Fédération des caisses Desjardins du Québec

Financial Report

Third quarter of 2018

The *Fédération des caisses Desjardins du Québec* (the Federation) is a cooperative entity of Desjardins Group (Desjardins Group or Desjardins). Desjardins Group comprises the Desjardins caisse 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 and of its main subsidiaries is presented in "The Federation's profile".

FINANCIAL HIGHLIGHTS

Financial results and indicators

(in millions of dollars and as a percentage)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018(1)	June 30, 2018(1)	September 30, 2017	**September 30, 2018(1)**	September 30, 2017
Net interest income	**$ 382**	$ 353	$ 364	**$ 1,103**	$ 1,047
Net premiums	**2,288**	2,225	2,007	**6,677**	6,112
Other operating income(2)	**885**	1,000	1,130	**2,849**	2,956
Operating income(2)	**3,555**	3,578	3,501	**10,629**	10,115
Investment income (loss)(2)	**(137)**	319	(316)	**477**	843
Total income	**3,418**	3,897	3,185	**11,106**	10,958
Provision for credit losses	**73**	63	72	**225**	204
Claims, benefits, annuities and changes in insurance contract liabilities	**1,380**	1,727	1,000	**4,763**	4,675
Non-interest expense	**1,598**	1,568	1,433	**4,794**	4,588
Income taxes on surplus earnings	**68**	75	89	**202**	256
Surplus earnings before dividends to member caisses	**$ 299**	$ 464	$ 591	**$ 1,122**	$ 1,235
Adjusted surplus earnings before dividends to member caisses(2)	**$ 299**	$ 335	$ 333	**$ 993**	$ 986
Contribution to consolidated surplus earnings by business segment(3)					
Personal and Business Services	**$ 72**	$ 71	$ 86	**$ 249**	$ 255
Wealth Management and Life and Health Insurance	**174**	331	121	**711**	453
Property and Casualty Insurance	**70**	52	318	**148**	398
Treasury and Other Support to Desjardins Group Entities	**(17)**	10	66	**14**	129
	$ 299	$ 464	$ 591	**$ 1,122**	$ 1,235
Indicators					
Return on equity(2)	**7.1%**	11.8%	15.3%	**9.4%**	11.1%
Adjusted return on equity(2)	**7.3**	8.6	8.5	**8.4**	8.9
Credit loss provisioning rate(2)	**0.47**	0.43	0.51	**0.50**	0.50

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(2) See "Basis of presentation of financial information".
(3) The breakdown by line item is presented in Note 13, "Segmented information", to the Interim Consolidated Financial Statements.

Balance sheet and indicators

(in millions of dollars and as a percentage)	As at September 30, 2018[1]	As at December 31, 2017
Balance sheet		
Assets	**$ 160,245**	$ 145,740
Net loans and acceptances	**61,972**	58,715
Deposits	**57,798**	52,149
Equity	**16,883**	16,019
Indicators		
Assets under administration	**$ 404,124**	$ 419,981
Assets under management[2]	**67,903**	66,653
Tier 1A capital ratio	**17.0%**	17.5%
Tier 1 capital ratio	**17.0**	17.5
Total capital ratio	**17.0**	17.5
Leverage ratio	**7.7**	7.9
Gross credit-impaired loans[3]/gross loans and acceptances[4]	**0.36**	0.14

(1) The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(2) Assets under management may also be administered by the Federation. When this is the case, they are included in assets under administration.
(3) Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(4) See "Basis of presentation of financial information".

MESSAGE FROM SENIOR MANAGEMENT

Lévis, November 13, 2018 – For the third quarter ended September 30, 2018, the Federation posted surplus earnings before dividends to member caisses of $299 million, a $292 million decrease compared to the corresponding quarter of 2017. It should be recalled that in the third quarter of 2017, there was a gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company. Adjusted surplus earnings[1] were therefore down $34 million, or 10.2%. This decrease was chiefly due to lower surplus earnings from treasury operations and derivative financial instruments associated with hedging activities as well as the higher claims experience in property and casualty insurance, partially mitigated by a more favourable claims experience in life and health insurance operations and growth in income from assets under management.

This result reflects the contribution of $72 million made by the Personal and Business Services segment. The Wealth Management and Life and Health Insurance segment and the Property and Casualty Insurance segment contributed $174 million and $70 million, respectively.

"Desjardins Group's overall performance in the third quarter was very good," said Guy Cormier, President and Chief Executive Officer. "We rolled out several innovative initiatives, in the area of sustainable development in particular, and posted strong membership growth. We launched new responsible investment funds and are now the financial institution with the broadest range of RI funds in Canada."

The Federation complies with Basel III rules and maintains very good capitalization. As at September 30, 2018, its Tier 1A and total capital ratios were both 17.0%, compared to 17.5% as at December 31, 2017.

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1 See "Basis of presentation of financial information".

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management's Discussion and Analysis (MD&A) dated November 13, 2018 presents the analysis of the results of and main changes to the Federation's balance sheet for the period ended September 30, 2018, in comparison to previous periods. 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.

This MD&A should be read in conjunction with the unaudited Condensed Interim Consolidated Financial Statements (the Interim Consolidated Financial Statements), including the notes thereto, as at September 30, 2018, and the Federation's 2017 Annual Report (the 2017 Annual Report), which contains the MD&A and the audited Annual Consolidated Financial Statements (the Annual Consolidated Financial Statements).

Additional information about the Federation is available on the SEDAR website at www.sedar.com (under the *Fédération des caisses Desjardins du Québec* profile), where its Annual Information Form can be found as well. Further information is available on the Desjardins website at www.desjardins.com/ca/about-us/investor-relations. However, 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 in this MD&A 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, among others, those appearing in the "Economic environment and outlook", "Review of financial results", "Balance sheet review" and "Additional information" sections 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 formulated may be incorrect, or 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", of the 2017 annual MD&A, such as credit, market, liquidity, operational, insurance, strategic and reputation risk. Additional factors include regulatory and legal 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 loss or reputational damage to the Federation as a result of environmental issues related to its operations or its financing, investment or insurance activities. 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 the 2017 annual 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 these 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 under "Economic outlook for 2018" in the 2017 annual MD&A. These assumptions may also be updated in the quarterly MD&As under "Economic environment and outlook". 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.

THE FEDERATION'S PROFILE

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 international capital markets. It provides its member caisses with a variety of services, including certain technical, financial and administrative services. The Federation's mission is also to ensure risk management and capital management for Desjardins Group and look after the financial health of the *Groupe coopératif Desjardins*, which comprises the Desjardins caisses in Quebec, the Federation and the *Fonds de sécurité Desjardins*, as well as its sustainability pursuant to the *Act respecting financial services cooperatives*. The Federation had 271 member caisses in Quebec and Ontario as at September 30, 2018.

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 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 interests in joint-stock companies through holding companies.

SIGNIFICANT EVENTS IN 2018

Creation of Aviso Wealth

On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction led to the creation of Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and a partnership between the Centrals and The CUMIS Group. A gain of $129 million, net of income taxes, related to this transaction, was recognized in the Consolidated Statements of Income for the nine-month period ended September 30, 2018. Desjardins Group's interest held in Aviso Wealth represents an investment in a joint venture and is recognized using the equity method of accounting in the Wealth Management and Life and Health Insurance segment. The results of the subsidiary Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P. were also presented in the Wealth Management and Life and Health Insurance segment.

