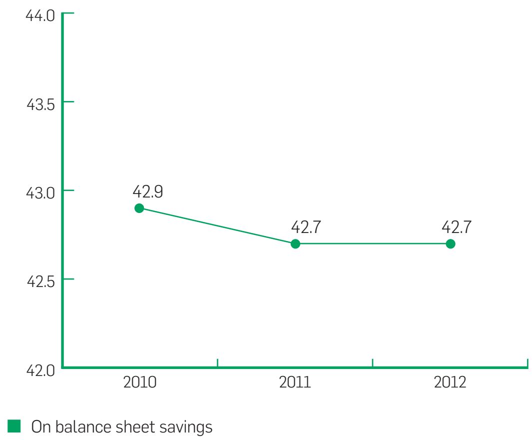
Individuals account for a dominant share of Desjardins Group's deposit liabilities. However, deposits by businesses and governments account for a considerable share as well. These deposits, which totalled $43.0 billion as at December 31, 2012, were up $3.9 billion, or 10.0%, over the year, compared to a gain of $5.4 billion, or 16.1%, during 2011.

Additional information about Desjardins Group's sources of financing can be found on pages 77 to 79, while its liquidity risk management policy is discussed on page 76.

QUEBEC MARKET SHARE
Personal savings recruitment activities
Securities and investment funds
(as a percentage)



QUEBEC MARKET SHARE
Personal savings recruitment activities
On-balance sheet savings
(as a percentage)



SAVINGS FROM INDIVIDUALS

Deposits by individuals represented 65.1% of Desjardins Group's deposit liabilities as at December 31, 2012, comparable to the proportion at year-end 2011, which was 66.8%. As at December 31, 2012, the volume of personal savings totalled $84.4 billion, an increase of $1.9 billion, or 2.3%, over the year, compared to an increase of $3.7 billion, or 4.7%, during 2011. This less-sustained growth in deposit recruitment occurred in a low interest rate environment with increased competition from off-balance sheet savings products.

Of the three broad categories of deposits offered by Desjardins Group to its individual members and clients, savings payable on a fixed date is the largest component. This type of deposit represented 63.7% of savings from individuals at year-end 2012, compared to 61.6% at year-end 2011. Savings payable on a fixed date rose $2.9 billion, or 5.7%, over the year, to $53.8 billion as at December 31, 2012, versus an increase of $1.6 billion, or 3.3%, during 2011. Savings payable on demand and upon notice, which accounted for 36.3% of deposits made by Desjardins Group's individual members and clients over the years, was down by $972 million, or 3.1%, over the year, to $30.7 billion at year-end 2012.

Desjardins Group still ranks as the leader in Quebec for on-balance sheet savings, with a market share estimated at 42.7% as at December 31, 2012.

SAVINGS FROM DEPOSIT-TAKING INSTITUTIONS AND OTHER SOURCES

Outstanding deposits by deposit-taking institutions, which totalled $2.2 billion as at December 31, 2012, grew by $363 million, or 20.0%, over the year, compared to a decrease of $417 million, or 18.7%, during 2011. This type of deposit represented only 1.7% of Desjardins Group's total deposit liabilities at the end of 2012, versus 1.5% a year earlier.

OTHER LIABILITIES

Other liabilities amounted to $48.0 billion as at December 31, 2012, compared to a volume of $49.4 billion recorded at year-end 2011, which represents a $1.4 billion, or 2.8%, decrease. These liabilities comprise mainly insurance and investment contract liabilities as well as commitments related to securities sold short and securities lent or sold under repurchase agreements. They totalled $17.8 billion, $5.0 billion and $8.0 billion, respectively, as at December 31, 2012.

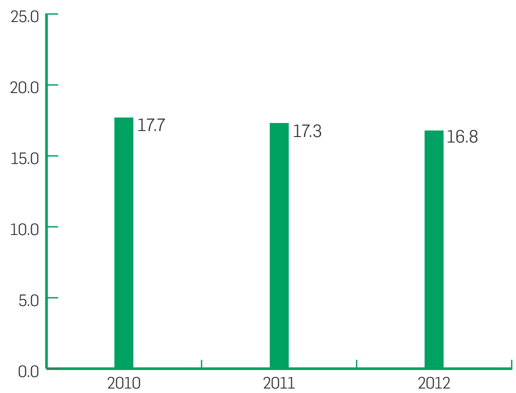
EQUITY

Equity amounted to $16.0 billion as at December 31, 2012, compared to $14.0 billion as at December 31, 2011, for an increase of $2.0 billion, or 14.4%. The main sources of this growth were the capital shares the Federation issued to caisse members, which totalled more than $1.0 billion, as well as net surplus earnings for the year after member dividends, which were $1.4 billion.

SECTION 3.2

CAPITAL MANAGEMENT

TIER 1 CAPITAL RATIO
(as a percentage)



Capital management is crucial to Desjardins Group's financial management, and takes into account its regulatory obligations, the economic and financial environment, its risk profile, and its cooperative difference and objectives.

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. As at December 31, 2012, Desjardins Group's Tier 1 capital and total capital ratios stood at 16.8% and 19.3%, respectively, compared to ratios of 17.3% and 19.3%, respectively, as at December 31, 2011. Desjardins Group's prudent management is further reflected in the credit ratings granted by the various rating agencies.

The 2008–2009 global financial crisis prompted the industry to place more emphasis on capitalization. Now more than ever, the 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 stricter capital adequacy requirements that will apply following the implementation of Basel III, in the first quarter of 2013. It was against this backdrop that Desjardins Group set its minimum target for Tier 1a capital at 15% and its minimum target for Tier 1 capital at 15% over the 2013–2016 horizon.

DESJARDINS GROUP'S INTEGRATED CAPITAL MANAGEMENT FRAMEWORK

The purpose of capital management is to ensure that the capital structure and level of Desjardins Group and its components are adequate in terms of the risks taken by the organization, profitability targets, growth objectives, rating agencies' expectations and regulators' requirements. In addition, capital management serves to optimize the allocation of capital and internal capital flow mechanisms, and support growth, development and asset risk management at Desjardins Group.

Broadly speaking, Desjardins Group's Integrated Capital Management Framework includes the policies and processes required to set targets for its capitalization and to assign targets to its components, 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 mechanisms.

Desjardins Group has set up a stress-testing program aimed to establish and measure the effect of various integrated scenarios, i.e. to simulate various economic scenarios for all of its components and assess the financial and regulatory repercussions. This procedure makes it possible to determine if the required capital, as established in the capitalization plan, is adequate in view of the risks to which Desjardins is exposed.

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 Finance and Risk Management Committee and the Asset/Liability Committee to ensure that Desjardins Group has a sufficient and reliable capital base. The Finance Executive Division and Office of the CFO is responsible for preparing, on an annual basis and with the help of Desjardins Group's components, a capitalization plan that sets and updates capital objectives and targets for all components.

The current situation and the forecast show that Desjardins Group has a solid capital base overall and, therefore, sufficient latitude to pursue its growth strategy.

BASEL II

Desjardins Group's regulatory capital ratios are calculated according to the AMF's guideline on adequacy of capital base applicable to financial services cooperatives. Since fiscal 2009, this regulatory framework has been largely based on the revised framework for international convergence of capital measurement and capital standards (Basel II) issued by the Bank for International Settlements. In this regard, the AMF allowed Desjardins Group to use the Internal Ratings-Based Approach, subject to compliance with conditions, for credit risk related to retail loan portfolios (individuals). Other credit exposures and market risk are assessed according to a Standardized Approach, while operational risk is calculated based on the Basic Indicator Approach.

The minimum total capital ratio recommended to institutions for compliance with the Bank for International Settlements' regulatory requirements and to be considered sufficiently capitalized is 8%. In addition, the Tier 1 capital ratio must represent at least half of the total capital ratio. With the coming into force of the Basel II regulatory framework, the AMF revised its minimum total capital ratio to 11.5%. Desjardins Group maintained its financial objective for the Tier 1 capital ratio at a minimum of 15% (the same level as the target for the total capital ratio), thus taking into account the prevailing global economic context and the framework of the AMF's guideline on adequacy of capital base.

At 16.8% and 19.3%, respectively, Desjardins Group's Tier 1 and total capital ratios exceed not only the minimum regulatory requirement but also Desjardins Group's own financial objective.

In addition to minimum Tier 1 and total capital ratios, the AMF requires that Desjardins Group maintain an assets-to-regulatory capital ratio that does not exceed 20 times to 1. This measure allows overall capital adequacy to be determined against the entity's total assets, including certain off-balance sheet items. With an assets-to-capital ratio of 11.5 times to 1 as at December 31, 2012, Desjardins Group is well below the limit set by the AMF.

Since the implementation of Basel II, Desjardins Group has applied the deferred treatment prescribed by the AMF, under which equity related to investments in its insurance subsidiaries made before January 1, 2007, was fully deducted from Tier 2 capital until the end of fiscal 2011. Effective January 1, 2012, this equity is deducted in equal shares of 50% from Tier 1 capital and Tier 2 capital. The end of the application of this deferred treatment had an unfavourable impact of approximately 130 basis points on the Tier 1 capital ratio as at December 31, 2012, while the total capital ratio remained the same.

Until the new Basel III requirements are implemented in 2013, regulators are revising certain regulations, in particular concerning market risk and the weighting of some securitization categories (Basel 2.5); these regulations have been effective since the first quarter of 2012. The changes concerning market risk had no significant impact on the increase in risk-weighted assets, while the changes concerning securitization generated an increase of $512 million in risk-weighted assets as at December 31, 2012, which was entirely offset by the resulting lower trigger point adjustment so that the impact on Desjardins Group's capital ratios is nil.

BASEL III

On December 16, 2010, and January 13, 2011, the Bank for International Settlements issued new requirements (Basel III) for the global regulation of capital standards. In fact, since 2009, various consultative proposals have been submitted to the banking industry as a whole to build a more secure financial system that is more resilient in periods of stress. The new rules, which will be phased in over the next few years, increase not only capital requirements (the minimum levels to be met) but also risk management requirements. The new framework, combined with global liquidity standards, forms an essential element of the global financial reform program. These new Basel III capital standards have been integrated into the AMF's guideline on adequacy of capital base applicable to financial services cooperatives, which was updated in December 2012.

The key points of the new regulatory capital standards set out in Basel III are:

1) Improvement in the quality of financial institutions' capital:
   - A new definition of the components of capital categories
   - A greater focus on the best Tier 1 capital component to absorb losses (Tier 1a capital or Common Equity Tier 1)
2) Increase in minimum capital requirements:
   - Tier 1a capital ratio of 7.0%, including a 2.5% capital conservation buffer
   - Tier 1 capital ratio of 8.5%, including a 2.5% capital conservation buffer
   - Total capital ratio of 10.5%, including a 2.5% capital conservation buffer
   - The Basel Committee also provides for the addition of a minimum leverage ratio to prevent the build-up of excessive leverage (a requirement already imposed on Desjardins Group by its regulatory authority)
3) Reduction of systemic risk:
   - Strong incentive from the Basel Committee to have a countercyclical capital buffer, ranging from 0% to 2.5%, in order to prevent risk from spreading throughout the entire financial system
4) Addition of supplementary criteria for capitalization instruments to ensure their capacity to absorb losses in insolvency

The increased minimum capital levels will be phased in between 2013 and 2019. The above-mentioned minimum capital requirements represent the minimum regulatory requirements for 2019. The AMF nevertheless expects that Desjardins Group will meet the minimum capital requirements for 2019 in the first quarter of 2013. Should these targets not be met, the AMF may impose measures that could take the form of restrictions on distributions. Desjardins Group was already well capitalized as at December 31, 2012, and expects to exceed these targets.

Capital instruments that do not meet the eligibility criteria for tier capital will be excluded from the tier effective January 1, 2013. However, instruments that meet certain conditions will be gradually eliminated from capital at an annual rate of 10% over a nine-year period beginning January 1, 2013, in accordance with the transitional provisions set out in the AMF guideline. These instruments include an amount of $2.3 billion in permanent shares and surplus shares that will be subject to the 10% amortization. These shares were eligible as Tier 1 capital under Basel II as at December 31, 2012. Desjardins Group is currently devising a strategy to mitigate the gradual impact of the amortization on its ratios.

Moreover, upon initial application of Basel III as at January 1, 2013, subordinated bonds will also be subject to the 10% amortization. In order to be fully eligible as Tier 2 capital, such subordinated bonds will need to meet Non-Viability Contingent Capital (NVCC) requirements. Discussions concerning the application of these requirements to cooperative entities are still in progress at the international level. Desjardins Group does not plan to issue any subordinated debt until these requirements are further clarified.

HIGHLIGHTS OF CAPITAL MANAGEMENT

- On June 18, 2012, the Federation introduced a program to issue capital shares for a maximum of $1.2 billion. An amount of $1,025 million had been issued as at December 31, 2012. These capital shares, currently included in Tier 1 capital under Basel II, meet the upcoming regulatory capital requirements (Basel III) for Tier 1a capital.
- On June 1, 2012, *Capital Desjardins inc.* called all outstanding Series C senior subordinated bonds, in the amount of $300 million.

ANALYSIS OF CAPITAL RATIOS

Desjardins Group is one of the best capitalized financial institutions in Canada: its Tier 1 and total capital ratios, measured under the Basel II regulatory framework, stood at 16.8% and 19.3%, respectively, as at December 31, 2012 (17.3% and 19.3%, respectively, as at December 31, 2011). Desjardins Group therefore still has excellent capitalization, with a Tier 1 capital ratio above its 15% objective. The high level of Tier 1 capital demonstrates the financial strength of Desjardins Group, even in a challenging economic environment.

The Tier 1 capital ratio as at December 31, 2012, at 16.8%, was down 50 basis points from its level a year earlier. This decline is mainly attributable to the end of the deferred treatment applicable to equity related to investments in its insurance subsidiaries made before January 1, 2007, as explained under "Basel II" above, and to the amortization of the initial IFRS impact, which were partially offset by the issuance of capital shares by the Federation and by organic growth. The total capital ratio remained unchanged as at December 31, 2012, compared to December 31, 2011. The issuance of capital shares by the Federation and organic growth offset the decline resulting from the amortization of the initial IFRS impact, the redemption of subordinated debt and the increase in deductions related mainly to the increase in the value of interests in deconsolidated subsidiaries for purposes of calculating regulatory capital.

As at January 1, 2011, the date of conversion to IFRS, Desjardins Group elected to use the transitional provisions permitted by the AMF. This election was irrevocable and made it possible to mitigate the impacts of the new accounting standards through a quarterly adjustment of eligible undistributed surplus earnings over a two-year period ending December 31, 2012. Accordingly, for purposes of calculating the Tier 1 capital ratio, Desjardins Group amortized, the eligible portion of the IFRS impact of $1.2 billion on a straight-line basis, for a quarterly amortization of $145 million, between January 1, 2011, and December 31, 2012. As at December 31, 2012, this impact had been completely amortized, and all impacts related to the first-time adoption of IFRS had been fully taken into account in the capital ratio calculations.

In addition to the impact of the implementation of Basel III on capital ratios, presented under "Basel III" above, capital ratios could be impacted, effective in the first quarter of 2013, by the amendments to IAS 19, "Employee Benefits", on accounting for defined benefit pension plans. These amendments stipulate in particular that the use of the "corridor approach" is no longer allowed and that all actuarial gains and losses must now be recognized when they occur. In addition, it is no longer permitted to amortize past service costs, which will accelerate its recognition. At the same time, the new standard allows risk-sharing features to be taken into account. The total negative impact, estimated as at today's date, of these amendments on Tier 1a capital would be about 65 basis points. However, the initial negative impact could be deferred and amortized on a straight-line basis over the period from January 1, 2013, to December 31, 2014, depending on whether Desjardins Group elects to use the transitional provision stipulated for that purpose by the AMF.

Furthermore, in preparation for the transition to the new Basel III requirements, Desjardins Group has initiated a process to refine all the processes and parameters used to calculate regulatory capital.

