Fédération des caisses Desjardins du Québec Management's Discussion and Analysis

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SECTION 1.0 ***Fédération des caisses Desjardins du Québec***

This section gives a brief overview of the *Fédération des caisses Desjardins du Québec* and its 2017 financial highlights. It also includes material events, a description of the economic environment in 2017, and the economic and financial outlook for 2018.

SECTION 2.0 **Review of financial results**

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

SECTION 3.0 **Balance sheet review**

This section provides commentary on the *Fédération des caisses Desjardins du Québec*'s balance sheet. It mainly addresses financing activities and recruitment of savings, as well as capital management and off-balance sheet arrangements.

SECTION 4.0 **Risk management**

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

SECTION 5.0 **Additional information**

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

Note to the reader

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

The role of the Federation is presented in the section "Profile and structure".

The Management's Discussion and Analysis (MD&A) dated February 26, 2018, presents the analysis of the results of and main changes to the Federation's balance sheet for the year ended December 31, 2017, in comparison to previous fiscal years. The Federation reports financial information in compliance with *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings* prescribed by the Canadian Securities Administrators (CSA). Information on the Federation's controls and procedures is presented in the "Additional information" section of this MD&A.

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

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

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

The Federation's public communications often include oral or written forward-looking statements. Such forward-looking statements are contained in this MD&A and may be incorporated in other filings with Canadian regulators or in any other communications. Forward-looking statements include, but are not limited to, comments about the Federation's objectives regarding financial performance, priorities, operations, the review of economic conditions and markets, as well as the outlook for the Canadian, U.S., European and other international economies. These forward-looking statements include those appearing in sections 1.3 "Financial outlook for 2018," 1.4 "Changes in the economy," 2.0 "Review of financial results", 3.0 "Balance sheet review" and 5.0 "Additional information" of this MD&A. Such statements are typically identified by words or phrases such as "believe", "expect", "anticipate", "intend", "estimate", "plan" and "may", words and expressions of similar import, and future and conditional verbs.

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

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

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

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

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

The significant economic assumptions underlying the forward-looking statements in this MD&A are described in the section "Economic outlook for 2018" of this MD&A. These assumptions may also be updated in the quarterly MD&As. Any forward-looking statements contained in this MD&A represent the views of management only as at the date hereof, and are presented for the purpose of assisting readers in understanding and interpreting the Federation'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. The Federation does not undertake to update any oral or written forward-looking statements that could be made from time to time by or on behalf of the Federation, except as required under applicable securities legislation.

BASIS OF PRESENTATION OF FINANCIAL INFORMATION

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

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

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

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

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

Adjusted surplus earnings of the Federation before dividends to member caisses

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

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

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

(in millions of dollars)	2017	2016	2015
Presentation of the surplus earnings before dividends to member caisses in the Consolidated Financial Statements	**$ 1,416**	$ 1,191	$ 1,137
Specific items, net of income taxes			
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company[1]	**(249)**	-	-
Gain and expenses related to the acquisition of State Farm's Canadian operations	**32**	33	(19)
Presentation of the adjusted surplus earnings before dividends to member caisses	**$ 1,199**	$ 1,224	$ 1,118

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

Adjusted net surplus earnings − Property and Casualty Insurance segment

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

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

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

[1] The difference with the data presented in the table for adjusted surplus earnings of the Federation before dividends to member caisses is related to intersegment expenses.
[2] The difference with the data presented in the table for adjusted surplus earnings of the Federation before dividends to member caisses is related to an amount from the Wealth Management and Life and Health Insurance segment.

Gross impaired loans/gross loans and acceptances ratio

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

Table 28 of the Federation's MD&A provides more detailed information on this indicator.

Loss ratio – Expense ratio – Combined ratio

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

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

The loss ratio is comprised of the following ratios:

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

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

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

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

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

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

Return on equity and adjusted return on equity

Return on equity is used to measure profitability resulting in value creation for members and clients. Expressed as a percentage, it is equal to surplus earnings before dividends to member caisses, excluding the non-controlling interests' share and interest paid to holders of PL and PL-2 investment shares (which are not eligible for the distribution of surplus earnings), divided by average equity before non-controlling interests and PL and PL-2 investment shares.

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

(in millions of dollars and as a percentage)	**2017**	2016	2015
Surplus earnings before dividends to member caisses	**$ 1,416**	$ 1,191	$ 1,137
Non-controlling interests' share	**(43)**	(85)	(180)
Interest paid to holders of PL and PL-2 investments shares	**-**	-	(20)
Group's share	**$ 1,373**	$ 1,106	$ 937
Average equity before non-controlling interests' share	**$ 14,584**	$ 13,033	$ 11,401
Return on equity	**9.4%**	8.5%	8.2%
Adjusted return on equity[1]	**7.9**	8.7	8.0

(1) Takes into account the specific items presented under "Adjusted surplus earnings of the Federation before dividends to member caisses" in this section.

Income

Operating income

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

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

Investment income

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

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

(in millions of dollars)	2017	2016[(1)]	2015[(1)]
Presentation of income in the Consolidated Financial Statements			
Net interest income	**$ 1,404**	$ 1,303	$ 1,203
Net premiums	**8,146**	7,263	7,006
Other income			
Assessments	**377**	393	339
Service agreements	**727**	699	760
Lending fees and credit card service revenues	**660**	575	547
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**457**	397	385
Net income on securities at fair value through profit or loss	**1,158**	572	687
Net income on available-for-sale securities	**405**	335	281
Net other investment income	**204**	201	242
Foreign exchange income	**77**	70	74
Other	**362**	140	250
Total income	**$ 15,064**	$ 13,054	$ 12,811
Presentation of income in the Management's Discussion and Analysis			
Net interest income	**$ 1,404**	$ 1,303	$ 1,203
Net premiums	**8,146**	7,263	7,006
Other operating income			
Assessments	**377**	393	339
Service agreements	**727**	699	760
Lending fees and credit card service revenues	**660**	575	547
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**457**	397	385
Foreign exchange income	**77**	70	74
Other	**362**	140	250
Operating income	**13,297**	11,946	11,601
Investment income			
Net income on securities at fair value through profit or loss	**1,158**	572	687
Net income on available-for-sale securities	**405**	335	281
Net other investment income	**204**	201	242
	1,767	1,108	1,210
Total income	**$ 15,064**	$ 13,054	$ 12,811

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

Provisioning rate

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

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

(in millions of dollars and as a percentage)	2017	2016	2015
Provision for credit losses	**$ 278**	$ 248	$ 302
Average gross loans	**55,101**	51,289	48,523
Average gross acceptances	**69**	108	483
Average gross loans and acceptances	**$ 55,170**	$ 51,397	$ 49,006
Provisioning rate	**0.50%**	0.48%	0.62%

REGULATORY ENVIRONMENT

Regulatory environment

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

Moreover, Desjardins Group, including the Federation, complies with the minimum regulatory capital requirements issued by the AMF, which reflect the provisions of the Basel III Accord. The Federation manages financial information in compliance with AMF *Regulation 52-109 respecting Certification of Disclosure in Issuers' Annual and Interim Filings*. The Federation's financial and corporate governance are discussed on page 86 of this MD&A and in the "Corporate governance" section of the Federation's 2017 Annual Report.

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

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

Changes in the regulatory environment

This section presents matters concerning changes in the regulatory environment that apply to Desjardins Group as a whole, including the Federation and its components.

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

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

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

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

Defined benefit pension plan legislation

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

Rules concerning capital instruments

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

Proceeds of Crime (Money Laundering) and Terrorist Financing Act

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

Recapitalization regime for domestic systemically important banks

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

Financial reforms in the U.S.

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

Standard for automatic exchange of financial information in tax matters

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

Data confidentiality and security

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

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

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

Capital adequacy requirements for life and health insurers

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

Report on Ontario's auto insurance plan

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

Guideline B-20 – Residential Mortgage Underwriting Practices and Procedures

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

Modernization of the Canadian payments system

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

Qualified Intermediary Agreement

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

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

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

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

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

Application of the new framework for European markets in financial instruments

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

1.0 Fédération des caisses Desjardins du Québec

1.1 Profile and structure

WHO WE ARE

The Federation is a cooperative entity which is responsible for assuming orientation, framework, coordination, treasury and development activities for Desjardins Group and acts as a financial agent on Canadian and foreign financial markets. It provides its member caisses–namely 293 member caisses in Quebec and Ontario as at December 31, 2017–with a variety of services, including certain technical, financial and administrative services.

The Federation enables the caisses and other Desjardins Group components to accelerate their development and better respond to the needs of their members and clients. The Federation's structure has been designed to take into account the needs of Desjardins Group's members and clients, as well as the markets in which it operates.

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

The Federation also has the right to participate in the Visa Inc. and MasterCard Inc. payment systems in Canada on behalf of Desjardins Group. In addition, it manages majority participations in joint-stock companies through holding companies.

WHAT MAKES US DIFFERENT

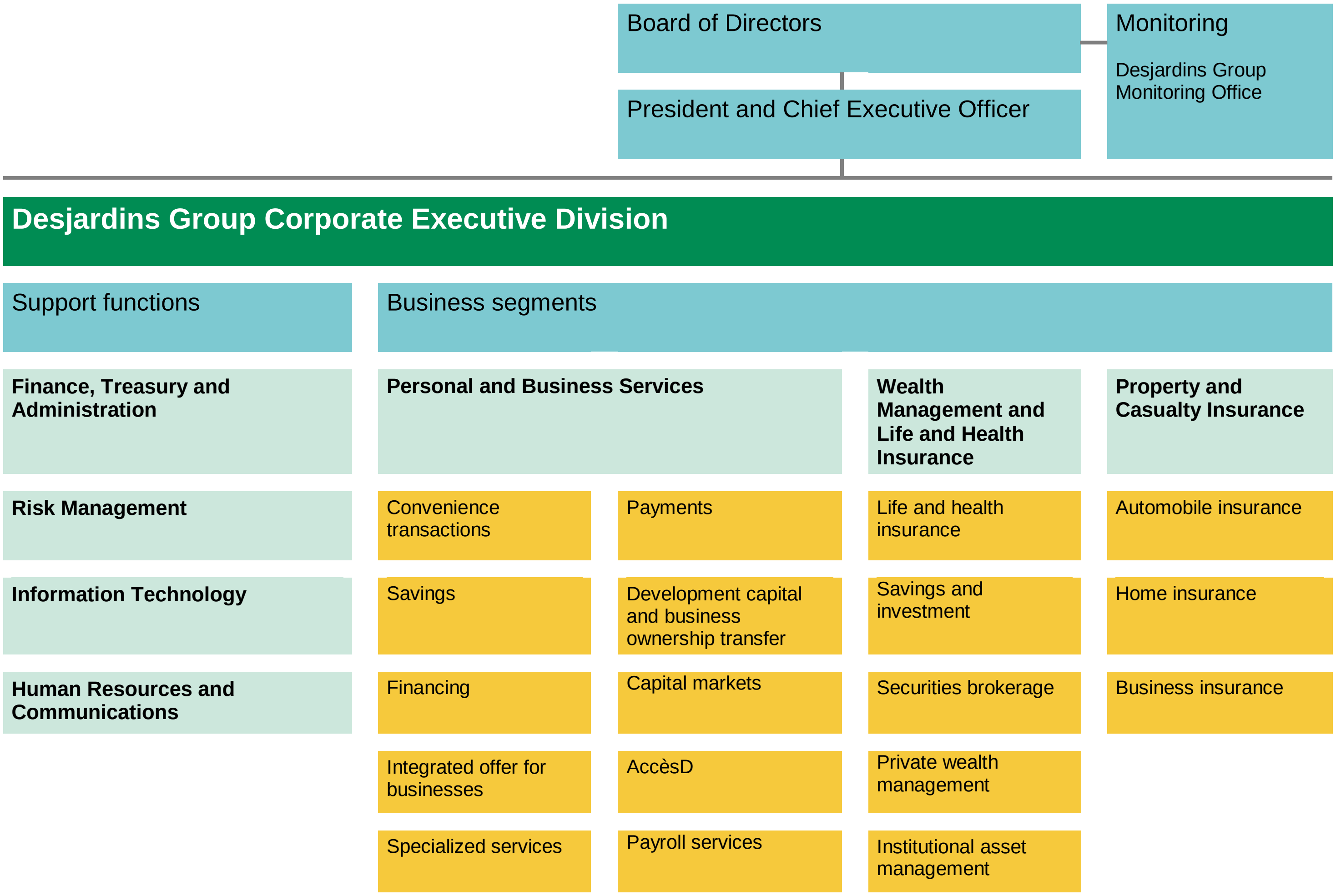
The Federation stands out from other Canadian financial institutions because of the cooperative nature of its component caisses. The resulting mission and values are the driving force for its officers, managers and employees. They are echoed in its orientations, and help it achieve its vision of sustainable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

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

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

STRUCTURE OF THE FEDERATION

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



The Federation's 2017 highlights

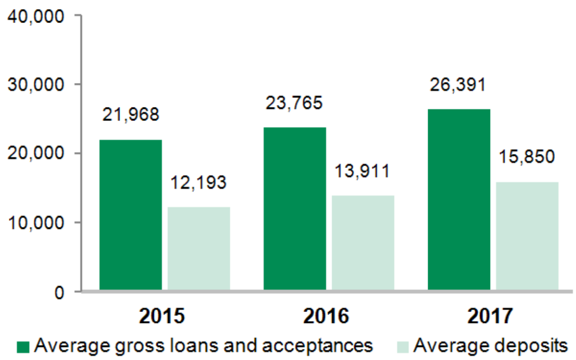
Surplus earnings before dividends	Loans and acceptances outstanding	Assets under management	Tier 1A capital ratio	Total asset growth
$1,416 million	**+ $6.3 billion**	**+ $7.2 billion**	**17.5%**	**+ $11.1 billion**

- Surplus earnings before dividends to member caisses up $225 million, or 18.9%, compared to 2016.
- Decrease of $25 million, or 2.0%, in adjusted surplus earnings(1) before dividends to member caisses, compared to 2016.
- Operating income(1) of $13,297 million, including a gain on the sale of subsidiaries, up 11.3% compared to 2016.
- Adjusted operating income(1) of $13,019 million, up 9.0% compared to 2016.
- Sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 to Trimont Financial Ltd., a subsidiary of The Wawanesa Mutual Insurance Company. A $249 million gain, net of expenses and after income taxes, was recorded for the third quarter of 2017.

2017 segment highlights

PERSONAL AND BUSINESS SERVICES

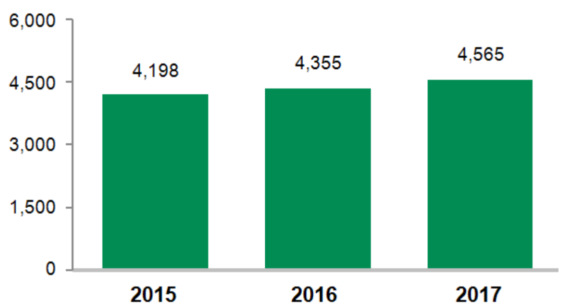
Average gross loans and acceptances and average deposits(1)
(in millions of dollars)



- Number one credit and debit card issuer in Quebec and fourth in Canada, Card and Payment Services has issued more than 6.8 million credit cards and 5.9 million debit cards in Canada.
- Growth of 9.4% compared to 2016 in business volume related to credit card products, Accord D, and auto and durables financing.
- Surplus earnings before dividends to member caisses totalled $317 million, down 9.2% compared to 2016, as a result of an increase in the provision for credit losses following a recovery of the collective allowance in 2016.
- Growth of 11.7% compared to 2016 in consumer, credit card and other personal loans outstanding.

WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

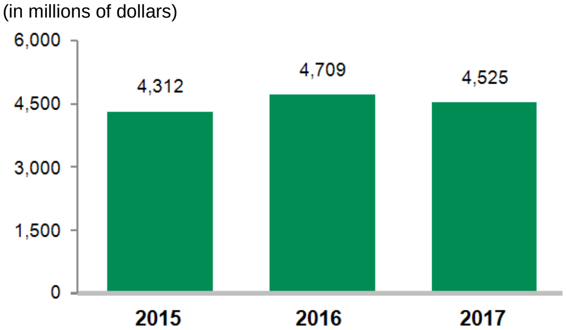
Written premiums
(in millions of dollars)



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

PROPERTY AND CASUALTY INSURANCE

Gross written premiums
(in millions of dollars)



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

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

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

(in millions of dollars and as a percentage)	2017	2016[(1)]	2015[(1)]
Results			
Net interest income	**$ 1,404**	$ 1,303	$ 1,203
Net premiums	**8,146**	7,263	7,006
Other operating income[(2)]	**3,747**	3,380	3,392
Operating income[(2)]	**13,297**	11,946	11,601
Investment income[(2)]	**1,767**	1,108	1,210
Total income	**15,064**	13,054	12,811
Provision for credit losses	**278**	248	302
Claims, benefits, annuities and changes in insurance contract liabilities	**6,795**	5,446	5,431
Non-interest expense	**6,239**	6,022	5,733
Income taxes on surplus earnings	**336**	147	208
Surplus earnings before dividends to member caisses	**$ 1,416**	$ 1,191	$ 1,137
Adjusted surplus earnings before dividends to member caisses[(2)]	**$ 1,199**	$ 1,224	$ 1,118
Contribution to consolidated surplus earnings by business segment[(3)]			
Personal and Business Services	**$ 317**	$ 349	$ 284
Wealth Management and Life and Health Insurance	**612**	461	503
Property and Casualty Insurance	**446**	296	360
Treasury and Other Support to Desjardins Group Entities	**41**	85	(10)
	$ 1,416	$ 1,191	$ 1,137
Indicators			
Return on equity[(2)]	**9.4%**	8.5%	8.2%
Adjusted return on equity[(2)]	**7.9**	8.7	8.0
Provisioning rate[(2)]	**0.50**	0.48	0.62

(1) Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
(2) See "Basis of presentation of financial information".
(3) The breakdown by line item is presented in Note 32, "Segmented information", to the Consolidated Financial Statements.

Table 2 – Balance sheets and indicators
As at December 31

(in millions of dollars and as a percentage)	2017	2016	2015
Balance sheet			
Assets	**$ 145,740**	$ 134,658	$ 128,657
Net loans and acceptances	**58,715**	52,441	51,084
Deposits	**52,149**	46,902	47,922
Equity	**16,019**	14,680	13,587
Indicators			
Assets under administration	**$ 419,981**	$ 428,106	$ 410,858
Assets under management[(1)]	**66,653**	59,490	53,561
Tier 1A capital ratio	**17.5%**	15.9%	N/A[(2)]
Tier 1 capital ratio	**17.5**	15.9	N/A[(2)]
Total capital ratio	**17.5**	15.9	N/A[(2)]
Leverage ratio	**7.9**	7.4	N/A[(2)]
Gross impaired loans/gross loans and acceptances[(3)]	**0.14**	0.18	0.17%

(1) Assets under management may also be administered by the Federation. When this is the case, they are included in assets under administration.
(2) The Federations issues its capital ratios calculated according to the AMF's guideline on adequacy of capital base standards for financial services cooperatives that took effect on January 1, 2017. The December 31, 2016 capital ratios are as at January 1, 2017.
(3) See "Basis of presentation of financial information".

1.2 Material events

Sale of subsidiaries

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

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

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

Creation of Aviso Wealth

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

1.3 Financial outlook for 2018

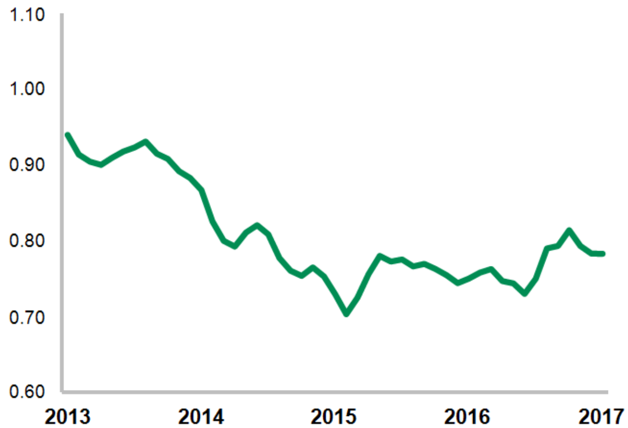
The Federation develops orientations and financial targets in support of Desjardins Group's ambitions. The Federation's actions and achievements are designed to help further the overall financial objectives of Desjardins Group. The financial outlook presented below therefore relates to Desjardins Group's strategic framework.