Additional financial information is presented in the section "Impact of significant transactions".

Zag Bank

On November 5, Zag Bank announced that it was winding down its operations, with a target of the second quarter of 2019 for closure. This decision is the result of a recent shift in focus by Desjardins Group, following a recent review of its operations in Ontario, the Atlantic Provinces and Western Canada, to growing its property and casualty insurance operations, wealth management activities and payment services. Given this focus, having a direct or online bank no longer fits into the long-term strategy of Desjardins Group, the Zag Bank's shareholder. The financial impact of this decision was reported mainly in the third quarter of 2018.

BASIS OF PRESENTATION OF FINANCIAL INFORMATION

The Annual and Interim 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. These Interim Consolidated Financial Statements of the Federation have been prepared in accordance with International Accounting Standard (IAS) 34, "Interim Financial Reporting". The accounting policies were applied as described in Note 2, "Basis of presentation and significant accounting policies", to the Annual Consolidated Financial Statements, except for the amendments described in Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements as a result of the adoption of IFRS 9, "Financial Instruments", IFRS 15, "Revenue from Contracts with Customers", and amendments to IFRS 4, "Insurance Contracts", on January 1, 2018. For more information about the accounting policies applied, see the Annual and Interim 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 Annual and Interim 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. The measures are defined as follows:

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, net of income taxes, related to the transaction involving Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P., completed on April 1, 2018, as part of the creation of Aviso Wealth.

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)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[(1)]	June 30, 2018[(1)]	September 30, 2017	**September 30, 2018[(1)]**	September 30, 2017
Presentation of the surplus earnings before dividends to member caisses in the Consolidated Financial Statements	**$ 299**	$ 464	$ 591	**$ 1,122**	$ 1,235
Specific items, net of income taxes					
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company	**-**	-	(258)	**-**	(249)
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	**-**	(129)	-	**(129)**	-
Presentation of the adjusted surplus earnings before dividends to member caisses	**$ 299**	$ 335	$ 333	**$ 993**	$ 986

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.

Adjusted net surplus earnings – Wealth Management and Life and Health Insurance segment

The net surplus earnings of the Wealth Management and Life and Health Insurance segment are adjusted to exclude the following specific item: the gain, net of income taxes, related to the transaction involving Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investment L.P., completed on April 1, 2018, as part of the creation of Aviso Wealth.

The following table presents a reconciliation of the net surplus earnings of the Wealth Management and Life and Health 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)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[(1)]	June 30, 2018[(1)]	September 30, 2017	**September 30, 2018[(1)]**	September 30, 2017
Presentation of the net surplus earnings of the Wealth Management and Life and Health Insurance segment in the Consolidated Financial Statements	**$ 174**	$ 331	$ 121	**$ 711**	$ 453
Specific item, net of income taxes					
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	**-**	(129)	-	**(129)**	-
Presentation of the adjusted net surplus earnings of the Wealth Management and Life and Health Insurance segment	**$ 174**	$ 202	$ 121	**$ 582**	$ 453

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim 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 item: 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.

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)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018(1)	June 30, 2018(1)	September 30, 2017	**September 30, 2018(1)**	September 30, 2017
Presentation of the net surplus earnings of the Property and Casualty Insurance segment in the Consolidated Financial Statements	**$ 70**	$ 52	$ 318	**$ 148**	$ 398
Specific item, net of income taxes					
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company(2)	**-**	-	(255)	**-**	(241)
Presentation of the adjusted net surplus earnings of the Property and Casualty Insurance segment	**$ 70**	$ 52	$ 63	**$ 148**	$ 157

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.
(2) The difference compared to the data presented in the table for the adjusted surplus earnings of the Federation before dividends to member caisses is related to intersegment transaction expenses.

Gross credit-impaired loans/gross loans and acceptances ratio

The gross credit-impaired loans/gross loans and acceptances ratio is used to measure loan portfolio quality and is equal to gross credit-impaired loans expressed as a percentage of total gross loans and acceptances. Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

The “Gross credit-impaired loans by borrower category” table of Federation’s MD&A provides more detailed information on this ratio.

Average loans and acceptances – Average deposits – Average equity

The average balances for these items are used to measure growth. They are equal to averages of the amounts presented in the Consolidated Financial Statements at the end of the quarters calculated starting from the quarter prior to the period concerned.

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 less 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 above two ratios.

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)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018	June 30, 2018	September 30, 2017	**September 30, 2018**	September 30, 2017
Net premiums	**$ 1,120**	$ 1,073	$ 967	**$ 3,252**	$ 2,913
Premiums excluded from the loss ratio[1]	**-**	-	-	**-**	(62)
Net premiums considered in the ratio denominators	**$ 1,120**	$ 1,073	$ 967	**$ 3,252**	$ 2,851
Claims, benefits, annuities, and changes in insurance contract liabilities	**$ 803**	$ 734	$ 643	**$ 2,352**	$ 1,956
Market yield adjustment (MYA)	**43**	18	63	**88**	72
Other items excluded from the loss ratio[1]	**-**	-	-	**-**	(20)
Claims, benefits, annuities and changes in insurance contract liabilities excluding the MYA	**$ 846**	$ 752	$ 706	**$ 2,440**	$ 2,008
Loss ratio	**75.5%**	70.1%	73.0%	**75.0%**	70.4%
Non-interest expense	**$ 271**	$ 280	$ 205	**$ 828**	$ 850
Other expenses excluded from the expense ratio[2]	**(2)**	(6)	30	**(12)**	(113)
Operating expenses	**$ 269**	$ 274	$ 235	**$ 816**	$ 737
Expense ratio	**24.0%**	25.5%	24.3%	**25.1%**	25.9%
Combined ratio	**99.5%**	95.6%	97.3%	**100.1%**	96.3%

(1) Comes mainly from the life insurance activities of Western Life Assurance Company, the sale of which was completed on July 1, 2017.
(2) Comes mainly from 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.

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, divided by average equity before non-controlling interests.

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)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[1]	June 30, 2018[1]	September 30, 2017	**September 30, 2018[1]**	September 30, 2017
Surplus earnings before dividends to member caisses	**$ 299**	$ 464	$ 591	**$ 1,122**	$ 1,235
Non-controlling interests' share	**(13)**	(11)	(15)	**(33)**	(34)
Group's share	**$ 286**	$ 453	$ 576	**$ 1,089**	**$** 1,201
Average equity before non-controlling interests' share	**$ 15,980**	$ 15,457	$ 14,912	**$ 15,561**	**$** 14,427
Return on equity[2]	**7.1%**	11.8%	15.3%	**9.4%**	11.1%
Adjusted return on equity[2][3]	**7.3%**	8.6%	8.5%	**8.4%**	8.9%

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(2) Corresponds to an annualized calculation that takes into account the number of days in the period concerned.
(3) 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 is 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 investment income on securities classified and designated as being at fair value through profit or loss, net investment income on securities classified as being at fair value through other comprehensive income, and net investment income on securities measured at amortized cost and other investment income included in the Consolidated Statements of Income under “Net investment income”. It also includes the overlay approach adjustment for insurance operations financial assets. 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, for which results 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 presentation of 2017 investment income does not take into account the standards and amendments adopted on January 1, 2018 and is therefore compliant with IAS 39. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