As at December 31, 2012, pro forma Tier 1a and Tier 1 capital ratios, which were calculated in accordance with this exercise and Basel III requirements, are both estimated at 16.3% (excluding the incidence of applying the amendments to IAS 19, "Employee Benefits", on accounting for defined benefit pension plans, whose incidence is described under "Analysis of capital ratios" above, and the 10% amortization, applicable as at January 1, 2013, of capital not eligible under Basel III, but eligible under transitional provisions). Tier 1 capital would fluctuate mainly as a result of the inclusion of other comprehensive income, the fact that a significant portion of the investments in the insurance subsidiaries would no longer be deducted from capital, but rather weighted at 250% under Basel III, and the treatment of unrated securitizations, which would no longer be deducted from capital but rather weighted at 1,250% under Basel III.

TABLE 19 – REGULATORY CAPITAL
As at December 31
(in millions of dollars and as a percentage)

	2012	2011
Tier 1 capital		
Eligible capital shares	$ 3,294	$ 2,186
Reserves	10,216	9,032
Undistributed surplus earnings	1,282	1,236
Deferral attributable to the adoption of IFRS	—	578
Non-controlling interests	60	60
Goodwill	(341)	(336)
Other deductions(1)	(1,586)	(423)
Total Tier 1 capital	12,925	12,333
Tier 2 capital		
Subordinated bonds	3,092	3,363
Eligible collective allowance	261	256
Other eligible securities	112	110
Non-controlling interests	15	68
Other deductions(1)	(1,578)	(2,379)
Total Tier 2 capital	1,902	1,418
Total regulatory capital	$ 14,827	$ 13,751
Capital ratios		
Tier 1 capital	16.8%	17.3%
Total capital	19.3	19.3

(1) Mainly includes the provision deficit related to the Internal Ratings-Based Approach ($309 million [$346 million as at December 31, 2011]), securitization exposures ($222 million [$117 million as at December 31, 2011]) and investments ($2,517 million [$2,254 million as at December 31, 2011]) in components deconsolidated for regulatory capital purposes (primarily Desjardins Financial Security Life Assurance Company and Desjardins General Insurance Group Inc.) as well as investments ($107 million [$80 million as at December 31, 2011]) in associates.

COMPLIANCE WITH REQUIREMENTS

With respect to regulatory capital, the capital adequacy and composition of Desjardins Group as a whole are evaluated using the guideline on adequacy of capital base standards issued by the AMF. The AMF requires that a minimum amount of capital be maintained on a combined basis by all the components, especially the caisses, the Federation (as a legal entity), *Caisse centrale Desjardins, Fonds de sécurité Desjardins, Capital Desjardins inc.,* Western Financial Group Inc., Desjardins Securities Inc. and Desjardins Trust Inc.

This capital takes into consideration investments made in other Desjardins Group components. Some of Desjardins Group's components are subject to separate requirements with respect to regulatory capital, liquidities and financing, which are set by organizations that regulate banking and securities. Their requirements may be subject to amendments to the regulations and differ by activity. The liquidity of Desjardins Group's main components is assessed on an ongoing basis, given the regulatory restrictions imposed by local administrations, as well as operational, tax, economic and other constraints on the flow of funds between components. In this way, Desjardins Group is able to manage and minimize the liquidities it maintains. It monitors and manages liquidity and capital requirements in these entities in order to ensure an efficient use of capital and continuous compliance, by each of these entities, with regional regulations. Additional details concerning the AMF guideline and the regulatory framework governing the capitalization of each Desjardins Group entity are presented in Note 31, "Capital management", to the Combined Financial Statements.

Desjardins Group and all its entities subject to minimum regulatory capital requirements were in compliance with these requirements as at December 31, 2012, as they were in 2011.

TABLE 20 – RISK-WEIGHTED ASSETS
As at December 31
(unaudited, in millions of dollars and as a percentage)

	Internal ratings-based approach		Standardized approach		2012 Total			2011 Total
	Exposure(1)	Risk-weighted assets	Exposure(1)	Risk-weighted assets	Exposure(1)	Risk-weighted assets	Average risk weighting rate	Risk-weighted assets
Sovereign borrowers	$ —	$ —	$ 13,317	$ —	$ 13,317	$ —	—%	$ —
Financial institutions	—	—	8,034	1,607	8,034	1,607	20	1,630
Businesses	—	—	40,555	30,627	40,555	30,627	76	27,632
Mortgages	51,252	4,332	193	41	51,445	4,373	9	4,790
Qualifying revolving retail exposures	27,604	7,589	—	—	27,604	7,589	27	8,596
Other retail exposures	37,498	4,093	3,940	2,560	41,438	6,653	16	6,470
Securitization	—	—	1,734	1,026	1,734	1,026	59	636
Equities	—	—	155	155	155	155	100	41
Trading portfolio	—	—	1,468	334	1,468	334	23	572
Other assets(2)	—	—	—	—	11,761	3,917	33	3,508
Scaling factor(3)	—	961	—	—	—	961	—	1,039
Total credit risk	116,354	16,975	69,396	36,350	197,511	57,242	—	54,914
Market risk	—	—	—	1,644	—	1,644	—	1,791
Operational risk(4)	—	—	—	—	—	11,884	—	11,281
Transitional adjustment for floor(5)	—	—	—	—	—	6,125	—	3,339
Total risk-weighted assets	$ 116,354	$ 16,975	$ 69,396	$ 37,994	$ 197,511	$ 76,895	—%	$ 71,325

(1) Net exposure, after credit risk mitigation (net of individual allowances under the Standardized Approach but not under the Internal Ratings-Based Approach, in accordance with the AMF guideline).
(2) The other assets are measured using a method other than the Standardized Approach or the Internal Ratings-Based Approach.
(3) The scaling factor is a 6.0% calibration of risk-weighted assets assessed using the Internal Ratings-Based Approach for credit exposures in accordance with Section 1.3 of the AMF guideline.
(4) The Basic Indicator Approach was used to assess operational risk.
(5) As prescribed in Section 1.6 of the AMF guideline.

SECTION 3.3

ANALYSIS OF CASH FLOWS

Because of the nature of Desjardins Group's operations, most of the items on the Combined Statements of Income and the Combined Balance Sheets are liquidities. Normal operations therefore cause considerable fluctuations in liquidity and influence numerous items such as loans, deposits and securities. The main changes in cash flows are explained in the following paragraphs.

During the year ended December 31, 2012, cash and cash equivalents increased by $313 million, compared to a decrease of $265 million during 2011. Cash and cash equivalents stood at $1,669 million as at December 31, 2012, versus $1,356 million a year earlier.

In 2012, cash flows used in operating activities totalled $437 million, chiefly because of an increase of $7,663 million in loans, and of $1,823 million in other operating assets and liabilities. These increases were for the most part offset by an increase of $6,221 million in deposits. In 2011, cash flows from operating activities amounted to $2,231 million, especially because of an increase of $9,406 million in deposits, a net change of $1,959 million in insurance and investment contract liabilities, and a decrease of $2,075 million in securities borrowed or purchased under reverse repurchase agreements. These changes were offset essentially by growth of $7,592 million in loans and by a decrease of $2,203 million and of $2,108 million, respectively, in commitments related to securities sold short and in commitments related to securities lent or sold under repurchase agreements.

Cash flows from financing activities totalled $712 million as at December 31, 2012, in particular because of the capital share issue of $1,026 million and the $87 million net change in capital stock, which were chiefly offset by the redemption of subordinated bonds in the amount of $300 million and the remuneration on permanent shares of $70 million, net of income tax recovery. In 2011, cash flows from financing activities totalled $569 million as a result of the issuance of subordinated bonds in the amount of $479 million and the $81 million net change in capital stock.

In addition, cash flows from investing activities were $38 million during the year ended December 31, 2012, primarily because of the proceeds from disposals and maturities of available-for-sale securities for the respective amounts of $34,883 million and $1,201 million, which were offset essentially by the purchase of available-for-sale securities amounting to $35,716 million and the purchase of property, plant and equipment and investment property for $322 million. In 2011, cash flows used in investing activities amounted to $3,065 million, particularly because of the purchase of available-for-sale securities for $28,954 million, offset mainly by the proceeds from the disposals and maturities of available-for-sale securities totalling $24,479 million and $1,902 million, respectively.

SECTION 3.4

OFF-BALANCE SHEET ARRANGEMENTS

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

ASSETS UNDER ADMINISTRATION AND ASSETS UNDER MANAGEMENT

As at December 31, 2012, Desjardins Group had assets totalling $313.1 billion under administration and under management on behalf of its members and clients, compared to $281.0 billion at the end of 2011. This represented an increase of $32.1 billion, or 11.4%, compared to an increase of $6.5 billion, or 2.4%, in the previous year. In addition, financial assets placed with Desjardins Group as asset manager amounted to $30.9 billion as at that date, for a year-over-year increase of $4.2 billion, or 15.6%, versus an increase of $1.5 billion, or 5.8%, during 2011.

Desjardins Group is one of Canada's leading trustees and wealth managers. It was able to capitalize on the improvement in stock market activity in Canada and the rest of the world. For instance, at the close of trading on the Toronto Stock Exchange on December 31, 2012, the S&P/TSX index was up 4.0% over the year, compared to a decline of 11.1% in 2011. The assets entrusted to Desjardins Group by its members and clients in the form of off-balance sheet savings products, such as investment funds and other securities, accounted for part of its assets under administration and under management. As at December 31, 2012, these off-balance sheet savings products outstanding had grown by $4.4 billion, or 9.0%, on an annual basis, to total $53.0 billion, compared to an increase of $160 million, or 0.3%, during 2011.

Assets under administration and under management are composed chiefly of financial assets in the form of investment funds, securities held in custody and assets accumulated by pension funds. As a result, they do not belong to Desjardins Group, but to its members and clients, and therefore are not recognized in the Combined Balance Sheets.

TABLE 21 – ASSETS UNDER ADMINISTRATION AND ASSETS UNDER MANAGEMENT
As at December 31
(in millions of dollars)

	2012	2011(1)	2010(1)
Assets under administration			
Individual and institutional trust and asset custody services	$ 267,401	$ 247,239	$ 246,016
Investment funds(2)	45,696	33,743	28,426
Total assets under administration	$ 313,097	$ 280,982	$ 274,442
Assets under management			
Institutions and individuals	$ 6,442	$ 8,006	$ 7,190
Investment funds(2)	24,434	18,694	18,055
Total assets under management	$ 30,876	$ 26,700	$ 25,245

(1) 2011 and 2010 data restated to conform with the presentation of 2012.
(2) Including Desjardins Funds and Northwest & Ethical Investments.

CREDIT INSTRUMENTS

In order to meet its members' and clients' financing needs, Desjardins Group makes credit instruments available to them. Credit instruments include guarantees and standby letters of credit, securities loans, and credit commitments representing authorized amounts that have not been used by members or clients. The risks associated with credit instruments are managed according to the same strict rules as those applied to Combined Balance Sheet items. In management's opinion, no unusual risk results from these off-balance sheet items.

These instruments expose Desjardins Group to credit and liquidity risks. Management of these risks is described on pages 67 to 73 and pages 76 to 80 of this MD&A. Table 22 shows the contractual amounts of the credit instruments by remaining maturities. Since several of these credit instruments will mature or will be terminated without any cash outflow, the contractual amounts of these commitments do not represent future liquidity needs.

Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements of Desjardins Group provides more detailed information on these credit instruments.

TABLE 22 – CREDIT INSTRUMENTS BY MATURITIES
As at December 31
(in millions of dollars)

	2012				2011	2010
	Less than 1 year	1 to 5 years	Over 5 years	Total	Total	Total
Guarantees and standby letters of credit	$ 724	$ 144	$ 38	$ 906	$ 733	$ 750
Securities lending	1,848	—	—	1,848	1,512	1,407
Credit commitments	55,236	6,103	21	61,360	55,704	50,756
Total credit instruments	$ 57,808	$ 6,247	$ 59	$ 64,114	$ 57,949	$ 52,913

CONTRACTUAL COMMITMENTS

Desjardins Group has contractual commitments to make future payments on borrowings, subordinated bonds and leases. Borrowings and subordinated bonds are presented on the Combined Balance Sheets, while other contractual commitments, including credit commitments and leases, are not. Note 6, "Securities", Note 15, "Other liabilities – Other", Note 16, "Subordinated bonds", and Note 27, "Commitments, guarantees and contingent liabilities", to Desjardins Group's Combined Financial Statements provide information on these contractual commitments.

FINANCIAL ASSETS HELD AS COLLATERAL

Desjardins Group holds or pledges financial assets as collateral as a result of transactions involving securities borrowed or purchased under reverse repurchase agreements. Such transactions are carried out under normal conditions for these types of transactions. Note 27, "Commitments, guarantees and contingent liabilities", to Desjardins Group's Combined Financial Statements provides additional information about financial assets held as collateral.

SPECIAL PURPOSE ENTITIES

In the normal course of operations, Desjardins Group enters into various financial transactions with special purpose entities (SPEs) to diversify its sources of financing and manage its capital. SPEs are usually created for a single and distinct purpose, and they often have a limited life. They are used to legally isolate the financial assets they hold from the transferring organization. SPEs are not operating entities and generally have no employees. Under IFRS, they can be included in the Combined Balance Sheets if, in substance, the relationship between this entity and Desjardins Group indicates that control exists. Details concerning significant exposure to SPEs are provided below.

MASTER ASSET VEHICLES (MAVs)

The MAV 1 and MAV 3 trusts are considered special purpose entities not included in Desjardins Group's Combined Balance Sheets. These trusts are composed of synthetic asset, ineligible asset and traditional asset transactions. Desjardins Group entered into several transactions of various nature to minimize the risk associated with the asset-backed term notes (ABTN) portfolio, the margin funding facility (MFF) related to the ABTN portfolio and other restructured securities. The implementation of credit index hedges on a significant portion of the MAV 1 portfolio, the acquisition of protection for Desjardins Group's commitments under the MFF, and the disposal of various restructured portfolios very significantly reduced the risk related to these portfolios.

These trusts had assets of approximately $15,962 million as at December 31, 2012, compared to $16,185 million as at December 31, 2011, and they had no equity. As at December 31, 2012, Desjardins Group had an MFF of $1,193 million and held notes with a fair value of $1,705 million, compared to the respective amounts of $1,193 million and $1,368 million in 2011. The total of the MFF and the notes represents the possible maximum risk of loss to which Desjardins Group is exposed. Note 6, "Securities", to Desjardins Group's Combined Financial Statements contains more information.

SECURITIZATION

Desjardins Group participates in the Mortgage-Backed Securities Program under the *National Housing Act* to manage its liquidities and capital. Transactions carried out under this program require the use of an SPE, the Canada Housing Trust (CHT), set up by Canada Mortgage and Housing Corporation (CMHC) under the Canada Mortgage Bonds (CMB) Program. Note 8, "Securitization and other transferred financial assets", to the Combined Financial Statements provides more information on the financial assets transferred by Desjardins Group through securitization transactions.

To carry out securitization transactions, Desjardins Group bundles CMHC-guaranteed residential mortgages into mortgage-backed securities (NHA MBSs), and transfers them to the SPE in return for monetary consideration. The SPE then finances these purchases by issuing CMBs to investors. However, as part of these transactions, Desjardins Group retains substantially all the risks and rewards related to the securities transferred. Consequently, the loans continue to be recognized on the Combined Balance Sheets, and a liability, which is equal to the consideration received from CMHC for the sale of the NHA MBSs that do not meet derecognition criteria, is recognized.

As at December 31, 2012, outstanding NHA MBSs issued by Desjardins Group and sold to CHT totalled $5.0 billion. However, some securitization transactions entered into before January 1, 2010, resulted in derecognition, as Desjardins Group elected to apply the derecognition requirements prospectively. At the time of transfer, these transactions were therefore recognized as sales, and Desjardins Group retains certain interests in excess interest margins, which are retained interests, and assumes the responsibility of managing the transferred mortgage loans. As at December 31, 2012, the aggregate outstanding of the original assets transferred and derecognized was $0.6 billion, compared to $1.8 billion at the end of 2011. At the same date, assets representing retained interests that Desjardins Group continues to recognize with respect to these transactions amounted to $7 million, compared to $28 million as at December 31, 2011.