FINANCIAL OUTLOOK FOR DESJARDINS GROUP

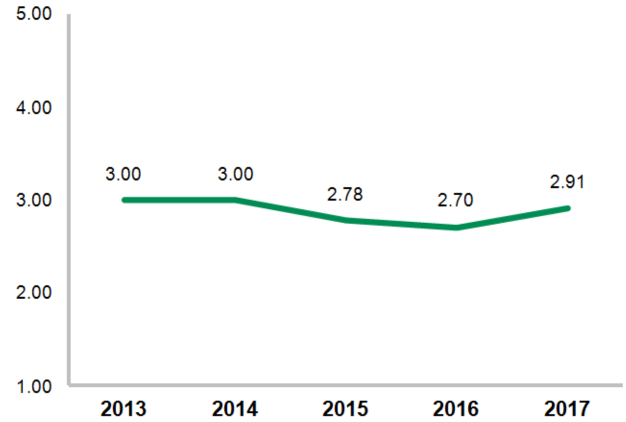
Desjardins Group will continue the year on a solid footing, with a level of capitalization that is higher than the average for the Canadian banking industry as well as increasing profitability in an economic environment that should remain at a satisfactory level over the coming year. Stiff competition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

1.4 Changes in the economy

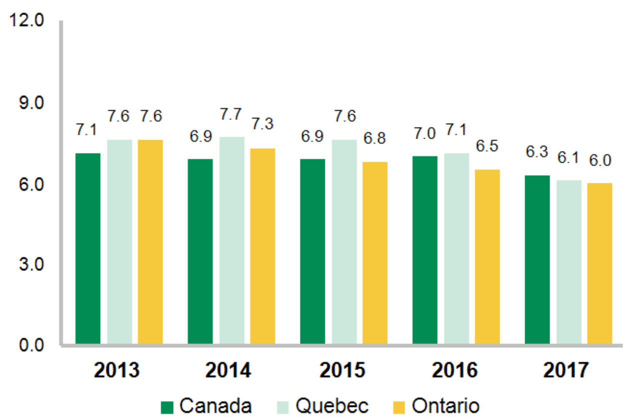
Changes in the Canadian dollar vs. the U.S. dollar (monthly average)
(Canadian dollars/U.S. dollars)



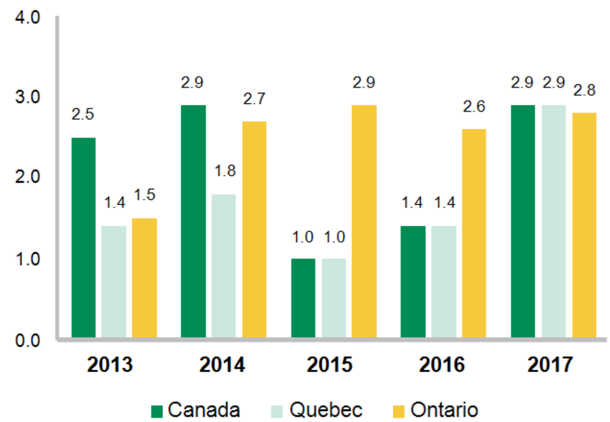
Changes in the prime rate (annual average)
(as a percentage)



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



Annual growth in GDP
(as a percentage)



ECONOMIC ENVIRONMENT IN 2017

Global economy

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

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

United States

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

Canada

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

Quebec

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

ECONOMIC OUTLOOK FOR 2018

Global economy

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

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

United States

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

Canada

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

Quebec

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

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

2.0 Review of financial results

2.1 Impact of the sale of subsidiaries

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

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

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

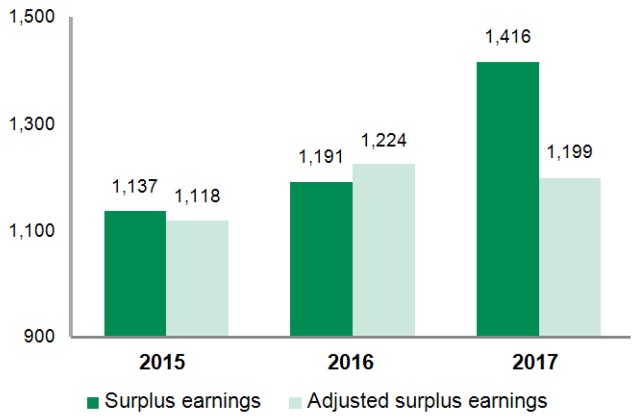
Table 3 – Impact of the sale of subsidiaries
For the years ended December 31

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

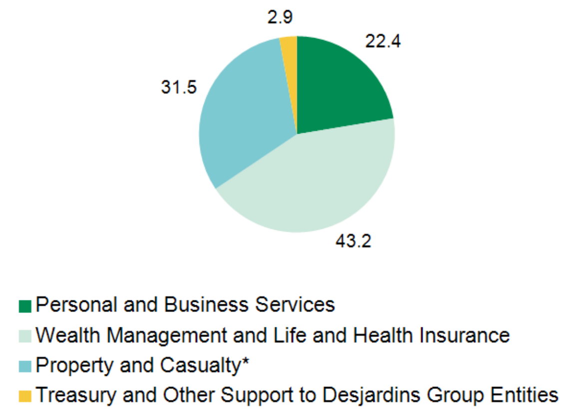
(1) Represents results for the period from January 1, 2017 to June 30, 2017 of Western Financial Group Inc. and Western Life Assurance Company considering that the sale was completed on July 1, 2017.
(2) See "Basis of presentation of financial information".

2.2 Analysis of 2017 results

Surplus earnings before dividends to member caisses
(in millions of dollars)



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



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

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

(in millions of dollars)	**2017**	2016[1]	2015[1]
Results			
Net interest income	**$ 1,404**	$ 1,303	$ 1,203
Net premiums	**8,146**	7,263	7,006
Other operating income[2]	**3,747**	3,380	3,392
Operating income[2]	**13,297**	11,946	11,601
Investment income[2]	**1,767**	1,108	1,210
Total income	**15,064**	13,054	12,811
Provision for credit losses	**278**	248	302
Claims, benefits, annuities and changes in insurance contract liabilities	**6,795**	5,446	5,431
Non-interest expense	**6,239**	6,022	5,733
Income taxes on surplus earnings	**336**	147	208
Surplus earnings before dividends to member caisses	**$ 1,416**	$ 1,191	$ 1,137
Adjusted surplus earnings before dividends to member caisses[2]	**$ 1,199**	$ 1,224	$ 1,118
Contribution to consolidated surplus earnings by business segment[3]			
Personal and Business Services	**$ 317**	$ 349	$ 284
Wealth Management and Life and Health Insurance	**612**	461	503
Property and Casualty Insurance[4]	**446**	296	360
Treasury and Other Support to Desjardins Group Entities	**41**	85	(10)
	$ 1,416	$ 1,191	$ 1,137

[1] Data for 2016 and 2015 have been reclassified to conform to the current year's presentation.
[2] See "Basis of presentation of financial information".
[3] The breakdown by line item is presented in Note 32, "Segmented information", to the Consolidated Financial Statements.
[4] Includes a $241 million gain in this segment related to the sale of subsidiaries.

2017 SURPLUS EARNINGS

For 2017, the Federation reported surplus earnings before dividends to member caisses of $1,416 million, an increase of $225 million, or 18.9%, compared to 2016. Surplus earnings adjusted for specific items totalled $1,199 million, which was down $25 million, or 2.0%, compared to $1,224 million in 2016.

Segment contributions to surplus earnings

- Personal and Business Services: **Contribution of $317 million**, down $32 million, or 9.2%, compared to 2016.
  - Higher provision for credit losses in 2017 following recovery of the collective allowance in 2016.
  - The segment contributed 22.4% to surplus earnings.
- Wealth Management and Life and Health Insurance: **Contribution of $612 million**, up $151 million, or 32.8%, compared to 2016.
  - Solid investment performance in 2017.
  - Favourable adjustments to actuarial assumptions in the normal course of business in 2017.
  - Higher income from growth in assets under management.
  - Offset by a less favourable claims experience in 2017.
  - The segment contributed 43.2% to surplus earnings.
- Property and Casualty Insurance, including the gain on the sale of subsidiaries: **Contribution of $446 million**, up $150 million compared to 2016.
  - Surplus earnings adjusted for specific items of $237 million, down $92 million compared to 2016.
  - Higher claims experience for the current year than in 2016, and favourable developments in prior-year claims, which were lower than in 2016.
  - The segment contributed 31.5% to surplus earnings.
- Treasury and Other Support to Desjardins Group Entities: **Contribution of $41 million**, down $44 million compared to 2016.
  - The segment contributed 2.9% to surplus earnings.

- **Return on equity was 9.4%**, compared to 8.5% for 2016.
- **Adjusted return on equity was 7.9%**, down compared to 8.7% for 2016, mainly because of the increase in members' equity.

OPERATING INCOME

Table 5 – Operating income
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Net interest income	**$ 1,404**	$ 1,303	$ 1,203
Net premiums	**8,146**	7,263	7,006
Other operating income[2] (see Table 6)	**3,747**	3,380	3,392
Total operating income[2]	**$ 13,297**	$ 11,946	$ 11,601

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

Operating income totalled $13,297 million, up $1,351 million, or 11.3%, compared to 2016. Excluding the gain of $278 million before taxes on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, operating income would have been $13,019 million, up $1,073 million, or 9.0%, compared to 2016.

Net interest income

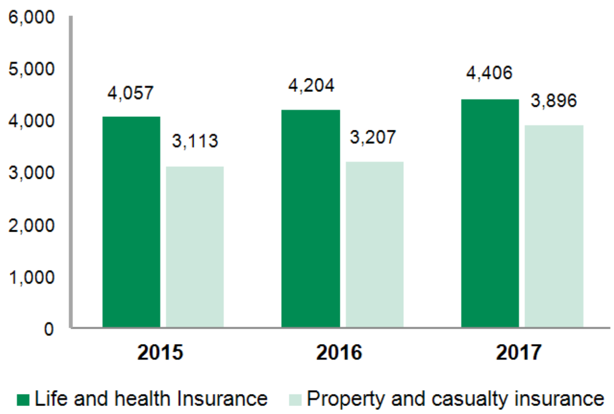
Net interest income is the difference between interest income earned on assets, such as loans and securities, and the interest expense related to liabilities, such as deposits, borrowings and subordinated notes. It is affected by interest rate fluctuations, funding and matching strategies, as well as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

- **Net interest income of $1,404 million**, up $101 million, or 7.8%.
  - Growth in the entire portfolio of loans and acceptances outstanding of $6.3 billion, or 12.0% over the year. This portfolio comprises financing activities in consumer, credit card and other personal loans, including point-of-sale financing, as well as loans to business and government.

Net premiums

Net premiums, comprising life and health insurance, annuity, and property and casualty insurance premiums, rose by $883 million, or 12.2%, to total $8,146 million as at December 31, 2017.

Net premiums(1)
(in millions of dollars)



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

Wealth Management and Life and Health Insurance segment

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

Property and Casualty Insurance segment

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

Other operating income

Table 6 – Other operating income
For the years ended December 31

(in millions of dollars)	2017	2016(1)	2015(1)
Assessments	**$ 377**	$ 393	$ 339
Service agreements	**727**	699	760
Lending fees and credit card service revenues	**660**	575	547
Brokerage and investment fund services	**1,087**	1,106	1,037
Management and custodial service fees	**457**	397	385
Foreign exchange income	**77**	70	74
Other	**362**	140	250
Total other operating income(2)	**$ 3,747**	$ 3,380	$ 3,392

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

Other operating income stood at $3,747 million for 2017, which is an increase of $367 million, or 10.9%, compared to the previous year. Excluding the gain before taxes of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company, other operating income would have been $3,469 million, up $89 million, or 2.6%, compared to 2016.

- Income from assessments and service agreements of $1,104 million, up $12 million, or 1.1%.
- Lending fees and credit card service revenues of $660 million, up $85 million, or 14.8%.
  - Growth in business volume from the various payment solutions offered by Card and Payment Services.
- Income from brokerage and investment fund services of $1,087 million, down $19 million, or 1.7%.
  - Decrease in commission income following the sale of Western Financial Group Inc., as presented in the "Impact of the sale of subsidiaries" section under other operating income.
  - Offset by growth in income from assets under management.
- Management and custodial service fees up $60 million, or 15.1%.
  - Growth in fees related to increase of $7.2 billion in assets under management.
- Other operating income of $362 million, up $222 million.
  - Gain before taxes of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company.
  - Offset by an increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.

INVESTMENT INCOME

Table 7 – Investment income
For the years ended December 31

(in millions of dollars)	2017	2016	2015
Net income on securities at fair value through profit or loss	**$ 1,158**	$ 572	$ 687
Net income on available-for-sale securities	**405**	335	281
Net other investment income	**204**	201	242
Total investment income[(1)]	**$ 1,767**	$ 1,108	$ 1,210

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

Investment income totalled $1,767 million for 2017, an increase of $659 million, or 59.5%, compared to the previous year.

- Net income on securities at fair value through profit or loss up $586 million.
  - Increase primarily due to change in the fair value of assets backing liabilities related to life and health insurance operations.
    - Increase largely offset by the change in actuarial liabilities that in turn led to higher expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
    - Changes for the most part due to fluctuations in the fair value of the portfolio of stocks, bonds and derivative products.
  - Increase in 2017 in the fair value of derivative financial instruments, including those associated with the Federation's hedging operations.
  - Offset by the decrease in income generated by asset-backed term note (ABTN) operations, which have been substantially settled since January 2017.
- Net income on available-for-sale securities up $70 million, or 20.9%, primarily because of higher gains on disposal of investments in 2017.
- Net other investment income of $204 million, stable compared to 2016.

TOTAL INCOME

Total income, comprising net interest income, net premiums, other operating income and investment income, amounted to $15,064 million, an increase of $2,010 million, or 15.4%, compared to 2016.

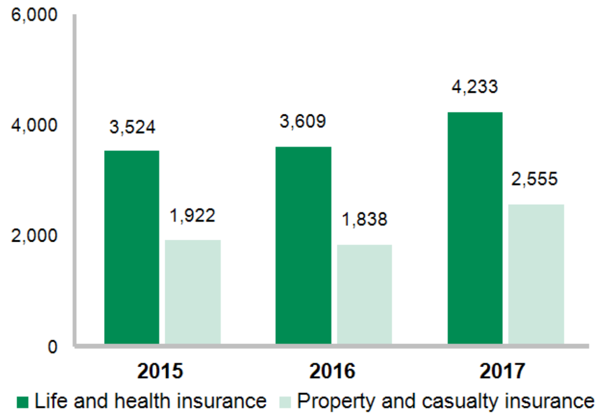
PROVISION FOR CREDIT LOSSES

The Federation's loan portfolio continued to be of high quality in 2017. The provision for credit losses totalled $278 million, up $30 million, or 12.1%. In 2016, there was a recovery of the collective allowance as a result of refining the methodology used in the models for calculating the collective allowance. Favourable developments in portfolio risk curbed the increase, however.

- The provisioning rate was 0.50% as at December 31, 2017, which is comparable to 2016.
- The ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.14% as at December 31, 2017, down from 0.18% a year earlier. Improved economic conditions helped to reduce the volume of gross impaired loans.

CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE CONTRACT LIABILITIES

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



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

Expenses related to claims, benefits, annuities and changes in insurance contract liabilities totalled $6,795 million, up $1,349 million, or 24.8%, compared to 2016.

Wealth Management and Life and Health Insurance segment

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

Property and Casualty Insurance segment

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

NON-INTEREST EXPENSE

Table 8 – Non-interest expense
For the years ended December 31

(in millions of dollars)	2017	2016[1]	2015[1]
Remuneration and other payments	**$ 536**	$ 492	$ 471
Salaries and fringe benefits			
Salaries	**1,842**	1,927	1,826
Fringe benefits	**413**	402	395
	2,255	2,329	2,221
Premises, equipment and furniture, including depreciation	**514**	437	397
Service agreements and outsourcing	**322**	306	327
Communications	**244**	265	254
Other	**2,368**	2,193	2,063
Total non-interest expense	**$ 6,239**	$ 6,022	$ 5,733

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

Non-interest expense totalled $6,239 million for 2017, up $217 million, or 3.6%, compared to 2016, mainly because of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations. Effective cost control following the implementation of productivity initiatives limited the increase in a context of operations growth.

- **Remuneration and other payments of $536 million**, up $44 million, or 8.9%.
  - Increase in payments to member caisses as a result of growth in network sales of various Desjardins products, such as Desjardins Funds.

- **Salaries and fringe benefits of $2,255 million**, down $74 million, or 3.2%, compared to 2016, mainly because of the following items:
  - Severance costs incurred in 2016 following changes in Desjardins Group's senior management.
  - Lower personnel expenses as a result of this reorganization.
  - Implementation of productivity initiatives, reflected in a reduction in payroll.
  - This expense item represented 36.1% of total non-interest expense, lower than the 38.7% recorded in 2016.
  - The ratio of fringe benefits to total base compensation was 22.4% in 2017, up compared to 20.9% in 2016, primarily because of the 2016 severance costs included in 2016 salaries.

- **Expenses related to premises, equipment and furniture (including depreciation) of $514 million**, up $77 million, or 17.6%, compared to 2016.
  - The increase resulted mainly from the purchase of computer hardware.

- **Service agreements and outsourcing of $322 million**, up slightly compared to 2016.

- **Communication expenses of $244 million**, down $21 million, or 7.9%, compared to 2016.
  - The decrease resulted from the implementation of productivity initiatives.

- **Other expenses of $2,368 million**, up $175 million, or 8.0%, compared to 2016.
  - Increase due in large part to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increased popularity of the BONUSDOLLARS Rewards Program with Card and Payment Services clients.
  - Business growth, particularly in credit card and point-of-sale financing activities and assets under management.
  - Write-off of intangible assets.
  - Offset by a decrease of $171 million in expenses following the sale of Western Financial Group Inc. and Western Life Assurance Company on July 1, 2017 as well as Western Financial Insurance Company on January 1, 2017, as presented in the "Impact of the sale of subsidiaries" section.

INCOME TAXES AND INDIRECT TAXES

The Federation is a cooperative financial group, and is considered a private and independent company for tax purposes, unlike the vast majority of other Canadian financial institutions, which are large public corporations. It therefore benefited until December 31, 2016, when tax rules allowed it, from certain preferential tax rates under the credit union tax regime. The Federation's entities that are not financial services cooperatives are subject to the large corporation tax regime.

- **Income taxes on surplus earnings before dividends to member caisses of $336 million**, up $189 million compared to 2016.
  - Effective tax rate of 19.2% for the year ended December 31, 2017, compared to 11.0% for 2016. If specific items are excluded, the effective tax rate would have been 21.0%, compared to 11.5% in 2016.
  - In 2016, income taxes on surplus earnings included a tax recovery related to remuneration on capital stock, which was not the case in 2017, and was the main factor in the increase in income taxes and the effective tax rate.

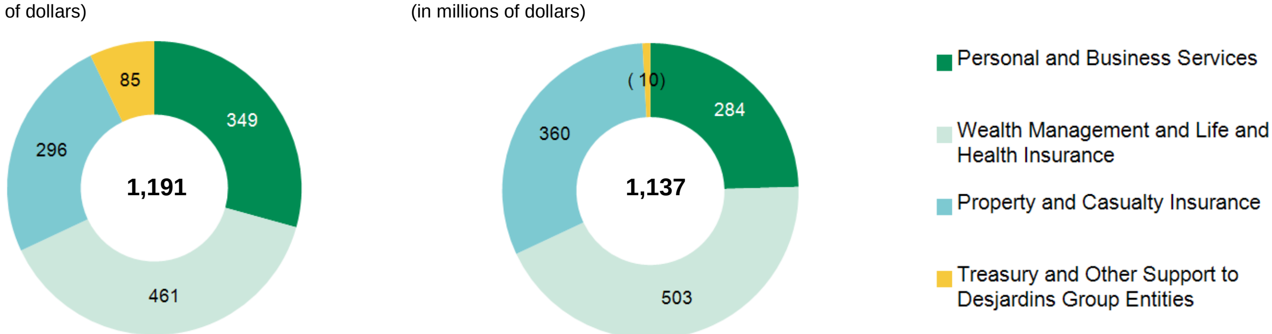
Note 27, "Income taxes on surplus earnings", to the Consolidated Financial Statements presents, among other things, a reconciliation of the statutory tax rate and the effective tax rate, expressed in dollars.

Indirect taxes consist of property and business taxes, payroll and social security taxes, the goods and services tax, and sales taxes. Indirect taxes are included in non-interest expense. For 2017, the Federation's entities paid $1,049 million in indirect taxes, compared to $1,009 million in 2016, mainly due to an increase in the compensation tax.

COMPARISON OF 2016 AND 2015

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

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



For 2016, the Federation posted surplus earnings before dividends to member caisses of $1,191 million, compared to $1,137 million for 2015. Surplus earnings adjusted for specific items totalled $1,224 million, which was up $106 million, or 9.5%. Return on equity was 8.5%, compared to 8.2% in 2015, while adjusted return on equity was 8.7% in 2016, compared to 8.0% in 2015.

Segment results

- **Personal and Business Services: Surplus earnings before dividends to member caisses of $349 million in 2016**, up $65 million compared to 2015.
  - Largely due to a decrease in the provision for credit losses following a recovery of the collective allowance as a result, in particular, of refining the methodology used in the models for calculating the allowance.
  - Growth in trading income related to capital markets.

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

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

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

Consolidated results

- **Operating income of $11,946 million in 2016**, up $345 million compared to 2015.
  - Net interest income of $1,303 million in 2016, up by $100 million.
    - Increase in consumer, credit card and other personal loans outstanding.
    - Increase in income from treasury operations.
  - Net premiums up $257 million in 2016, mainly because of the following:
    - Business growth related to Wealth Management and Life and Health Insurance segment insurance operations.
    - Increase in net premiums as a result of the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Other operating income of $3,380 million, down $12 million in 2016, essentially due to the following:
    - Income from assessments and service agreements stable, but the distribution between the categories had changed due to a revision of financing methods.
    - Other income down $110 million in 2016 as a result of an increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations and the gain realized at the time of this acquisition in 2015.

    This decrease was partly offset by the following:
    - Increase of $69 million in income from brokerage and investment fund services chiefly due to a larger volume of assets under management from the sale of various financial products.
    - Increase of $28 million in lending fees and credit card service revenues as a result of business volume growth.

- **Investment income of $1,108 million**, down $102 million compared to 2015.
  - Net income on securities at fair value through profit or loss down $115 million in 2016.
    - Decrease mainly due to fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
      - Decrease partly offset by the change in actuarial liabilities that in turn led to a reduction in expenses related to claims, benefits, annuities and changes in insurance contract liabilities. These differences were mostly attributable to changes in the fair value of the bond portfolio.
    - Favourable changes in the fair value of derivative financial instruments associated with the Federation's hedging operations and in the fair value of derivative financial instruments in the Property and Casualty Insurance segment in 2016.
  - Income from available-for-sale securities up $54 million in 2016.
    - A loss in share value had been recorded in 2015 as a result of strong market volatility.
  - Net other investment income down $41 million in 2016.
    - Smaller gains on the disposal of real estate investments in 2016.

- **Provision for credit losses of $248 million in 2016**, down $54 million compared to 2015.
  - Decrease mainly due to the recovery of the collective allowance as a result, in particular, of refining the methodology used in the models for calculating the allowance, combined with a high-quality loan portfolio.
  - Ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, of 0.18% as at December 31, 2016, compared to 0.17% as at December 31, 2015.
  - Provisioning rate of 0.48% as at December 31, 2016, down from 0.62% as at December 31, 2015.

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

- **Non-interest expense** up $289 million in 2016, mainly due to the following:
  - Additional investment in innovative technology platforms in 2016.
  - Payment of severance allowances in 2016.
  - Business growth, particularly in credit card, point-of-sale financing and insurance activities.
  - Offset by strict cost control that made it possible to limit the increase in non-interest expense in 2016.

2.3 Analysis of business segment results

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

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

2.3.1 Personal and Business Services

PROFILE

Personal and Business Services is central to Desjardins Group's operations. This segment is responsible for finetuning a comprehensive, integrated line of products and services designed to meet the needs of individuals, businesses, institutions, non-profit organizations and cooperatives offered through the Desjardins caisse network, its Desjardins Business centres, and specialized teams. This is what makes Desjardins Group is a leader in financial services in Quebec and a player on the financial services scene in Ontario as well.

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

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

To meet the constantly changing needs of caisse members and clients, the Federation supports the caisse network and its service centres in distributing products and services by optimizing the performance and profitability of the physical and virtual networks through setting up and managing complementary access methods by phone, online, via applications for mobile devices, and at ATMs.

The shared services which the Federation provides to this segment, formerly presented in the Treasury and Other Support to Desjardins Entities category, have been recorded in this segment since the first quarter of 2017.

Additional information about the Personal and Business Services segment's principal risks is presented on page 57 of the "Risk management" section of this MD&A.

SERVICES

Convenience and savings operations comprise variable savings, including current accounts and term savings, as well as specialty services, such as foreign exchange and funds transfers.