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

(in millions of dollars)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[1]	June 30, 2018[1]	September 30, 2017	**September 30, 2018[1]**	September 30, 2017
Presentation of income in the Consolidated Financial Statements					
Net interest income	**$ 382**	$ 353	$ 364	**$ 1,103**	$ 1,047
Net premiums	**2,288**	2,225	2,007	**6,677**	6,112
Other income					
Assessments	**97**	99	93	**295**	283
Service agreements	**179**	186	187	**549**	548
Lending fees and credit card service revenues	**172**	164	154	**522**	478
Brokerage and investment fund services	**235**	239	241	**745**	826
Management and custodial service fees	**135**	128	109	**390**	326
Net investment income (loss)[2]	**(213)**	299	(316)	**212**	843
Overlay approach adjustment for insurance operations financial assets	**76**	20	N/A	**265**	N/A
Foreign exchange income	**15**	21	16	**63**	55
Other	**52**	163	330	**285**	440
Total income	**$ 3,418**	$ 3,897	$ 3,185	**$ 11,106**	$ 10,958
Presentation of income in the MD&A					
Net interest income	**$ 382**	$ 353	$ 364	**$ 1,103**	$ 1,047
Net premiums	**2,288**	2,225	2,007	**6,677**	6,112
Other operating income					
Assessments	**97**	99	93	**295**	283
Service agreements	**179**	186	187	**549**	548
Lending fees and credit card service revenues	**172**	164	154	**522**	478
Brokerage and investment fund services	**235**	239	241	**745**	826
Management and custodial service fees	**135**	128	109	**390**	326
Foreign exchange income	**15**	21	16	**63**	55
Other	**52**	163	330	**285**	440
Operating income	**3,555**	3,578	3,501	**10,629**	10,115
Investment income (loss)					
Net investment income (loss)[2]	**(213)**	299	(316)	**212**	843
Overlay approach adjustment for insurance operations financial assets	**76**	20	N/A	**265**	N/A
	(137)	319	(316)	**477**	843
Total income	**$ 3,418**	$ 3,897	$ 3,185	**$ 11,106**	$ 10,958

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

(2) The breakdown of this line item is presented in Note 12, “Net interest income and net investment income (loss)”, to the Interim Consolidated Financial Statements.

Credit loss provisioning rate

The credit loss 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 credit loss provisioning rate as presented in the MD&A.

(in millions of dollars and as a percentage)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[1]	June 30, 2018[1]	September 30, 2017	September 30, 2018[1]	September 30, 2017
Provision for credit losses	**$ 73**	$ 63	$ 72	**$ 225**	$ 204
Average gross loans	**61,200**	59,055	55,458	**59,805**	54,155
Average gross acceptances	**147**	43	100	**92**	79
Average gross loans and acceptances	**$ 61,347**	$ 59,097	$ 55,558	**$ 59,897**	$ 54,234
Credit loss provisioning rate[2]	**0.47%**	0.43%	0.51%	**0.50%**	0.50%

[1] The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

[2] Corresponds to an annualized calculation that takes into account the number of days in the period concerned.

CHANGES IN THE REGULATORY ENVIRONMENT

This section presents items related to changes in the regulatory environment that apply to Desjardins Group as a whole, including those specific to the Federation and its components.

Desjardins Group closely monitors changes in regulation as they relate to financial products and services, as well as new developments in fraud, corruption, tax evasion, protection of personal information, money laundering, terrorist financing and domestic and international economic sanctions in order to mitigate any negative impact on its operations, and aims to comply with best practices in this regard. Additional information can be found in the “Regulatory environment” section of the 2017 annual MD&A, and the “Capital management” section presents further information on regulatory developments relating to capital.

The *Act mainly to improve the regulation of the financial sector, the protection of deposits of money and the operation of financial institutions*

On June 13, 2018, the Quebec National Assembly passed 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 Act), which applies to all institutions and intermediaries operating in Quebec’s financial sector. The main goal of the Act is 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 Act affects a series of laws, such as 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* has been amended, among other things, to prescribe the rules for organizing a network of financial services cooperatives and a financial group, and the rules for issuing capital shares and investment shares.

The Act also adds a chapter concerning the *Groupe coopératif Desjardins* (the cooperative group), which comprises the Desjardins caisses in Quebec, the Federation and the *Fonds de sécurité* Desjardins. The chapter aims to strengthen financial solidarity mechanisms within Desjardins, among other things. In this way, the Act affirms the Federation’s mission to look after Desjardins Group’s risk management and see to the financial health of the cooperative group and its sustainability. The Federation and the *Fonds de sécurité Desjardins* have additional special powers of supervision and intervention regarding the protection of creditors, including depositors, and the public interest. As well, the Federation may, in accordance with its mission and when it considers that the financial position of the cooperative group so warrants, give written instructions to any caisse or order it to adopt and apply a recovery plan. For its part, the *Fonds de sécurité Desjardins* is required to ensure the distribution of capital and other assets among the components of the cooperative group so that each one can perform its obligations to its depositors and other creditors in full, correctly and without delay. It is required to intervene with a component of the cooperative group each time it appears necessary to do so in order to protect the component’s creditors. The *Fonds de sécurité Desjardins* may, in such circumstances, order the assignment of any part of the business of a caisse, order the amalgamation or dissolution of caisses or establish a legal entity to facilitate the liquidation of a caisse’s bad assets. Furthermore, the *Fonds de sécurité Desjardins* mutualizes the cost of its interventions between the components belonging to the cooperative group. In addition, if it considers that its financial resources are inadequate to carry out its mission, it may set a special assessment and require any component of the cooperative group to pay it. The revised Act also provides that all the caisses, the Federation and the *Fonds de sécurité Desjardins* may be amalgamated into a single legal entity to be wound up, as these entities cannot be wound up in any other manner.

The amendments to the *Deposit Insurance Act* (to be renamed the *Deposit Institutions and Deposit Protection Act*) provide for new rules for 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 Act introduces a new *Insurers Act* that provides for revised supervision for Quebec insurers. A significant change in this new legislation is to allow insurers to sell insurance over the Internet. A few changes aimed at modernizing the *Act respecting the distribution of financial products and services* were also introduced, such as rules for insurance brokers in offering products and new rules applicable to distributing products without a representative. In addition, in property and casualty insurance, the Act makes it mandatory for divided co-owners to have co-ownership insurance (commonly known as condominium insurance).

Generally speaking, the provisions of the Act applicable to financial services cooperatives came into force on July 13, 2018, one month after assent, but there are several exceptions. Among these, the chapter concerning the cooperative group is scheduled to come into force within six months after the Act has received assent, when the first internal by-law of the cooperative group is adopted. The new provisions of the *Insurers Act*, for their part, will come into force on June 13, 2019 or subsequently, as the case may be, along with a large portion of the amendments to the *Act respecting the distribution of financial products and services.*

Desjardins Group is continuing its work to update its frameworks in order to reflect the new requirements.

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 for financial services cooperatives, 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, given that discussions with the AMF are still underway on how Desjardins Group will apply them.

The Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA)

In June 2018, proposals for significant changes to the PCMLTFA and its regulations were published by the Department of Finance Canada. Desjardins Group is participating in work sessions with the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), the Department of Finance Canada and other industry players to discuss these and other changes to the Canadian money laundering and terrorist financing (ML/TF) regime. While preparing for the implementation of these legislative changes, Desjardins Group is continuing to closely monitor developments to assess their impact on its operations.