4.0 RISK MANAGEMENT

SECTION 4.1

RISK MANAGEMENT

The shaded boxes 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 Management's Discussion and Analysis (MD&A). Consequently, the shaded boxes are an integral part of the Combined Financial Statements, as explained in Note 29, "Financial instrument risk management", to the Combined Financial Statements.

Desjardins Group is exposed to different types of risk in its normal course of operations, including credit risk, counterparty and issuer risk, market risk, liquidity risk, operational risk, insurance risk, strategic risk and reputation risk. Strict and effective management of these risks is a priority for Desjardins Group, its purpose being to support its major directions, particularly regarding its financial stability as well as its sustained and profitable growth, while complying with Basel requirements.

INTEGRATED RISK MANAGEMENT FRAMEWORK

Desjardins Group's objective in risk management is to optimize the risk-return trade-off, within set tolerance limits, by applying integrated risk management and control strategies, policies and procedures to all its activities. It also aims to provide, through the Integrated Risk Management Framework, a prudent and appropriate framework that complies with accepted accountability and independence principles.

As integral parts of this management framework, risk appetite and tolerance determine the type and level of risk that Desjardins is prepared to assume to achieve its business and strategic objectives. They provide a basis for integrated risk management by promoting a better understanding of the risks and their impact on the risk profile. This framework provides for a system of risk indicators that are monitored on a regular basis to ensure that Desjardins Group's risk profile matches the level of risk appetite and tolerance sought by senior management and the Board of Directors in view of Desjardins Group's mission, vision and values. The Board of Directors is responsible for approving the risk appetite and tolerance framework and ensuring it reflects Desjardins Group's financial and strategic objectives.

Desjardins Group's Integrated Risk Management Framework also includes the overall operational infrastructure and the risk management governance structure, which are supported by all implicit or explicit rules, values and ways of thinking and acting within Desjardins Group. This framework promotes exchanges between Desjardins Group's risk management function and its business sectors and regulated entities.

To promote sound risk management and enhance risk management capabilities, risk management training sessions are held on a regular basis. Desjardins Group has a continuing professional development plan, through which it intends to continue updating the knowledge of the members of participating bodies.

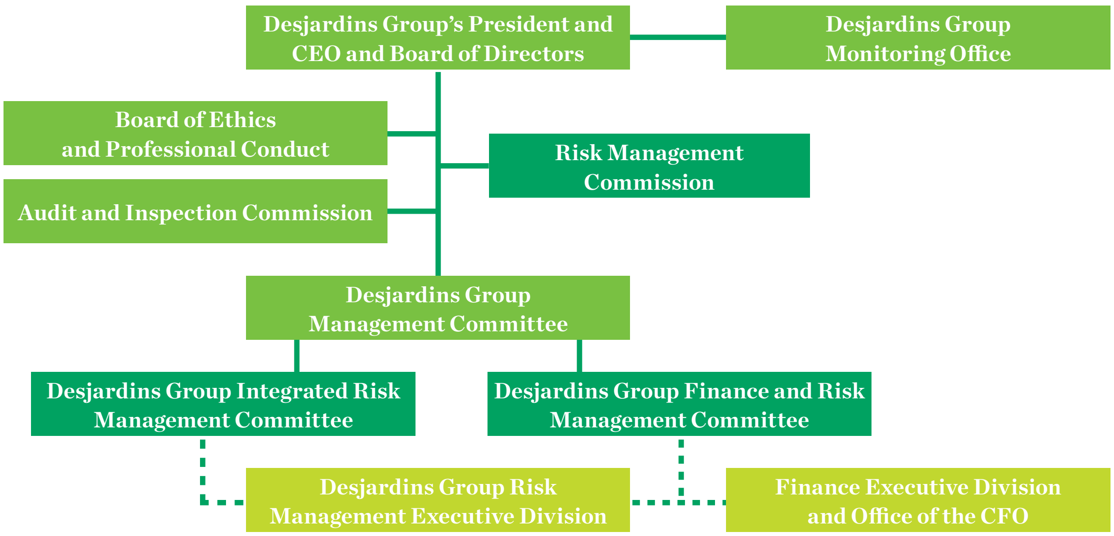
RISK MANAGEMENT GUIDELINES

The Integrated Risk Management Framework is based on risk management guidelines that provide for the following:

- The accountability of Desjardins Group's business sectors with regard to the risks inherent to their operations
- Application at every level of the organization to obtain a comprehensive vision of risk exposure
- The existence of a 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 introducing projects with a strong financial impact

RISK MANAGEMENT GOVERNANCE

The Integrated Risk Management Framework is based on a solid risk governance structure and reflects Desjardins Group's organizational structure.
The main risk management decision-making bodies are as follows:



The Board of Directors of the *Fédération des caisses Desjardins du Québec* 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. The Board of Directors is primarily responsible for adopting the general directions and strategies proposed by senior management as well as risk management policies aimed at ensuring sound and prudent management of operations. To discharge its specific risk management responsibilities, the Board is supported by the Risk Management Commission, the Audit and Inspection Commission and the Board of Ethics and Professional Conduct. Further information about these bodies is available on pages 183 to 202 of the Corporate Governance section of the *2012 Desjardins Group Annual Report*.

The Desjardins Group Management Committee must make recommendations to the Board of Directors concerning risk management policies and strategies and ensure that they are implemented effectively and efficiently. Two committees support the Management Committee in discharging its risk management responsibilities: the Integrated Risk Management Committee and the Finance and Risk Management Committee, which are made up of the heads of Desjardins Group's strategic functions and Desjardins experts. These two committees are themselves supported by subcommittees that specialize in specific aspects of risk management.

Two independent functional units complete Desjardins Group's risk management governance infrastructure. The Risk Management Executive Division is a strategic function whose main purpose is to serve as a partner in Desjardins Group's growth by identifying, measuring and managing risks while ensuring the longevity of Desjardins. In partnership with the business sectors, the Desjardins Group risk management function is responsible for recommending and establishing risk management policies, and setting up the appropriate infrastructure, processes and practices to target all major Desjardins-wide risks. Monitoring and control of the various risks is a shared responsibility at Desjardins Group that is partly assumed by the business sectors and teams responsible for regulatory compliance and financial governance. They complement the work of those responsible for risk management to ensure that services are delivered in line with growing regulatory requirements.

The Desjardins Group Monitoring Office is an independent and objective assurance and advisory body that assists Desjardins Group's management personnel 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's subsidiaries and other components as well as the audit and inspection services for the caisse network.

RISK MEASUREMENT AND DISCLOSURE

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.

Risks are quantified based on both the current economic context as well as hypothetical situations simulating crises applied across the entire organization. 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 distress conditions. The results of these analyses help detect potential vulnerabilities to risk factors for various operations

RISK DISCLOSURE

Risk reports on all significant risks are regularly prepared for the Integrated Risk Management Committee, the Finance and Risk Management Committee, the Desjardins Group Operations Committee, the Desjardins Group Management Committee, the Risk Management Commission, the Audit and Inspection Commission, and the Board of Directors. These reports provide risk indicators as well as information about capital, particularly capital adequacy in relation to Desjardins Group's risk profile. These reports are regularly updated to include the latest risk management developments so that decision-making bodies receive up-to-date information on major risks that is both practical and forward-looking.

BASEL II CAPITAL ACCORD

Basel II 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 II framework is 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 II, Desjardins Group uses the Internal Ratings-Based Approach, subject to conditions, for credit risk related to retail loan portfolios (personal). Other credit and market risk exposures are currently assessed using the Standardized Approach, while operational risk is calculated using the Basic Indicator Approach. This provision is used to calculate Desjardins Group's capital ratios, among other things.

Again this year, numerous efforts were made throughout Desjardins Group to support 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 industry best practices for the main 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, which regulators will integrate progressively into their guidelines effective January 1, 2013, will increase not only capital requirements but also risk management requirements. In addition to the changes made to the level and definition of eligible capital and measurement of risk-weighted assets, Basel III has, under Pillar 2, introduced new requirements for liquidity and raised expectations for a number of management practices. Disclosure standards, which fall under Pillar 3, have also been enhanced. Desjardins will continue its development by integrating these new regulatory requirements into its risk management framework.

Additional information about capital management is presented in section 3.2, "Capital management", on pages 55 to 60.

CREDIT RISK

Credit risk is the risk of losses resulting from a borrower'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 represented 67.4% of assets on the Combined Balance Sheets as at December 31, 2012, compared to 65.8% a year earlier. It is also exposed through its various other commitments, including letters of credit, foreign exchange lines and transactions involving derivative financial instruments and securities.

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 clientele. The units and components that make 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 a certain amount of latitude in terms of frameworks, approvals, and the corresponding management and monitoring tools and structures.

To provide assistance in this area, Desjardins Group has set up centralized structures and procedures to ensure that its risk management framework allows for effective, sound and prudent management.

Desjardins Group has a Risk Management Executive Division, which includes two credit risk management divisions. These divisions share responsibilities based on major activities: credit approval, quantification, monitoring and reporting.

CREDIT RISK FRAMEWORK

A set of policies 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.

Approval and credit risk management units assume responsibility for credit granting and management and for providing a framework specific to their products and operations. These units establish their own policies and practices, based on their products and clients and in compliance with the general policies that govern all credit activities.

Together, these frameworks, policies and practices govern Desjardins's risk management and control activities

CREDIT GRANTING

The caisses, Desjardins business centres and other business centres in contact with clients are primarily responsible for approving files. Some approval limits are set, and loans for any amount above these limits are approved by the Risk Management Executive Division.

Professionals are assigned to one of the two previously mentioned divisions according to client type. Their qualifications, their approval responsibilities and the depth of the analysis required are used to match them to specific products, as well as the complexity and extent of the transaction risk.

RETAIL LOANS

Retail portfolios consist of residential mortgages, personal loans, credit card loans to individuals, and loans to small businesses. To assess the risk of credit activities involving individuals and smaller businesses, credit scoring systems based on proven statistics are used.

These systems were developed based on a history of behaviour among borrowers with a profile or characteristics similar to those of the applicant and based on the products used, including the type of collateral offered, to determine the transaction risk.

Such systems are used for initial approval as well as subsequently, when behavioural ratings, calculated using member-borrowers' transaction data, are used to assess portfolio risk on an ongoing basis. A monthly update is obtained for existing borrowers' risk level for proactive management of a portfolio's credit risk.

The performance of these systems is continually assessed and adjustments are made regularly with a view to determining transaction and borrower risk as adequately as possible.

Risk parameters are set for each exposure category analyzed and make it possible to determine probabilities of default, loss given default and gross exposures at default for groups with similar characteristics.

The units responsible for the development process ensure that adequate controls are in place to guarantee the stability and performance of rating systems and internal models. These, in turn, are validated by a unit independent from the development process to ensure that they are conceptually sound and properly take into account all major risks. This validation is performed when the model is initially set up and subsequently, on an annual basis, as well as when major changes are made to it. A validation policy determines the events requiring validation by an independent unit, the approved rating systems and internal models, and the scope and nature of the validation work.

BUSINESS LOANS

The granting of credit to businesses is based on an analysis of the various parameters of each file, where each borrower is assigned a risk rating. These ratings are assigned individually following a detailed examination of the financial, market and management characteristics of the business. The scoring system used for the main commercial portfolios has 19 ratings, broken down into 12 levels, each representing a probability of default.

Table 23 provides a comparison of internal ratings and ratings assigned by external agencies.

TABLEAU 23 – RATINGS BY RISK LEVEL

Ratings	Moody's	S&P	Description
1 to 2	Aaa to Aa3	AAA to AA-	
2.5	A1 to A3	A+ to A-	High quality
3 to 4	Baa1 to Baa3	BBB+ to BBB-	
4.5 to 5.5	Ba1 to Ba3	BB+ to BB-	
6 to 7.5	B1 to Caa1	B+ to CCC+	Lower quality
8 and 9	Caa2 to C	CCC to C-	
10 to 12	D	D	Impaired loans or loans in default

The following table presents the credit quality of the business and government loan portfolio recorded on the Combined Balance Sheets. The amounts presented are before the impact of the allowance for credit losses.

TABLE 24 – CREDIT RISK EXPOSURE OF THE BUSINESS AND GOVERNMENT LOAN PORTFOLIO

As at December 31
(in millions of dollars)

	2012		2011	
Business and government loans				
High quality	$ 10,685	37.4%	$ 10,775	38.6%
Lower quality	17,375	60.9	16,672	59.6
Impaired loans or loans in default	484	1.7	501	1.8
Total	$ 28,544	100.0%	$ 27,948	100.0%

The characteristics of each borrower are analyzed using models based on internal and external historical data, taking into account the specific features of the borrower's economic sector and the performance of comparable businesses. These analyses are performed using systems that can make quantitative comparisons, and are supplemented by the professional judgment of the personnel involved with the file.

The use of internal ratings and estimates has been expanded to other risk management and governance activities such as establishing analysis requirements and file authorization levels, the different types of follow-up activities, and the assessment and disclosure of portfolio risk quality.

MITIGATING CREDIT RISK

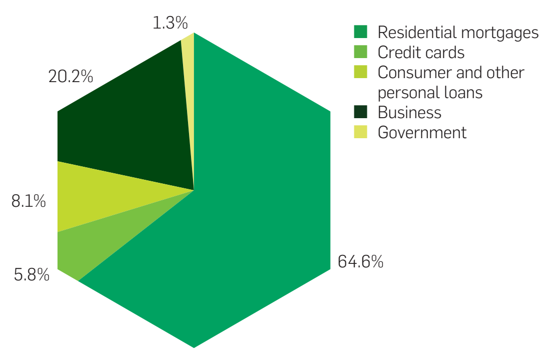
In its lending operations, Desjardins Group obtains collateral, if deemed necessary, for a member's or client's borrowing facility following an assessment of their creditworthiness. Collateral normally takes the form of assets, such as capital assets, receivables, inventory, cash, government securities or equities. For some portfolios, programs offered by organizations such as Canada Mortgage and Housing Corporation and *La Financière agricole du Québec* are used in addition to customary collateral. Loans guaranteed by governments and other public and parapublic organizations represented 30.4% of total gross loans as at December 31, 2012, compared to 28.9% a year earlier, as shown in Table 17 on page 52. Policies and procedures, adapted to each product, contain the requirements for appraising collateral, its legal validation and follow-up.

Where required, Desjardins Group uses mechanisms for sharing risk with other financial institutions, such as loan syndication. Lending in Quebec makes up 93.1% of total loans, with 6.7% in the rest of Canada and 0.2% in the United States.

The large number of borrowers—for the most part individuals, but also small- and medium-sized businesses from most sectors of the economy—helps ensure the sound diversification of the financing portfolio.

LOAN DISTRIBUTION BY BORROWER CATEGORY

(as at December 31, 2012)



The above chart presents the distribution of loans by borrower category. Over half of the portfolio consists of residential mortgages, for which, statistically, the loss experience is lower. Additional information about credit risk is presented in Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

COUNTERPARTY AND ISSUER RISK

Counterparty and issuer risk is a credit risk relative to different types of transactions involving securities, derivative financial instruments and securities loans.

The Risk Management Executive Division sets the maximum exposure for each counterparty and issuer based on quantitative and qualitative criteria. The amounts are then allocated to the various components based on their needs.

To manage its risk properly, Desjardins Group assigns a credit rating to each counterparty and issuer, based on the ratings of four external credit rating agencies (DBRS, Moody's, S&P and Fitch). This rating is used to establish exposure limits and to calculate capital requirements using the Standardized Approach. These four external credit rating agencies meet the eligibility criteria of the Basel Accord and are authorized by the AMF and the OSFI.