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

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

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

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

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

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

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

2017 ACHIEVEMENTS

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

INDUSTRY

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

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

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

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

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

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

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

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

2018 STRATEGY AND PRIORITIES

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

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

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

More specifically, this segment's priorities for 2018 are to:
- Accelerate the shift to a member- and client-focused culture across Desjardins Group.
- Continue the digital transformation of products and services across all distribution channels.
- Facilitate interactions with members and clients throughout Desjardins components and across all channels (mobile, website, call centres, caisses, Desjardins Business centres, online business centres, etc.).
- Offer members and clients proactive support and the expertise of the entire Desjardins Group to help them grow their businesses.
- Ensure a high level of satisfaction among members and clients.

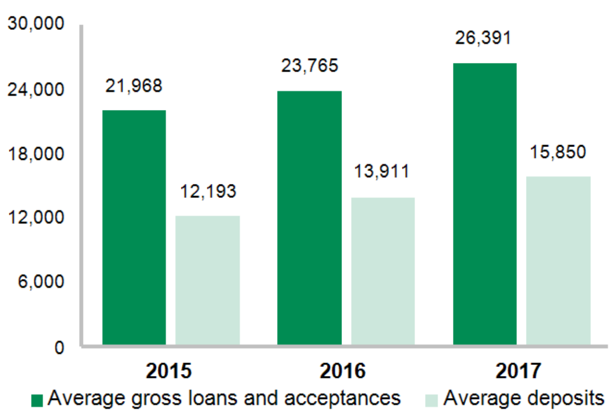
ANALYSIS OF FINANCIAL RESULTS FOR THE PERSONAL AND BUSINESS SERVICES SEGMENT

Table 9 – Personal and Business Services – Segment results
For the years ended December 31

(in millions of dollars and as a percentage)	2017	2016[1]	2015[1]
Net interest income	**$ 1,089**	$ 1,031	$ 975
Other operating income[2]	**1,617**	1,489	1,432
Operating income[2]	**2,706**	2,520	2,407
Investment income[2]	**39**	33	4
Total income	**2,745**	2,553	2,411
Provision for credit losses	**274**	248	302
Non-interest expense	**2,032**	1,877	1,756
Income taxes on surplus earnings	**122**	79	69
Surplus earnings before dividends to member caisses	**317**	349	284
Dividends to member caisses, net of tax recovery	**-**	18	-
Net surplus earnings for the year after dividends to member caisses	**$ 317**	$ 331	$ 284
Of which:			
Group's share	**$ 317**	$ 325	$ 280
Non-controlling interests' share	**-**	6	4
Indicators			
Average gross loans and acceptances[2]	**$ 26,391**	$ 23,765	$ 21,968
Average deposits[2]	**15,850**	13,911	12,193
Provisioning rate[2]	**1.04%**	1.04%	1.37%
Gross impaired loans/gross loans and acceptances ratio[2]	**0.28**	0.38	0.35

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

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



COMPARISON OF 2017 AND 2016 – PERSONAL AND BUSINESS SERVICES

- **Surplus earnings before dividends to member caisses of $317 million**, down $32 million, or 9.2%.
  - Increase in the provision for credit losses, which decreased significantly in 2016 as a result of refining the methodology used in calculating the provision.

- **Operating income of $2,706 million**, up $186 million, or 7.4%.
  - Increase of $58 million in net interest income mainly as a result of year-over-year growth of $3.5 billion, or 14.1%, in the entire portfolio of loans and acceptances outstanding. This portfolio comprises financing activities in consumer, credit card and other personal loans, including point-of-sale financing and loans to business.
  - Other operating income of $1,617 million, up $128 million, or 8.6%, mainly due to the following:
    - Growth in business volume from the various payment solutions offered by Card and Payment Services.
    - Growth in income from capital markets.

- **Investment income of $39 million**, up $6 million, or 18.2%.
  - Growth in trading income on capital markets.

- **Total income of $2,745 million**, up $192 million, or 7.5%.

- **Provision for credit losses of $274 million**, up $26 million, or 10.5%. This provision had decreased significantly in 2016 as a result of refining the methodology used in calculating the collective allowance. However, favourable developments in portfolio risk curbed this increase.

- **Non-interest expense of $2,032 million**, up $155 million, or 8.3%.
  - Business growth, especially in credit card and point-of-sale financing activities that had an effect on bonus programs.
  - Increase in remuneration paid to the caisses as a result of the change in pricing for outstandings of medium-sized enterprises.

2.3.2 Wealth Management and Life and Health Insurance

PROFILE

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

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

One of the greatest strengths of the Wealth Management and Life and Health Insurance segment is its vast and diversified Canada-wide distribution network, which mainly includes:

- Employees of the caisse network and Desjardins Business centres.
- Financial security advisers dedicated to caisse members.
- Investment advisers and private managers.
- Exclusive agents and independent partners.
- Actuarial consulting firms and group plan representatives.

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

Additional information about the Wealth Management and Life and Health Insurance segment's principal risks is presented on page 57 of the "Risk management" section of this MD&A.

SERVICES

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

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

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

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

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

2017 ACHIEVEMENTS

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

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

INDUSTRY

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

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

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

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

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

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

2018 STRATEGY AND PRIORITIES

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

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

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

To summarize, the top three priorities of the Wealth Management and Life and Health Insurance segment are:
- Build exceptional member and client relationships and ensure the excellence of its services.
- Help actively promote Desjardins Group's cooperative difference.
- Capitalize on Desjardins Group's strengths as an expansive cooperative group.

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

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

Table 10 – Wealth Management and Life and Health Insurance – Segment results
For the years ended December 31

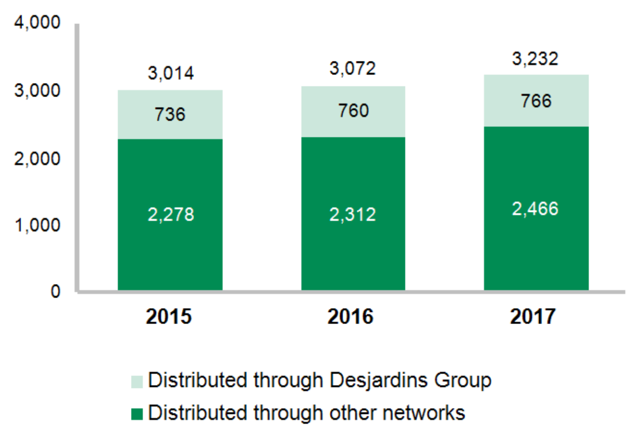
(in millions of dollars)	**2017**	2016	2015
Net interest income	**$ 1**	$ -	$ -
Net premiums	**4,406**	4,204	4,057
Other operating income[1]	**1,514**	1,386	1,263
Operating income[1]	**5,921**	5,590	5,320
Investment income[1]	**1,406**	795	942
Total income	**7,327**	6,385	6,262
Provision for credit losses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

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

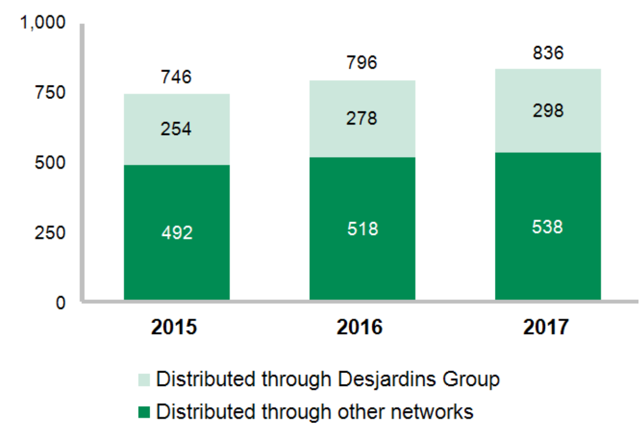
Table 11 – Expenses attributable to policyholders
For the years ended December 31

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

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



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



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

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

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

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

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

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

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

2.3.3 Property and Casualty Insurance

PROFILE

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

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

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

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

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, Western Financial Group Inc. and Western Life Assurance Company, while Western Financial Insurance Company was sold on January 1, 2017. Additional information concerning these transactions is presented in the "Impact of the sale of subsidiaries" section on page 19.

Additional information about the Property and Casualty Insurance segment's principal risks is presented on page 57 of the "Risk management" section of this MD&A.

SERVICES

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

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

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

2017 ACHIEVEMENTS

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

INDUSTRY

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

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

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

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

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

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

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

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

2018 STRATEGY AND PRIORITIES

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

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

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

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

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

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

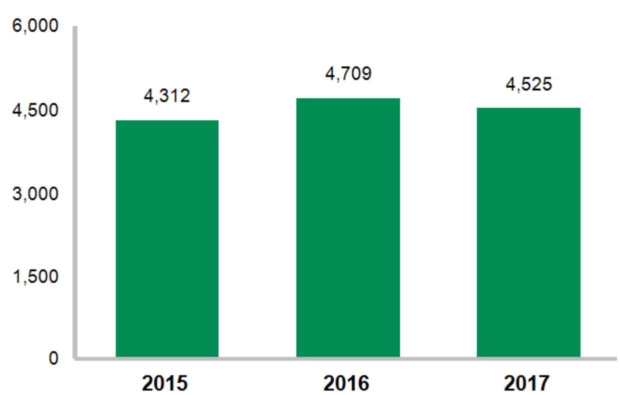
ANALYSIS OF FINANCIAL RESULTS FOR THE PROPERTY AND CASUALTY INSURANCE SEGMENT

Table 12 – Property and Casualty Insurance – Segment results
For the years ended December 31

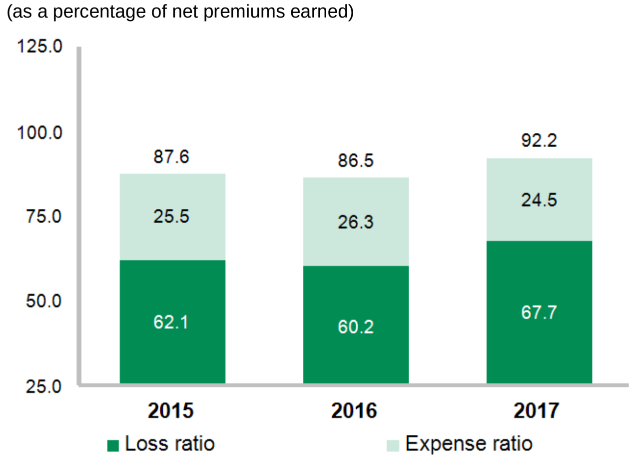
(in millions of dollars and as a percentage)	2017	2016	2015
Net interest income	$ 1	$ 1	$ 1
Net premiums	3,896	3,207	3,113
Other operating income (loss)[1]	78	(55)	104
Operating income[1]	3,975	3,153	3,218
Investment income[1]	214	206	228
Total income	4,189	3,359	3,446
Claims, benefits, annuities and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

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

Gross written premiums
(in millions of dollars)



Combined ratio
(as a percentage of net premiums earned)



COMPARISON OF 2017 AND 2016 – PROPERTY AND CASUALTY INSURANCE

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

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

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

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

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

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

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

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

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

2.3.4 Treasury and Other Support to Desjardins Group Entities category

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

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

Table 13 – Treasury and Other Support to Desjardins Group Entities
For the years ended December 31

(in millions of dollars)	**2017**	2016[1]	2015[1]
Treasury activities	**$ 113**	$ 110	$ 111
Activities related to derivatives associated with hedging activities	**89**	27	(20)
Other[2]	**(161)**	(52)	(101)
Net surplus earnings before dividends to member caisses	**41**	85	(10)
Dividends to member caisses, net of tax recovery	**44**	-	-
Net surplus earnings (deficit) for the year	**$ (3)**	$ 85	$ (10)
Of which:			
Group's share	**$ (3)**	$ 78	$ (18)
Non-controlling interests' share	**-**	7	8

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

COMPARISON OF 2017 AND 2016 – CONTRIBUTION BY TREASURY AND OTHER SUPPORT TO DESJARDINS GROUP ENTITIES TO SURPLUS EARNINGS

- **Net surplus earnings of $41 million,** compared to $85 million in 2016.

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

- **Activities related to derivatives associated with hedging activities totalling $89 million**, up $62 million compared to 2016.
  - Increase in the fair value of swaps because of higher interest rates in 2017, compared to 2016.

- **Other activities recorded a $161 million deficit**, compared to a $52 million deficit in 2016.
  - Other activities affected, in 2017 and 2016, by expenses related to the continued implementation of Desjardins-wide strategic projects, in particular, to improve systems and processes as well as to create innovative technology platforms, thereby enhancing the member and client experience and improving productivity. In addition, certain technology assets were written off in 2017.
  - Income tax expense in 2016 partially reduced by a tax recovery related to the remuneration of capital stock, which was not the case in 2017.
  - Decline in income from asset-backed term notes (ABTN) activities given that substantially all ABTN were settled in January 2017. ABTM activities generated surplus earnings of $10 million in 2016.
  - Offset by severance costs incurred in 2016, following changes in Desjardins Group's senior management.

2.4 Analysis of fourth quarter results and quarterly trends

Table 14 – Results for the previous eight quarters

(unaudited, in millions of dollars and as a percentage)	**2017**				2016			
	Q4	Q3	Q2	Q1	Q4[1]	Q3[1]	Q2[1]	Q1[1]
Net interest income	**$ 357**	$ 364	$ 344	$ 339	$ 331	$ 332	$ 321	$ 319
Net premiums	**2,034**	2,007	2,099	2,006	1,857	1,897	1,764	1,745
Other operating income[2]								
Assessments	**94**	93	91	99	98	99	114	82
Service agreements	**179**	187	194	167	174	175	158	192
Lending fees and credit card service revenues	**182**	154	153	171	151	138	135	151
Brokerage and investment fund services	**261**	241	307	278	281	279	286	260
Management and custodial service fees	**131**	109	111	106	108	99	97	93
Foreign exchange income	**22**	16	21	18	20	21	17	12
Other	**(78)**	330	47	63	(13)	(17)	76	94
Operating income[2]	**3,182**	3,501	3,367	3,247	3,007	3,023	2,968	2,948
Investment income (loss)[2]								
Net income (loss) on securities at fair value through profit or loss	**806**	(440)	497	295	(1,204)	396	870	510
Net income on available-for-sale securities	**80**	66	183	76	93	91	84	67
Net other investment income	**38**	58	54	54	49	51	51	50
	924	(316)	734	425	(1,062)	538	1,005	627
Total income	**4,106**	3,185	4,101	3,672	1,945	3,561	3,973	3,575
Provision for credit losses	**74**	72	59	73	48	70	58	72
Claims, benefits, annuities and changes in insurance contract liabilities	**2,120**	1,000	1,922	1,753	(104)	1,727	2,065	1,758
Non-interest expense	**1,651**	1,433	1,605	1,550	1,560	1,458	1,536	1,468
Income taxes on surplus earnings	**80**	89	100	67	27	32	43	45
Surplus earnings before dividends to member caisses	**181**	591	415	229	414	274	271	232
Dividends to member caisses, net of tax recovery	**44**	-	-	-	18	-	-	-
Net surplus earnings for the period after dividends to member caisses	**$ 137**	$ 591	$ 415	$ 229	$ 396	$ 274	$ 271	$ 232
Of which:								
Group's share	**$ 128**	$ 576	$ 401	$ 224	$ 370	$ 261	$ 248	$ 209
Non-controlling interests' share	**9**	15	14	5	26	13	23	23
Contribution to consolidated surplus earnings by business segment:								
Personal and Business Services	**$ 62**	$ 86	$ 85	$ 84	$ 97	$ 88	$ 87	$ 77
Wealth Management and Life and Health Insurance	**159**	121	189	143	114	126	124	97
Property and Casualty Insurance	**48**	318	98	(18)	182	26	49	39
Treasury and Other Support to Desjardins Group Entities	**(88)**	66	43	20	21	34	11	19
	$ 181	$ 591	$ 415	$ 229	$ 414	$ 274	$ 271	$ 232
Total assets	**$ 145,740**	$148,020	$144,206	$142,927	$ 134,658	$ 136,100	$ 136,770	$ 135,481
Indicators								
Return on equity[2]	**4.5%**	15.3%	11.2%	6.5%	11.3%	7.8%	7.8%	6.8%
Tier 1A capital ratio	**17.5**	17.7	15.8	15.2	15.9	N/A[3]	N/A[3]	N/A[3]
Total capital ratio	**17.5**	17.6	15.8	15.2	15.9	N/A[3]	N/A[3]	N/A[3]

(1) Prior-period data have been reclassified to conform to the current period's presentation.
(2) See "Basis of presentation of financial information".
(3) The Federation publishes its capital ratios calculated according to the guideline on the adequacy of capital base standards applicable to financial services cooperatives issued by the AMF on January 1, 2017. The ratios as at December 31, 2016 are as at January 1, 2017.

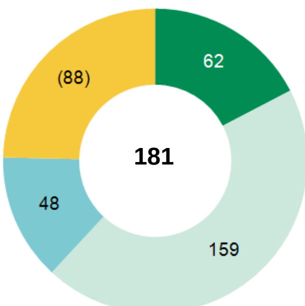
FOURTH QUARTER CONSOLIDATED RESULTS

For the fourth quarter of 2017, the Federation posted surplus earnings before dividends to member caisses of $181 million, down $233 million, compared to the same period in 2016.

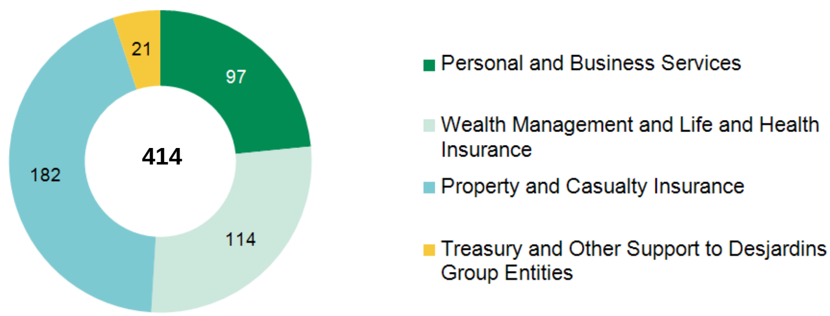
Contribution of segments to surplus earnings

- Personal and Business Services: **Contribution of $62 million**, down $35 million compared to the same period in 2016, mainly due to the increase in the provision for credit losses, which had decreased significantly in 2016 as a result of refining the methodology used to calculate the collective allowance.
- Wealth Management and Life and Health Insurance: **Contribution of $159 million**, up $45 million compared to the same period in 2016, primarily due to favourable adjustments to actuarial assumptions made during the normal course of operations.
- Property and Casualty Insurance: **Contribution of $48 million**, down $134 million compared to the same period in 2016, mainly as a result of the following:
  - Less favourable developments in prior-year claims than in the corresponding quarter of 2016, which had been very favourable.
  - Claims experience for the current year higher than in the corresponding quarter of 2016.
  - Increase in non-interest expense caused largely by the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
- Treasury and Other Support to Desjardins Group Entities category: **Deficit of $88 million**, compared to surplus earnings of $21 million in 2016. The surplus earnings in 2016 included a tax recovery related to remuneration on capital stock, which was not the case in 2017.

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



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



- **Return on equity of 4.5%, compared to 11.3**% for the fourth quarter of 2016.
  - Decrease mainly caused by the decline in surplus earnings, as previously explained.

- **Operating income of $3,182 million**, up $175 million, or 5.8%.

- **Net interest income of $357 million**, up $26 million, or 7.9%, chiefly as a result of the growth of $6.3 billion, or 12.0%, for the year in the entire loans and acceptances portfolio outstanding, which is made up of financing operations in the area of consumer, credit card and other personal loans, including point-of-sale financing as well as business and government loans.

- **Net premiums of $2,034 million,** up $177 million, or 9.5%.

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

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

- **Other operating income of $791 million**, down $28 million, or 3.4%, chiefly due to the following:
  - Increase in the contingent consideration payable as part of the acquisition of State Farm's Canadian operations.
  - Lower income on account of the subsidiaries sold in 2017, as presented in the "Impact of the sale of subsidiaries" section.
  - Offset by higher income from assets under management and from growth in credit card and point-of sale financing activities.

- **Investment income of $924 million**, up $1,986 million.
  - Increase mainly due to the fluctuation in the fair value of assets backing liabilities related to life and health insurance operations.
    - Increase offset for the most part by the change in actuarial liabilities that in turn led to an increase in expenses related to claims, benefits, annuities and changes in insurance contract liabilities.
    - Differences mostly attributable to changes in the fair value of the portfolio of stocks, bonds and derivatives.
  - Increase in the fair value of bonds in the Property and Casualty Insurance segment as a result of a slight drop in long-term interest rates on markets, while an increase had been recorded in the fourth quarter of 2016.
    - Change in the value of bonds offset by a similar increase in cost of claims because of a matching strategy.
  - Increase in the fair value of derivative financial instruments, including those associated with hedging operations for the Federation.
  - Offset by lower gains on disposal of investments for the fourth quarter of 2017, than for the corresponding quarter of 2016.

- **Total income of $4,106 million**, up $2,161 million.

- **Provision for credit losses of $74 million**, up $26 million, or 54.2%.
  - Recovery of the collective allowance in the fourth quarter of 2016 as a result, in particular, of refining the methodology used in the models for calculating the allowance. The Federation's loan portfolio continued to be of high quality.
  - Ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.14% as at December 31, 2017, down from 0.18% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of $2,120 million,** up $2,224 million.
  - **Wealth Management and Life and Health Insurance:** Expenses totalling $1,513 million, up $1,791 million compared to the same period in 2016, mainly as a result of an increase of $1,725 million in actuarial liabilities recognized under "Insurance contract liabilities", which included the effect of an increase in the fair value of matched investments.

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

- **Non-interest expense of $1,651 million**, up $91 million, or 5.8%, compared to 2016.
  - Increase caused for the most part by the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations as well as business growth, particularly in credit card and point-of-sale financing activities and assets under management.
  - Increase also due to purchases of computer hardware and the write-off of intangible assets.
  - Remuneration and other payments of $133 million, up $8 million, or 6.4%, compared to 2016.
    - Higher payments to member caisses as a result of the growth in sales by the network of various Desjardins Group products such as Desjardins Funds.

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

QUARTERLY TRENDS

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

Consolidated surplus earnings

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

Consolidated results

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

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

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

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

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

Surplus earnings from business segments

- **Surplus earnings before dividends to member caisses from the Personal and Business Services segment trending up steadily over the past eight quarters, except in fourth quarter 2017.**
  - Net interest income up on account of growth in the entire average portfolio of loans and acceptances outstanding.
  - Business growth as a result, in particular, of credit card and point-of-sale financing activities.
  - Growth in capital market activities.
  - Fourth quarter 2017 affected by a higher provision for credit losses while fourth quarter 2016 had benefited from the recovery of the collective allowance.