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. The deregulation bill of U.S. Congress and the American regulators has been set in motion, in particular with the enactment of a statute providing some relief concerning certain rules prescribed by the *Dodd-Frank Wall Street Reform and Consumer Protection Act* and a proposal for a draft regulation simplifying the Volcker rule which deals with proprietary trading and hedge fund ownership interests. Desjardins Group continues to closely monitor developments in these draft reforms, for which the scope and timetable remain uncertain at this time.

Recapitalization regime for domestic systemically important banks

On April 18, 2018, the Department of Finance Canada published the final version of three regulations to implement the main features of the Bank Recapitalization (Bail-in) Regime and the OSFI issued the final version of its guideline on Total Loss Absorbing Capacity (TLAC). 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. These regulations and the TLAC guideline came into force on September 23, 2018. 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 to Desjardins Group because it is regulated by the AMF. Furthermore, the amendments to the *Deposit Insurance Act* (to be renamed the *Deposit Institutions and Deposit Protection Act*) passed by the Quebec government on June 13, 2018, as mentioned above, provide for certain recovery and resolution mechanisms in the event of the failure of deposit-taking institutions. On October 25, 2018, the AMF issued for comment its draft regulations on a bail-in regime for a cooperative group as well as a draft TLAC guideline. The comment period initiated by the AMF will end on November 23, 2018. Desjardins Group will continue to monitor developments in this file and is expecting the adoption and implementation of a recapitalization regime similar to the federal one described above.

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) came into force on November 1, 2018. 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 came into force on May 25, 2018, provides for new obligations that will apply internationally to entities that control or process the personal data of citizens in the territory of the European Union. Although the impact of this regulation is not considered significant for Desjardins Group, the organization must closely monitor this file since several of its competitors are subject to it in whole or in part. In Quebec, consultations took place concerning amendments to *An Act respecting the protection of personal information in the private sector* (ARPPIPS). As a result, 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 financial disclosure 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 for financial services cooperatives, 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. In the third quarter of 2018, the AMF presented a draft update of its guideline. The changes would be effective in 2019 and include requirements resulting from the second phase of the standard related to the third pillar, particularly with respect to composition of capital and total loss absorbing capacity.

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 replaced the *Capital Adequacy Requirements Guideline (CAR) – Life and Health Insurance* as of January 1, 2018. The subsidiary Desjardins Financial Security Life Assurance Company complies with the requirements of the new guideline.

Report on Ontario's auto insurance plan

Before the election, in June 2018, of a new majority government in Ontario, the Ontario Finance Minister at the time unveiled the Fair Auto Insurance Plan in December 2017, aimed at making automobile insurance more affordable for drivers and providing better care for accident victims. The Plan was based on a report by David Marshall on the province of Ontario's automobile insurance system, released in April 2017, and provided for the implementation by the government of various initiatives in the short- and medium-term. In spite of the uncertainty surrounding the potential implementation of the recommendations as a result of the change in government, Desjardins Group continues to monitor and support developments in Ontario's automobile insurance system.

Guideline on granting residential mortgages

In February 2018, the AMF issued the revision of its guideline on granting residential mortgages, which went into effect in March 2018. The AMF's requirements are similar to those of the OSFI, issued in October 2017, which aim to encourage mortgage lenders to remain prudent in their mortgage underwriting practices and set a minimum interest rate or "stress test" for uninsured mortgages. Desjardins Group has already applied these practices since January 1, 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 multiyear 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. In May 2018, the Department of Finance Canada launched consultations as part of the review of the *Canadian Payments Act*. 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 future changes.

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. Until the end of 2020, the withholding tax and reporting obligations determined in section 871(m) will 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.

Regulation 93-101, Derivatives: Business Conduct and *Regulation 93-102, Derivatives: Registration*

In April 2017, the Canadian Securities Administrators (CSA) issued draft *National Instrument 93-101 – Derivatives: Business Conduct* and draft *Companion Policy 93-101 Derivatives: Business Conduct* to establish a comprehensive regime for regulating the business conduct of participants in over-the-counter derivatives markets. In June 2018, the CSA published a second version of these drafts for comment. The consultation ended in September 2018. In April 2018, the CSA published for consultation draft *National Instrument 93-102 – Derivatives: Registration* and draft *Companion Policy 93-102 – Derivatives: Registration* for derivatives dealers, derivatives advisers and potentially other derivatives market participants. This consultation also ended in September 2018. 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 (MiFID 2), in the form of the *Markets in Financial Instruments Directive* and the *Markets in Financial Instruments Regulation*. The regulatory requirements related to the MiFID 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 in Canada and the notices issued in this regard by the CSA.

Report on Climate change-related Disclosure Project

On April 5, 2018, the CSA issued CSA *Staff Notice 51-354, Report on Climate change-related Disclosure Project*. The report summarizes the findings of its project to review the disclosure by reporting issuers of risks and financial impacts associated with climate change, and its plans for future work. The Staff Notice also mentions that the CSA will continue to monitor the quality of issuers' disclosure with respect to climate change-related matters, best practices in the area of climate change-related disclosure and the development of disclosure frameworks. Desjardins Group welcomes these findings and supports the development of climate change-related disclosure. Desjardins Group is closely monitoring regulatory developments in this regard.

ECONOMIC ENVIRONMENT AND OUTLOOK

Global economy

The global economy has continued to post strong gains, but over the last few months the growth appears to have stabilized somewhat. Global trade has even slowed since last winter as a result of the protectionist measures taken by the U.S. government and retaliation by other countries. In the eurozone, real GDP is expected to grow only 2.0% in 2018 following a 2.5% increase in 2017. This is due to slower growth in many of the zone's member countries in the first two quarters of the year. Since the Brexit referendum, the United Kingdom has been unable to profit from the improved global economic conditions as much as the other industrialized economies. The political uncertainties surrounding Brexit have not been quelled, and we still do not know what type of agreement will govern relations between the United Kingdom and the European Union after the separation. As for China, escalating trade tensions with the U.S. are giving cause for concern. The U.S. has already added tariffs on numerous imported Chinese goods, including steel and aluminum, and President Donald Trump has floated the idea of imposing as much again in tariffs on other Chinese imports. China quickly retaliated with tariffs on many imported goods from the U.S. Certain Chinese indicators are already showing the strain of these trade constraints. China's real GDP is expected to grow 6.5% this year, on the heels of a 6.9% gain last year. Real global GDP is expected to increase from 3.7% in 2017 to 3.8% in 2018 and 2019. However, the protectionist threat from the U.S. weighs on these prognoses.

The last few months have been particularly difficult for the emerging countries, as trade tensions and a strengthening U.S. dollar have placed considerable pressure on countries with structural weaknesses. This has led to sharp drop in metal prices, but oil prices have been rising as the deadline approaches for sanctions to be imposed on Iranian oil exports. European stock markets have also experienced difficulties, the political situation in Italy still a concern, and several European banks are considered at risk should there be defaults in Turkey. These international uncertainties have had minimal impact on North American financial markets, although the Toronto Stock Exchange was adversely affected by the drop in metal prices and the considerable uncertainties still hanging over the future of NAFTA. In contrast, the New York Stock Exchange posted its best quarter since the fall of 2013, with the S&P 500 rising over 7% on the strong economy and excellent corporate profits.