A large proportion of Desjardins's exposure is to the different levels of government in Canada, Quebec public and parapublic entities, and major Canadian banks. For most of these, the credit rating is A- or higher. Desjardins Group is not directly exposed to the sovereign debt of the European countries most affected by the recent financial crisis, namely Greece, Portugal, Italy, Ireland and Spain. Its exposure to U.S. and European financial institutions is marginal.

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

It uses derivative financial instruments primarily for asset and liability management purposes. Derivative financial instruments are contracts whose value is mainly based on an underlying asset, such as interest rates or exchange rates. The vast majority of derivative financial instruments are negotiated by mutual agreement between Desjardins Group and the 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 transactions are carried out as part of regulated trades and mainly consist of futures.

The credit risk associated with derivative financial instruments 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. The credit risk associated with derivative financial instruments normally corresponds to a small fraction of the notional amount. The replacement cost and the credit risk equivalent are two measurements used to evaluate this risk. The replacement cost refers to the current replacement cost of all contracts having a positive fair value. The credit risk equivalent is equal to the sum of this replacement cost and the potential credit exposure.

Desjardins Group limits the credit risk associated with derivative financial instruments by doing business with counterparties that have a high credit rating. Note 17, "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 virtually all counterparties have credit ratings of between AAA and 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.

Desjardins Group also limits credit risk related to certain counterparties by using master agreements called International Swaps and Derivatives Association (ISDA) agreements, which define the terms and conditions for the transactions. These agreements are legal contracts that bind the counterparties. Most of Desjardins Group's 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. Taking into account master netting agreements, the risk-weighted balance for all Desjardins Group's derivative financial instruments as at December 31, 2012, amounted to $344 million, compared to $311 million at year-end 2011. As at December 31, 2012, the amount of collateral that Desjardins Group would have to provide in the event of a downgrade was marginal because the replacement cost was positive for the majority of the contracts.

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 credit risk and requires a percentage of collateralization (a pledge) on these transactions.

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

Additional information about credit risk is presented in Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

MAXIMUM CREDIT RISK EXPOSURE

Table 25 presents the maximum credit risk for financial instruments other than those recognized on the Combined Balance Sheets, without taking into account collateral held or other credit enhancements. Maximum credit risk for the financial instruments recognized is equal to the carrying amount.

TABLE 25 – MAXIMUM CREDIT RISK EXPOSURE

As at December 31
(in millions of dollars)

	2012	2011
Recognized on the Combined Balance Sheets		
Deposits with financial institutions	$ 496	$ 173
Securities		
Debt securities held for trading	8,952	9,448
Debt securities designated as at fair value through profit or loss	12,305	12,385
Available-for-sale debt securities	16,915	17,485
Off-balance sheet		
Guarantees and standby letters of credit	$ 906	$ 733
Credit commitments(1)	61,360	55,704

(1) Includes the credit facility related to the restructuring plan of the Montreal Accord. Additional information is provided in Note 6, "Securities", to the Combined Financial Statements.

Additional information about credit risk is presented in Note 17, "Derivative financial instruments and hedging activities", and Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

ADDITIONAL CREDIT RISK INFORMATION

Probability of default (PD) is the likelihood of a borrower defaulting on its obligations within a one-year time horizon. Loss given default (LGD) is the magnitude of loss that may be incurred in the event a borrower defaults. Exposure at default (EAD) is the amount likely to be engaged in the event of default.

The following tables present additional credit risk information. Used and unused exposures are made up of the core credit risks. Off-balance sheet exposures include credit equivalent amounts for comparable transactions, over-the-counter derivatives, other off-balance sheet exposures and any trading portfolios.

TABLE 26 – RISK EXPOSURE BY ASSET CLASS (EXPOSURE AT DEFAULT [EAD])

As at December 31, 2012
(in millions of dollars)

	Exposure categories(1)				
	Used exposure	Unused exposure	Off-balance sheet exposure(2)	Total	Net exposure(3)
Standardized Approach					
Sovereign borrowers	$ 12,680	$ 587	$ 69	$ 13,336	$ 13,317
Financial institutions	5,874	1,813	4,636	12,323	8,034
Businesses	37,324	3,317	1,362	42,003	40,555
Mortgages	193	—	—	193	193
Other retail exposures	4,399	870	31	5,300	3,940
Securitization	1,734	—	—	1,734	1,734
Equities	155	—	—	155	155
Trading portfolio	—	—	11,517	11,517	1,468
Internal Ratings-Based Approach					
Mortgages	44,595	6,658	—	51,253	51,252
Revolving retail exposures	9,383	18,214	7	27,604	27,604
Other retail exposures	31,131	6,367	1	37,499	37,498
Total	$ 147,468	$ 37,826	$ 17,623	$ 202,917	$ 185,750

(1) The definition of exposure categories related to regulatory capital requirements differs from the accounting classification.
(2) Including repo-style transactions, over-the-counter derivatives and other off-balance sheet exposures.
(3) After credit risk mitigation (CRM) techniques including the use of collateral, guarantees and credit derivatives.

TABLE 27 – RISK EXPOSURE BY ASSET CLASS(1) AND BY RISK TRANCHE (STANDARDIZED APPROACH)(2)

As at December 31, 2012
(in millions of dollars)

	Risk tranches							
	0%	20%	35%	50%	75%	100%	Other	Total
Sovereign borrowers	$ 13,336	$ —	$ —	$ —	$ —	$ —	$ —	$ 13,336
Financial institutions	—	12,323	—	—	—	—	—	12,323
Businesses	—	1,187	—	234	—	40,252	402	42,075
Mortgages	—	—	187	—	—	7	—	194
Other retail exposures	—	—	—	—	5,255	27	39	5,321
Securitization	—	7	—	—	—	703	1,024	1,734
Equities	—	—	—	—	—	155	—	155
Trading portfolio	1,916	8,062	—	58	—	1,481	—	11,517
Total	$ 15,252	$ 21,579	$ 187	$ 292	$ 5,255	$ 42,625	$ 1,465	$ 86,655

(1) The definition of exposure categories related to regulatory capital requirements differs from the accounting classification.
(2) Exposures before individual allowances for credit losses and before CRM.

TABLE 28 – RISK EXPOSURE BY ASSET CLASS(1) AND REMAINING CONTRACTUAL TERM TO MATURITY

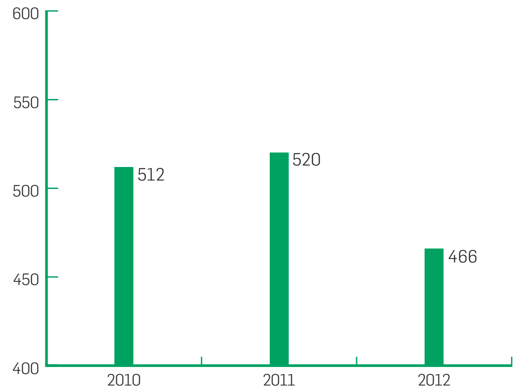
As at December 31, 2012
(in millions of dollars)

	Less than 1 year	1 to 5 years	Over 5 years	Total
Internal Ratings-Based Approach				
Mortgages	$ 21,174	$ 29,896	$ 183	$ 51,253
Revolving retail exposures	27,604	—	—	27,604
Other retail exposures	11,020	22,885	3,594	37,499
Total	$ 59,798	$ 52,781	$ 3,777	$ 116,356

(1) The definition of exposure categories related to regulatory capital requirements differs from the accounting classification.

QUALITY OF LOAN PORTFOLIO

GROSS IMPAIRED LOANS
(in millions of dollars)



Desjardins Group's loan portfolio continues to be of excellent quality. As at December 31, 2012, gross impaired loans outstanding were $466 million, down $54 million compared to December 31, 2011. The gross impaired loans ratio, as a percentage of the total gross loan portfolio, was 0.35% at year-end 2012, showing an improvement over the ratio of 0.41% as at December 31, 2011. Individual allowances for credit losses, which totalled $138 million as at December 31, 2012, made it possible to obtain a total coverage ratio of 29.6% of the gross impaired loans portfolio as at December 31, 2012, while this ratio was 30.6% at year-end 2011.

The collective allowance stood at $281 million as at December 31, 2012, versus $306 million as at year-end 2011. In addition, an allowance related to off-balance sheet exposures of $101 million as at December 31, 2012, compared to $92 million as at the same date the prior year, was recognized under "Other liabilities – Other" in the Combined Balance Sheets. The collective allowance reflects management's best estimate of allowances for credit losses regarding loans not yet individually identified as impaired. The volume of gross impaired loans declined by 10.4%, from $520 million as at December 31, 2011, to $466 million at year-end 2012. This decline can be seen across all portfolios. These results confirm that the organization's entire portfolio is performing well. The methods for measuring the collective allowance and individual allowances, as well as the method for determining an impaired loan, are described in section 5.4, "Critical accounting policies and estimates – Impairment of financial assets", on page 90 of this MD&A.

Tables 29 and 30 present impaired loans by borrower category as well as the individual coverage ratio for these loans.

TABLE 29 – IMPAIRED LOANS BY BORROWER CATEGORY
As at December 31
(in millions of dollars and as a percentage)

	2012					2011	2010
	Gross loans	Gross impaired loans		Individual allowances for credit losses	Net impaired loans	Net impaired loans	Net impaired loans
Residential mortgages	$ 85,931	$ 129	0.15%	$ 13	$ 116	$ 120	$ 128
Consumer, credit card and other personal loans	18,520	84	0.45	31	53	52	49
Business and government	28,544	253	0.89	94	159	189	176
Total	$ 132,995	$ 466		$ 138	$ 328	$ 361	$ 353
As a percentage of gross loans			0.35%		0.25%	0.29%	0.30%

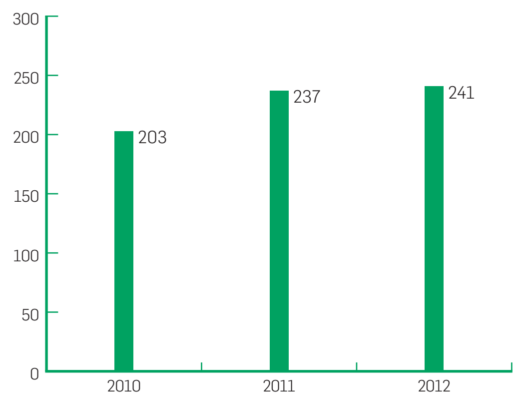
TABLE 30 – SPECIFIC COVERAGE RATIO
As at December 31
(as a percentage)

	2012	2011	2010
Residential mortgages	10.1%	9.1%	8.6%
Consumer, credit card and other personal loans	36.9	42.2	42.4
Business and government	37.2	36.6	38.7
Coverage ratio of impaired loans	29.6	30.6	31.1

PROVISION FOR CREDIT LOSSES

The provision for credit losses totalled $241 million for 2012, up $4 million compared to the corresponding period in 2011. This provision comprises the provision for loan losses of $232 million and the provision for off-balance sheet commitments of $9 million for 2012, compared to $219 million and $18 million, respectively, for 2011. The provision for loan losses represented 0.19% of average gross loans, the same figure as in 2011.

PROVISION FOR CREDIT LOSSES
(in millions of dollars)



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 primarily through positions taken in the course of its traditional financing and savings recruitment activities. It is also exposed to market risk through its trading activities. Desjardins Group and its components have adopted policies that set out the principles, limits and procedures to use in managing market risk.

INTEREST RATE RISK MANAGEMENT

Desjardins Group is exposed to interest rate risk, which represents the potential impact of interest rate fluctuations on net interest income and the economic value of equity. Interest rate 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.

Sound and prudent management is used to achieve the objective of optimizing net interest income while minimizing the negative incidence of interest rate movements. The established policies describe the principles, limits and procedures that apply to 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.

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 this data. These assumptions concern changes in the structure of assets and liabilities, including modelling for non-maturity deposits and equity, member behaviour and 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 interest rate risk management policies.

Table 31 presents the impact before income taxes on the non-trading portfolio of a sudden and sustained 100-basis-point increase or decrease in interest rates on net interest income and the economic value of equity.

TABLE 31 – INTEREST RATE SENSITIVITY (BEFORE INCOME TAXES)
As at December 31
(in millions of dollars)

	2012		2011	
	Net interest income(1)	Economic value of equity(2)	Net interest income(1)	Economic value of equity(2)
Impact of a 100-basis-point increase in interest rates	$ 5	$ (96)	$ 56	$ 118
Impact of a 100-basis-point decrease in interest rates	(26)	41	(87)	(71)

(1) Represents interest rate sensitivity of net interest income for the next 12 months.
(2) Represents the sensitivity of the present value of assets, liabilities and off-balance sheet instruments.

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

FOREIGN EXCHANGE RISK

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.

Overall, Desjardins Group's exposure to this risk is limited because the majority of its transactions are conducted in Canadian dollars. However, in certain specific situations, Desjardins Group and its components may become exposed to foreign exchange risk, particularly with respect to the U.S. dollar. This exposure mainly arises from their intermediation activities with members and clients, and its financing and investment activities. To ensure that exposure is properly controlled and limited, Desjardins Group and its components use derivative financial instruments such as forward exchange contracts and currency swaps.

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. The main tool used to measure the market risk of trading portfolios is "Value-at-Risk" (VaR), which represents an estimate of the potential loss over a certain period of time 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.

Table 32 presents the aggregate VaR of the trading activities by risk category as well as the diversification effect, which represents the difference between aggregate VaR and the sum of VaR for different risk categories. Equity price risk, interest rate risk and foreign exchange risk are the three risk categories to which Desjardins Group is exposed. The definition of a trading portfolio meets the criteria defined in the Basel Capital Accord.

TABLE 32 – VaR BY RISK CATEGORY (TRADING PORTFOLIO)
(in millions of dollars)

	As at December 31, 2012	For the year ended December 31, 2012			As at December 31, 2011	For the year ended December 31, 2011		
		Average	High	Low		Average	High	Low
Equities	$ 0.1	$ 0.2	$ 0.4	$ 0.1	$ 0.4	$ 0.4	$ 1.1	$ 0.2
Foreign exchange	0.1	0.1	0.1	—	0.1	0.1	0.6	—
Interest rate	1.9	3.0	7.8	1.1	3.5	4.0	6.7	2.2
Diversification effect(1)	(0.2)	(0.3)	N/A(2)	N/A(2)	(0.3)	(0.5)	N/A(2)	N/A(2)
Aggregate VaR	$ 1.9	$ 3.0	$ 7.7	$ 1.1	$ 3.7	$ 4.0	$ 6.6	$ 2.2

(1) Risk reduction related to diversification, namely the difference between the sum of the VaR for the various market risks and the aggregate VaR.
(2) Not applicable: The highs and lows of the various market risk categories can refer to different dates.

As at December 31, 2012, the aggregate VaR was $1.9 million, the interest rate VaR being the largest component. Aggregate VaR was $3.0 million below its annual average. Risk mitigation related to diversification amounted to $0.2 million as at December 31, 2012.

BACK TESTING

Back testing is conducted to validate the VaR model used. This involves a daily comparison of the VaR with the profits and losses (P&L) on portfolios.

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.

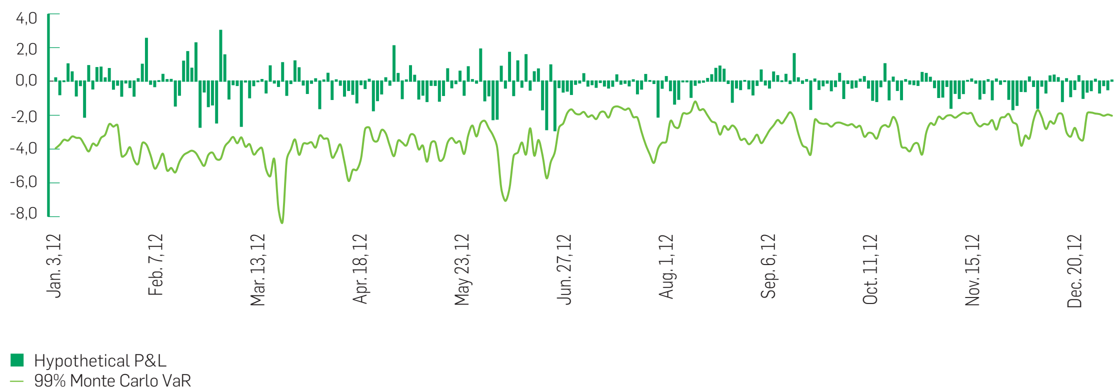
The following chart presents changes in VaR for trading activities as well as profits and losses related to these activities. During the fourth quarter of 2012, the hypothetical P&L did not exceed VaR.