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

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

3.0 Balance sheet review

3.1 Balance sheet management

Table 15 – Consolidated Balance Sheets
As at December 31

(in millions of dollars and as a percentage)	2017		2016		2015	
Assets						
Cash and deposits with financial institutions	**$ 1,731**	**1.2%**	$ 1,212	0.9%	$ 1,006	0.8%
Securities	**46,904**	**32.2**	44,937	33.4	43,115	33.5
Securities borrowed or purchased under reverse repurchase agreements	**9,377**	**6.4**	7,713	5.7	8,046	6.3
Net loans and acceptances	**58,715**	**40.3**	52,441	38.9	51,084	39.7
Segregated fund net assets	**13,379**	**9.2**	11,965	8.9	9,781	7.6
Derivative financial instruments	**3,772**	**2.6**	3,706	2.8	4,879	3.8
Other assets	**11,862**	**8.1**	12,684	9.4	10,746	8.3
Total assets	**$ 145,740**	**100.0%**	$ 134,658	100.0%	$ 128,657	100.0%
Liabilities and equity						
Deposits	**$ 52,149**	**35.8%**	$ 46,902	34.8%	$ 47,922	37.2%
Commitments related to securities sold short	**9,112**	**6.3**	8,196	6.1	5,464	4.2
Commitments related to securities lent or sold under repurchase agreements	**10,062**	**6.9**	9,870	7.3	9,283	7.2
Derivative financial instruments	**3,677**	**2.5**	2,540	1.9	2,478	1.9
Insurance contract liabilities	**28,300**	**19.4**	27,493	20.4	26,734	20.8
Segregated fund net liabilities	**13,354**	**9.2**	11,957	8.9	9,776	7.6
Other liabilities	**11,679**	**7.9**	11,642	8.7	11,529	9.0
Subordinated notes	**1,388**	**1.0**	1,378	1.0	1,884	1.5
Equity	**16,019**	**11.0**	14,680	10.9	13,587	10.6
Total liabilities and equity	**$ 145,740**	**100.0%**	$ 134,658	100.0%	$ 128,657	100.0%

TOTAL ASSETS

As at December 31, 2017, the Federation's total assets stood at $145.7 billion, up by $11.1 billion, or 8.2%, over the year, compared to growth of $6.0 billion, or 4.7%, for 2016. This growth was largely due to an increase in net loans and acceptances as well as securities, including those borrowed or purchased under reverse repurchase agreements.

CASH AND DEPOSITS WITH FINANCIAL INSTITUTIONS, AND SECURITIES

As at December 31, 2017, the Federation's cash and deposits with financial institutions amounted to $1.7 billion, an increase of $519 million, or 42.8%, over the year, compared to an increase of $206 million, or 20.5%, in 2016. Securities, including those borrowed or purchased under reverse repurchase agreements, totalled $56.3 billion, an increase of $3.6 billion, or 6.9%, over the year, compared to a volume of $52.7 billion in 2016, and an increase of $1.5 million, or 2.9% in 2016. The Federation's market and deposit activities generated the increase.

LOANS AND CLIENTS' LIABILITY UNDER ACCEPTANCES

Loans

As at December 31, 2017, the Federation's outstanding loan portfolio, including clients' liability under acceptances, net of the allowance for credit losses, was $58.7 billion, an increase of $6.3 billion, or 12.0%, compared to growth of $1.4 billion, or 2.7%, during 2016. Among the different borrower categories presented in Table 16 are loans to business and government, which accounted for 62.9% of the Federation's total portfolio as at December 31, 2017. The amount outstanding on that date was $37.0 billion, up $3.6 billion, or 10.8%, since December 31, 2016, compared to a decrease of $279 million, or 0.8%, a year earlier. Loans to member caisses, which are included in loans to business and government, increased by $2.3 billion compared to December 31, 2016, to stand at $26.2 billion at the end of the year, compared to a decrease of $79 million a year earlier.

Table 16 – Loans and acceptances
As at December 31

(in millions of dollars and as a percentage)	2017		2016		2015	
Residential mortgages	**$ 4,323**	**7.3%**	$ 3,486	6.6%	$ 2,861	5.6%
Consumer, credit card and other personal loans	**17,547**	**29.8**	15,720	29.9	14,697	28.7
Business and government	**37,043**	**62.9**	33,427	63.5	33,706	65.7
	58,913	**100.0%**	52,633	100.0%	51,264	100.0%
Allowance for credit losses	**(198)**		(192)		(180)	
Total loans and acceptances by borrower category	**$ 58,715**		$ 52,441		$ 51,084	
Loans guaranteed or insured[(1)]	**$ 5,609**		$ 5,196		$ 5,553	
Loans guaranteed or insured[(1)] as a percentage of total gross loans and acceptances	**9.5%**		9.9%		10.8%	

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

Consumer, credit card and other personal loans accounted for 29.8% of the Federation's total loan portfolio as at December 31, 2017. These loans increased by $1.8 billion, or 11.6%, over the year, to total $17.5 billion at year-end, compared to growth of $1.0 billion, or 7.0%, as at December 31, 2016. Loans from Card and Payment Services generated most of this growth as a result, in particular, of an increase in loans related to automobile and durable goods financing.

The Federation's outstanding residential mortgages, which accounted for 7.3% of its total portfolio, totalled $4.3 billion, an increase of $837 million, or 24.0%, since December 31, 2016, compared to an increase of $625 million, or 21.8%, a year earlier.

Credit quality

As at December 31, 2017, the Federation's loan portfolio continued to be of high quality. Outstanding gross impaired loans stood at $84 million, down $11 million, or 11.6%, since the end of 2016, compared to an increase of $10 million, or 11.8%, a year earlier. The gross impaired loan ratio, as a percentage of the total gross loan portfolio, was 0.14% at the end of 2017, down from the ratio of 0.18% in 2016. Improved economic conditions helped to reduce the volume of gross impaired loans.

The Federation's loans guaranteed or insured by governments and other public and parapublic institutions accounted for 9.5% of its total loan portfolio as at December 31, 2017.

Additional information about the quality of the Federation's loan portfolio is presented in section 4.2, "Risk management", on pages 65 to 68 of this MD&A.

DEPOSITS

Table 17 – Deposits
As at December 31

(in millions of dollars and as a percentage)	2017					2016		2015	
	Payable on demand	**Payable upon notice**	**Payable on a fixed date**	**Total**	**Total**	Total		Total	
Individuals	**$ 3,154**	**$ 50**	**$ 1,149**	**$ 4,353**	**8.3%**	$ 3,817	8.1%	$ 2,518	5.3%
Business and government	**3,452**	**-**	**37,511**	**40,963**	**78.6**	36,780	78.5	38,925	81.2
Deposit-taking institutions	**2,757**	**-**	**4,076**	**6,833**	**13.1**	6,305	13.4	6,479	13.5
Total deposits	**$ 9,363**	**$ 50**	**$ 42,736**	**$ 52,149**	**100.0%**	$ 46,902	100.0%	$ 47,922	100.0%

As at December 31, 2017, the Federation's outstanding deposits totalled $52.1 billion, up by $5.2 billion, or 11.2%, since the end of 2016, compared to a decrease of $1.0 billion, or 2.1%, a year earlier. This increase in the Federation's deposits was largely the result of growth in business and government deposits, which accounted for 78.6% of its total outstanding deposit portfolio as at the end of 2017. Business and government loans outstanding amounted to $41.0 billion as at December 31, 2017, up $4.2 billion, or 11.4%, since December 31, 2016, compared to a decrease of $2.1 billion, or 5.5%, a year earlier. This increase was due in particular to the various securities issued on U.S., Canadian and European markets, which supported the growth in Desjardins Group's funding requirements.

Deposits from individuals were up $536 million, or 14.0%, on an annual basis to total $4.4 billion at year-end 2017, compared to an increase of $1.3 billion, or 51.6%, during 2016. Deposits from deposit-taking institutions stood at $6.8 billion as at December 31, 2017, up $528 million, or 8.4%, whereas they had decreased by $174 million, or 2.7% a year earlier. Deposits from member caisses, included in the deposits from deposit-taking institutions, were down by $16 million to total $5.0 billion.

Additional information about sources of financing can be found on pages 74 and 75, while the Federation's liquidity risk management policy is discussed on page 73.

INSURANCE CONTRACT LIABILITIES

As at December 31, 2017, the Federation's insurance contract liabilities were $28.3 billion, up $807 million, or 2.9%, from December 31, 2016, compared to a $759 million, or 2.8%, increase observed a year earlier. This growth is partially due to higher actuarial liabilities as a result of life and health insurance operations, which grew by $854 million.

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

EQUITY

As at December 31, 2017, equity totalled $16.0 billion, up $1.3 billion, or 9.1% compared to an increase of $1.1 billion, or 8.0%, a year earlier. Net surplus earnings after dividends to member caisses, totalling $1,372 million, were a source of this growth. In addition, the Federation issued F capital shares for proceeds of $249 million, net of issuance expenses, as well as F capital shares having a value of $125 million for the payment of interest when the holder has elected to receive remuneration in F capital shares. Payments of $68 million to member caisses as well as remuneration of $167 million on the Federation's capital shares reduced equity.

Note 22, "Capital stock", to the Annual Consolidated Financial Statements provides additional information about the Federation's capital stock.

3.2 Capital management

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

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

The global financial crisis prompted the industry to place more emphasis on sound capitalization of its operations. Now more than ever, rating agencies and the market favour the best-capitalized institutions. These factors argue in favour of a general increase in the level and quality of capital issued by financial institutions. This is also reflected in the enhanced requirements under Basel III implemented on January 1, 2013.

Desjardins Group's Integrated Capital Management Framework

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

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

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

Regulatory framework and internal policies

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

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

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

The minimum amount of Tier 1A capital that the Federation must maintain is 8%. In addition, the Tier 1 and total capital ratios must be above 9.5% and 11.5%, respectively. The minimum requirement for the leverage ratio is 3%.

This capital takes into consideration investments made in subsidiaries of the Federation. Some of these subsidiaries are subject to separate requirements regarding regulatory capital, liquidity and financing, which are set by regulatory authorities governing banks, insurers and securities, in particular. The Federation oversees and manages the capital requirements of these entities to ensure efficient use of capital and continuous compliance with the applicable regulation.

In this regard, it should be mentioned that the life and health insurance subsidiaries under provincial jurisdiction are subject to the Capital Adequacy Requirements Guideline (CARLI) issued by the AMF. The property and casualty insurance subsidiaries under provincial jurisdiction must comply with the Guideline on Capital Adequacy Requirements issued by the AMF. The property and casualty insurance subsidiaries under federal jurisdiction must comply with the OSFI's Minimum Capital Test (MCT) Guideline for federally regulated property and casualty insurance companies. Developments in these guidelines are presented in the "Changes in the regulatory environment" section on pages 9 to 11 of this MD&A.

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

Regulatory developments

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

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

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

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

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

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

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

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

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

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

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

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

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

Compliance with requirements

As at December 31, 2017, the Tier 1A, Tier 1 and total capital ratios, calculated in accordance with Basel III requirements, were all 17.5%. The leverage ratio was 7.9%.

The Federation and its subsidiaries, which are subject to minimum regulatory requirements with respect to capitalization were in compliance with said requirements as at December 31, 2017.

Regulatory capital

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

Table 18 – Main capital components

	Total capital		
	Tier 1 capital		Tier 2 capital
	Tier 1A[1]	Tier 1B[1]	
Eligible items	• Reserves and undistributed surplus earnings • Eligible accumulated other comprehensive income • Capital shares	• Non-controlling interests[2]	• Eligible collective allowance • Subordinated notes subject to phase-out • Eligible qualifying shares
Regulatory adjustments	• Goodwill • Software • Other intangible assets • Deferred tax assets essentially resulting from loss carryforwards • Shortfall in allowance • Cross-investments[3]		
Deductions	• Mainly significant investments in financial institutions[4]		• Investment in preferred shares of a component deconsolidated for regulatory capital purposes • Subordinated financial instrument

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

Table 19 – Regulatory capital
As at December 31

(in millions of dollars and as a percentage)	2017	2016
Tier 1A capital		
Federation's capital shares	**$ 4,501**	$ 4,127
Other capital shares	**4,036**	3,939
Reserves	**540**	524
Undistributed surplus earnings	**5,655**	4,765
Eligible accumulated other comprehensive income	**456**	386
Non-controlling interests	**-**	32
Deductions(1)(2)	**(6,026)**	(6,456)
Total Tier 1A capital	**9,162**	7,317
Non-controlling interests	**13**	19
Deductions(1)	**(13)**	(19)
Total Tier 1B capital	**-**	-
Total Tier 1 capital	**9,162**	7,317
Tier 2 capital		
Subordinated notes subject to phase-out	**1,032**	1,200
Eligible collective allowance	**126**	132
Other eligible instruments	**-**	-
Non-controlling interests	**-**	6
Deductions(1)	**(1,158)**	(1,338)
Total Tier 2 capital	**-**	-
Total regulatory capital (Tiers 1 and 2)	**$ 9,162**	$ 7,317
Ratios and leverage ratio exposure		
Tier 1A capital ratio(3)	**17.5%**	15.9%
Tier 1 capital ratio(3)	**17.5**	15.9
Total capital ratio(3)	**17.5**	15.9
Leverage ratio(4)	**7.9**	7.4
Leverage ratio exposure	**$ 115,915**	$ 98,892

(1) As prescribed by the guideline, when an entity is required to make a deduction from a given capital component but is not adequately provisioned, the difference is deducted from the component of the next highest quality. If Tier 2 capital is insufficient to absorb a deduction, the undeducted portion will be deducted from Tier 1B, and then from Tier 1A, if necessary.
(2) Deductions from Tier 1A are comprised of regulatory adjustments ($2,152 million in 2017 and $1,886 million in 2016), of which cross-investments ($1,634 million in 2017 and $1,318 million in 2016), significant investments ($3,137 million in 2017 and $3,841 million in 2016), deferred tax assets attributable to temporary differences ($0 million in 2017 and $16 million in 2016), and items that could not be deducted from Tiers 1B and 2 because of insufficient capital in these tiers ($737 million in 2017 and $713 2016).
(3) As prescribed by the guideline, the capital ratios are expressed as a percentage of regulatory capital to risk-weighted assets.
(4) The leverage ratio is calculated according to the guideline as a nonrisk-based measure and is defined as the capital measure (namely Tier 1 capital) divided by the exposure measure. The exposure measure includes: 1) on-balance sheet exposures, 2) securities financing transaction exposures, 3) derivative exposures, and 4) off-balance sheet items.

In compliance with Basel III requirements, capital instruments that no longer meet the eligibility criteria for capital tiers have been excluded from them effective January 1, 2013, as prescribed. In accordance with the transitional provisions set out in the guideline, instruments that meet certain conditions are being phased out from capital at an annual rate of 10% over a nine-year period that began on January 1, 2013. The subordinated notes issued by Desjardins Capital Inc. are also subject to the 10% amortization. In order to be fully eligible for Tier 2 capital, such notes must meet Non-Viability Contingent Capital (NVCC) requirements. Desjardins Group has not issued any instruments of this type as discussions concerning the application of these regulations by Desjardins Group are still in progress with the AMF.

On December 21, 2017, the Federation filed a new short-form prospectus and obtained a receipt allowing it to issue, in the 12 months following the date of the receipt, F capital shares for a maximum amount of $125 million. This new issue started on January 23, 2018. During 2017, the Federation issued F capital shares for proceeds of $249 million, net of issuance expenses. It also issued F capital shares for an amount of $125 million in order to pay interest where a holder elected to receive remuneration in capital shares.

The Federation issued A capital shares during the year for a cash consideration of $25 million. In addition, on October 27, 2016, the Federation's Board of Directors approved the creation of a new class of capital shares, class G. On January 1, 2017, namely the date of the merger, the CCD capital shares issued and outstanding were converted into G capital shares issued to members of the Federation. CCD capital shares have not been part of the Federation's authorized share capital since the merger date. The Federation issued G capital shares for a cash consideration of $72 million in 2017.

On December 7, 2017, the Federation's Board of Directors approved the distribution to member caisses of net income of $60 million and $8 million, respectively, in respect of FIN-5A and INV capital shares.

As at December 31, 2017, the Tier 1A capital ratio was up 156 basis points compared to a year earlier. The positive impact of growth in surplus earnings and reserves, as well as the issuance of F capital shares was offset by the increase in risk-weighted assets. On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, Western Financial Group Inc. and Western Life Assurance Company, which contributed to the increase in the Tier 1A capital ratio.

Table 20 – Change in regulatory capital
As at December 31

(in millions of dollars)	2017
Tier 1A capital	
Balance at beginning of year	**$ 7,317**
Increase in reserves and undistributed surplus earnings[1]	**906**
Eligible accumulated other comprehensive income	**70**
Federation's capital shares	**374**
Other capital shares	**97**
Non-controlling interests	**(32)**
Deductions	**430**
Balance at end of year	**9,162**
Tier 1B capital	
Balance at beginning of year	**-**
Non-controlling interests	**(6)**
Deductions	**6**
Balance at end of year	**-**
Total Tier 1 capital	**9,162**
Tier 2 capital	
Balance at beginning of year	**-**
Non-controlling interests	**(6)**
Senior notes subject to phase-out	**(168)**
Eligible collective allowance	**(6)**
Deductions	**180**
Balance at end of year	**-**
Total capital	**$ 9,162**

[1] Amount including the change in defined benefit pension plan liabilities.

Risk-weighted assets (RWA)

The Federation calculates the risk-weighted assets for credit risk, market risk and operational risk. It uses the Internal Ratings-Based Approach for credit risk related to retail loan portfolios − Personal. Other exposures to credit and market risk are measured according to the Standardized Approach. On June 19, 2017, the Federation received the AMF's authorization to use the Standardized Approach for calculating operational risk as of the second quarter of 2017.

As indicated in the table below, risk-weighted assets totalled $52.4 billion as at December 31, 2017. Of this amount, $42.5 billion was for credit risk, $2.0 billion for market risk and $8.1 billion for operational risk. As at December 31, 2016, risk-weighted assets stood at $45.9 billion.

Table 21 - Risk-weighted assets

	Internal Ratings-Based Approach		Standardized Approach		Total as at December 31, 2017				Total as at December 31, 2016
(in millions of dollars and as a percentage)	Exposure[1]	Risk-weighted assets	Exposure[1]	Risk-weighted assets	Exposure[1]	Risk-weighted assets	Capital requirement[2]	Average risk weighting rate	Risk-weighted assets
Credit risk other than counterparty risk									
Sovereign borrowers	**$ -**	**$ -**	**$ 5,669**	**$ 21**	**$ 5,669**	**$ 21**	**$ 2**	**0.4%**	$ -
Financial institutions	**-**	**-**	**37,772**	**7,601**	**37,772**	**7,601**	**608**	**20.1**	5,330
Businesses	**-**	**-**	**13,331**	**12,989**	**13,331**	**12,989**	**1,039**	**97.4**	12,491
Securitizations	**-**	**-**	**6**	**75**	**6**	**75**	**6**	**1,250.0**	1,138
Equities	**-**	**-**	**152**	**241**	**152**	**241**	**19**	**158.6**	98
SMEs similar to other retail client exposures	**-**	**-**	**1,681**	**1,288**	**1,681**	**1,288**	**103**	**76.6**	1,048
Mortgages	**1,806**	**183**	**411**	**146**	**2,217**	**329**	**26**	**14.8**	207
Other retail client exposures (excluding SMEs)	**5,791**	**2,986**	**278**	**221**	**6,069**	**3,207**	**257**	**52.8**	2,396
Qualifying revolving retail client exposures	**29,819**	**8,110**	**-**	**-**	**29,819**	**8,110**	**649**	**27.2**	6,881
Subtotal - Credit risk other than counterparty risk	**37,416**	**11,279**	**59,300**	**22,582**	**96,716**	**33,861**	**2,709**	**35.0**	29,589
Counterparty risk									
Sovereign borrowers	**-**	**-**	**8**	**-**	**8**	**-**	**-**	**-**	-
Financial institutions	**-**	**-**	**1,711**	**343**	**1,711**	**343**	**27**	**20.0**	316
Businesses	**-**	**-**	**5**	**4**	**5**	**4**	**-**	**80.0**	8
Trading portfolio	**-**	**-**	**1,312**	**374**	**1,312**	**374**	**30**	**28.5**	192
Credit valuation adjustment charge	**-**	**-**	**-**	**-**	**-**	**910**	**74**	**-**	808
Additional requirements for banking and trading portfolio	**-**	**-**	**-**	**-**	**68**	**1**	**-**	**-**	1
Subtotal - Counterparty risk	**-**	**-**	**3,036**	**721**	**3,104**	**1,632**	**131**	**52.6**	1,325
Other assets[3]	**-**	**-**	**-**	**-**	**16,805**	**6,340**	**507**	**37.7**	4,320
Scaling factor[4]	**-**	**677**	**-**	**-**	**-**	**677**	**54**	**-**	551
Total credit risk	**37,416**	**11,956**	**62,336**	**23,303**	**116,625**	**42,510**	**3,401**	**36.5**	35,785
Market risk									
Interest rate position risk	**-**	**-**	**-**	**1,692**	**-**	**1,692**	**135**	**-**	1,428
Currency risk	**-**	**-**	**-**	**151**	**-**	**151**	**12**	**-**	262
Additional requirements for other risks[5]	**-**	**-**	**-**	**122**	**-**	**122**	**10**	**-**	120
Total market risk	**-**	**-**	**-**	**1,965**	**-**	**1,965**	**157**	**-**	1,810
Operational risk[6]	**-**	**-**	**-**	**8,143**	**-**	**8,143**	**651**	**-**	8,612
Total risk-weighted assets before threshold	**37,416**	**11,956**	**62,336**	**33,411**	**116,625**	**52,618**	**4,209**	**-**	46,207
Risk-weighted assets (RWA) after the transitional provisions for the credit valuation adjustment charge[7]									
RWA for Tier 1A capital	**-**	**-**	**-**	**-**	**-**	**52,364**	**4,189**	**-**	45,916
RWA for Tier 1 capital	**-**	**-**	**-**	**-**	**-**	**52,409**	**4,193**	**-**	45,972
RWA for total capital	**-**	**-**	**-**	**-**	**-**	**52,445**	**4,196**	**-**	46,021
Total risk-weighted assets	**$ 37,416**	**$ 11,956**	**$ 62,336**	**$ 33,411**	**$ 116,625**	**$ 52,364**	**$ 4,189**	**-%**	$ 45,916

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

3.3 Off-balance sheet arrangements

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

ASSETS UNDER MANAGEMENT AND UNDER ADMINISTRATION

As at December 31, 2017, the Federation administered, for the account of its members and clients, assets totalling $420.0 billion. This represented an annual decrease of $8.1 billion, or 1.9%, compared to an increase of $17.2 billion, or 4.2%, recorded as at December 31, 2016. The decrease was mainly due to custodial services for institutional securities. Financial assets placed with the Federation as wealth manager amounted to $66.7 billion at the close of 2017, compared to $59.5 billion as at December 31, 2016, for an increase of $7.2 billion, or 12.0% on an annual basis, compared to an increase of $5.9 billion, or 11.1%, in 2016. The increase was chiefly due to growth in Desjardins Funds.