Yields on North American bonds were low through most of the summer, but recently have begun trending upward. It would appear that a favourable economic outlook, rising inflation and wage growth, as well as the optimistic tone among the monetary authorities have begun to convince investors that key interest rates will continue to rise. The U.S. Federal Reserve (the Fed) announced more monetary tightening at the end of September. This was the fourth consecutive quarter in which the Fed raised the Federal Fund Rate by 0.25%, and all signals suggest that this pace will be maintained over the next year. The Bank of Canada also raised its key policy rate by 0.25% in October and has clearly signalled its intention to continue its monetary tightening efforts. Other gradual increases in key interest rates are expected on both sides of the border next year, but they should be implemented more slowly in Canada where high household debt levels effectively magnify the impacts of monetary tightening. In this environment, the recent upward trend in bond yields appears set to continue, although yields should remain relatively low from a historical perspective. Profiting from higher oil prices, the Canadian dollar has been relatively stable over the last few months vis-à-vis a strong U.S. dollar. The Canadian dollar has benefited from the announcement of a new trade agreement between the U.S., Canada and Mexico, but an expected widening of interest rate spreads with the U.S. could limit the dollar's gains against its U.S. counterpart.

United States

The U.S. economy rallied in the spring. Real GDP grew at an annualized rate of 4.2%, the economy's best performance since the summer of 2014. After a rather weak start to the year, consumer spending rose sharply, for annualized growth of 3.8%. The expansion was also supported by a temporary jump in exports and good growth in non-residential construction. Household and business confidence was particularly strong, and the economy continued to reap dividends from tax cuts. However, it remains to be seen how the U.S. economy will react to the protectionist measures implemented by the Trump administration. For now, real GDP is expected to have grown 2.9% in 2018, with another 2.7% increase in 2019. Labour market conditions should continue to improve, while inflation is expected to grow at a faster pace.

Canada

After growing only 1.4% in the first quarter of 2018, the Canadian economy rallied in the second quarter, posting a 2.9% gain (annualized rate). Moreover, consumer spending picked up and residential investment stabilized following a difficult period at the beginning of the year related to the new restrictive rules. In the spring, the external sector made a major contribution to economic growth due to a substantial rise in exports. The Canadian economy may nevertheless benefit from greater stability over the next few quarters, and real GDP should grow by approximately 2% on average. In domestic demand, household consumption will continue to benefit from various factors in its favour. The outlook for non-residential investment over the next few quarters is quite positive. The disappearance of excess production capacity is imposing more and more constraints. According to a Bank of Canada survey, close to 57% of businesses will have difficulty satisfying the expected increase in demand. Many businesses will therefore invest more in order to meet the current and future demand. On the other hand, the announcement of a new trade agreement between Canada, the U.S. and Mexico should dispel fears that the U.S. will impose new tariffs, particularly on automotive products. Under these conditions, the climate of uncertainty should begin to lift, and this may bode well for the investment projects of many companies. In the final analysis, Canadian real GDP may grow 2.1% in 2018 and another 2.0% in 2019.

Quebec

The Quebec economy grew at a healthy pace in the second quarter of 2018, with real GDP expanding at an annualized rate of 2.5%. The strength of consumption and investment has proven to be a strong foundation. Household spending has been stable despite a decline in employment since the beginning of the year. A low unemployment rate, at around 5.5%, and more generous wage increases are helping maintain a high level of confidence among Quebecers. The residential sector continues to grow at a good pace, despite gradually rising mortgage rates. Existing homes sales continue to grow, and the shortage of properties for sale is slowly pushing up average sales prices. The increase from last year is from 3% to 5% in most regions of the province. The high level of confidence among SMEs in Quebec, as measured by the Business Barometer®, is apparent in rising business investment. The new trade agreement between Canada and the U.S. should dispel much of the uncertainty. However, the tariffs on steel and aluminum will probably not be lifted, and their impact will gradually move through the industrial chain of these products. Our scenario suggests real GDP growth of 2.6% in 2018, slower than the 3.0% recorded for 2017.

REVIEW OF FINANCIAL RESULTS

IMPACT OF SIGNIFICANT TRANSACTIONS

Creation of Aviso Wealth in 2018

On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction led to the creation of Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and the partnership between the Centrals and The CUMIS Group. For Desjardins Group, the interest held in Aviso Wealth represents an investment in a joint venture and is recognized using the equity method of accounting in the Wealth Management and Life and Health Insurance segment. A $3 million share in Aviso Wealth was recognized in the Consolidated Statements of Income for the nine-month period ended September 30, 2018.

The table below presents the operating results of the subsidiary Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P., included in the Federation's financial results for the Wealth Management and Life and Health Insurance segment.

(in millions of dollars)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018	June 30, 2018	September 30, 2017	**September 30, 2018**	September 30, 2017
Other operating income[1]	**$ -**	$ -	$ 30	**$ 49**	$ 90
Operating income[1]	**-**	-	30	**49**	90
Non-interest expense	**-**	-	28	**44**	84
Income taxes on surplus earnings	**-**	-	-	**1**	1
Surplus earnings before member dividends	**$ -**	$ -	$ 2	**$ 4**	$ 5

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

Sale of Western Financial Group Inc. and Western Life Assurance Company in 2017

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.

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

(in millions of dollars)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018	June 30, 2018	September 30, 2017	**September 30, 2018**	September 30, 2017
Net interest income	**$ -**	$ -	$ -	**$ -**	$ 3
Net premiums	**-**	-	-	**-**	65
Other operating income[1]	**-**	-	-	**-**	97
Operating income[1]	**-**	-	-	**-**	165
Investment income[1]	**-**	-	-	**-**	9
Total income	**-**	-	-	**-**	174
Claims, benefits, annuities and changes in insurance contract liabilities	**-**	-	-	**-**	22
Non-interest expense	**-**	-	-	**-**	124
Income taxes on surplus earnings	**-**	-	-	**-**	9
Surplus earnings before dividends to member caisses	**$ -**	$ -	$ -	**$ -**	$ 19

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

ANALYSIS OF RESULTS

Financial results and indicators

(in millions of dollars and as a percentage)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[1]	June 30, 2018[1]	September 30, 2017	**September 30, 2018[1]**	September 30, 2017
Results					
Net interest income	**$ 382**	$ 353	$ 364	**$ 1,103**	$ 1,047
Net premiums	**2,288**	2,225	2,007	**6,677**	6,112
Other operating income[2]					
Assessments	**97**	99	93	**295**	283
Service agreements	**179**	186	187	**549**	548
Lending fees and credit card service revenues	**172**	164	154	**522**	478
Brokerage and investment fund services	**235**	239	241	**745**	826
Management and custodial service fees	**135**	128	109	**390**	326
Foreign exchange income	**15**	21	16	**63**	55
Other	**52**	163	330	**285**	440
Operating income[2]	**3,555**	3,578	3,501	**10,629**	10,115
Investment income (loss)[2]					
Net investment income (loss)	**(213)**	299	(316)	**212**	843
Overlay approach adjustment for insurance operations financial assets	**76**	20	N/A	**265**	N/A
	(137)	319	(316)	**477**	843
Total income	**3,418**	3,897	3,185	**11,106**	10,958
Provision for credit losses	**73**	63	72	**225**	204
Claims, benefits, annuities and changes in insurance contract liabilities	**1,380**	1,727	1,000	**4,763**	4,675
Non-interest expense	**1,598**	1,568	1,433	**4,794**	4,588
Income taxes on surplus earnings	**68**	75	89	**202**	256
Surplus earnings before dividends to member caisses	**$ 299**	$ 464	$ 591	**$ 1,122**	$ 1,235
Adjusted surplus earnings before dividends to member caisses[2]	**$ 299**	$ 335	$ 333	**$ 993**	$ 986
Contribution to consolidated surplus earnings by business segment[3]					
Personal and Business Services	**$ 72**	$ 71	$ 86	**$ 249**	$ 255
Wealth Management and Life and Health Insurance	**174**	331	121	**711**	453
Property and Casualty Insurance	**70**	52	318	**148**	398
Treasury and Other Support to Desjardins Group Entities	**(17)**	10	66	**14**	129
	$ 299	$ 464	$ 591	**$ 1,122**	$ 1,235
Indicators					
Return on equity[2]	**7.1%**	11.8%	15.3%	**9.4%**	11.1%
Adjusted return on equity[2]	**7.3**	8.6	8.5	**8.4**	8.9