STRESS TESTING

From time to time, certain events that are considered highly unlikely may occur and may have a significant impact on trading portfolios. These events are at the tail-end of the distribution and are the result of extreme situations.

The approach used to measure the risk related to highly unlikely but plausible events involves applying a stress-testing program (sensitivity tests, historical scenarios and hypothetical scenarios) at regular intervals. Stress-testing results are analyzed together with VaR calculations in order to detect Desjardins Group's vulnerability to such events. The stress-testing program is reviewed periodically to ensure that it is kept current.

VaR COMPARED TO HYPOTHETICAL P&L OF TRADING ACTIVITIES
(in millions of dollars)



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 is exposed to liquidity risk in potential crisis situations that would result in unusual cash outflows and make it necessary for Desjardins Group Treasury to find the funding needed to meet sudden demands. For instance, such an extreme situation could occur in the event caisse members begin making massive withdrawals due to a lack of confidence in the organization's financial stability. 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 and tolerance thresholds, and procedures that apply to liquidity risk management.

LIQUIDITY RISK MANAGEMENT

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 funding, monitoring indicators, and adopting a contingency plan to implement in the event of a liquidity crisis.

Policies and standards are reviewed on a regular basis to ensure that they are appropriate for the operating environment and prevailing market conditions. They are also updated according to regulatory requirements and sound liquidity risk management practices.

LIQUIDITY RESERVES

The minimum liquidity reserves that must be maintained by the caisse network, the Federation and *Caisse centrale Desjardins* are prescribed in policies and standards specific to each entity. Day-to-day management of securities and the reserve level to be maintained is centralized at Desjardins Group Treasury and is subject to risk management monitoring under the supervision of the Desjardins Group Finance and Risk Management Committee. Eligible securities must meet high security and negotiability standards.
Securities held in these funds are largely Canadian government securities.

The aggregate liquidity reserves held in these funds provide manoeuvring room for Desjardins Group and are monitored daily. In addition to complying with specific policies and standards, the levels maintained must provide assurance of their adequacy in the event of a possible severe liquidity crisis directly affecting Desjardins Group, such as if its credit rating were downgraded by rating agencies. A Desjardins-wide crisis scenario program has been implemented for this purpose. This program incorporates the concepts put forward by the Bank for International Settlements (BIS) under the document entitled "Basel III – International Framework for Liquidity Risk Measurement, Standards and Monitoring". The scenarios make it possible to measure the magnitude of potential cash outflows in a crisis situation, to implement liquidity ratios and levels to be maintained throughout Desjardins Group, and to assess the potential marginal cost of such events, depending on the type, severity and level of the crisis.

The introduction of Basel III will also strengthen international minimum liquidity requirements. This accord will introduce a liquidity coverage ratio (LCR) to allow financial institutions to cope with potential liquidity crisis ("illiquidity") situations, and a net stable funding ratio (NSFR) to address mismatches between assets and funding sources. Even though the Basel Committee is still studying these two ratios and an observation period is currently underway, the AMF expects Desjardins Group to calculate these ratios in order to benefit from an observation period before the planned effective dates of January 1, 2015, for the LCR, and January 1, 2018, for the NSFR. Desjardins Group already monitors these two ratios on a regular basis for management information purposes and intends to comply with the new standards once they become effective.

SOURCES OF FUNDING

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 financing needs.

It should be noted that systems are in place for the issuance of covered bonds and the securitization of CHMC-insured loans. Furthermore, Desjardins Group is eligible for the Bank of Canada's various intervention programs and loan facilities for Emergency Lending Assistance advances.

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. For each liquidity indicator defined, warning levels are established and are subject to an escalation process. 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.

The indicators are divided into two categories: indicators specific to Desjardins Group and capital market indicators. The first category includes indicators that monitor the level of Desjardins Group's room for manoeuvre, member behaviour, credit spreads faced by *Caisse centrale Desjardins*, and the effectiveness of institutional funding sources. Market indicators focus primarily on credit spreads observed for financial institutions and the provinces relative to federal bonds.

CONTINGENCY PLAN

Desjardins Group has developed a liquidity contingency plan that includes setting up an internal crisis committee vested with special decision-making powers to deal with crisis situations. This plan also lists the sources of liquidity available in exceptional situations. In addition, it sets out the decision-making and information process based on the severity level of a possible crisis.

The scope of a liquidity crisis depends on its possible duration, the amount of cash outflows, the efficiency of sources of funding, and its potential threat to the solvency of Desjardins Group. The crisis levels affecting Desjardins Group Treasury's normal operations are as follows:

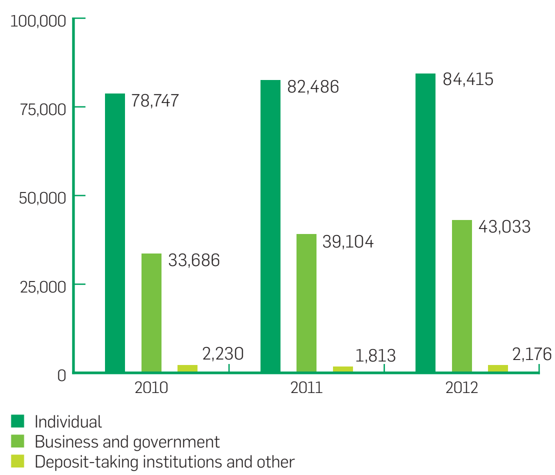
1. Pre-crisis or temporary decline in liquidity reserves
2. Major decline in liquidity reserves for an extended period of time but solvency not affected
3. Liquidity seriously compromised but solvency not affected
4. Liquidity seriously compromised and solvency threatened
5. Illiquidity and imminent or declared insolvency

The aim of the plan is to enable quick and efficient action in order to minimize disruptions caused by sudden changes in member and client behaviour and potential disruptions in capital markets or economic conditions.

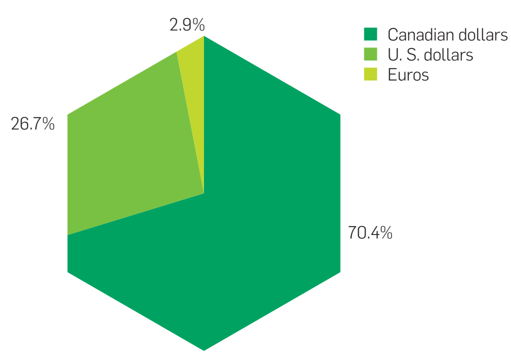
SOURCES OF FINANCING

Core funding, which includes capital, long-term liabilities and a diversified deposit portfolio, is the foundation of Desjardins Group's liquidity position. As at December 31, 2012, Desjardins Group's outstanding deposit totalled $129.6 billion, up $6.2 billion, or 5.0%, from December 31, 2011. This growth was mainly due to business and government deposits, which totalled $43.0 billion, up $3.9 billion, or 10.0%, from $39.1 billion as at December 31, 2011. Deposits from individuals, business and government make up the main source of reliable funding and are Desjardins Group's preferred category of funds. This solid base alone accounted for 98.3% of the deposit liabilities as at December 31, 2012.

DEPOSITS BY CATEGORY
(in millions of dollars)



FUNDING BY CURRENCY
(as at December 31, 2012)



As Desjardins Group's treasurer, *Caisse centrale Desjardins* meets the needs of the organization's members and clients. Its first priority is to implement appropriate strategies to identify, measure and manage risks. These activities are regulated by a liquidity sufficiency and administration policy and a refinancing management policy.

In order to maintain stable and diversified refinancing, *Caisse centrale Desjardins* ensures the diversification of its sources of financing from institutional capital markets. It therefore regularly turns to the capital markets when conditions are favourable, and occasionally makes public and private issues of term notes on Canadian, U.S. and European markets.

In 2012, *Caisse centrale Desjardins* managed to maintain sufficient liquidity levels to meet Desjardins Group's needs through its strong treasury policy, solid institutional refinancing and the contribution of the caisse network. *Caisse centrale Desjardins*'s strict treasury management strategy also put it in a good position to deal with the current period of global financial recovery.

In keeping with its strategy of increasing the duration of its institutional refinancing and its mission as Desjardins Group's treasurer, *Caisse centrale Desjardins* issued debt securities on various markets in 2012. In fact, in March, *Caisse centrale Desjardins* issued medium-term covered bonds in the amount of US$1.5 billion on the U.S. market. In October 2012, it also issued medium-term notes in the amount of $800 million. This issuance, the largest of its kind on the Canadian market by *Caisse centrale Desjardins*, was very well received by investors. The presence of Desjardins Group on these different markets also helped expand its pool of institutional investors.

Caisse centrale Desjardins continued to be present in the federally guaranteed mortgage loan securitization market under the Canada Mortgage Bond (CMB) Program. It was in fact active in this area, participating in new issues of approximately $1.5 billion in 2012, namely four five-year fixed rate CMB issuances and one five-year floating rate CMB issuance. The main objective of this program is to obtain a source of long-term financing at the lowest price on the market.

Capital Desjardins inc. is a subsidiary of Desjardins Group. Its mandate is to issue securities on capital markets and to invest the proceeds in subordinated notes issued by the member caisses of the Federation. On June 1, 2012, *Capital Desjardins inc.* called all its outstanding Series C Senior Notes due in 2017, in the amount of $300 million.

Overall, these issuances 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.

The following is a summary of the various *Caisse centrale Desjardins* borrowing programs:

On the Canadian market:

- A medium-term deposit note program of up to $5 billion

On the international market:

- A European short-term deposit note program of €1 billion
- A U.S. short-term deposit note program of US$5 billion
- A global multi-currency medium-term deposit note program of €7 billion

As at December 31, 2012, *Caisse centrale Desjardins*'s borrowings and medium-term notes totalled $10.5 billion, up $575 million compared to the same date in 2011. As for *Capital Desjardins inc.*, its subordinated bonds amounted to $3.1 billion as at December 31, 2012, versus $3.4 billion as at December 31, 2011.

CREDIT RATINGS

The credit ratings assigned to Desjardins Group by the rating agencies are instrumental in ensuring access to sources of wholesale financing and the cost of such financing, and they also impact Desjardins Group's credibility and recognition among institutional investors.

Rating agencies assign credit ratings to securities issued by Desjardins Group, based on its financial stability, its capitalization, the stability of its operating surplus earnings, its leading role in its local markets and the quality of its assets.

On December 13, 2012, Standard & Poor's downgraded the credit ratings of *Caisse centrale Desjardins* and *Capital Desjardins inc.*, as well as five other Canadian financial institutions. The agency said it was concerned about Canadian debt levels and the possible consequences on financial institutions, particularly on their mortgage portfolios and credit loss volumes. It expects a slowdown in credit demand and greater pressure on the margins of the country's financial institutions, in a low interest rate environment.

In addition, on January 28, 2013, Moody's downgraded the credit ratings of *Caisse centrale Desjardins* and *Capital Desjardins inc.*, as well as the ratings of five other Canadian financial institutions. The agency stated that its decision was due to the economic situation in Canada, which is showing signs for concern, such as high consumer debt levels and elevated housing prices. Moody's also said that financial institutions are more vulnerable than in the past to downside risks weighing on the Canadian economy.

Management is of the opinion that these decisions have more to do with the agencies' concerns about Canada's economic situation than with the quality of Desjardins Group's loan portfolio or balance sheet.

Even after the downgrade, the ratings of *Caisse centrale Desjardins* and *Capital Desjardins inc.* remain among the best in Canada and compare favourably with those of many large international and Canadian financial institutions.

The credit ratings and outlooks assigned by Fitch and DBRS to the various securities of *Caisse centrale Desjardins* and *Capital Desjardins inc.* were unchanged in 2012.

TABLE 33 – CREDIT RATINGS OF SECURITIES ISSUED

	DBRS	STANDARD & POOR'S	MOODY'S	FITCH
Caisse centrale Desjardins				
Short-term	R-1 (high)	A-1	P-1	F1+
Medium- and long-term, senior	AA	A+	Aa2	AA-
Capital Desjardins inc.				
Medium- and long-term, senior	AA (low)	A	A2	A+

CONTRACTUAL OBLIGATIONS

Contractual obligations are commitments with respect to minimum future payments and impact Desjardins Group's liquidity needs. Such contractual obligations are recognized in the Combined Balance Sheets or are off-balance sheet.

Table 34 presents financial liabilities as well as other obligations by remaining contractual maturity term. The amounts presented include principal and interest, if any.

TABLE 34 – CONTRACTUAL OBLIGATIONS BY TERM TO MATURITY

As at December 31
(in millions of dollars)

	2012				
	Payable on demand	Less than 1 year	1 to 5 years	Over 5 years	Total
Liabilities					
Deposits	$ 46,100	$ 42,415	$ 44,599	$ 338	$ 133,452
Acceptances	—	841	—	—	841
Commitments related to securities sold short	4,790	131	44	18	4,983
Commitments related to securities lent or sold under repurchase agreements	1	7,982	—	—	7,983
Subordinated bonds	—	175	746	3,425	4,346
Amounts payable to clients, brokers and financial institutions	1,752	797	—	—	2,549
Other financial liabilities	31	1,704	89	2	1,826
Guarantees and standby letters of credit	490	234	144	38	906
Credit commitments	22,576	32,660	6,103	21	61,360
Derivative financial instruments with net settlement	—	167	265	13	445
Derivative financial instruments with gross settlement(1)					
Cash flows to be paid on liabilities	—	4,896	1,422	—	6,318
Cash flows to be paid on assets	—	4,420	2,737	—	7,157

	2011				
	Payable on demand	Less than 1 year	1 to 5 years	Over 5 years	Total
Liabilities					
Deposits	$ 42,734	$ 39,622	$ 44,210	$ 780	$ 127,346
Acceptances	—	676	—	—	676
Commitments related to securities sold short	5,119	168	57	2	5,346
Commitments related to securities lent or sold under repurchase agreements	3	8,497	—	—	8,500
Subordinated bonds	—	187	777	3,836	4,800
Amounts payable to clients, brokers and financial institutions	2,191	1,695	—	—	3,886
Other financial liabilities	10	2,000	80	3	2,093
Guarantees and standby letters of credit	381	107	245	—	733
Credit commitments	20,325	29,936	4,226	1,217	55,704
Derivative financial instruments with net settlement	—	330	437	23	790
Derivative financial instruments with gross settlement(1)					
Cash flows to be paid on liabilities	—	7,842	1,544	—	9,386
Cash flows to be paid on assets	—	2,011	1,690	7	3,708

(1) The "Derivative financial instruments with gross settlement" category includes cash flows to be paid on both derivative financial instruments recorded as liabilities and derivative financial instruments recorded as assets. Contractual cash outflows for derivative financial instruments with gross settlement are accompanied by related cash inflows that are not included in this table.

OPERATIONAL RISK

Operational risk is defined as 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 MANAGEMENT

Operational risk is inherent to all business activities as well as internal and outsourced activities. Losses can mainly arise from fraud, damage to tangible assets, illegal acts, system failures, or problems in process management.

OPERATIONAL RISK MANAGEMENT FRAMEWORK

The primary objective of the operational risk management framework is to maintain operational risk at an acceptable level while focusing on the quality of service provided to Desjardins Group members and clients and on organizational agility. The development of policies, guidelines and rules to identify, measure, track, monitor and disclose operational risk ensures its sound and prudent management.