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

Table 22 – Assets under management and under administration
As at December 31

(in millions of dollars)	2017	2016	2015
Assets under management			
Institutions and individuals	**$ 15,263**	$ 12,205	$ 11,595
Investment funds[1]	**51,390**	47,285	41,966
Total assets under management	**$ 66,653**	$ 59,490	$ 53,561
Assets under administration			
Individual and institutional trust and custodial services	**$ 313,517**	$ 326,798	$ 321,401
Investment funds[1]	**106,464**	101,308	89,457
Total assets under administration	**$ 419,981**	$ 428,106	$ 410,858

[1] Including Desjardins Funds and Northwest and Ethical Investments.

CREDIT INSTRUMENTS

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

Note 28, "Commitments, guarantees and contingent liabilities", to the Federation's Consolidated Financial Statements provides more detailed information about these credit instruments.

GUARANTEES

The Federation also enters into various guarantee and indemnification agreements with its clients in the normal course of operations. These agreements remain off-balance sheet arrangements and include guarantees, standby letters of credit and credit default swaps. Note 28, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements provides information about these off-balance sheet arrangements.

ASSETS PLEDGED AND HELD AS COLLATERAL

In the normal course of business, the Federation holds financial assets as collateral as a result of transactions involving securities borrowed or those purchased under reverse repurchase agreements. Note 28, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements provides additional information about assets held as collateral.

STRUCTURED ENTITIES

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

Master Asset Vehicle (MAV) trusts

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

Securitization of the Federation's financial assets

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

4.0 Risk management

The shaded areas and tables marked with an asterisk (*) in this section contain information about credit, market and liquidity risks in accordance with IFRS 7, "Financial Instruments: Disclosures". They also contain an analysis of how the Federation assesses its risks as well as a description of its risk management objectives, policies and methods. IFRS 7 provides that risk disclosures may be included in the MD&A. Consequently, the shaded areas and tables marked with an asterisk (*) are an integral part of the Consolidated Financial Statements, as explained in Note 30, "Financial instrument risk management", to the Consolidated Financial Statements.

4.1 Risk factors that could impact future results

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

Principal risks and emerging risks

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

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

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

Other risk factors that could impact future results

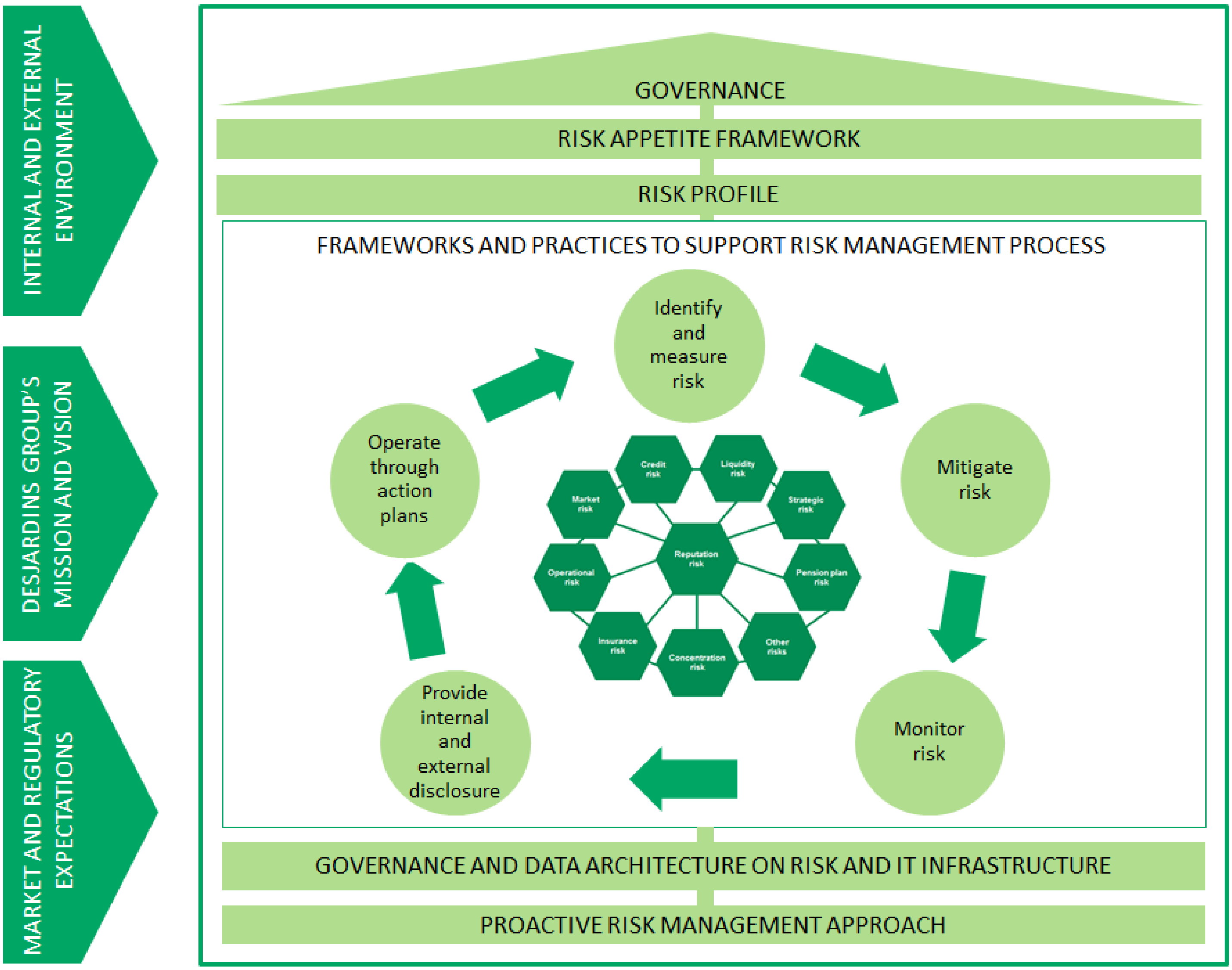
Risk factors	Description
General economic and business conditions in regions in which Desjardins Group operates	General economic and business conditions in the regions in which Desjardins Group operates may significantly affect its revenues and surplus earnings. These conditions include short and long-term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

Risk factors	Description
Critical accounting estimates and accounting standards	The Consolidated Financial Statements were prepared in accordance with the IFRS. The accounting policies used by Desjardins Group determine how it reports its financial position and results of operations, and management may be required to make estimates or rely on assumptions about matters that are inherently uncertain. Any change in these estimates and assumptions may have a significant impact on Desjardins Group's financial position and results of operations. Also note the upcoming compliance with IFRS 9, which incorporates a forward-looking perspective in calculating allowances for credit losses (2018 implementation), and IFRS 17, which has just amended the measurement rules for actuarial liabilities in insurance (scheduled implementation in 2021). These new standards may affect the organization's financial results.
New products and services to maintain or increase market share	Strong competitive pressures from Canadian financial institutions and the emergence of new competitors have led Desjardins Group to develop new products and services at a faster pace to maintain or increase its attractiveness as a financial institution with its clients. Developing these new products and services could require large investments by Desjardins or involve risks not identified at the time of their development. Desjardins cannot be certain that the new products and services it offers will result in the anticipated financial benefits.
Geographic concentration	The Federation's operations are heavily concentrated in Quebec. As at December 31, 2017, Desjardins Group's loans to Quebec members and clients therefore accounted for 84.8% of its aggregate loan portfolio. As a result of this significant geographic concentration, its results largely depend on economic conditions in Quebec. Any deterioration in these conditions could adversely impact: • past due loans; • problem assets and foreclosed property; • claims and lawsuits; • the demand for products and services; • the value of collateral available for loans, especially mortgages, and by extension, clients' and members' borrowing capacity, the value of assets associated with impaired loans and collateral coverage.
Acquisitions and joint arrangements	Desjardins Group has implemented a rigorous internal control environment for the acquisition and joint arrangement processes. Nevertheless, its financial or strategic objectives could fail to be met because of unexpected factors such as delays in approval of transactions by regulators or their imposing of additional conditions, the inability to apply the strategic plan in its original form, difficulties in integrating or retaining clients, an increase in regulatory costs, unexpected expenses, or changes in the economic and competitive environment. As a result, synergies, higher income, cost savings, increased market share and other expected benefits may not materialize or may be delayed, thereby impacting Desjardins Group's future surplus earnings. The integration of State Farm's Canadian operations within Desjardins Group is progressing satisfactorily, particularly with regard to the consolidation of the functions related to the use of State Farm banners and trademark during a certain period of time after the closing. Similarly, the agreement regarding the rendering of certain transitional services to Desjardins Group by State Farm during the period agreed upon after the closing is working out as scheduled. However, fully achieving the benefits anticipated by Desjardins Group will depend on its ability to capitalize on growth opportunities. Desjardins Group still risks experiencing problems up to the end of the integration and transition process, which could have an unfavourable impact on its operations, financial position, results of operations and cash flows.
Credit ratings	The credit ratings assigned to Desjardins Group by rating agencies are instrumental to its access to sources of wholesale funding and the cost of such funding. These ratings may be revised or withdrawn at any time by the agencies. In addition, a significant downgrade to various ratings could raise Desjardins Group's cost of funding, reduce its access to capital markets, and increase additional obligations required by its counterparties.
Catastrophes and climate change	Catastrophes are events whose unforeseeable nature and severity may have a material impact on Desjardins Group's results. More specifically, the financial results of Desjardins P&C insurance subsidiaries, given the nature of their operations, are more significantly affected by natural disasters. The risks associated with catastrophes and climate change are subject to specific governance within the P&C insurance subsidiaries as well as to mitigation measures, the most important of which is still the catastrophe reinsurance treaty, under which the volatility of financial results can be reduced. Desjardins Group understands the challenge posed by climate change to its P&C insurance operations and is an active participant in various industry initiatives. Moreover, Desjardins and its P&C insurance subsidiaries have set up a management structure to coordinate their activities and promote the rapid deployment of personnel in order to provide the best possible support to their insureds given the sufficiently high frequency of such extreme weather events.
Other factors	Other factors that may have an impact on Desjardins Group's future results include changes in tax laws, unexpected changes in consumer spending and saving habits, the ability to implement Desjardins Group's disaster recovery plan within a reasonable time, the possible impact of international conflicts on operations, and Desjardins Group's ability to anticipate and manage the risks associated with these factors properly despite a disciplined risk management environment. Desjardins Group cautions the reader that factors other than the foregoing could affect future results. Investors and other stakeholders relying on forward-looking statements to make decisions with respect to Desjardins Group should carefully consider these factors as well as other uncertainties, potential events, and industry factors or other items specific to Desjardins Group that could adversely impact its future results.

4.2 Risk management

Integrated risk management framework

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



RISK IDENTIFICATION

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

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

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

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

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

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

RISK MEASUREMENT

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

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

Desjardins-wide integrated stress testing

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

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

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

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

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

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

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

Governance and model validation

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

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

RISK DISCLOSURE

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

RISK APPETITE

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

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

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

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

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

PROACTIVE RISK MANAGEMENT APPROACH

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

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

Other methods used to support the proactive risk management approach and to promote accountability for risk include:

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

Risk management and the Integrated Risk Management Framework are based on the following guidelines that provide in particular for:

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

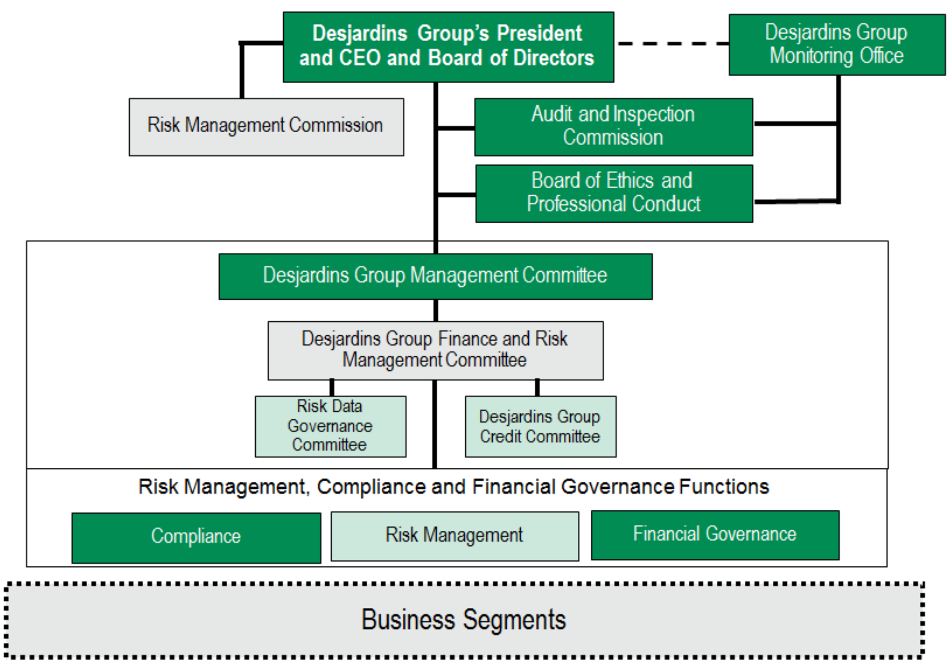
Compensation in relation to risk management

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

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

RISK MANAGEMENT GOVERNANCE

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



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

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

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

Operations management approach based on the Three Lines of Defence model

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

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

1st Line of Defence

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

2nd Line of Defence

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

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

3rd Line of Defence

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

Basel capital accord

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

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

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

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

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

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

Credit risk

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

The Federation is exposed to credit risk first through its direct personal, business and government loans, which accounted for 40.3% of assets on the Consolidated Balance Sheets as at December 31, 2017, compared to 38.9% at the end of 2016. It is also exposed through various other commitments, including letters of credit and transactions involving derivative financial instruments as well as securities transactions.

CREDIT RISK MANAGEMENT

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

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

Framework

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

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

Assessment of credit and counterparty risk

The Federation uses two approaches to calculate its credit and counterparty risk, namely the Standardized Approach and the Internal Ratings-Based Approach. The Federation has adopted the Internal Ratings-Based Approach for credit risk related to loan portfolios of retail clients – Personal. Credit risk exposures are presented in the capital management section on page 51.

Credit granting

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

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

Retail loans

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

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

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

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

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

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

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

Table 23 presents PD tranches in relation to risk levels.

Table 23 – Probabilities of default of retail clients by risk level*

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

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

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

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

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

More specifically for PD, such back testing takes the form of various statistical tests to assess the following criteria:
- model's discriminating power;
- calibration of the model;
- stability of model results.

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

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

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

Table 24 – Exposure to credit risk of retail loan portfolios[(1)]*
As at December 31

	2017				2016
	EAD				
(in millions of dollars)	**Exposures related to residential mortgage loans**	**Qualifying revolving retail client exposures**	**Other retail client exposures**	**Total**	Total
Excellent	**$ 420**	**$ 9,205**	**$ 11**	**$ 9,636**	$ 16,974
Very low	**499**	**11,954**	**236**	**12,689**	3,550
Low	**792**	**6,366**	**2,187**	**9,345**	8,138
Average	**81**	**1,054**	**3,122**	**4,257**	3,101
High	**10**	**1,132**	**195**	**1,337**	1,377
Default	**4**	**108**	**40**	**152**	147
Total	**$ 1,806**	**$ 29,819**	**$ 5,791**	**$ 37,416**	$ 33,287

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

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

Table 25 – Exposures to retail clients by risk tranche[(1)]*
As at December 31

	2017								2016
	Risk tranches								
(in millions of dollars)	**0%**	**20%**	**35%**	**50%**	**75%**	**100%**	**Other**	**Total**	Total
Residential mortgages	**$ -**	**$ -**	**$ 408**	**$ -**	**$ -**	**$ 3**	**$ -**	**$ 411**	$ 143
Other retail client exposures (except for SMEs)	**-**	**-**	**-**	**-**	**1,455**	**49**	**1**	**1,505**	1,538
Total	**$ -**	**$ -**	**$ 408**	**$ -**	**$ 1,455**	**$ 52**	**$ 1**	**$ 1,916**	$ 1,681

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

Loans to businesses, sovereign borrowers and financial institutions

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

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

Table 26 – Exposures to businesses, sovereign borrowers and financial institutions by risk tranche[(1)]*

As at December 31

	2017								2016
	Risk tranches								
(in millions of dollars)	0%	20%	35%	50%	75%	100%	Other	Total	Total
Sovereign borrowers	$ 931	$ -	$ -	$ -	$ -	$ -	$ -	$ 931	$ 694
Financial institutions	-	34,765	-	13	-	24	3	34,805	25,084
Businesses	-	-	-	566	-	11,680	245	12,491	11,650
SMEs similar to other retail client exposures	-	-	-	-	1,496	72	13	1,581	1,368
Total	**$ 931**	**$ 34,765**	**$ -**	**$ 579**	**$ 1,496**	**$ 11,776**	**$ 261**	**$ 49,808**	$ 38,796

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

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

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

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

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

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

Other segments

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

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

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

Credit risk mitigation

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

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

For some portfolios, programs offered by various organizations, in particular Canada Mortgage and Housing Corporation (CMHC) and *La Financière agricole du Québec*, are used in addition to customary collateral. As at December 31, 2017, the Federation's guaranteed or insured loans represented 9.5% of the total gross loans, compared to 9.9% at the end of 2016.

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

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

Loan debt relief

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

File monitoring and management of higher risk files

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

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

Default situations

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

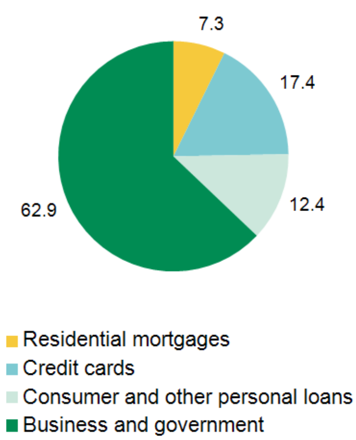
Monitoring of portfolio and reporting

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

BREAKDOWN AND QUALITY OF LOAN PORTFOLIO

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

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



Loans by borrower category and by industry are presented in the table below. As at December 31, 2017, the main sectors of the business loan portfolio were finance and insurance, real estate, and manufacturing, which accounted for 84.9% of the business loan portfolio amounting to $35.1 billion. The main industries are the same as they were as at December 31, 2016.

Table 27 – Loans by borrower category and by industry
As at December 31

(in millions of dollars)	**2017**		2016		2015	
	Gross loans	**Gross impaired loans**	Gross loans	Gross impaired loans	Gross loans	Gross impaired loans
Residential mortgages	**$ 4,323**	**$ 8**	$ 3,486	$ 2	$ 2,861	$ 3
Consumer, credit card and other personal loans	**17,547**	**72**	15,720	82	14,697	73
Public bodies[(1)]	**1,910**	**-**	1,037	-	1,863	-
Business						
Agriculture	**125**	**-**	196	1	114	1
Mining, and oil and gas	**258**	**-**	201	-	332	-
Utilities	**379**	**1**	321	-	283	-
Construction	**730**	**-**	644	1	551	1
Manufacturing	**1,193**	**2**	902	5	1,002	4
Wholesale trade	**384**	**-**	258	-	255	-
Retail trade	**478**	**-**	480	1	405	-
Transportation	**468**	**-**	436	-	401	-
Information industry	**218**	**-**	196	-	164	-
Finance and insurance	**26,804**	**-**	24,254	-	23,552	-
Real estate	**1,810**	**-**	3,510	1	3,266	1
Professional services	**166**	**-**	169	-	127	-
Management of companies	**168**	**-**	87	-	128	-
Administrative services	**13**	**-**	39	-	47	-
Education	**-**	**-**	6	-	3	-
Health care	**126**	**1**	42	-	40	-
Arts and entertainment	**79**	**-**	91	-	91	-
Accommodation	**36**	**-**	89	1	73	-
Other services	**147**	**-**	206	-	165	-
Other businesses	**1,520**	**-**	252	1	468	2
Total business loans	**$ 35,102**	**$ 4**	$ 32,379	$ 11	$ 31,467	$ 9
Total loans	**$ 58,882**	**$ 84**	$ 52,622	$ 95	$ 50,888	$ 85

(1) Including loans to governments.

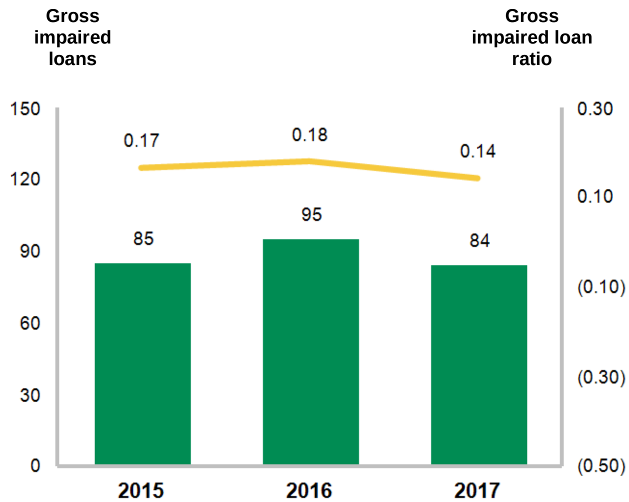
The chart below presents gross impaired loans. As at December 31, 2017, gross impaired loans outstanding stood at $84 million, down $11 million since December 31, 2016. The ratio of gross impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.14% at the end of 2017, down from 0.18% as at December 31, 2016. Improved economic conditions helped to reduce the volume of gross impaired loans. The Federation's loan portfolio continues to be of high quality.

Individual allowances for credit losses, which totalled $9 million as at December 31, 2017, made it possible to obtain a total coverage ratio of 10.7% of the gross impaired loan portfolio, compared to a ratio of 5.3% at the end of 2016.

The collective allowance stood at $189 million as at December 31, 2017, which was up slightly from $187 million recorded at the end of 2016. In addition, an allowance for risk related to off-balance sheet arrangements of $40 million was recognized as at December 31, 2017 under "Other liabilities – Other" on the Consolidated Balance Sheets, down $6 million compared to the amount posted as at December 31, 2016. The collective allowance reflects the best estimate of the allowance for credit losses that have not yet been designated individually as impaired loans.

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

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



Tables 28 and 29 present the gross impaired loans by Federation borrower category and the change in the gross impaired loan balance.