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(2) See "Basis of presentation of financial information".
(3) The breakdown by line item is presented in Note 13, "Segmented information", to the Interim Consolidated Financial Statements.

COMPARISON OF THE THIRD QUARTERS OF 2018 AND 2017

Surplus earnings

For the third quarter ended September 30, 2018, the Federation posted surplus earnings before dividends to member caisses of $299 million, a $292 million decrease compared to the corresponding quarter of 2017. Surplus earnings, adjusted for the gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, were down $34 million, or 10.2%. This decrease was chiefly due to lower surplus earnings from treasury operations and derivative financial instruments associated with hedging activities as well as the higher claims experience in property and casualty insurance, partially mitigated by a more favourable claims experience in life and health insurance operations and growth in income from assets under management.

Business segment contributions to surplus earnings

- Personal and Business Services: **Contribution of $72 million,** down $14 million, or 16.3% compared to the same period in 2017.
  - Expenses related to the winding down of Zag Bank's operations recognized in the third quarter of 2018.
  - The segment contributed 24.1% to surplus earnings.
- Wealth Management and Life and Health Insurance: **Contribution of $174 million,** up $53 million compared to the third quarter of 2017.
  - More favourable claims experience.
  - Higher income as a result of growth in assets under management.
  - The segment contributed 58.2% to surplus earnings.
- Property and Casualty Insurance: **Contribution of $70 million,** down $248 million, and net surplus earnings adjusted for specific items, up $7 million compared to the same period in 2017.
  - Increase in investment income.
  - Partially offset by a higher claims experience than in the comparative quarter of 2017, particularly due to one catastrophe as well as favourable changes in prior year claims, which were lower than in the comparative quarter.
  - The segment contributed 23.4% to surplus earnings.

- **Return on equity was 7.1%,** compared to 15.3% for the quarter ended September 30, 2017.
- **Adjusted return on equity was 7.3%,** down compared to the 8.5% rate in the quarter ended September 30, 2017, mainly because of the decrease in adjusted surplus earnings, as explained earlier.

Operating income

Operating income totalled $3,555 million, up $54 million, or 1.5%, compared to the third quarter of 2017. Excluding the gross gain of $278 million related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, operating income would have been up $332 million, or 10.3%, compared to the same period in 2017.

Net interest income was up $18 million, or 4.9%, to total $382 million, compared to $364 million for the same period in 2017, because of growth in the entire portfolio of loans and acceptances outstanding of $6.0 billion, or 10.6%, over the year. This portfolio comprises financing activities in consumer, credit card and other personal loans, as well as loans to business and government, and growth in the securities portfolio.

Net premiums were up $281 million, or 14.0%, compared to the third quarter of 2017, to total $2,288 million as at September 30, 2018.

Wealth Management and Life and Health Insurance segment

- **Net insurance and annuity premiums of $1,209 million,** up $131 million, or 12.2%, due to business growth.
  - Premiums up $131 million, with annuities accounting for $116 million and individual insurance for $14 million.

Property and Casualty Insurance segment

- **Net premiums of $1,120 million,** up $153 million, or 15.8%, essentially due to the following:
  - Increase of $100 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of the Canadian operations of State Farm Mutual Automobile Insurance Company (State Farm), mainly due to a change in the rate of cession stipulated in the treaty, which provides for the scaling 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.

Other operating income stood at $885 million, which is a decrease of $245 million, or 21.7%, compared to the third quarter of 2017. Excluding the gross gain of $278 million related to the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, other operating income would have been up $33 million, or 3.9%, compared to the same period in 2017, mainly on account of the following:

- Higher income as a result of growth in assets under management.
- Growth in business volumes from card payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.

This increase was partially offset by:

- Decrease in income following the transaction involving Qtrade Canada Inc.

Investment income

A loss of $137 million, presented under "Investment income (loss)", compared to a $316 million loss recognized in the comparative quarter, essentially because of the following:

- Smaller loss primarily due to changes 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.
  - Changes for the most part due to fluctuations in the fair value of the bond portfolio as a result of a smaller increase in market interest rates than in the comparative quarter.
- Higher dividend income than in the comparative quarter of 2017, particularly due to income reinvestment, including prior period adjustments.
- Smaller reduction in the fair value of matched bonds in the Property and Casualty Insurance segment than in the third quarter of 2017, mainly on account of a smaller increase in market interest rates than in the comparative quarter. It should be remembered that this reduction in the value of bonds was offset by a similar reduction in the cost of claims because of a matching strategy.
- Partially offset by a decrease in trading income.

Total income

Total income amounted to $3,418 million, an increase of $233 million, or 7.3%, compared to the same period in 2017.

Provision for credit losses

The provision for credit losses totalled $73 million, which is stable compared to the same quarter in 2017. The Federation has continued to present a quality loan portfolio in 2018.

- The credit loss provisioning rate was 0.47% for the third quarter of 2018, compared to 0.51% in the corresponding period of 2017.
- The ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.36% compared to 0.13% as at September 30, 2017. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered negligible.

Claims, benefits, annuities and changes in insurance contract liabilities

Expenses related to claims, benefits, annuities and changes in insurance contract liabilities totalled $1,380 million, up $380 million, or 38.0%, compared to the corresponding quarter of 2017.

Wealth Management and Life and Health Insurance segment

- **Cost of claims of $573 million,** up $216 million, or 60.5%. This change was basically due to the following:
  - Increase of $244 million in actuarial liabilities under "Insurance contract liabilities", which included the effect of the increase in the fair value of matched investments.
  - However, the more favourable claims experience partially offset by increase in actuarial liabilities.

Property and Casualty Insurance segment

- **Cost of claims of $803 million,** up $160 million, or 24.9%, essentially as a result of the following:
  - Growth in business, which led to a higher cost of claims.
  - Increase due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - The loss ratio was 75.5% for the period ended September 30, 2018, compared to 73.0% for the corresponding period in 2017:
    - Higher ratio attributable to the greater impact of catastrophes and major events compared to third quarter 2017, 3.5% vs. 2.0%. The third quarter of 2018 was marked by a catastrophe in September, namely damage caused by high winds and tornadoes, mainly in the Ottawa and Gatineau regions. In the corresponding quarter of 2017, two major events were noted, but no catastrophes.
    - Less positive developments than in third quarter 2017 concerning prior year claims, (8.0)% vs. (9.5)%.