There are practices in place to foster efficient and proactive management of events that could lead to operational risk. These include practices for risk assessment, management of outsourcing risks, protection of information, insurance coverage, business continuity and crisis management.

The operational risk management framework is periodically reviewed based on regulatory authorities' expectations and industry practices

BUSINESS CONTINUITY AND CRISIS MANAGEMENT

Desjardins Group has enhanced its business continuity program, the purpose of which is to ensure that service delivery to members and clients will be maintained in essential operations in the event of business interruptions, system disruptions or crises.

INFORMATION RISK MANAGEMENT

Desjardins Group is aware of the importance of protecting information and has implemented an information risk management program as well as a training and awareness program to protect privacy and ensure the safety of its members' and clients' property.

TECHNOLOGY RISK MANAGEMENT

Desjardins Group has updated its technology risk management by implementing a specific framework for all technology services provided by Desjardins Technology Group Inc. This framework defines the concept of technology risks for Desjardins Group, the scope of application of the technology risk management approach, the governance structure and related management activities.

OUTSOURCING RISK MANAGEMENT

A program has been put in place to manage Desjardins Group's outsourcing activities. All material outsourcing agreements are monitored in order to ensure they are properly managed.

INSURANCE RISK

Insurance risk arises from the uncertainty 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.

The risk associated with designing and pricing products is the risk that the initial pricing is or will become insufficient. The risk of incorrectly estimating actuarial reserves is due to the possibility of selecting an inadequate model for estimating the loss ratio or calculating the reserves. Loss ratio means the estimated amount of benefits that will be required to be paid, contractual clause management and risk selection.

INSURANCE RISK MANAGEMENT

Product design and pricing 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. Insurance components adopt strict pricing standards and policies and perform spot checks to compare forecasts with actual results. Some product pricing may be adjusted depending on the accuracy of forecasts.

Desjardins Group limits potential losses through reinsurance treaties. Such treaties do not, however, release the insurance components from their obligations toward clients in the event that reinsurers experience financial difficulties. Consequently, the components are also exposed to a credit risk related to the reinsurers. To minimize this risk, the components enter into reinsurance treaties with stable, financially solid and, in most cases, duly accredited companies.

The insurance subsidiaries comply with the standards for sound management practices established by the regulatory bodies that govern them and are subject to dynamic capital adequacy testing. Various pessimistic scenarios were tested during the year to measure their effect on the capitalization ratio; the capital proved adequate in each case.

STRATEGIC RISK

Strategic risk refers to a possible loss attributable to an inability to adapt to a changing environment because of a failure to act, an inappropriate choice of strategies 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 Desjardins Group's strategic directions according to the consultation processes specific to Desjardins. Events that could compromise the achievement of Desjardins Group's strategic objectives and initiatives are systematically and regularly monitored by Desjardins Group's officers and senior management.

REPUTATION RISK

Reputation risk is the risk of being perceived negatively by stakeholders, whether justifiably or not, because of practices, actions or lack of action, which could have an unfavourable impact on Desjardins Group's income and equity, and the trust of its stakeholders.

Reputation is of critical importance and cannot be managed separately from other risks. Consequently, managing reputation risk in all its spheres of activity is a constant concern for Desjardins Group.

Desjardins Group has defined guidelines, a management framework, and roles and responsibilities with regard to reputation risk. This framework is in addition to various processes already in place, such as the regulatory compliance function and ethical requirements, to encourage sound reputation risk management. All management personnel and employees are required to perform their duties in accordance with these principles and Desjardins Group's values.

OVERVIEW OF OTHER RISKS

ENVIRONMENTAL RISK

Environmental risk 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.

Environmental risk is an integral part of Desjardins Group's Integrated Risk Management Framework. Desjardins Group has been a pioneer in responsible investing for more than a decade, offering investment products that support businesses with clearly defined social responsibility and environmental values. Desjardins Group also supports climate change action by promoting businesses that are making positive contributions to combat climate change.

LEGAL AND REGULATORY ENVIRONMENT RISK

Legal and regulatory environment risk represents the consequences of not complying with the laws, regulations, standards and practices governing our operations.

The financial services industry is one of the most strictly regulated sectors. In recent years, the regulations governing the financial sector 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, market crises, financial fraud, and the fight against money laundering and terrorist financing, 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 in Quebec, Canadian securities authorities, the OSFI, the Mutual Fund Dealers Association of Canada, and the Investment Industry Regulatory Organization of Canada. Complying with major legislative and regulatory changes such as the *Foreign Account Tax Compliance Act* (FATCA), the *Dodd-Frank Act* and the Basel accords requires Desjardins Group to make significant investments of financial and human resources.

Legal and regulatory environment risk entails effectively preventing and handling possible legal disputes and claims which may lead to judgments or decisions by a court of law or regulatory agency that could result in financial penalties. They may also end in unfavourable judgments, decisions or settlements that could negatively affect how Desjardins Group conducts its operations and lead to further costs associated with legal proceedings that could have an adverse impact on Desjardins Group's financial position and corporate image.

Desjardins Group manages the risk related to the legal and regulatory environment by promoting a strong culture of compliance and by setting up a compliance management framework in order to identify risks of non-compliance, to assess the potential consequences of such risks and to implement practices to manage them effectively. In addition, a Chief Compliance Officer supervises all Desjardins Group teams that conduct compliance activities. This compliance management structure provides reasonable assurance that Desjardins Group's operations comply with applicable regulations.

The compliance function is responsible for developing, updating and maintaining the compliance management framework. It is based on a number of principles, including the identification and monitoring of regulatory obligations and the functional units subject to them. To do so, regulatory developments and their impact on operations are monitored on an ongoing basis. The compliance function provides support in an advisory capacity to managers in charge of the business sectors so that they can effectively manage their risks while conducting periodic inspections of operations supported by training programs. Lastly, a formal reporting process is in place for Desjardins Group's senior management and decision-making bodies.

SECTION 4.2

RISK FACTORS THAT COULD IMPACT FUTURE RESULTS

As indicated in the warning about forward-looking statements, general and 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.

GENERAL ECONOMIC AND BUSINESS CONDITIONS IN REGIONS IN WHICH DESJARDINS GROUP OPERATES

The general economic and business conditions in the regions in which Desjardins Group operates may significantly affect its revenues. These conditions include short- and long-term interest rates, inflation, debt securities market fluctuations, foreign exchange rates, the volatility of capital markets, including tighter liquidity conditions in certain markets, the strength of the economy, and the volume of business conducted by Desjardins Group in a given region.

FOREIGN EXCHANGE RATES

Exchange rate fluctuations in the Canadian dollar, the U.S. dollar and other foreign currencies may affect Desjardins Group's financial situation and its future surplus earnings. Fluctuations in the Canadian dollar may also adversely impact the earnings of Desjardins Group's business clients in Canada.

MONETARY POLICIES

The monetary policies of the Bank of Canada and the Federal Reserve Board in the United States, as well as other interventions in financial markets, have an impact on Desjardins Group's income. The general level of interest rates may affect Desjardins Group's profitability. Fluctuations in interest rates affect the spread between interest paid on deposits and interest earned on loans, which could change Desjardins Group's net interest income. Desjardins Group has no control over changes in monetary policies or financial market conditions, and it therefore cannot forecast or anticipate them with any consistency.

COMPETITION

The level of competition in markets in which Desjardins Group operates affects its performance. Client retention depends on many factors, such as product and service pricing, changes to the products and services offered, and customer service delivery.

CHANGES IN STANDARDS, LAWS AND REGULATIONS

Changes made to standards, laws and regulations, including changes affecting their interpretation or implementation, could have an impact on Desjardins Group by restricting its product or service offer or by enhancing the ability of competitors to compete with its products or services. In addition, shoud Desjardins Group fail to comply with any applicable laws, regulations or other guiding principles, even though it takes care to avoid such a possibility, it could be subject to penalties and fines that may have an unfavourable impact on its reputation and financial results.

ACCURACY AND COMPLETENESS OF INFORMATION CONCERNING CLIENTS AND COUNTERPARTIES

Desjardins Group relies on the accuracy and completeness of the information it collects on its clients and counterparties. When deciding to authorize credit or other transactions with clients or counterparties, Desjardins Group may use information provided by the clients or counterparties themselves, 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 financial statements. The financial position and income of Desjardins Group could be adversely affected if it relies on financial statements that are not compliant with accounting standards, are misleading or do not accurately present, in all material respects, the financial position or operating results of its clients and counterparties.

ACCOUNTING POLICIES USED BY DESJARDINS GROUP

The accounting policies that Desjardins Group uses determine how it reports its financial position and operating results, and they may require management to make estimates or rely on assumptions about matters that are inherently uncertain. Any change to these estimates and assumptions may have a significant impact on Desjardins Group's operating results and financial position.

NEW PRODUCTS AND SERVICES TO MAINTAIN OR INCREASE DESJARDINS GROUP'S MARKET SHARE

The ability of Desjardins Group to maintain or increase its market share depends partly on its skill in adapting its products and services to changing standards in the financial services industry. Financial services companies are subject to increasing pressure regarding the pricing of their products and services. This factor may reduce net interest income or revenues from fee-based products and services. Moreover, the adoption of new technologies could require Desjardins Group to modify or adapt its products and services, resulting in major expenses.

ABILITY TO RECRUIT AND RETAIN KEY MANAGEMENT PERSONNEL, INCLUDING SENIOR MANAGEMENT

Desjardins Group's future performance depends partly on its ability to recruit and retain key management personnel, including senior management. In addition, there is intense competition to retain the best people in the financial services industry. Desjardins Group cannot, however, be sure that it will be able to continue to recruit and retain key management personnel, including senior management, although this is one of the objectives of its resources management policies and practices.

BUSINESS INFRASTRUCTURE

Third parties provide some of the essential components of Desjardins Group's business infrastructure, such as Internet connections and network access. Interruptions in network access or other communication services provided by such third parties could adversely affect the ability of Desjardins Group to offer products and services to customers and otherwise conduct its business.

GEOGRAPHIC CONCENTRATION

As at December 31, 2012, Desjardins Group's lending in Quebec accounted for 93.1% of its aggregate loan portfolio. Moreover, its operations are heavily concentrated in Quebec. 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 the collateral available for loans, especially mortgages, and by extension clients' borrowing capacity, the value of assets associated with impaired loans, and collateral coverage

ACQUISITIONS AND PARTNERSHIPS

Desjardins Group has implemented a rigorous internal control environment for the acquisition and partnership process. Nevertheless, its financial or strategic objectives could fail to be met because of unexpected factors such as delays in approval of transactions by regulators and shareholders, the inability to apply the strategic plan in its original form, difficulties in integrating or retaining key employees or clients, 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, thereby impacting Desjardins Group's future surplus earnings.

CREDIT RATINGS

The credit ratings assigned to Desjardins Group by rating agencies are instrumental in its access to sources of wholesale financing and the cost of such financing. There is no guarantee that the credit ratings and outlooks assigned by the agencies to Desjardins Group's various securities will be maintained. Furthermore, a downgrade to any of Desjardins Group's ratings could raise its cost of financing and limit its access to capital markets.

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 savings habits, technological developments, the ability to implement Desjardins Group's disaster recovery plan within a reasonable time, the potential impact of international conflicts or natural disasters on Desjardins Group's business, and Desjardins Group's ability to anticipate and manage the risks associated with these factors properly despite a disciplined risk 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 items specific to Desjardins Group which could adversely impact its future results.

SECTION 4.3

ADDITIONAL INFORMATION RELATED TO EXPOSURE TO CERTAIN RISKS

The tables below provide further details about more complex financial instruments with a higher degree of risk.

TABLE 35 – ASSET-BACKED SECURITIES

As at December 31
(in millions of dollars)

	2012		2011	
	Notional amounts	Fair value	Notional amounts	Fair value
Commercial mortgage-backed securities(1)	$ 236	$ 249	$ 249	$ 260
Financial asset-backed securities(2)	94	91	71	59

(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 are 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 "Available-for-sale securities".

TABLE 36 – DERIVATIVE FINANCIAL INSTRUMENTS

As at December 31
(in millions of dollars)

	2012			2011		
	Notional amounts	Positive value	Negative value	Notional amounts	Positive value	Negative value
Credit default swaps(1)	$ 559	$ 1	$ —	$ 601	$ —	$ 8
Total return swaps(2)	7	—	—	8	—	—

(1) Desjardins Group's commitment and the nature of the underlying assets are provided in the "Credit default swaps" section of Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements. 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 37 – LEVERAGED FINANCE LOANS AND SUBPRIME LOANS

As at December 31
(in millions of dollars)

	2012	2011
Leveraged finance loans(1)	$ 165	$ 90
Alt-A mortgage loans(2)	36	43
Subprime residential mortgage loans(3)	2	1

(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. Only one of these loans is currently in default. Subprime residential mortgages are recorded on the Combined Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

5.0 ADDITIONAL INFORMATION

SECTION 5.1

CONTROLS AND PROCEDURES

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

During 2012, Desjardins Group carried out work so that it could provide certification as at December 31, 2012, of the design and effectiveness of its disclosure controls and procedures, as well as of the design and effectiveness of its internal control over financial reporting.

DISCLOSURE CONTROLS AND PROCEDURES

In accordance with the CSA guidance in Regulation 52-109, the Chair of the Board, President and CEO as well as the Senior Vice-President of Finance and Chief Financial Officer of Desjardins Group designed, or caused to be designed, disclosure controls and procedures, which are supported in particular by a process for regular 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 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, 2012, in accordance with the recognized control framework of the Committee of Sponsoring Organizations (COSO) of the Treadway Commission, Desjardins Group management assessed the design and effectiveness of its disclosure controls and procedures.

The design and effectiveness of disclosure controls and procedures were therefore assessed by Desjardins Group management, under the supervision of the Chair of the Board, President and CEO, and the Senior Vice-President of Finance and Chief Financial Officer of Desjardins Group. Based on the results of this assessment, they concluded that the disclosure controls and procedures are adequately designed and effective, and do not contain any material weakness, thereby ensuring that the information required to be disclosed in reports filed or submitted under Canadian securities legislation is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms and thereby providing investors with complete and reliable information.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Desjardins Group management caused an adequate internal control over the financial reporting process to be designed and has maintained it. Such internal control 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.

As in the case of the assessment of disclosure controls and procedures, the design and effectiveness of internal control over financial reporting were also assessed in accordance with the COSO control framework.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements, whether due to error or fraud. Moreover, 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.

An assessment of the design and effectiveness of internal control over financial reporting was therefore carried out by Desjardins Group management under the supervision of the Chair of the Board, President and CEO, and the Senior Vice-President of Finance and Chief Financial Officer of Desjardins Group. Based on the results of this assessment, they have concluded that, as at December 31, 2012, internal control over financing reporting is adequately designed and effective, and does not contain any material weakness.

Moreover, as at December 31, 2012, there were three Desjardins Group components, namely *Caisse centrale Desjardins, Capital Desjardins inc.* and, since May 1, 2012, the *Fédération des caisses Desjardins du Québec* (as a venture issuer), that complied with the requirements under Regulation 52-109. Note that the subsidiary Western Financial Group Inc. was a non-venture reporting issuer as at December 31, 2012, but that since February 13, 2013, it no longer has this status as a result of Desjardins Group's redemption of its securities on the market. Consequently, Western Financial Group Inc. is no longer subject to the requirements of Regulation 52-109.

Under the supervision of the certifying officers, the respective management of *Caisse centrale Desjardins* and *Capital Desjardins inc.* therefore assessed the design and effectiveness of disclosure controls and procedures and of internal control over financial reporting. These assessments 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, 2012, 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 governance are examined in more detail on pages 183 to 202 of the *2012 Desjardins Group Annual Report*.

SECTION 5.2

RELATED PARTY DISCLOSURES

In the normal course of business, Desjardins Group offers financial services and enters into agreements for operating services with related parties. 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 management personnel and its employees as well as to persons related to them.

Desjardins Group has set up a process to obtain assurance that all transactions with its management personnel and the persons who are related to them have been carried out as arm's-length transactions and in compliance with the legislative framework for its various components.