Table 28 – Gross impaired loans by borrower category
As at December 31

(in millions of dollars and as a percentage)	**2017**					2016		2015	
	Gross loans and acceptances	**Gross impaired loans**		**Individual allowances for credit losses**	**Net impaired loans**	Gross impaired loans	Net impaired loans	Gross impaired loans	Net impaired loans
Residential mortgages	**$ 4,323**	**$ 8**	**0.19%**	**$ 5**	**$ 3**	$ 2	$ 2	$ 3	$ 3
Consumer, credit card and other personal loans	**17,547**	**72**	**0.41**	**-**	**72**	82	82	73	73
Business and government	**37,043**	**4**	**0.01**	**4**	**-**	11	6	9	6
Total	**$ 58,913**	**$ 84**		**$ 9**	**$ 75**	$ 95	$ 90	$ 85	$ 82
As a percentage of gross loans and acceptances[1]			**0.14%**		**0.13%**	0.18%	0.17%	0.17%	0.16%

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

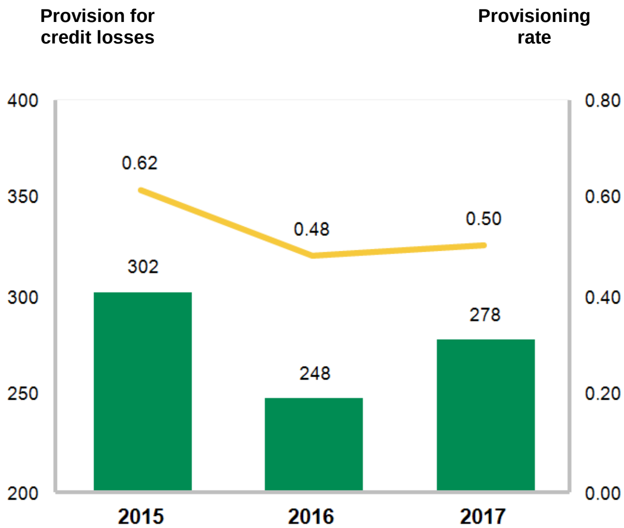
Table 29 – Change in gross impaired loan balance
As at December 31

(in millions of dollars)	**2017**	2016	2015
Gross impaired loans at the beginning of the year	**$ 95**	$ 85	$ 76
Gross impaired loans since the last year	**441**	466	453
Loans returned to unimpaired status	**(225)**	(205)	(187)
Write-offs and recoveries	**(278)**	(281)	(271)
Other changes	**51**	30	14
Gross impaired loans at the end of the year	**$ 84**	$ 95	$ 85

Provision for credit losses

The Federation's provision for credit losses totalled $278 million for 2017, up $30 million compared to 2016. A recovery of the collective allowance resulted in 2016 owing to refinements of the methodology used in models for calculating this allowance. Favourable developments in the risk related to this portfolio nevertheless mitigated the increase. The provisioning rate was 0.50% at the end of 2017, up slightly from 0.48% as at December 31, 2016.

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



Counterparty and issuer risk

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

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

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

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

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

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

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

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

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

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

Additional information about the Federation's credit risk is presented in Note 5, "Offsetting financial assets and liabilities", Note 19, "Derivative financial instruments and hedging activities", and Note 28, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.

Market risk

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

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

GOVERNANCE

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

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

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

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

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

Table 30 presents the aggregate VaR and the aggregate SVaR for Desjardins Group's trading activities by risk category as well as the diversification effect. Equity price risk, foreign exchange risk, interest rate risk and specific interest rate risk are the four risk categories to which the Federation is exposed. These risk factors are taken into account in measuring the market risk of the trading portfolio. They are reflected in the VaR table presented below. The definition of a trading portfolio meets the various criteria defined in the Basel Capital Accord.

Table 30 – VaR by risk category (trading portfolio)*

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

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

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

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

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

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

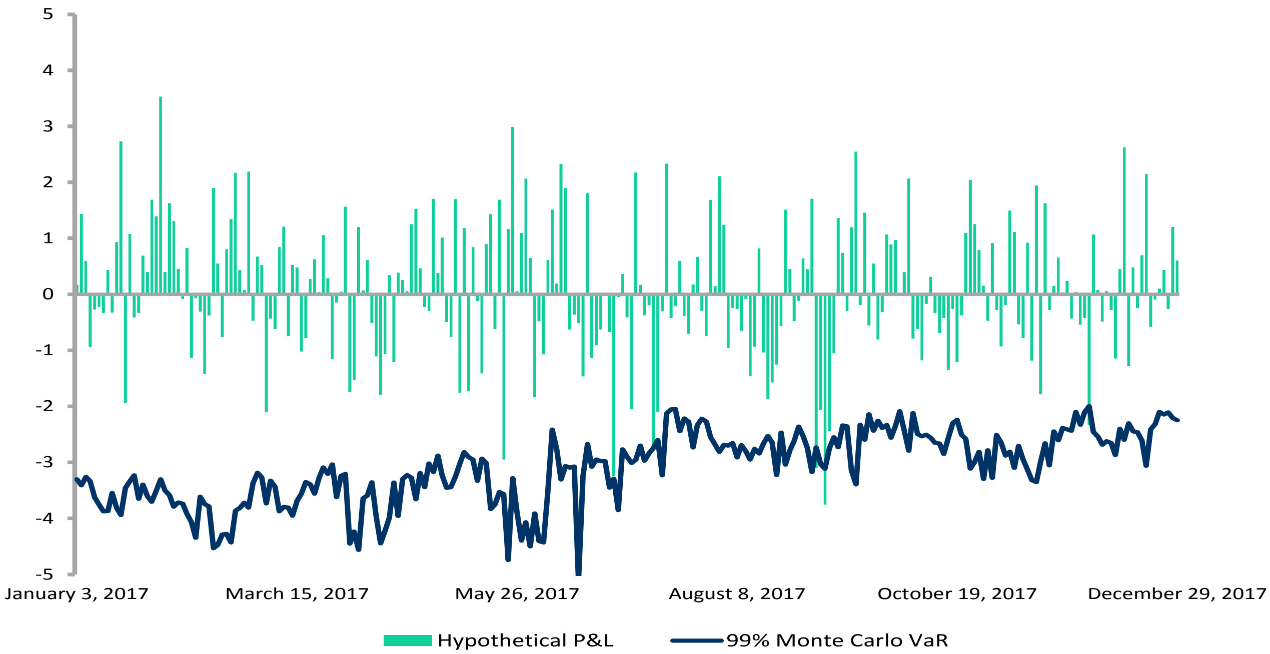
Back testing

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

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

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

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



Stress testing

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

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

STRUCTURAL INTEREST RATE RISK MANAGEMENT

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

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

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

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

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

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

Table 31 presents the potential impact before income taxes, with regard to structural interest rate risk management associated with banking activities, of a sudden and sustained 100 basis point increase or decrease in interest rates on net interest income and the economic value of equity for the Federation. The impact related to insurance activities is presented in Note 1 of this table.

Table 31 – Interest rate sensitivity (before income taxes)[(1)]*
As at December 31

(in millions of dollars)	**2017**		2016	
	Net interest income[(2)]	**Economic value of equity**[(3)]	Net interest income[(2)]	Economic value of equity[(3)]
Impact of a 100-basis-point increase in interest rates	**$ (8)**	**$ -**	$ (26)	$ (2)
Impact of a 100-basis-point decrease in interest rates[(4)]	**9**	**-**	(29)	12

(1) Interest rate sensitivity related to insurance activities is not reflected in the amounts above. For these activities, a 100-basis-point increase in interest rates would result in a $226 million decrease in the economic value of equity before taxes as at December 31, 2017, and a $205 million decrease as at December 31, 2016. A 100-basis-point decrease in interest rates would result in an increase of $205 million in the economic value of equity before taxes as at December 31, 2017 and of $177 million as at December 31, 2016. Additional information is provided in the "Interest rate risk management" section of Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements.
(2) Represents the interest rate sensitivity of net interest income for the next 12 months.
(3) Represents the sensitivity of the present value of assets, liabilities and off-balance sheet instruments.
(4) The results of the impact of a decrease in interest rates take into consideration the use of a floor to avoid negative interest rates.

FOREIGN EXCHANGE RISK MANAGEMENT

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

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

PRICE RISK MANAGEMENT

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

Management of price risk related to real estate activities

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

Management of price risk related to stock markets

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

Liquidity risk

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

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

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

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

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

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

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

Liquidity risk measurement and monitoring

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

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

In addition to complying with regulatory ratios, a Desjardins-wide stress testing program has been set up. This program incorporates the concepts put forward by the Basel Committee on Banking Supervision in "Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring". The scenarios, based on a downgrade of Desjardins Group combined with a shock on capital markets, make it possible to:
- measure the extent, over a one-year period, of potential cash outflows in a crisis situation;
- implement liquidity ratios and levels to be maintained across Desjardins Group;
- assess the potential marginal cost of such events, depending on the type, severity and level of the crisis.

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

Liquidity risk indicators

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

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

SOURCES OF FINANCING

Core funding, which includes capital, long-term liabilities and a diversified deposit portfolio, is the foundation upon which the Federation's liquidity position depends. The solid base of deposits from member caisses combined with wholesale funding, diversified in terms of the programs used as well as the staggering of contractual maturities, allows high regulatory liquidity ratios to be maintained while ensuring their stability. The deposits of member caisses are presented on the Consolidated Balance Sheets, under "Deposits – Deposit-taking institutions" and accounted for 3.9% of total consolidated liabilities as at December 31, 2017, compared to 4.2% a year earlier. Total deposits, including wholesale funding, presented on the Consolidated Balance Sheets amounted to $52.1 billion as at December 31, 2017, up $5.2 billion since December 31, 2016. Additional information on deposits is found in Section 3.1 "Balance sheet management" of this MD&A.

Financing programs and strategies

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

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

The main programs currently used by the Federation are:

Table 32 – Main financing programs
As at December 31, 2017

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

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

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

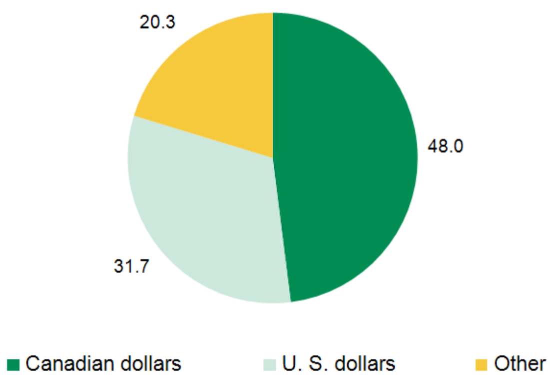
Table 33 – Remaining contractual term to maturity of wholesale funding
As at December 31

(in millions of dollars)	2017								2016
	Less than 1 month	1 to 3 months	3 to 6 months	6 to 12 months	Total - Less than 1 year	1 to 2 years	Over 2 years	Total	Total
Bearer discount notes	$ 2,011	$ 757	$ 17	$ 17	$ 2,802	$ -	$ -	$ 2,802	$ 1,908
Commercial paper	3,856	2,614	1,101	1,705	9,276	-	-	9,276	5,842
Medium-term notes	2,764	-	-	1,249	4,013	688	6,329	11,030	10,938
Mortgage securitization	-	383	556	814	1,753	1,631	5,780	9,164	8,009
Covered bonds	-	-	-	-	-	3,012	1,505	4,517	6,255
Subordinated notes	-	-	-	-	-	-	1,388	1,388	1,378
Total	$ 8,631	$ 3,754	$ 1,674	$ 3,785	$ 17,844	$ 5,331	$ 15,002	$ 38,177	$ 34,330
Including:									
Secured	$ -	$ 383	$ 556	$ 814	$ 1,753	$ 4,643	$ 8,673	$ 15,069	$ 15,642
Unsecured	8,631	3,371	1,118	2,971	16,091	688	6,329	23,108	18,688

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

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

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



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

Outstanding notes issued under the Federation's medium-term financing programs amounted to $24.7 billion as at December 31, 2017, compared to $25.2 billion a year earlier. The outstanding notes for these issues are presented under "Deposits – Business and government" in the Consolidated Balance Sheets. Desjardins Capital Inc.'s senior notes outstanding totalled $1.4 billion as at December 31, 2017, unchanged from a year earlier. Furthermore, to round out its financing and increase its capital base, in 2017, Desjardins Group, through the Federation, issued F capital shares for proceeds of $249 million, net of issuance expenses, as well as F capital shares having a value of $125 million for the payment of interest when the holder has elected to receive remuneration in F capital shares.

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

CREDIT RATINGS OF SECURITIES ISSUED

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

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

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

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

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

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

Table 34 – Credit ratings of securities issued

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

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

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

Table 35 presents assets and liabilities recorded on the Consolidated Balance Sheets and off-balance sheet commitments at their carrying amount and classified according to their residual contractual maturities. The classification of maturities is an information source with regard to liquidity and financing risk, but it differs from the analysis performed by the Federation to determine the expected maturity of the items for liquidity risk management purposes. Many factors other than contractual maturity are taken into consideration to measure expected future cash flows and liquidity risk.

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

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

Table 35 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments*
As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Assets										
Cash and deposits with financial institutions	$ 1,343	$ 378	$ -	$ -	$ -	$ -	$ -	$ -	$ 10	$ 1,731
Securities										
Securities at fair value through profit or loss(1)	45	541	1,152	835	2,112	2,195	7,181	15,881	1,712	31,654
Available-for-sale securities(1)	2,361	515	815	299	265	1,098	3,957	2,663	3,277	15,250
Securities borrowed or purchased under reverse repurchase agreements	8,982	257	123	15	-	-	-	-	-	9,377
Loans										
Residential mortgages(2)	39	49	227	93	120	505	1,934	1,350	6	4,323
Consumer, credit card and other personal loans(2)	41	84	196	209	273	1,128	4,473	4,472	6,671	17,547
Business and government(2)	6,579	2,364	1,270	1,378	1,465	5,432	8,753	3,318	6,453	37,012
Allowance for credit losses	-	-	-	-	-	-	-	-	(198)	(198)
Segregated fund net assets	-	-	-	-	-	-	-	-	13,379	13,379
Clients' liability under acceptances	31	-	-	-	-	-	-	-	-	31
Premiums receivable	173	62	13	3	-	-	-	-	1,847	2,098
Derivative financial instruments	99	115	174	159	162	699	2,228	136	-	3,772
Amounts receivable from clients, brokers and financial institutions	1,519	3	-	-	-	(8)	-	-	49	1,563
Reinsurance assets	35	71	72	63	60	213	423	1,038	227	2,202
Investment property	-	-	-	-	-	-	-	-	817	817
Property, plant and equipment	-	-	-	-	-	-	-	-	780	780
Goodwill	-	-	-	-	-	-	-	-	121	121
Intangible assets	-	-	-	-	-	-	-	-	466	466
Deferred tax assets	-	-	-	-	-	-	-	-	746	746
Other assets	443	68	109	2	5	8	21	-	1,532	2,188
Assets of the disposal group held to be transferred	-	-	-	-	-	-	-	-	881	881
Total assets	$ 21,690	$ 4,507	$ 4,151	$ 3,056	$ 4,462	$ 11,270	$ 28,970	$ 28,858	$ 38,776	$ 145,740

See page 80 for footnotes.

Table 35 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2017

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Liabilities and equity										
Deposits										
Individuals(3)	$ 42	$ 75	$ 122	$ 72	$ 76	$ 237	$ 526	$ 3	$ 3,200	$ 4,353
Business and governments(3)	9,246	3,768	1,703	1,653	2,134	5,383	12,019	1,602	3,455	40,963
Deposit-taking institutions(3)	685	192	279	186	200	687	1,840	6	2,758	6,833
Acceptances	31	-	-	-	-	-	-	-	-	31
Commitments related to securities sold short(4)	155	595	114	108	21	1,366	2,225	4,526	2	9,112
Commitments related to securities lent or sold under repurchase agreements	10,062	-	-	-	-	-	-	-	-	10,062
Derivative financial instruments	156	126	191	172	166	558	2,166	142	-	3,677
Amounts payable to clients, brokers and financial institutions	2,628	1	-	-	-	-	-	-	1,618	4,247
Insurance contract liabilities	412	732	897	834	766	1,885	4,121	16,379	2,274	28,300
Segregated fund net liabilities	-	-	-	-	-	-	-	-	13,354	13,354
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	1,741	1,741
Deferred tax liabilities	-	-	-	-	-	-	-	-	204	204
Other liabilities	1,923	427	347	8	9	60	81	741	1,198	4,794
Liabilities of the disposal group held to be transferred	-	-	-	-	-	-	-	-	662	662
Subordinated notes	-	-	-	-	-	-	898	490	-	1,388
Total equity	-	-	-	-	-	-	-	-	16,019	16,019
Total liabilities and equity	$ 25,340	$ 5,916	$ 3,653	$ 3,033	$ 3,372	$ 10,176	$ 23,876	$ 23,889	$ 46,485	$ 145,740
Off-balance sheet commitments										
Credit commitments(5)	$ 3,569	$ 110	$ 149	$ 225	$ 397	$ 2,957	$ 7,031	$ 243	$ 80,604	$ 95,285
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	2,024	2,024
Commitments under lease contracts	4	7	11	11	11	41	102	212	-	399
Documentary letters of credit	-	-	-	-	1	-	-	-	-	1
Guarantees and standby letters of credit	38	70	37	201	226	-	13	78	4	667
Credit default swaps	-	-	-	-	-	-	540	-	-	540

See page 80 for footnotes.

Table 35 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2016[6]

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Assets										
Cash and deposits with financial institutions	$ 968	$ 241	$ 3	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,212
Securities										
Securities at fair value through profit or loss[1]	818	317	1,094	577	1,263	2,564	7,410	15,566	1,396	31,005
Available-for-sale securities[1]	358	321	601	153	344	2,088	4,311	2,656	3,100	13,932
Securities borrowed or purchased under reverse repurchase agreements	7,649	64	-	-	-	-	-	-	-	7,713
Loans										
Residential mortgages[2]	18	36	103	105	61	541	1,311	1,311	-	3,486
Consumer, credit card and other personal loans[2]	46	71	158	171	251	1,183	4,061	3,622	6,157	15,720
Business and government[2]	5,273	1,484	786	1,013	1,146	5,303	11,203	2,609	4,599	33,416
Allowance for credit losses	-	-	-	-	-	-	-	-	(192)	(192)
Segregated fund net assets	-	-	-	-	-	-	-	-	11,965	11,965
Clients' liability under acceptances	7	4	-	-	-	-	-	-	-	11
Premiums receivable	168	60	12	2	-	-	-	-	1,719	1,961
Derivative financial instruments	74	698	157	413	415	637	1,288	24	-	3,706
Amounts receivable from clients, brokers and financial institutions	1,895	4	3	-	-	-	-	-	639	2,541
Reinsurance assets	39	78	72	60	56	190	454	1,072	561	2,582
Investment property	-	-	-	-	-	-	-	-	806	806
Property, plant and equipment	-	-	-	-	-	-	-	-	769	769
Goodwill	-	-	-	-	-	-	-	-	471	471
Intangible assets	-	-	-	-	-	-	-	-	690	690
Deferred tax assets	-	-	-	-	-	-	-	-	724	724
Other assets	327	88	129	18	11	14	32	9	1,512	2,140
Total assets	$ 17,640	$ 3,466	$ 3,118	$ 2,512	$ 3,547	$ 12,520	$ 30,070	$ 26,869	$ 34,916	$ 134,658

See page 80 for footnotes.

Table 35 – Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)*
As at December 31, 2016[(6)]

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Liabilities and equity										
Deposits										
Individuals[(3)]	$ 20	$ 27	$ 33	$ 40	$ 94	$ 337	$ 583	$ 1	$ 2,682	$ 3,817
Business and governments[(3)]	5,065	5,916	704	3,080	1,263	5,794	11,380	935	2,643	36,780
Deposit-taking institutions[(3)]	214	226	378	233	248	832	1,508	4	2,662	6,305
Acceptances	7	4	-	-	-	-	-	-	-	11
Commitments related to securities sold short[(4)]	418	62	315	92	-	1,012	2,208	4,089	-	8,196
Commitments related to securities lent or sold under repurchase agreements	9,870	-	-	-	-	-	-	-	-	9,870
Derivative financial instruments	57	90	120	144	145	634	1,305	45	-	2,540
Amounts payable to clients, brokers and financial institutions	2,399	4	-	-	-	-	-	-	2,256	4,659
Insurance contract liabilities	406	717	873	783	792	1,917	4,292	15,581	2,132	27,493
Segregated fund net liabilities	-	-	-	-	-	-	-	-	11,957	11,957
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	1,478	1,478
Deferred tax liabilities	-	-	-	-	-	-	-	-	247	247
Other liabilities	1,261	796	325	9	20	75	141	43	2,577	5,247
Subordinated notes	-	-	-	-	-	-	1,378	-	-	1,378
Total equity	-	-	-	-	-	-	-	-	14,680	14,680
Total liabilities and equity	$ 19,717	$ 7,842	$ 2,748	$ 4,381	$ 2,562	$ 10,601	$ 22,795	$ 20,698	$ 43,314	$ 134,658
Off-balance sheet commitments										
Credit commitments[(5)]	$ 3,591	$ 340	$ 388	$ 816	$ 595	$ 2,438	$ 6,165	$ 256	$ 73,366	$ 87,955
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	1,772	1,772
Commitments under lease contracts	4	7	12	12	11	35	81	92	-	254
Documentary letters of credit	-	1	3	-	1	-	-	-	-	5
Guarantees and standby letters of credit	54	104	137	92	185	24	4	73	3	676
Credit default swaps	-	-	-	-	-	-	644	-	-	644

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

Operational risk

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

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

OPERATIONAL RISK MANAGEMENT FRAMEWORK

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

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

GOVERNANCE

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

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

Approaches to identifying, measuring and monitoring operational risk

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

	Description
Risk identification and measurement	A standard inventory of operational risks to which Desjardins Group is exposed has been prepared and is used as the basis for determining the most significant operational risks and evaluating the effectiveness of the mitigation measures in place to reduce them. The risk and control assessments, carried out on a periodic basis, can be related to projects, products, systems, processes and activities, as well as to strategic initiatives and important new products. Consideration of internal and external events (losses, audit findings, etc.) is an integral part of these assessments. When the results indicate operational risk exposures that exceed the established tolerance level, action plans are prepared to reduce exposure to an acceptable level.
Collection of data on operational losses	The collection of internal data on operational losses is carried out to list and quantify losses according to predetermined thresholds. Operational losses are indexed in a database. Through analysis, causes are better understood, trends are determined, and corrective measures are taken when necessary. In addition, external operational risk events in the industry are monitored to detect potential or emerging risks and increase risk management at Desjardins Group, if need be. The main trends identified through analysis of operational losses are reported to the various committees on a regular basis. During 2017, operational losses were consistent with the limits set for risk appetite by senior management and the Board of Directors. Contingent liabilities, including the impact of litigation, are presented in Note 28, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.
Key risk indicators	To monitor their risk profile and track developments in it, the business segments and support functions establish operational risk indicators to help them proactively monitor any increase in their exposure to the most significant risks and act accordingly when the tolerance level is reached.

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

Insurance risk

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

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

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

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

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

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

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

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

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

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

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

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

Strategic risk

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

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

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

Reputation risk

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

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

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

Pension plan risk

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

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

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

Environmental risk

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

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

Environmental risk is an integral part of Desjardins Group's Integrated Risk Management Framework. In December 2017, Desjardins Group announced the introduction of four management practices aimed at strengthening environmental risk mitigation in the short term and making reduction of Desjardins's carbon footprint a reality:
- Offsetting greenhouse gas emissions generated by its activities.
- For its own investments, focusing its direct energy infrastructure investments on renewable energy. The Desjardins Group Pension Plan has made the same commitment.
- For its own investments, reducing its carbon footprint by 25% by 2020 with regard to its portfolios invested in public markets compared to the benchmark indexes.
- Integrating Environmental, Social and Governance (ESG) factors into its business decisions (financing, investment, placement and insurance). Tools are being developed to support teams in phasing in this positioning, as the objective is to be consistent across the organization.