Non-interest expense

- Non-interest expense totalled $1,598 million, up $165 million, or 11.5%, compared to the third quarter of 2017, mainly because of:
  - Increase in expense due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increase in expense related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Business growth, particularly in assets under management.

  This increase was partially offset by the following:
  - Decrease in expense following the transaction involving Qtrade Canada Inc.

- Remuneration and other payments included in non-interest expense were $140 million, for a $5 million, or 3.7%, increase compared to the same period in 2017 due to growth in sales of various Desjardins Group products by the caisse network.

Income taxes

- **Income taxes on surplus earnings before dividends to member caisses of $68 million,** down $21 million compared to the third quarter of 2017.
  - Effective tax rate of 18.5% for the quarter ended September 30, 2018, up compared to 13.1% for the corresponding period in 2017.
  - Excluding the effect of the specific items, the effective tax rate would have been 18.5% for the third quarter of 2018, compared to 17.0% for the same period in 2017.

COMPARISON OF THE FIRST NINE MONTHS OF 2018 AND 2017

Surplus earnings

For the first nine months ended September 30, 2018, the Federation posted surplus earnings before dividends to member caisses of $1,122 million, a $113 million, or 9.1%, decrease compared to the same period in 2017. Surplus earnings, adjusted for the gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in the second quarter of 2018, and the gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, were up $7 million, or 0.7%, and totalled $993 million.

Business segment contributions to surplus earnings

- Personal and Business Services: **Contribution of $249 million,** down $6 million, or 2.4%, compared to the same period in 2017.
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses related to the winding down of Zag Bank's operations recognized in the third quarter of 2018.
  - Lower income from trading and new issues on capital markets.
  - Offset by the profit related to the restructuring of Interac Corp.
  - The segment contributed 22.2% to surplus earnings.
- Wealth Management and Life and Health Insurance: **Contribution of $711 million,** up $258 million, and surplus earnings, adjusted for specific items, up $129 million compared to the corresponding period in 2017.
  - Higher gains on the disposal of securities and real estate investments in 2018.
  - More favourable claims experience.
  - Higher income as a result of growth in assets under management.
  - The segment contributed 63.4% to surplus earnings.
- Property and Casualty Insurance: **Contribution of $148 million,** down $250 million, or 62.8%, and surplus earnings, adjusted for specific items, down $9 million, or 5.7%, compared to the corresponding period in 2017.
  - Impact of the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.
  - Higher claims experience than in the first nine months of 2017.
  - Offset by an increase in investment income.
  - The segment contributed 13.2% to surplus earnings.

- **Return on equity was 9.4%,** compared to 11.1% for the nine months ended September 30, 2017.
- **Adjusted return on equity was 8.4%,** compared to 8.9% for the nine months ended September 30, 2017.

Operating income

Operating income totalled $10,629 million, up $514 million, or 5.1%, compared to the first nine months of 2017. Excluding the gain before income taxes of $132 million related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in the second quarter of 2018, and the gross gain of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, operating income would have been $10,497 million, up $660 million, or 6.7%, compared to the same period in 2017.

Net interest income was up $56 million, or 5.3%, to total $1,103 million, compared to $1,047 million for the same period in 2017, because of growth in the entire portfolio of loans and acceptances outstanding of $6.0 billion, or 10.6% over the year. This portfolio comprises financing activities in consumer, credit card and other personal loans, as well as loans to business and government, and growth in the securities portfolio.

Net premiums were up $565 million, or 9.2%, compared to the first nine months of 2017, to total $6,677 million as at September 30, 2018.

Wealth Management and Life and Health Insurance segment

- **Net insurance and annuity premiums of $3,542 million,** up $224 million, or 6.8%, due to business growth.
  - Premiums up $224 million, with annuities accounting for $131 million, group insurance for $64 million, and individual insurance for $29 million.

Property and Casualty Insurance segment

- **Net premiums of $3,252 million,** up $339 million, or 11.6%, essentially due to the following:
  - Increase of $258 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, mainly due to a change in the rate of cession stipulated in the treaty, which provides for the scaling 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.

Other operating income stood at $2,849 million, which is a decrease of $107 million, or 3.6%, compared to the first nine months of 2017. Excluding the gain, before income taxes, of $132 million related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P. recognized in the second quarter of 2018, and the gross gain of $278 million on the sale of the subsidiaries Western Financial Group Inc. and Western Life Assurance Company recognized in the third quarter of 2017, other operating income would have been $2,717 million, up $39 million, or 1.5%, compared to the same period in 2017, mainly on account of the following items:

- Higher income as a result of growth in assets under management.
- Growth in business volumes from card payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.
- Offset by a decrease in commission income following the sale of Western Financial Group Inc. and the transaction involving Qtrade Canada Inc.

Investment income

Investment income totalled $477 million, a decrease of $366 million compared to the first nine months of 2017, essentially because of the following:

- Decrease primarily due to changes in the fair value of assets backing liabilities related to life and health insurance operations.
  - Offset by the change in actuarial liabilities leading to lower 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 bond portfolio as a result of higher interest rates.
- Lower trading income.
- Reduction in the fair value of derivative financial instruments associated with the Federation's hedging activities.

This decrease was partially offset by the following:

- Higher gains on the disposal of securities and real estate investments in the first nine months of 2018.
- Higher dividend income than in the same period of 2017, particularly due to income reinvestment, including prior period adjustments.
- Profit related to the restructuring of Interac Corp.

Total income

Total income amounted to $11,106 million, an increase of $148 million, or 1.4%, compared to the same period in 2017.

Provision for credit losses

The provision for credit losses totalled $225 million, up $21 million, or 10.3%. The increase is mainly due to growth in loans outstanding, the revision of economic scenarios and the migration of borrower ratings. The adoption of IFRS 9 as at January 1, 2018 made the allowance for credit losses more volatile. In spite of this increase, the Federation has continued to present a quality loan portfolio in 2018.

- The credit loss provisioning rate was 0.50% for the first nine months of 2018, the same ratio as in the corresponding period of 2017.
- The ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.36% compared to 0.13% as at September 30, 2017. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered negligible.

Claims, benefits, annuities and changes in insurance contract liabilities

Expenses related to claims, benefits, annuities and changes in insurance contract liabilities totalled $4,763 million, up $88 million, or 1.9%, compared to the corresponding period of 2017.

Wealth Management and Life and Health Insurance segment

- **Cost of claims of $2,407 million,** down $313 million, or 11.5%. This reduction was basically the result of the following:
  - Decrease of $322 million in the actuarial liabilities recognized under "Insurance contract liabilities", which includes the effect of a decrease in the fair value of matched investments. More favourable product claims experience contributed to reducing actuarial liabilities.
  - Offset by an increase in benefits and actuarial liabilities related to growth in operations.

Property and Casualty Insurance segment

- **Cost of claims of $2,352 million,** up $396 million, or 20.2%, essentially as a result of the following:
  - Growth in business, which led to a higher cost of claims.
  - Increase due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - The P&C insurers' loss ratio was 75.0% for the nine-month period ended September 30, 2018, compared to 70.4% for the corresponding period in 2017.
    - Higher ratio primarily attributable to the less favourable change than in the first nine months of 2017 concerning prior year claims, (9.9)% vs. (12.6)%, mainly in automobile insurance.
    - Greater impact of catastrophes and major events than in the first nine months of 2017, 4.3% compared to 2.9%.