Such related party transactions are explained in Note 33, "Related party disclosures", to Desjardins Group's annual Combined Financial Statements, on page 181 of the *2012 Desjardins Group Annual Report*.

SECTION 5.3

MATERIAL EVENTS

CHAIR OF THE BOARD, PRESIDENT AND CEO OF DESJARDINS GROUP

On January 31, 2012, Desjardins Group announced that Monique F. Leroux had been re-elected as Chair of the Board, President and CEO of Desjardins Group for a second mandate of four years.

TMX GROUP INC.

On July 31, 2012, TMX Group Limited (formerly Maple Group Acquisition Corporation), a corporation in which Desjardins Group has a stake as an investor along with 12 other Canadian financial institutions and pension funds, announced that the offer to purchase all the shares of TMX Group Limited had been successful. Under the transaction, Desjardins Group invested $98 million in equity in TMX Group Limited. This investment is presented under "Securities – Available-for-sale securities" on the Combined Balance Sheets.

On September 14, 2012, as part of an arrangement, TMX Group Limited acquired all outstanding TMX Group Inc. shares in exchange for common shares of TMX Group Limited, on a one-for-one basis. The Toronto Stock Exchange approved the listing of TMX Group Limited shares.

ACQUISITIONS

Through Western Financial Group Inc., the Federation acquired Roblin Insurance Travel and Realty Agencies Ltd., based in Manitoba, on January 3, 2012; Brown & Ward Insurance Ltd., a leading property and casualty insurance broker in Alberta, on February 1, 2012; and Hodges & Company Insurance Services Ltd., a network of experienced brokers specialized in commercial insurance, on May 17, 2012. Hodges & Company is based in Victoria, and its acquisition was Western Financial Group Inc.'s first foray into British Columbia. In 2012, Western Financial Group Inc. also acquired BC Yacht Insurance Brokers Inc., based in Sidney, British Columbia, on July 1, 2012, and Orion Insurance Brokers Ltd., whose offices are in Winnipeg, Manitoba, on September 1, 2012.

SUBSEQUENT EVENT – QTRADE CANADA INC.

On February 4, 2013, Desjardins Group entered into a final agreement, through Desjardins Financial Corporation Inc., a wholly owned subsidiary of the Federation, to purchase between 25% and 40% of the outstanding shares of Qtrade Canada Inc. (Qtrade), a company specializing in online brokerage and wealth management services, primarily for credit unions.

This transaction qualifies as a business combination since Desjardins Group will obtain control over Qtrade's operations, and it will be accounted for using the acquisition method. The allocation of the purchase price to the assets acquired and liabilities assumed will be completed on the transaction's closing date, which is scheduled for the second quarter of 2013. Qtrade's results will be included in the Combined Financial Statements of Desjardins Group from the transaction's closing date.

SECTION 5.4

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, 2012. The significant accounting policies are described in Note 2, "Significant accounting policies", to the Combined Financial Statements. Some of these policies are particular important in presenting Desjardins Group's financial position and operating results since they require management to make assumptions and estimates that may involve uncertainties, and, since any change to these assumptions and estimates could have a significant impact on the Combined Financial Statements of Desjardins Group. The following paragraphs summarize these accounting policies.

SPECIAL PURPOSE ENTITIES

Desjardins Group includes in its Combined Financial Statements the operations of the distinct legal structures specifically created to manage a transaction or a group of similar transactions (special purpose entities), even if it has no equity interest in these entities, provided that it exercises control in substance based on the following criteria:

- The activities of the entity are being conducted exclusively on behalf of Desjardins Group, such that Desjardins Group benefits from the entity's operations.
- Desjardins Group has the decision-making and management powers needed to obtain the majority of the benefits from the ongoing activities of the entity. These powers are characterized by the ability to dissolve the entity, to modify its statutes or to veto any modification thereto formally.
- Desjardins Group has the ability to obtain the majority of the benefits of the entity and therefore may be exposed to risks incident to the entity's activities. These benefits may take the form of the right to receive some or all of the entity's profit or loss, measured on an annual basis, or a share of its net assets, or the right to sell one or more assets or to receive the majority of the residual assets in the event of liquidation.
- Desjardins Group retains the majority of the risks taken by the entity in order to obtain benefits from its activities; this would be the case if Desjardins Group remained exposed to the initial losses on the asset portfolio held by the entity.

FAIR VALUE MEASUREMENT OF FINANCIAL INSTRUMENTS

There is little subjectivity in the determination of the fair value of financial instruments, especially securities, obtained from quoted prices on active markets.

If there are no quoted prices on active markets, the fair value is determined using either models based on observable market data or models that are not based on observable market data. When no quoted prices are available, the fair value is estimated using present value or other valuation methods, which are influenced by the assumptions used concerning the amount and timing of estimated future cash flows and discount rates, which reflect varying degrees of risk, including liquidity risk, credit risk, and risks related to interest rates, exchange rates and price and rate volatility. 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 for this reason cannot be representative of future fair values. It also cannot be considered as being realizable in the event of immediate settlement of these instruments.

LOANS

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 results in a favourable or unfavourable difference compared to their carrying amount. The fair value of loans is estimated by discounting expected cash flows using market interest rates charged for similar new loans at the reporting date. The fair value of impaired loans is assumed to be equal to their carrying amount.

DEPOSITS

The fair value of deposits with floating-rate features or with no stated maturity is assumed to be equal to their carrying amount. 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.

SUBORDINATED BONDS

The fair value of subordinated bonds is based on the market rates for similar issues or debt securities, or on the rates currently offered to Desjardins Group for debt securities with the same remaining term.

DERIVATIVE FINANCIAL INSTRUMENTS

The fair value of derivative financial instruments is determined using pricing models that incorporate the current market prices and the contractual prices of the underlying instruments, the time value of money, yield 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.

FINANCIAL INSTRUMENTS WHOSE FAIR VALUE EQUALS THEIR CARRYING AMOUNT

The carrying amount of certain financial instruments that mature within 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", "Clients' liability under acceptances", "Amounts receivable from clients, brokers and financial institutions", "Other assets – Other", "Acceptances", "Amounts payable to clients, brokers and financial institutions" and "Other liabilities – Other".

The fair value of financial instruments is presented in Note 5, "Fair value of financial instruments", to the Combined Financial Statements.

DERECOGNITION OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

A financial asset is derecognized when the contractual rights to the cash flows from the asset expire or when the contractual rights to the cash flows from the financial asset and substantially all risks and rewards of ownership of the asset are transferred to a third party.

When the cash flows from a financial asset have been transferred but Desjardins Group has retained substantially all the risks and rewards of ownership of the financial asset, it recognizes a separate asset and a separate liability presented in the Combined Balance Sheets, which represent 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.

A financial liability is derecognized when the related obligation is discharged, cancelled, or expires.

IMPAIRMENT OF FINANCIAL ASSETS

ALLOWANCE FOR CREDIT LOSSES

Measuring the allowance for credit losses is very important for Desjardins Group given the size of its loan portfolio. Certain factors may influence management's judgment, and any material change to estimates or parameters could result in a change in the currently recognized amount for the allowance for credit losses. The allowance for credit losses reflects management's best estimate of potential credit losses.

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 either the fair value of any security underlying the loan, net of expected costs of realization, or the observable market price for the loan. The security may vary depending on the type of loan.

The allowance resulting from this impairment is established using two components: individual allowances and collective allowance.

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 an individual allowance has not been established are then included in groups of assets having similar credit risk characteristics and are subject to a collective allowance.

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 also depends on management's interpretation of current credit quality trends with respect to business segments, the impact of changes to its credit policies and economic conditions.

Additional information about accounting for 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 monitored on a regular basis to determine whether there is any objective evidence that they are impaired. In measuring the decline in value, Desjardins Group takes into account many facts specific to each investment and all the factors that could indicate that there has been impairment. 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 its judgment to determine when to recognize an impairment loss.

Debt securities classified in the "Available for sale" category are individually assessed by Desjardins Group 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 the fair value below cost.

Additional information about the recognition of available-for-sale securities and fair value measurement is presented in Note 4, "Carrying amount of financial instruments", Note 5, "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 an indication 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 is the higher of its fair value less costs to sell and its value in use, which corresponds to the present value of the recoverable future cash flows. Any impairment loss recognized in the Combined Statements of Income represents the excess of the carrying amount of the asset over the recoverable amount. Impairment losses on that asset may be subsequently reversed and are recognized in the Combined Statements of Income in the year in which they occur.

Estimating the recoverable amount of a non-financial asset to determine if 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.

GOODWILL

Goodwill is tested for impairment once a year and when events or changes in circumstances indicate that the carrying amount may not be recoverable.

The goodwill impairment test is performed based on the recoverable amount of each cash-generating unit (CGU) (or each group of CGUs) to which goodwill is allocated.

The recoverable amount represents the higher of the fair value less costs to sell and the value in use. Fair value represents the best estimate of the amount obtainable from the sale, less costs to sell, 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 estimated future cash flows.

When the recoverable amount is less than the carrying amount, an impairment loss is recognized in the Combined Statement of Income for the year and is first recorded 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. Nevertheless, the allocation of the impairment loss to the assets of the CGU (or group of CGUs) must not result in their carrying amount being lower than the highest of the following amounts: the fair value of the assets less costs to sell, their value in use, and zero. Goodwill impairment losses cannot be reversed.

INSURANCE CONTRACT LIABILITIES

LIFE AND HEALTH INSURANCE CONTRACT LIABILITIES

The calculation of the insurance contract liabilities of the life and health insurance subsidiaries requires that assumptions be made with respect to the timing of many factors such as death, disability, investment income, inflation, policy cancellations, expenses, income taxes, premiums, commissions and participating policyholders' dividends as well as the amounts they represent. To predict underwriting experience, the life and health subsidiaries use best estimate assumptions. Some of these assumptions refer to events that are likely to occur in the distant future and they may need to be changed.

PROPERTY AND CASUALTY INSURANCE CONTRACT LIABILITIES

The calculation of the provisions for claims and adjustment expenses related to the property and casualty insurance subsidiaries' insurance policies takes into consideration assumptions based on characteristics of the business lines, settlement history and other relevant factors. The estimating methods used to make this calculation are based on best estimate assumptions, taking into account currently known data, which are regularly reviewed and updated.

The provisions for claims and adjustment expenses include individual loss estimates for each claim reported. In addition, a provision is established for adjustment expenses, changes in reported claims and incurred but not reported claims, based on previous experience and portfolio contracts. These estimates are regularly reviewed and updated, and any resulting adjustment is recognized in the Combined Statement 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 underlying asset rate, with a margin for adverse deviation.

Note 14, "Insurance and investment contract liabilities", to the Combined Financial Statements provides information about accounting for the various insurance contract liabilities, the main assumptions used and the impact on results 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.

Charges to and reversals of provisions are recognized in profit or loss under the items corresponding to the nature of the future expenditures covered.

CONTINGENT LIABILITIES

In the normal course of its business operations, Desjardins Group is involved in various litigation matters and lawsuits relating to its various products, services, investments and other activities.

It is not currently possible to determine the outcome of some of such litigation matters and lawsuits, the timing of such outcome as well as the possible impact on Desjardins Group's financial position. In management's opinion, the fair value of the contingent liabilities resulting from such litigation matters and lawsuits, to the extent that it can be measured, could have an impact on Desjardins Group's profit or loss for a specific period, but would not have a significant adverse impact on Desjardins Group's combined financial position.

Additional information about contingent liabilities is presented in Note 27, "Commitments, guarantees and contingent liabilities", to the Combined Financial Statements.

DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

Derivative financial instruments are financial contracts whose value depends on assets, interest rates, foreign exchange rates and other financial indexes. The vast majority of derivative financial instruments are negotiated by mutual agreement between Desjardins Group and the 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 transactions are carried out as part of regulated trades and mainly consist of futures.

Derivative financial instruments, including embedded derivatives which are required to be recognized separately, are recognized on the Combined Balance Sheets at fair value.

Desjardins Group uses derivative financial instruments for trading purposes or for asset/liability management purposes. Derivative financial instruments held for trading purposes are used to meet the needs of members and clients, and to allow Desjardins Group to generate income on its own trading activities. Derivative financial instruments held for asset/liability management purposes are used to manage current and expected risks related to market risk. These instruments enable Desjardins Group to transfer, manage or reduce the interest rate and foreign currency exposures of assets and liabilities recorded in the Combined Balance Sheets, as well as firm commitments and forecasted transactions.

When derivative financial instruments are used to manage assets and liabilities, Desjardins Group must determine, for each derivative, whether or not hedge accounting is appropriate. To qualify for hedge accounting, a hedging relationship must be designated and documented at its inception. Such documentation must address the specific strategy for managing risk, the asset, liability or cash flows that are being hedged as well as the measure of hedge effectiveness. Consequently, the effectiveness of each hedging relationship must be assessed, regularly and on an individual basis, to determine with reasonable assurance whether the relationship is effective and will continue to be effective. The derivative financial instrument must prove highly effective to offset changes in the fair value or the cash flows of the hedged item attributable to the risk being hedged.

Additional information about derivative financial instruments and hedging activities is presented in Note 17, "Derivative financial instruments and hedging activities", to the Combined Financial Statements.

INCOME TAXES ON SURPLUS EARNINGS

The income tax expense on surplus earnings comprises the current tax expense and the deferred tax expense. Income taxes on surplus earnings are recognized in the Combined Statements of Income unless they relate to items that were recognized outside profit or loss directly in the Combined Statements of Comprehensive Income or the Combined Statements of Changes in Equity. In such case, income taxes on surplus earnings are also not recognized outside profit or loss.

The calculation of income taxes on surplus earnings is based on the expected tax treatment of transactions. To determine the current and deferred portions of income taxes on surplus earnings, assumptions must be made concerning the dates on which deferred income tax assets and liabilities will be reversed. If Desjardins Group's interpretation differs from that of taxation authorities or if the reversal dates do not correspond with the forecasted dates, the provision for income taxes on surplus earnings may increase or decrease in subsequent years.

Note 25, "Income taxes on surplus earnings", to the Combined Financial Statements provides additional information on income taxes on surplus earnings.

PROVISION FOR MEMBER DIVIDENDS

The board of directors of each caisse recommends for approval the surplus earnings distribution plan at the annual general meeting of member, which is held in the four months following year-end. The amount of member dividends to be paid is part of this plan. The amount of the provision is 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 with the Desjardins Group Capitalization Plan, which sets capitalization targets. The difference between the amount of member dividends actually paid, in cash or in shares, following the 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 surplus earnings distribution plan takes into account a program under which members may elect to receive their dividends in the form of shares, in which case the value is greater than the equivalent dividends paid in cash. The caisses can pay out member dividends when legal and regulatory requirements have been met.

EMPLOYEE BENEFITS

Desjardins Group offers a majority of its employees pension plans and supplemental pension plans, which provide pension benefits in excess of statutory limits. 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. Benefits are calculated on the basis of the number of years of membership in the pension plans and take into consideration the average salary of the employee's five most highly paid years. Since the terms of the 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 fair value of the defined benefit plan obligation are generally actuarially determined using the projected unit credit method. These calculations are made based on management's best estimate assumptions primarily concerning the expected rate of return on the plans' investments and the plan obligation discount rate, and also, but to a lesser extent, salary increases, the retirement age of employees, the mortality rate and the rate of increase in pension benefits. A complete actuarial valuation is performed each year by a qualified actuary.

Actuarial gains (losses) result from the difference between the actual return on pension plan assets and the expected return for funded plans, the changes made to the actuarial assumptions used to determine the defined benefit plan obligation and the experience gains or losses on this obligation. Any net actuarial gain or loss exceeding 10% of the greater of the value of the defined benefit plan obligation and the fair value of plan assets at the end of the previous year is amortized over the expected average remaining working lives of the plan members.