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

Legal and regulatory environment risk

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

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

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

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

On October 5, 2017, the Quebec Minister of Finance tabled Bill 141, *An Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions* (the Bill). The Bill, once it takes effect, will have significant impacts on all institutions and intermediaries operating in Quebec's financial sector. For further information, see page 9 in the "Changes in the regulatory environment" section, which presents changes in the regulations applicable to Desjardins Group.

4.3 Additional information related to certain risk exposures

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

Table 36 – Asset-backed securities
As at December 31

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

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

Table 37 – Derivative financial instruments
As at December 31

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

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

Table 38– Leveraged finance loans and subprime loans
As at December 31

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

(1) Leveraged finance loans are defined as loans to large corporations and finance companies whose credit rating is between BB+ and D, and whose level of indebtedness is very high compared to other companies in the same industry.
(2) Alt-A mortgages are defined as loans to borrowers with non-standard income documentation. These loans are presented in the Consolidated Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.
(3) These loans are defined as loans to borrowers with a high credit risk profile. Subprime residential mortgages are recorded in the Consolidated Balance Sheets under "Loans – Residential mortgages" and are measured at amortized cost.

5.0 Additional information

5.1 Controls and procedures

The Federation complies with certain requirements of the regulations prescribed by the Canadian Securities Administrators (CSA) respecting continuous disclosure obligations, oversight of external auditors, certification of financial disclosures, and audit committees.

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

DISCLOSURE CONTROLS AND PROCEDURES

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

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

INTERNAL CONTROL OVER FINANCIAL REPORTING

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

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

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

The assessment of the design and effectiveness of internal control over financial reporting was performed by the Federation's management under the supervision of the President and CEO, and of the CFO. Based on the results of this assessment, these senior officers concluded that as at December 31, 2017, internal control over financing reporting was adequately designed and effective, and did not contain any material weakness. These controls provide reasonable assurance regarding the reliability of the Federation's financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

CHANGE IN INTERNAL CONTROL OVER FINANCIAL REPORTING

During the year ended December 31, 2017, the Federation did not make any changes to its internal control over financial reporting that had materially affected, or may materially affect, its operations.

Various other aspects of corporate governance are examined in more detail in section "Corporate governance" of the Federation's 2017 Annual Report.

5.2 Related party disclosures

In the normal course of business, the Federation offers financial services to related parties, including its associates and other related companies, and enters into agreements for operating services with them. It also pays its key management personnel compensation under normal market conditions.

The Federation and its subsidiaries carry out transactions with related parties, primarily member caisses. Services provided to the member caisses include various technical, administrative and financial services, for which income, such as assessments and fees, are collected. At the same time, the member caisses receive remuneration from the Federation on products and services such as credit cards, payroll services and investment fund and financial engineering services. The Federation also acts as treasurer, thereby allowing the member caisses to borrow or lend liquidities. Member caisses and the Federation also enter into swap contracts.

Through Desjardins Investments Inc., the Federation receives management fees as manager for Desjardins Funds in exchange for the following services: accounting, record keeping, custody of securities, portfolio management and transfer agent services. Through Desjardins Trust Inc., the Federation also receives fees as fund depositary. Finally, it receives management income from pension plans and interest expense paid to the Desjardins Group Pension Plan.

Furthermore, the Federation provides its financial products and services, under normal market conditions, to its directors, its key management personnel and the persons related to them.

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

Additional information about related party transactions is presented in Note 33, "Related party disclosures", to the Annual Consolidated Financial Statements.

5.3 Critical accounting policies and estimates

A description of the accounting policies used by the Federation is essential to understanding the Consolidated Financial Statements as at December 31, 2017. The significant accounting policies are described in Note 2, "Basis of presentation and significant accounting policies", to the Consolidated Financial Statements. Some of these policies are of particular importance in presenting the Federation's financial position and operating results because they require management to make judgments as well as estimates and assumptions that may affect the reported amounts of some assets, liabilities, income and expenses, as well as related information. The significant accounting policies that required management to make difficult, subjective or complex judgments, often involving uncertainties, are discussed below.

STRUCTURED ENTITIES

A structured entity is consolidated when it is controlled by the Federation. Management must make significant judgments when it assesses the various elements and all related facts and circumstances as a whole to determine whether control exists, especially in the case of structured entities.

A structured entity is an entity that has been designed so that voting rights or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. A structured entity often has some or all of the following features or attributes: restricted activities, a narrow and well-defined objective, insufficient equity to permit it to finance its activities without subordinated financial support, or financing in the form of multiple contractually linked instruments issued to investors.

Additional information about structured entities is presented in Note 13, "Interests in other entities", to the Consolidated Financial Statements.

DETERMINATION OF THE FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value measurement of financial instruments is determined using a three-level hierarchy, reflecting the importance of the inputs used for the measurements. Level 1 denotes measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities, while level 2 designates valuation techniques based primarily on observable market data. Level 3 concerns valuation techniques not based primarily on observable market data.

There is little subjectivity in the determination of the fair value of financial instruments, especially securities and commitments related to securities sold short, obtained from quoted prices on active markets. This fair value is based on the quoted price within the bid-ask spread that is most representative of fair value in the circumstances.

If there are no quoted prices on active markets, fair value is determined using models that maximize the use of observable inputs and minimize the use of unobservable inputs. In such cases, fair value estimates are established using valuation techniques such as cash flow discounting, comparisons with similar financial instruments, option pricing models and other techniques commonly used by market participants, if these techniques have been demonstrated to provide reliable estimates. Valuation techniques rely on assumptions concerning the amount and timing of estimated future cash flows and discount rates that are mainly based on observable data, such as interest rate yield curves, exchange rates, credit curves and volatility factors. When one or several material inputs are not observable on the market, fair value is determined mainly based on internal inputs and estimates that take into account the characteristics specific to the financial instrument and any factor relevant to the measurement. For complex financial instruments, significant judgment is used in determining the valuation technique to be used and in selecting inputs and adjustments associated with this technique. Due to the need to use estimates and make judgments when applying many valuation techniques, fair value estimates for identical or similar assets may differ between entities. Fair value reflects market conditions on a given date and may not be representative of future fair values. It should not be considered as being realizable in the event of immediate settlement of these instruments.

Loans

The fair value of loans is determined by discounting expected contractual cash flows using market interest rates charged for similar new loans at the reporting date and takes estimated prepayments into account. Changes in interest rates and in the creditworthiness of borrowers are the main causes of changes in the fair value of loans held by the Federation, which result in a favourable or unfavourable difference compared to their carrying amount. The fair value of impaired loans is assumed to be equal to their carrying amount.

Deposits

The fair value of fixed-rate deposits is determined by discounting expected cash flows using market interest rates currently being offered for deposits with substantially the same term and takes estimated prepayments into account. The fair value of deposits with floating-rate features or with no stated maturity is assumed to be equal to their carrying amount.

Subordinated notes

The fair value of subordinated notes is based on brokers' quotes.

Derivative financial instruments

The fair value of derivative financial instruments is determined using pricing models that incorporate current market prices and the contractual prices of the underlying instruments, the time value of money, interest rate yield curves, credit curves and volatility factors. The fair value of derivative financial instruments is presented without taking into account the impact of legally enforceable master netting agreements. However, the Federation adjusts the measurement of these instruments based on credit risk, and such adjustments reflect the financial ability of the counterparties to the contracts and the creditworthiness of the Federation, as well as credit risk mitigation measures such as legally enforceable master netting agreements.

Financial instruments whose fair value equals their carrying amount

The carrying amount of certain financial instruments that mature in the next 12 months is a reasonable approximation of their fair value. These financial instruments include the following items: "Cash and deposits with financial institutions", "Securities borrowed or purchased under reverse repurchase agreements", "Clients' liability under acceptances", "Premiums receivable", "Amounts receivable from clients, brokers and financial institutions", some items included in "Other assets – Other", "Acceptances", "Commitments related to securities lent or sold under repurchase agreements", "Amounts payable to clients, brokers and financial institutions" and some items included in "Other liabilities – Other".

Additional information on the fair value of financial instruments is presented in Note 4, "Fair value of financial instruments", to the Consolidated Financial Statements.

DERECOGNITION OF FINANCIAL ASSETS

A financial asset is derecognized from the Consolidated Balance Sheets when the contractual rights to the cash flows from the asset expire, when the contractual rights to receive these cash flows are retained but the Federation has the obligation to pay them to a third party under certain conditions, or when the Federation transfers the contractual rights to receive the cash flows and substantially all the risks and rewards of ownership of the asset have been transferred.

When substantially all the risks and rewards of ownership of the transferred financial asset are retained by the Federation, such asset is not derecognized from the Consolidated Balance Sheets and a financial liability is recognized, when appropriate.

When substantially all the risks and rewards related to a financial asset are neither transferred nor retained, the Federation derecognizes the financial asset over which it does not retain control and recognizes an asset or a liability representing the rights and obligations created or retained in the asset transfer. If control of the financial asset is retained, the Federation continues to recognize the asset in the Consolidated 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 Consolidated Statements of Income for an amount equal to the difference between the carrying amount of the asset and the value of the consideration received.

Management must use its judgment to determine whether the contractual rights to the cash flows have expired, have been transferred or have been retained with an obligation to pay them to a third party. With respect to the transfer of substantially all the risks and rewards of ownership of the assets, management evaluates the Federation's exposure before and after the transfer as well as the changes in the amount and timing of the net cash flows of the transferred asset. Lastly, management must make judgments to determine whether it controls the financial asset and to measure retained rights.

Additional information about the derecognition of financial assets is presented in Note 8, "Derecognition of financial assets", to the Consolidated Financial Statements.

IMPAIRMENT OF FINANCIAL ASSETS

At the reporting date, the Federation assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Allowance for credit losses

Objective evidence of impairment results from a loss event that occurred after a loan was granted but before the reporting date, and that has an impact on the estimated future cash flows of the loan.

The impairment of a loan or a group of loans is determined by estimating the recoverable amount of these financial assets. The allowance is equal to the difference between this amount and the carrying amount. To determine the estimated recoverable amount of a loan, the Federation discounts the estimated future cash flows at the effective interest rate inherent to the loan. When the amounts and timing of future cash flows cannot be estimated with reasonable reliability, the estimated recoverable amount is determined using the fair value of the collateral underlying the loan, net of expected costs of realization, or the observable market price for the loan. The collateral may vary depending on the type of loan.

The allowance for credit losses represents management's best estimate for loan impairment at the reporting date. As part of its evaluation, management must make judgments to determine the data, assumptions and estimates to be used, including determining when a loan is considered impaired and the amount that could be recovered. Changing these estimates and assumptions would have an impact on the allowance for credit losses and the provision for credit losses for the year.

The allowance for credit losses related to impaired loans is measured either individually or collectively for loans that are not individually material, while the allowance for credit losses is measured collectively for unimpaired loans.

For individual allowances, the Federation 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 Consolidated Statements of Income. Loan portfolios for which there is no objective evidence of impairment are included in groups of financial assets having similar credit risk characteristics and are subject to a collective allowance.

For certain impaired loan portfolios comprised of a large number of homogeneous balances that are not individually material, the Federation establishes a collective allowance for these impaired loans based on the portfolio's historical net loss rate.

The method used by the Federation to determine the collective allowance takes into account the risk parameters of the various loan portfolios, in particular through the integration of sophisticated credit risk models. These collective allowance models take into account certain factors such as the probabilities of default (loss frequency), loss given default (extent of losses) and gross exposures at default. These parameters, which are based on historical losses, are determined according to the category and risk rating of each loan. The measurement of the collective allowance relies heavily on management's judgment and depends on management's assessment of current credit quality trends for business segments, the impact of changes in its credit policies and economic conditions.

Additional information about loans and the allowance for credit losses is presented in Note 7, "Loans and allowance for credit losses", to the Consolidated Financial Statements.

Available-for-sale securities

Securities classified in the "Available-for-sale" category are examined at the reporting date to determine whether there is any objective evidence that they are impaired. In measuring the impairment loss, the Federation takes into account many factors specific to each investment and all the factors that could indicate such a loss. Factors considered include, but are not limited to, a significant or prolonged decline in fair value, significant financial difficulties of the issuer, a breach of contract, the increasing probability that the issuer will enter bankruptcy or a restructuring and the disappearance of an active market for the financial asset in question. Management also uses judgment to determine when to recognize an impairment loss.

The Federation individually assesses debt securities classified as "Available-for-sale", including preferred shares with characteristics and behaviour similar to those of debt instruments, to determine whether there is any objective evidence of impairment. For equity securities classified in the "Available-for-sale" category, the objective evidence would also include a "significant" or "prolonged" decline in fair value below cost.

Additional information about the recognition of available-for-sale securities and fair value measurement is presented in Note 3, "Carrying amount of financial instruments", Note 4, "Fair value of financial instruments", and Note 6, "Securities", to the Consolidated Financial Statements.

IMPAIRMENT OF NON-FINANCIAL ASSETS

The Federation assesses at the reporting date whether there is evidence that an asset may be impaired. An impairment loss is recognized when the carrying amount of the asset exceeds its recoverable amount.

The recoverable amount represents the higher of the fair value less costs of disposal and the value in use. Fair value represents the best estimate of the amount that could be obtained from the sale of the asset in an arm's-length transaction between knowledgeable and willing parties. The value in use is calculated using the most appropriate method, generally by discounting recoverable future cash flows.

Estimating the recoverable amount of a non-financial asset to determine whether it is impaired also requires that management make estimates and assumptions, and any change in these estimates and assumptions could impact the determination of the recoverable amount of non-financial assets and, therefore, the outcome of the impairment test. The main estimates and assumptions used in calculating the recoverable amount are future cash flows estimated based on internal financial forecasts, expected future earnings, the growth rate and the discount rate.

Goodwill and intangible assets with indefinite useful lives

Goodwill and intangible assets with indefinite useful lives are tested for impairment once a year and when there is possible evidence of impairment.

The impairment test for goodwill and intangible assets with indefinite useful lives is performed based on the recoverable amount of the asset or each cash-generating unit (CGU) (or each group of CGUs) to which goodwill or the intangible asset with an indefinite useful life applies. Significant judgments must be made to estimate the data taken into account in the model used to determine the recoverable amount of each intangible asset with an indefinite useful life or each CGU.

When the recoverable amount of the asset or the CGU is less than the carrying amount, an impairment loss is recognized in the Consolidated Statements of Income for the year and is first recorded as a reduction of the intangible asset with an indefinite useful life or, in the case of a CGU, as a reduction of the goodwill allocated to the CGU (or group of CGUs) and then as a reduction of the other identifiable assets of the CGU (or group of CGUs) pro rata on the basis of their carrying amount in the unit. The allocation of an impairment loss to the assets of a CGU (or group of CGUs) must however not result in their carrying amount being lower than the highest of the following amounts: fair value of the assets less costs to sell, their value in use, and zero. Goodwill impairment losses cannot be reversed.

Note 11, "Goodwill and intangible assets", to the Consolidated Financial Statements provides further information about the impairment of non-financial assets.

INSURANCE CONTRACT LIABILITIES

Life and health insurance contract liabilities

Life and health insurance contract liabilities consist of actuarial liabilities, benefits payable, provisions for claims not reported, provisions for dividends and experience refunds as well as policyholder deposits.

Actuarial liabilities represent the amounts which, together with estimated future premiums and net investment income, will provide for all the life and health insurance subsidiaries' commitments regarding estimated future benefits, policyholder dividends and related expenses. The appointed actuary of each life and health insurance subsidiary is required to determine the actuarial liabilities needed to meet its future commitments. The actuarial liabilities of these subsidiaries are determined using the Canadian Asset Liability Method (CALM), in accordance with Canadian accepted actuarial practices, and they are equal to the value in the Consolidated Balance Sheets of the assets that back them.

Property and casualty insurance contract liabilities

Property and casualty insurance contract liabilities consist of unearned premiums, provisions for claims and adjustment expenses.

Unearned premiums represent the portion of premiums remaining to be earned at the reporting date.

The provisions for claims and adjustment expenses related to the insurance policies of the property and casualty insurance subsidiaries are estimated using actuarial techniques that consider best estimate assumptions, taking into account currently known data, which are regularly reviewed and updated. Any resulting adjustment is recognized in the Consolidated Statements of Income for the year in which the revision occurs. The provision for claims and adjustment expenses is reported on a discounted basis using the rate of return of the underlying assets, with a margin for adverse deviations.

Note 15, "Insurance contract liabilities", to the Consolidated Financial Statements provides information about accounting for the various life and health and property and casualty insurance contract liabilities, the main assumptions used and the impact on profit or loss of changes to assumptions.

PROVISIONS

Provisions are liabilities of uncertain timing or amount. A provision is recognized when the Federation has an obligation (legal or constructive) as a result of a past event, the settlement of which should result in an outflow of resources embodying economic benefits, and when a reliable estimate can be made of the amount of the obligation. The amount of the obligation is discounted where the effect of the time value of money is material.

Provisions are based on management's best estimate of the amounts required to settle the obligation on the reporting date, taking into account the relevant risks and uncertainties. As these estimates are forward-looking in nature, management must use its judgment to forecast the timing and amount of future cash flows. Actual results may differ significantly from these forecasts.

CONTINGENT LIABILITIES

In the normal course of its operations, the Federation is involved in various litigation and legal proceedings.

Additional information about contingent liabilities is presented in Note 28, "Commitments, guarantees and contingent liabilities", to the Consolidated Financial Statements.

INCOME TAXES ON SURPLUS EARNINGS

The income tax expense on surplus earnings recognized in the Consolidated Statements of Income comprises the current and deferred tax expense on operating surplus earnings as well as the income tax consequences of remuneration on capital stock and dividends when certain conditions are met. The total income tax expense includes the income tax expense on surplus earnings recognized in the Consolidated Statements of Income as well as current and deferred taxes on items recognized outside profit or loss directly in the Consolidated Statements of Comprehensive Income or the Consolidated Statements of Changes in Equity.

The total income tax expense is based on the expected tax treatment of the transactions. To determine the current and deferred portions of income taxes on surplus earnings, management must make judgments to establish assumptions concerning the dates on which deferred income tax assets and liabilities will be reversed. Significant judgment must be used to interpret the relevant tax legislation in order to determine the income tax expense. If the Federation's interpretation differs from that of taxation authorities or if the reversal dates do not correspond to the forecasted dates, the provision for income taxes on surplus earnings may increase or decrease in subsequent years.

Note 27, "Income taxes on surplus earnings", to the Consolidated Financial Statements provides additional information on income taxes on surplus earnings.

DIVIDENDS TO MEMBER CAISSES

Dividends to member caisses recognized in the Consolidated Statements of Income reflect management's best estimate. They are based on a resolution of the Board of Directors to recommend to the General Meeting that payment of these dividends be approved. The annual dividends are determined on the basis of the distribution of the surplus earnings that the Annual General Meeting of the Federation has approved. Transfers to the reserves are recognized when approved by the member caisses. Dividends to member caisses are mainly allocated within the Personal and Business Services segment.

EMPLOYEE BENEFITS

The Federation participates in a pension plan and a supplemental pension plan through Desjardins Group's defined benefit group plans. It offers the majority of its employees a defined benefit pension plan and a defined benefit supplemental pension plan. The Federation also offers a post-retirement benefit plan that provides medical, dental and life insurance to retiring employees and their dependents.

The Federation participates in defined benefit group pension plans whose risks are shared by entities under common control. The Federation's share in the cost recognized and the net liability for the defined benefit group pension plans of Desjardins Group is mainly determined based on funding rules, as described in the plan's by-laws. The main Desjardins Group pension plan is funded by both employee and employer contributions, which are based on the financial position and the funding policy of the plan. Employers' contributions are determined using a percentage of the assessable payroll for their employees participating in the plan.

The Federation's share in the cost of the group post-retirement benefit plan of Desjardins Group is determined based on the number of active insureds of the Federation as a percentage of the total number of active insureds for Desjardins Group as a whole.

Note 16, "Net defined benefit plan liabilities", to the Consolidated Financial Statements provides further information on accounting for defined benefit plans and on the sensitivity of the key assumptions.

5.4 Future accounting changes

Accounting standards and amendments issued by the IASB but not yet effective as at December 31, 2017 are presented below. Regulatory authorities have stated that early adoption of these standards will not be permitted, unless they indicate otherwise.

IFRS 15, "REVENUE FROM CONTRACTS WITH CUSTOMERS"

In May 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers", which introduces a single, comprehensive revenue recognition model for all contracts with customers other than those within the scope of other standards, such as financial instruments, insurance contracts and leases. The majority of the Federation's revenues will not be affected by the adoption of this standard. IFRS 15 supersedes IAS 18, "Revenue" and related interpretations. The core principle of this standard is that revenue recognition should depict the transfer of goods or services in an amount that reflects the consideration received or expected to be received in exchange for these goods or services.

In April 2016, the IASB issued amendments to IFRS 15 to further clarify revenue recognition and transition provisions with respect to the initial application.

The Federation will have to adopt IFRS 15 retrospectively as at January 1, 2018. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 15 will be recognized in the opening Consolidated Balance Sheets. The Federation decided not to restate comparative periods upon adopting the provisions of IFRS 15. Consequently, the retrospective impact of applying IFRS 15 will be recognized in the Consolidated Balance Sheets as at January 1, 2018, which is the effective date of the new standard.

The Federation estimates that adopting IFRS 15 should not result in a significant impact on "Equity – Group's share" as at January 1, 2018.

IFRS 9, "FINANCIAL INSTRUMENTS"

In July 2014, the IASB issued the complete and final version of IFRS 9, "Financial Instruments", which will replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 includes the requirements for the classification and measurement of financial assets and liabilities and the impairment of financial assets, as well as general requirements for hedge accounting. Concurrently with the issuance of IFRS 9, IFRS 7, "Financial Instruments: Disclosures", was amended to enhance the required qualitative and quantitative disclosures, which will have to be provided for the years beginning on or after January 1, 2018.

The Federation will have to adopt IFRS 9 retrospectively as at January 1, 2018. However, the restatement of comparative periods is not mandatory, as the standard includes an exemption under which comparative periods may be presented using the previous accounting framework in certain conditions. In such case, any adjustment resulting from the application of IFRS 9 will be recognized in the opening Consolidated Balance Sheets. The Federation decided not to restate comparative periods upon adopting the provisions of IFRS 9. Consequently, the retrospective impact of applying IFRS 9 will be recognized in the Consolidated Balance Sheets as at January 1, 2018, which is the effective date of the new standard on financial instruments.

The Federation estimates that adopting IFRS 9 should result in a decrease in "Equity – Group's share" of approximately $215 million, net of income taxes, as at January 1, 2018, and in a decrease of approximately 43 basis points in regulatory capital ratios. This impact is mainly due to the increase in the allowance for credit losses resulting from the application of the new financial asset impairment model. The Federation continues to refine its processes relating to the new impairment model in preparation for reporting its financial information for the first quarter of 2018.

Governance and project management

The adoption of IFRS 9 is a major initiative for the Federation, which developed an organization-wide project based on a formal governance structure including various committees comprised of key members from the Finance Executive Division and Office of the CFO as well as Risk Management, and a structured implementation plan. This plan is divided into three main components, corresponding to the three sections of the new standard on financial instruments:

- classification and measurement;
- impairment;
- hedge accounting.

A multidisciplinary team made up of stakeholders from various sectors, such as risk management, including modelling, accounting standardization and information technology, has been assigned to the project and focuses on the following items for each of the above-mentioned components: changes in disclosure and financial reporting as well as in systems, controls and procedures, communications and training. Reports on the progress of the project as well as the main orientations implemented have been presented to the Audit and Inspection Commission, the Risk Management Commission and senior management.

The progress of each of the components of the implementation plan is monitored, and the project continues to advance according to schedule.

Following is a summary of the new IFRS 9 concepts and the progress of the work for each of the above-mentioned components.

Classification and measurement

IFRS 9 sets out a new classification and measurement model for financial assets to determine whether a financial asset should be classified as at amortized cost, at fair value through profit or loss or at fair value through other comprehensive income. This model is based on the contractual cash flow characteristics of the financial asset and the business model under which the financial asset is held.

The classification of debt instruments giving rise to cash flows that are solely payments of principal and interest will be determined, at initial recognition, based on the business model for managing these financial assets:

- Financial assets held within a business model whose objective is to collect contractual cash flows will be classified as at amortized cost.
- Financial assets held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets will be classified as at fair value through other comprehensive income.
- Financial assets managed either for trading purposes or on a fair value basis will be classified as at fair value through profit or loss.

In all cases, if a debt instrument does not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest, the financial asset will be classified as at fair value through profit or loss.

Lastly, the Federation may make, at initial recognition, an irrevocable election to classify a debt instrument as at fair value through profit or loss if such designation eliminates or significantly reduces a measurement or recognition inconsistency for the financial asset and if regulatory requirements are met.

Equity instruments will be classified as at fair value through profit or loss unless, at initial recognition, an irrevocable election is made, on an instrument-by-instrument basis, to classify them as at fair value through other comprehensive income. If such election is made, gains and losses will be recognized in other comprehensive income with no subsequent reclassification to profit or loss.

Certain financial assets that will be reclassified upon adopting IFRS 9 will be designated for purposes of applying the overlay approach. For more details, see IFRS 4, "Insurance Contracts", below.

Derivative financial instruments will continue to be recognized at fair value through profit or loss.

For the classification and measurement of financial liabilities, the new standard essentially carries forward the current requirements of IAS 39, without any significant difference, except for financial liabilities designated as at fair value through profit or loss, for which the change in fair value related to a change in the issuing entity's own credit risk will have to be recognized in other comprehensive income. Since the Federation does not hold any financial liabilities designated as at fair value through profit or loss at the transition date, the new standard will have no impact on the classification and measurement of financial liabilities.

Impairment

Overall comparison of the IFRS 9 and the IAS 39 impairment models

IFRS 9 introduces a new single financial asset impairment model requiring the recognition of expected credit losses instead of incurred losses, as the impairment model under IAS 39 requires. Under the current standard, loss allowances are recognized solely when there is objective evidence of impairment (identified on an individual or collective basis), which is when a loss event occurred after initial recognition, but before the reporting date, and this has an impact on the estimated cash flows from the financial asset. Under IFRS 9, credit losses will be recognized before a loss event occurs, which should result in faster recognition of credit losses than is actually the case with the current model.

The impairment model under IFRS 9 is therefore more forward-looking in nature than the impairment model under IAS 39. Under IFRS 9, assessing changes in credit risk since initial recognition and estimating expected credit losses must take into account the relevant information available at the reporting date, including information about past events and current conditions, as well as reasonable and supportable forward-looking information about economic conditions and future events.

Scope

The impairment model applies to all financial assets as well as loan commitments and financial guarantee contracts, except financial instruments measured or designated as at fair value through profit or loss and those designated as at fair value through other comprehensive income.

General expected credit loss impairment model

The general expected credit loss impairment model comprises three different stages:
- Stage 1: For financial instruments that have not had a significant increase in credit risk since initial recognition and are not considered as credit-impaired financial assets, a loss allowance amounting to 12-month expected credit losses is recognized.
- Stage 2: For financial instruments that have had a significant increase in credit risk since initial recognition but are not considered as credit-impaired financial assets, a loss allowance amounting to the lifetime expected credit losses is recognized.
- Stage 3: For financial assets considered as credit-impaired, a loss allowance amounting to the lifetime expected credit losses continues to be recognized.

The credit-impaired financial asset definition under IFRS 9 will correspond to the internal default definition used for credit risk management purposes, which takes relevant qualitative factors into consideration. Under IAS 39, loans are considered impaired financial assets when they meet the criteria for classification as "impaired loans" set out in Note 2, "Basis of presentation and significant accounting policies" to the Consolidated Financial Statements. Consequently, the concept of credit-impaired financial asset will differ from the concept currently used under IAS 39.

Financial instruments may, over their life, move from one general impairment model stage to another based on the improvement or deterioration of their credit risk. Instruments will always be classified in the various stages of the general impairment model based on the change in credit risk between the reporting date and the initial recognition date of the financial instrument.

Expected life

The expected life of most financial instruments is equal to the maximum contractual term during which the Federation is exposed to a credit risk, including extension options that may be exercised solely by the borrower. The exception to this rule concerns revolving credit exposures, which consist of personal and business lines of credit and credit card loans. The life of these instruments is estimated as being the period, as of the reporting date, over which there is exposure to credit risk without mitigation of the expected credit losses through normal credit risk management measures.

Determination of significant increases in credit risk

To determine whether, at the reporting date, credit risk has significantly increased since initial recognition, the Federation must base its assessment on the change in default risk over the expected life of the financial instrument in accordance with the requirements of IFRS 9, which will require a high degree of judgment.

In order to determine whether there has been a significant increase in credit risk since initial recognition, the Federation will compare the probability of default (PD) on the financial instrument at the reporting date with the PD at the date of initial recognition, also taking into consideration reasonable and supportable information that is indicative of significant increases in credit risk since initial recognition, including information about future economic conditions, to the extent that such information affects the assessment of the instrument's PD. In order to determine the PD of an instrument, PD assessment models for calculating regulatory capital according to the Internal Ratings-Based Approach will be used, but will be adjusted to comply with IFRS 9. The criteria used to determine a significant increase in credit risk will be mainly based on a relative change combined with an absolute change in the PD and will vary depending on the type of client base.

The Federation has also elected not to rebut the presumption that the credit risk has increased significantly when payments on loans are more than 30 days past due. This would be the latest date on which a financial instrument will be deemed to have experienced a significant increase in credit risk.

Measurement of loss allowances for expected credit losses

Loss allowances for expected credit losses will reflect an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, which will take into consideration reasonable and supportable information about past events, current conditions and forecasts of future economic conditions.

Loss allowances for expected credit losses will be measured on a collective or individual basis. For financial instruments included in stage 1 and stage 2 of the general impairment model, the loss allowance for expected credit losses will be measured on a collective basis. For financial assets included in stage 3, the loss allowance for expected credit losses will be measured on an individual or collective basis.

Loss allowances for expected credit losses measured on a collective basis will be based mainly on the parameters used to calculate regulatory capital under the Internal Ratings-Based Approach, namely PD, LGD and EAD, as defined under "Credit risk" in Section 4.2, "Risk management". However, these parameters will be adjusted to comply with IFRS 9.

The following table presents the main differences between the parameters used to calculate regulatory capital and those used to calculate loss allowances for expected credit losses under IFRS 9.

	Regulatory capital	IFRS 9
PD	• Estimated using a long-term average for a full economic cycle. • Projected over the next 12 months. • Definition of default associated with an instrument for which payments have been past due for over 90 days, plus certain other criteria.	• Estimated at a point in time for the next 12 months or for the lifetime of the instrument. • Based on past experience, current conditions and relevant forward-looking information. • Will correspond to the definition of default used for regulatory capital purposes.
LGD	• Based on losses that would be expected during an economic downturn. • Subject to certain regulatory floors. • Takes into account all direct and indirect recovery costs. • Discounted to account for the recovery period until default using the discount rate required for regulatory capital purposes.	• Based on past experience, current conditions and relevant forward-looking information. • Excessive conservatism and floors are excluded. • Takes into account only direct recovery costs. • Discounted to account for the recovery period until default using the initial effective interest rate.
EAD	• Corresponds to drawn amounts plus expected use of undrawn amounts before default. • Amount may not be lower than the balance of drawn amounts.	• Based on the expected balance of amounts in default projected over the next 12 months or the lifetime of the instrument based on forward-looking expectations.
Discounting	• No discounting between the date of default and the reporting date.	• Discounted from the date of default to the reporting date using the initial effective interest rate.

Three different economic scenarios prepared by the Federation's economists, namely, a base case scenario and two alternative scenarios (bull and bear) to be probability-weighted, will be incorporated into the calculation process for the loss allowance for expected credit losses. The main variables for future economic conditions to be used for establishing the loss allowance for expected credit losses include, in particular, gross domestic product (GDP), unemployment rate, the Consumer Price Index, housing prices and the corporate financing spread. Significant judgment will be required in using forward-looking information and the necessary estimates. Given the forward-looking nature of the IFRS 9 impairment model, the Federation expects that the loss allowance for expected credit losses established according to this standard may be more volatile than that established according to the current model.

The technology solution retained for calculating expected credit losses, which was implemented in fiscal 2017, will track financial asset classification included in each of the stages under the new expected credit loss (ECL) model, handle the impact of expected economic variables and incorporate risk parameters and certain credit risk modelling processes.

In fiscal 2017, the Federation also finalized the development and validation of the impairment model for purposes of calculating expected credit losses, and calculations were simulated. In addition, internal documentation relating to accounting policies, internal controls and procedures were updated, and business and financial reporting processes were modified. Changes were also made to the existing governance process with respect to the allowance for credit losses under IAS 39, in particular by revising the role of the Governance Committee – Collective Allowance, composed of officers from the Finance Executive Division and Office of the CFO as well as Risk Management and Economic Studies and in charge of approving work related to the determination of collective allowances and evaluating the relevance of the amounts to be included in the Consolidated Financial Statements.

Documents issued by regulatory authorities

In December 2015, the BCBS issued the final version of *Guidance on credit risk and accounting for expected credit losses*, which sets out supervisory guidance on sound credit risk practices associated with the implementation and ongoing application of expected credit loss accounting frameworks. In September 2016, the AMF issued a notice relating to the application of IFRS 9. This notice states that the AMF adheres to the principles and guidance published by the BCBS and expects financial services cooperatives, such as the Federation, to comply with them. the Federation is taking into consideration this guidance in the implementation and ongoing application of the expected credit loss impairment model under IFRS 9.

Documents regarding the regulatory treatment of accounting provisions were also issued. More information about these documents is found in Section 3.2, "Capital management".

Hedge accounting

IFRS 9 sets out a new hedge accounting model to align hedge accounting more closely with risk management activities.

However, as permitted by IFRS 9, the Federation decided to continue applying the hedge accounting requirements of IAS 39 instead of adopting the provisions of IFRS 9. Nevertheless, the new disclosures resulting from amendments to IFRS 7, "Financial Instruments: Disclosures", will have to be provided.

IFRS 4, "INSURANCE CONTRACTS"

In September 2016, the IASB issued amendments to IFRS 4, "Insurance Contracts", which are designed to address the concerns of insurers and their representative bodies about the different effective dates of IFRS 9, "Financial Instruments", which is January 1, 2018, and of new IFRS 17, "Insurance Contracts".

The amendments permit, but do not require, an entity that issues insurance contracts to elect to use one of two options in connection with adopting IFRS 9: deferring the initial application date of IFRS 9 to January 1, 2021 or applying the overlay approach.

The Federation elected to apply the overlay approach, which is the only option proposed by these amendments that it may apply, to financial assets that are eligible and designated in accordance with certain specific criteria. The overlay approach involves reclassifying between net surplus earnings and other comprehensive income, for designated financial assets, the difference between the amount reported in the Consolidated Statements of Income under IFRS 9 and the amount that would have been reported in the Consolidated Statements of Income if the Federation had continued to apply IAS 39 in such a way that net surplus earnings related to designated financial instruments reported in the Consolidated Statements of Income correspond to the amount that would have been reported if the Federation had continued to apply IAS 39.

The Federation will have to adopt the amendments to IFRS 4 as at January 1, 2018, which is the date of initial application of IFRS 9. According to the transition approach used for adopting IFRS 9, the retrospective impact of the overlay approach will be recognized in the Consolidated Balance Sheets as at January 1, 2018, and comparative periods will not be restated.

For financial assets reclassified from the "Available for sale" category under IAS 39 to financial assets "Classified as at fair value through profit or loss" under IFRS 9 that have been designated for purposes of applying the overlay approach, the Federation estimates that adopting the amendments to IFRS 4 should result in a reclassification of approximately $405 million, after taxes, from "Undistributed surplus earnings" to "Accumulated other comprehensive income" as at January 1, 2018.

IFRS 16, "LEASES"

In January 2016, the IASB issued IFRS 16, "Leases", to replace the current standard IAS 17, "Leases". IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 introduces a single recognition model for the lessee that requires recognizing lease assets and liabilities for most leases on the balance sheet, thereby eliminating the current distinction between operating and finance leases. For the lessor, the distinction between operating and finance leases remains similar.

The Federation is currently assessing the impact of adopting IFRS 16, which will be effective for annual periods beginning on or after January 1, 2019.

IFRS 17, "INSURANCE CONTRACTS"

In May 2017, the IASB issued IFRS 17, "Insurance Contracts", which will replace the current standard, IFRS 4, "Insurance Contracts". IFRS 17 sets out the recognition, measurement, presentation and disclosure requirements applicable to all insurance contracts.

IFRS 17 requires that insurance contract liabilities be measured using a general model based on current value. This general model uses assumptions as at the reporting date to estimate the amount, timing and uncertainty of future cash flows and takes into account market interest rates and the impact of insurance contract holder options and guarantees.

In addition, under IFRS 17, profits on the sale of insurance policies will no longer be recognized upon initial recognition, but will instead be deferred as a separate liability and recognized in profit or loss over the contract term as services are provided.

The Federation is currently assessing the impact of adopting IFRS 17, which will be effective for annual periods beginning on or after January 1, 2021.

5.5 Five-year statistical review

Table 39 – Consolidated Balance Sheets
For the years ended December 31

(in millions of dollars)	2017	2016	2015	2014	2013
ASSETS					
Cash and deposits with financial institutions	**$ 1,731**	$ 1,212	$ 1,006	$ 1,232	$ 524
Securities					
Securities at fair value through profit or loss	**31,654**	31,005	28,715	24,846	23,536
Available-for-sale securities	**15,250**	13,932	14,400	11,616	11,323
	46,904	44,937	43,115	36,462	34,859
Securities borrowed or purchased under reverse repurchase agreements	**9,377**	7,713	8,046	10,143	8,043
Loans					
Residential mortgages	**4,323**	3,486	2,861	2,367	2,308
Consumer, credit card and other personal loans	**17,547**	15,720	14,697	13,827	12,506
Business and government	**37,012**	33,416	33,330	29,891	23,325
	58,882	52,622	50,888	46,085	38,139
Allowance for credit losses	**(198)**	(192)	(180)	(163)	(132)
	58,684	52,430	50,708	45,922	38,007
Segregated fund net assets	**13,379**	11,965	9,781	8,695	7,252
Other assets					
Clients' liability under acceptances	**31**	11	376	858	985
Premiums receivable	**2,098**	1,961	1,665	1,130	1,126
Derivative financial instruments	**3,772**	3,706	4,879	3,153	2,448
Amounts receivable from clients, brokers and financial institutions	**1,563**	2,541	2,041	1,751	1,901
Reinsurance assets	**2,202**	2,582	1,964	785	648
Investment property	**817**	806	669	551	457
Property, plant and equipment	**780**	769	745	655	604
Goodwill	**121**	471	472	472	456
Intangible assets	**466**	690	660	569	507
Deferred tax assets	**746**	724	678	599	468
Other	**2,188**	2,140	1,852	1,689	1,613
Assets of the disposal group held to be transferred	**881**	-	-	-	-
	15,665	16,401	16,001	12,212	11,213
TOTAL ASSETS	**$ 145,740**	$ 134,658	$ 128,657	$ 114,666	$ 99,898

Table 39 – Consolidated Balance Sheets (continued)
For the years ended December 31

(in millions of dollars)	2017	2016	2015	2014	2013
LIABILITIES AND EQUITY					
LIABILITIES					
Deposits					
Individuals	**$ 4,353**	$ 3,817	$ 2,518	$ 2,055	$ 2,266
Business and government	**40,963**	36,780	38,925	33,535	25,748
Deposit-taking institutions	**6,833**	6,305	6,479	5,532	6,610
	52,149	46,902	47,922	41,122	34,624
Other liabilities					
Acceptances	**31**	11	376	858	985
Commitments related to securities sold short	**9,112**	8,196	5,464	6,304	7,754
Commitments related to securities lent or sold under repurchase agreements	**10,062**	9,870	9,283	13,021	8,738
Derivative financial instruments	**3,677**	2,540	2,478	2,194	2,180
Amounts payable to clients, brokers and financial institutions	**4,247**	4,659	4,713	3,713	3,752
Insurance contract liabilities	**28,300**	27,493	26,734	19,435	17,070
Segregated fund net liabilities	**13,354**	11,957	9,776	8,706	7,260
Net defined benefit plan liabilities	**1,741**	1,478	1,548	1,576	1,024
Deferred tax liabilities	**204**	247	218	201	195
Other	**4,794**	5,247	4,674	3,245	3,269
Liabilities of the disposal group held to be transferred	**662**	-	-	-	-
	76,184	71,698	65,264	59,253	52,227
Subordinated notes	**1,388**	1,378	1,884	2,564	3,063
TOTAL LIABILITIES	**129,721**	119,978	115,070	102,939	89,914
EQUITY					
Capital stock	**8,537**	8,066	7,505	7,050	5,641
Undistributed surplus earnings	**5,674**	4,781	3,977	3,290	3,021
Accumulated other comprehensive income	**458**	393	265	386	266
Reserves	**540**	524	507	440	543
Equity – Group's share	**15,209**	13,764	12,254	11,166	9,471
Non-controlling interests	**810**	916	1,333	561	513
TOTAL EQUITY	**16,019**	14,680	13,587	11,727	9,984
TOTAL LIABILITIES AND EQUITY	**$ 145,740**	$ 134,658	$ 128,657	$ 114,666	$ 99,898

Table 40 – Consolidated Statements of Income
For the years ended December 31

(in millions of dollars)	2017	2016[(1)]	2015[(1)]	2014[(1)]	2013[(1)]
Interest income					
Loans	**$ 2,070**	$ 1,866	$ 1,762	$ 1,595	$ 1,446
Securities	**195**	182	167	188	159
	2,265	2,048	1,929	1,783	1,605
Interest expense					
Deposits	**783**	660	598	593	530
Subordinated notes and other	**78**	85	128	135	157
	861	745	726	728	687
Net interest income	**1,404**	1,303	1,203	1,055	918
Net premiums	**8,146**	7,263	7,006	6,018	5,662
Other income					
Assessments	**377**	393	339	304	313
Service agreements	**727**	699	760	684	671
Lending fees and credit card service revenues	**660**	575	547	533	482
Brokerage and investment fund services	**1,087**	1,106	1,037	970	855
Management and custodial service fees	**457**	397	385	374	325
Net income (loss) on securities at fair value through profit or loss	**1,158**	572	687	1,948	(686)
Net income on available-for-sale securities	**405**	335	281	273	215
Net other investment income	**204**	201	242	236	228
Foreign exchange income	**77**	70	74	70	58
Other	**362**	140	250	323	341
	5,514	4,488	4,602	5,715	2,802
Total income	**15,064**	13,054	12,811	12,788	9,382
Provision for credit losses	**278**	248	302	265	203
Claims, benefits, annuities and changes in insurance contract liabilities	**6,795**	5,446	5,431	6,303	3,259
Non-interest expense					
Remuneration and other payments	**536**	492	471	428	377
Salaries and fringe benefits	**2,255**	2,329	2,221	1,907	1,794
Premises, equipment and furniture, including depreciation	**514**	437	397	351	321
Service agreements and outsourcing	**322**	306	327	251	228
Communications	**244**	265	254	233	228
Other	**2,368**	2,193	2,063	1,957	1,715
	6,239	6,022	5,733	5,127	4,663
Operating surplus earnings	**1,752**	1,338	1,345	1,093	1,257
Income taxes on surplus earnings	**336**	147	208	198	257
Surplus earnings before dividends to member caisses	**1,416**	1,191	1,137	895	1,000
Dividends to member caisses	**60**	25	-	9	60
Tax recovery on dividends to member caisses	**(16)**	(7)	-	(2)	(15)
Net surplus earnings for the year after dividends to member caisses	**$ 1,372**	$ 1,173	$ 1,137	$ 888	$ 955
Of which:					
Group's share	**$ 1,329**	$ 1,088	$ 957	$ 825	$ 929
Non-controlling interests' share	**43**	85	180	63	26

(1) Prior-year data have been reclassified to conform to the current year's presentation.

Table 41 – Selected financial measures
For the years ended December 31

(in millions of dollars and as a percentage)	**2017**	2016	2015	2014	2013
Tier 1A capital ratio	**17.5%**	15.9%	N/A[1]	N/A[1]	N/A[1]
Tier 1 capital ratio	**17.5**	15.9	N/A[1]	N/A[1]	N/A[1]
Total capital ratio	**17.5**	15.9	N/A[1]	N/A[1]	N/A[1]
Leverage ratio	**7.9**	7.4	N/A[1]	N/A[1]	N/A[1]
Return on equity[2]	**9.4**	8.5	8.2%	8.6%	11.9%
Gross impaired loans / gross loans and acceptances ratio[2]	**0.14**	0.18	0.17	0.16	0.17
Average assets[2]	**$ 143,110**	$ 134,333	$ 130,051	$ 108,698	$ 94,611
Average net loans and acceptances[2]	**54,977**	51,213	48,831	42,618	36,354
Average deposits[2]	**52,256**	48,376	44,985	37,953	32,862

[1] The Federation publishes its capital ratios calculated according to the guideline on the adequacy of capital base standards applicable to financial services cooperatives issued by the AMF on January 1, 2017. The ratios as at December 31, 2016 are as at January 1, 2017.
[2] See "Basis of presentation of financial information".