Defined benefit plan assets or liabilities correspond to the present value of the obligation of these plans less the unrecognized past service cost, the fair value of pension plan assets and unamortized actuarial losses, plus unamortized actuarial gains. The value of any asset is limited to the total of actuarial losses, the unrecognized past service costs and the present value of any economic benefits available in the form of refunds from the plans or reductions in future contributions to the pension plans.

Note 26, "Defined benefit plans", to the Combined Financial Statements provides further information on the recognition of defined benefit plans and on the sensitivity of the key assumptions.

SECTION 5.5

FUTURE ACCOUNTING CHANGES

Accounting standards that have been issued but are not yet effective are listed below. Regulatory authorities have also stated that early adoption of these standards will not be permitted.

DATE OF APPLICATION: JANUARY 1, 2013

IFRS 10, "CONSOLIDATED FINANCIAL STATEMENTS"

In May 2011, the IASB issued IFRS 10, "Consolidated Financial Statements", which defines the principle of control and establishes that control serves as the basis to determine which entities are included in the scope of consolidation. This new standard supersedes the requirements on consolidated financial statements included in IAS 27, "Consolidated and Separate Financial Statements", and SIC 12, "Consolidation – Special Purpose Entities".

Desjardins Group is currently assessing the impact of the adoption of this new standard, which must be applied retrospectively.

IFRS 11, "JOINT ARRANGEMENTS"

In May 2011, the IASB issued IFRS 11, "Joint Arrangements", which supersedes IAS 31, "Interests in Joint Ventures", and SIC 13, "Jointly Controlled Entities – Non-Monetary Contributions by Venturers". This standard establishes principles for accounting for two types of joint arrangements, namely joint operations and joint ventures, and eliminates the possibility of recognizing joint ventures using the proportionate consolidation method.

The adoption of this new standard will have no impact on Desjardins Group since interests in joint ventures are already recognized using the equity method. This new standard must be applied retrospectively.

IFRS 12, "DISCLOSURE OF INTERESTS IN OTHER ENTITIES"

In May 2011, the IASB issued IFRS 12, "Disclosure of Interests in Other Entities", which expands disclosure requirements for interests held by an entity in subsidiaries, joint arrangements, associates, and unconsolidated structured entities. Some of the disclosures were already required by the current standards, while others are new, such as disclosures about significant judgments and assumptions the entity has made in determining the nature of its interests in another entity as well as the nature and extent of, and risks associated with, its interests in other entities.

IFRS 12 is a new presentation standard that will have no impact on Desjardins Group's results or financial position. It must be applied retrospectively.

IFRS 13, "FAIR VALUE MEASUREMENT"

In May 2011, the IASB issued IFRS 13, "Fair Value Measurement", which defines fair value and sets out a single framework for measuring the fair value of all transactions and balances for which IFRS require or permit fair value measurement. This standard aims at improving the consistency between the various fair value concepts defined in various existing standards. In addition, IFRS 13 carries forward disclosure requirements concerning the fair value of financial instruments and expands the scope to all items measured at fair value.

With respect to fair value measurements, Desjardins Group does not expect the adoption of this new standard, which is applicable prospectively, to have a significant impact.

IAS 1, "PRESENTATION OF FINANCIAL STATEMENTS"

In June 2011, the IASB issued amendments to IAS 1, "Presentation of Financial Statements", which improve the presentation of items of other comprehensive income. The amendments require the presentation by nature of items of other comprehensive income by distinguishing those that will be reclassified to the statement of income in a subsequent period from those that will not.

IAS 1 is a presentation standard whose objective is to provide information to enable users to better understand financial statements, among other things. The amendments to this standard will have no impact on Desjardins Group's results or financial position. They must be applied retrospectively.

IAS 19, "EMPLOYEE BENEFITS"

In June 2011, the IASB issued an amended version of IAS 19, "Employee Benefits" (IAS 19(R)), which requires that the funding status of a defined benefit plan be entirely reflected in the Combined Balance Sheets. This change therefore eliminates the option to defer the recognition of actuarial gains and losses, known as the "corridor approach". All actuarial gains and losses will now be recognized immediately in other comprehensive income. The calculation of the interest cost recognized in the Combined Statements of Income is also amended. This interest cost will now be calculated by multiplying the net defined benefit plan asset or liability by the rate used to discount the obligation, and the difference between the actual return on plan assets and the amount recognized as interest cost will be recognized in other comprehensive income. In addition, all past service costs will now be directly recognized in profit or loss when they occur.

Furthermore, the risk-sharing features between employers and employees for defined benefit plans will now be taken into account when determining the liability to be recognized in the Combined Balance Sheets and the expense to be recognized in the Combined Statements of Income. The presentation and recognition of changes in the defined benefit plan obligation and plan assets will therefore be modified, and disclosures about the characteristics of defined benefit plans and the risks to which an entity is exposed through its participation in such plans will be enhanced. Desjardins Group will have to apply this new standard retrospectively.

Accordingly, the main impact of Desjardins Group adopting IAS 19(R) will be the recognition of unamortized actuarial losses and unrecognized past service cost under "Defined benefit plan liabilities" in the Combined Balance Sheets. This will result in a decrease in "Undistributed surplus earnings" (for more information, refer to Note 26, "Defined benefits plans", to the Combined Financial Statements).

In addition, taking into account the risk-sharing features between employers and employees for the main group pension plan will result in a decrease in "Defined benefit plan liabilities" and a corresponding increase in "Undistributed surplus earnings". Desjardins Group is currently assessing the impact of the changes related to risk sharing. The initial impact of these amendments on capital ratios could be deferred and amortized on a straight-line basis over the period from January 1, 2013, to December 31, 2014, depending on whether Desjardins Group elects to use the transitional provision stipulated for that purpose by the regulatory authorities.

IFRS 7, "FINANCIAL INSTRUMENTS: DISCLOSURES" – OFFSETTING FINANCIAL ASSETS AND FINANCIAL LIABILITIES

In December 2011, the IASB issued amendments to IFRS 7, "Financial Instruments: Disclosures". These amendments improve the disclosure requirements with respect to offsetting of financial assets and liabilities. The objective of these amendments is to help users of financial statements better evaluate the impact of netting agreements on the financial position of an entity and understand how an entity manages the credit risk associated with such agreements.

IFRS 7 is a presentation standard whose objective is to provide disclosures to enable the users, among other things, to better understand and evaluate the significance of financial instruments for the entity's financial position and performance. Since the amendments to this standard specifically concern disclosures, they have no impact on Desjardins Group's results or financial position. They must be applied retrospectively.

ANNUAL IMPROVEMENTS

In May 2012, the IASB issued amendments to several standards as part of its annual improvement process. Except for the amendment to IAS 32, "Financial Instruments: Presentation", these amendments are minor and will have no impact on Desjardins Group's results or financial position.

The amendment to IAS 32 specifies that the income tax consequences of dividends and remuneration on capital stock should now be recognized in accordance with IAS 12, "Income Taxes". Therefore, when certain conditions are met, the income tax consequences of dividends and remuneration on capital stock will have to be presented in profit or loss rather than in equity. This amendment will be applied retrospectively.

Accordingly, there will be no impact on Desjardins Group's financial position as at January 1 and December 31, 2012. However, certain comparative figures will have to be reclassified from the Combined Statement of Changes in Equity to the Combined Statement of Income for the year ended December 31, 2012. "Income tax recovery on remuneration of permanent shares", in the Combined Statement of Changes in Equity, will decrease by $25 million, and "Income taxes on surplus earnings", in the Combined Statement of Income, will decrease by a corresponding amount.

DATE OF APPLICATION: JANUARY 1, 2014

IAS 32, "FINANCIAL INSTRUMENTS: PRESENTATION"

In December 2011, the IASB issued amendments to IAS 32, "Financial Instruments: Presentation", to clarify the criteria for offsetting a financial asset and a financial liability.

Desjardins Group is currently assessing the impact of the amendments made to this standard, which must be applied retrospectively.

DATE OF APPLICATION: JANUARY 1, 2015

IFRS 9, "FINANCIAL INSTRUMENTS"

The IASB issued in November 2009 and amended in October 2010 the first phase of a project that will replace IAS 39, "Financial Instruments: Recognition and Measurement". This standard defines a new way of classifying and measuring financial assets and liabilities. Financial assets will be classified in two categories (amortized cost and fair value through profit or loss) based on the entity's business model for managing its financial assets and the contractual cash flow characteristics of the financial assets. However, a new exposure draft issued in November 2012 proposes the introduction of a third financial instrument category for debt securities: fair value through other comprehensive income.

Financial liabilities will be classified in the same categories as those defined in IAS 39, but measurement of financial liabilities under the fair value option has been modified.

The impairment of financial asset methodology and hedging activities will be covered in future phases.

Desjardins Group is currently assessing the impact of the adoption of IFRS 9. The application of all phases of this standard is expected to be prospective.

SECTION 5.6

FIVE-YEAR STATISTICAL REVIEW

TABLE 38 – COMBINED BALANCE SHEETS

For the years ended December 31
(in millions of dollars)

	2012	2011	2010	2009(1)	2008(1)
ASSETS					
Cash and deposits with financial institutions	$ 1,669	$ 1,356	$ 1,621	$ 1,086	$ 1,489
Securities					
Securities at fair value through profit or loss	21,986	22,479	21,490	19,349	17,746
Available-for-sale securities	18,326	18,726	15,930	12,064	11,338
Securities held to maturity	—	—	—	18	19
	40,312	41,205	37,420	31,431	29,103
Securities borrowed or purchased under reverse repurchase agreements	4,377	4,959	7,034	5,055	6,130
Loans					
Residential mortgages	85,931	79,686	74,466	67,667	63,220
Consumer, credit card and other personal loans	18,520	17,985	17,504	16,915	15,982
Business and government	28,544	27,948	26,777	26,259	26,086
	132,995	125,619	118,747	110,841	105,288
Allowance for credit losses	(419)	(465)	(489)	(541)	(532)
	132,576	125,154	118,258	110,300	104,756
Segregated fund assets	6,132	5,427	4,774	—	—
Other assets					
Clients' liability under acceptances	841	676	672	751	428
Derivative financial instruments	2,238	3,059	2,006	2,647	4,588
Amounts receivable from clients, brokers and financial institutions	970	1,274	771	453	659
Investment property	512	597	616	—	—
Property, plant and equipment	1,312	1,218	1,187	1,008	1,025
Deferred tax assets	758	856	871	—	—
Other	5,009	4,356	3,701	4,711	4,354
	11,640	12,036	9,824	9,570	11,054
TOTAL ASSETS	$ 196,706	$ 190,137	$ 178,931	$ 157,442	$ 152,532
LIABILITIES AND EQUITY					
Liabilities					
Deposits					
Individuals	$ 84,415	$ 82,486	$ 78,747	$ 75,420	$ 71,958
Business and government	43,033	39,104	33,686	28,101	27,611
Deposit-taking institutions	2,176	1,813	2,230	2,640	1,867
	129,624	123,403	114,663	106,161	101,436
Other liabilities					
Acceptances	841	676	672	751	428
Commitments related to securities sold short	4,977	5,341	7,544	5,038	4,112
Commitments related to securities lent or sold under repurchase agreements	7,983	8,500	10,608	10,080	11,905
Derivative financial instruments	1,222	1,593	1,774	1,852	2,773
Amounts payable to clients, brokers and financial institutions	2,504	3,762	2,612	2,355	2,798
Insurance and investment liabilities	17,777	17,008	14,942	13,453	12,874
Segregated fund liabilities	6,141	5,427	4,774	—	—
Defined benefit plan liabilities	1,746	2,102	2,125	782	694
Deferred tax liabilities	342	431	258	—	—
Other	4,427	4,517	3,998	3,950	3,919
	47,960	49,357	49,307	38,261	39,503
Subordinated bonds	3,081	3,350	2,805	1,294	748
Total liabilities	180,665	176,110	166,775	145,716	141,687
Equity					
Capital stock	3,322	2,210	2,129	1,608	915
Share capital	80	78	70	71	69
Undistributed surplus earnings (deficit)	1,317	1,261	996	805	(96)
Accumulated other comprehensive income	694	1,044	617	489	685
Reserves	10,216	9,032	8,015	8,373	8,456
Equity – Group's share	15,629	13,625	11,827	11,346	10,029
Non-controlling interests	412	402	329	380	816
Total equity	16,041	14,027	12,156	11,726	10,845
TOTAL LIABILITIES AND EQUITY	$ 196,706	$ 190,137	$ 178,931	$ 157,442	$ 152,532

(1) In accordance with GAAP in effect prior to the adoption of IFRS.

TABLE 39 – COMBINED STATEMENTS OF INCOME

For the years ended December 31
(in millions of dollars)

	2012	2011	2010	2009(1)	2008(1)
Interest income					
Loans	$ 5,474	$ 5,462	$ 5,250	$ 5,068	$ 5,573
Securities	391	428	439	438	474
	5,865	5,890	5,689	5,506	6,047
Interest expense					
Deposits	1,851	1,818	1,692	1,920	2,590
Subordinated bonds and other	166	151	105	64	39
	2,017	1,969	1,797	1,984	2,629
Net interest income	3,848	3,921	3,892	3,522	3,418
Net premiums	5,126	4,851	4,360	4,247	4,131
Other operating income(2)					
Deposit and payment service charges	499	512	535	513	497
Lending fees and credit card service revenues	517	483	451	444	410
Brokerage, investment fund and trust services	700	676	656	581	617
Other	610	493	240	343	467
	2,326	2,164	1,882	1,881	1,991
Operating income(2)	11,300	10,936	10,134	9,650	9,540
Investment income(2)					
Net income (loss) on securities at fair value through profit or loss	674	1,706	984	666	(1,001)
Net income (loss) on available-for-sale securities	268	299	174	79	(405)
Net income from other investments	236	264	251	275	239
	1,178	2,269	1,409	1,020	(1,167)
Total income	12,478	13,205	11,543	10,670	8,373
Provision for credit losses	241	237	203	260	223
Claims, benefits, annuities and changes in insurance and investment contract liabilities	4,397	5,292	4,136	3,758	3,144
Non-interest expense					
Salaries and fringe benefits	2,882	2,782	2,601	2,423	2,250
Premises, equipment and furniture, including depreciation	415	428	425	415	393
Service agreements and outsourcing	228	270	363	371	322
Communications	271	247	258	237	252
Restructuring expenses	—	—	—	101	—
Other	1,964	1,896	1,733	1,602	1,588
	5,760	5,623	5,380	5,149	4,805
Operating surplus earnings	2,080	2,053	1,824	1,503	201
Income taxes on surplus earnings	489	471	438	412	113
Surplus earnings before member dividends	1,591	1,582	1,386	1,091	88
Provision for member dividends	279	320	299	311	215
Tax recovery on provision for member dividends	(73)	(90)	(81)	(98)	(62)
Net surplus earnings (deficit) for the year after member dividends	$ 1,385	$ 1,352	$ 1,168	$ 878	$ (65)
Of which:					
Group's share	$ 1,310	$ 1,314	$ 1,153	$ 861	$ (64)
Non-controlling interests' share	75	38	15	17	(1)

(1) In accordance with GAAP in effect prior to the adoption of IFRS.
(2) See "Basis of presentation of financial information" on page 15.

TABLE 40 – SELECTED FINANCIAL MEASURES

For the years ended December 31
(in millions of dollars and as a percentage)

	2012	2011	2010	2009(1)	2008(1)
Tier 1 capital ratio	16.8%	17.3%	17.7%	15.8%	13.6%
Total capital ratio	19.3	19.3	18.7	15.8	13.0
Return on equity	10.4	12.2	12.2	10.2	0.9
Productivity index	71.3	71.1	72.6	74.5	91.9
Gross impaired loans as a percentage of gross loans	0.35	0.41	0.43	0.46	0.40
Average assets	$ 195,384	$ 186,232	$ 174,132	$ 158,689	$ 149,722
Average net loans	128,683	121,279	114,323	107,229	99,764
Average deposits	127,409	119,424	111,020	104,584	99,288

(1) In accordance with GAAP in effect prior to the adoption of IFRS.