Non-interest expense

- Non-interest expense totalled $4,794 million, up $206 million, or 4.5%, compared to the first nine months of 2017. Remuneration and other payments included in non-interest expense were $423 million, a $20 million, or 5.0%, increase compared to the same period in 2017 due to growth in sales of various Desjardins Group products by the caisse network. If this item were excluded, non-interest expense would have been up $186 million, or 4.4%, essentially because of:
  - Business growth, particularly in card payment and financing activities and in assets under management.
  - Increase in expense due to the reinsurance treaty signed as part of the acquisition of State Farm's Canadian operations.
  - Increase in expense related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Offset by a decrease in expense following the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017 as well as the transaction involving Qtrade Canada Inc.

Income taxes

- **Income taxes on surplus earnings before dividends to member caisses of $202 million,** down $54 million compared to the corresponding period in 2017.
  - Effective tax rate of 15.3% for the first nine months of 2018, down compared to 17.2% for the corresponding period in 2017.
  - Excluding the effect of the specific items, the effective tax rate would have been 16.7% for the first nine months of 2018 and 18.7% for the same period in 2017. The lower rate is mainly due to the following:
    - Income tax recovery on remuneration of G capital shares in the first quarter of 2018.
    - Gains on disposals taxable at 50% in the first nine months of 2018.

RESULTS BY BUSINESS SEGMENT

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 the Federation operates, and on its internal management structure. 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.

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 financial markets.

Additional information about each business segment, particularly its profile, activities, industry and 2018 strategies and priorities, can be found on pages 27 to 39 of the 2017 annual MD&A.

Personal and Business Services

The Personal and Business Services segment is central to Desjardins Group's operations. It is responsible for developing a comprehensive, integrated line of products and services designed to meet the needs of individuals, businesses, institutions, non-profit organizations and cooperatives through the Desjardins caisse network, the Desjardins Business centres and specialized teams. It thereby enables Desjardins Group to be a leader in financial services in Quebec and a player on the financial services scene in Ontario as well. 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 physical and virtual networks through implementing and managing complementary access methods, by phone, online, via applications for mobile devices, and at ATMs. The shared services which the Federation provides to the Personal and Business Services segment are recorded in this segment.

Personal and Business Services – Segment results

(in millions of dollars and as a percentage)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[(1)]	June 30, 2018[(1)]	September 30, 2017[(2)]	**September 30, 2018[(1)]**	September 30, 2017[(2)]
Net interest income	**$ 286**	$ 273	$ 278	**$ 835**	$ 808
Other operating income[(3)]	**403**	406	382	**1,226**	1,163
Operating income[(3)]	**689**	679	660	**2,061**	1,971
Investment income[(3)]	**8**	7	6	**68**	40
Total income	**697**	686	666	**2,129**	2,011
Provision for credit losses	**74**	67	72	**230**	204
Non-interest expense	**522**	518	477	**1,561**	1,460
Income taxes on surplus earnings	**29**	30	31	**89**	92
Net surplus earnings for the period before dividends to member caisses	**$ 72**	$ 71	$ 86	**$ 249**	$ 255
Of which:					
Group's share	**$ 72**	$ 71	$ 86	**$ 249**	$ 255
Indicators					
Average gross loans and acceptances[(3)]	**$ 30,225**	$ 29,181	$ 26,863	**$ 29,225**	$ 25,938
Average deposits[(3)]	**19,163**	18,559	16,710	**18,159**	15,860
Credit loss provisioning rate[(3)]	**0.97%**	0.92%	1.06%	**1.05%**	1.05%
Gross credit-impaired loans[(4)]/gross loans and acceptances[(3)]	**0.72**	0.69	0.27	**0.72**	0.27

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and for the three-month period ended June 30, 2018 takes into account standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
(2) Data for 2017 have been reclassified to conform to the current period's presentation, notwithstanding the standards and amendments adopted on January 1, 2018.
(3) See "Basis of presentation of financial information".
(4) Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.

COMPARISON OF THE THIRD QUARTERS OF 2018 AND 2017 – PERSONAL AND BUSINESS SERVICES

- **Surplus earnings before dividends to member caisses of $72 million,** down $14 million, or 16.3%, essentially due to expenses related to the winding down of Zag Bank's operations.

- **Operating income of $689 million,** up $29 million, or 4.4%.
  - Increase of $8 million in net interest income as a result of year-over-year growth of $3.4 billion, or 12.5%, in the average portfolio of loans and acceptances outstanding. This portfolio includes financing activities in the area of consumer loans and other personal loans, as well as business loans.
  - Other operating income of $403 million, up $21 million, or 5.5%, mainly due to the following:
    - Growth in business volume as a result of card payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.
    - Offset by lower income from new capital market issues.

- **Investment income of $8 million,** up $2 million compared to the corresponding period in 2017.

- **Total income of $697 million,** up $31 million, or 4.7%.

- **Provision for credit losses of $74 million,** unchanged from the comparative period in 2017.

- **Non-interest expense of $522 million,** up $45 million, or 9.4%, mainly as a result of:
  - Expenses related to the winding down of Zag Bank's operations.
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Business growth, especially in activities intended to enhance the offer of services to caisse members and clients.

COMPARISON OF THE FIRST NINE MONTHS OF 2018 AND 2017 – PERSONAL AND BUSINESS SERVICES

- **Surplus earnings before dividends to member caisses of $249 million,** down $6 million, or 2.4%, mainly due to the following:
  - Higher expenses for the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses related to the winding down of Zag Bank's operations.
  - Decrease in income from trading and from new capital market issues.
  - Offset by the profit related to the restructuring of Interac Corp.

- **Operating income of $2,061 million,** up $90 million, or 4.6%.
  - Increase of $27 million in net interest income as a result of year-over-year growth of $3.3 billion, or 12.7%, in the average portfolio of loans and acceptances outstanding. This portfolio includes financing activities in the area of consumer loans and other personal loans, as well as business loans.
  - Other operating income of $1,226 million, up $63 million, or 5.4%, mainly due to:
    - Growth in business volume as a result of card payment activities, including the acquisition and set-up of new Canada-wide credit card portfolios.
    - Offset by lower income from new capital market issues.

- **Investment income of $68 million,** up $28 million, mainly due to:
  - Profit related to the restructuring of Interac Corp.
  - Offset by a decrease in capital market trading income.

- **Total income of $2,129 million,** up $118 million, or 5.9%.

- **Provision for credit losses of $230 million,** up $26 million, or 12.7%, mainly as a result of:
  - Growth in outstandings.
  - Revision of economic scenarios.
  - Migration of borrower ratings.
  - The adoption of IFRS 9 as at January 1, 2018 made the allowance for credit losses more volatile.

- **Non-interest expense of $1,561 million,** up $101 million, or 6.9%, mainly as a result of:
  - Higher expenses related to the acquisition and set-up of new Canada-wide credit card portfolios.
  - Expenses related to the winding down of Zag Bank's operations.
  - Business growth, especially in activities intended to enhance the service offer to caisse members and clients.

Wealth Management and Life and Health Insurance

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 greatest strengths of the Wealth Management and Life and Health Insurance segment include its vast and diversified Canada-wide distribution networks, which are mainly comprised of:

- 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 also distributed directly via customer care centres, online or through applications for mobile devices. Online services are constantly being finetuned so that they meet clients' changing requirements.

On April 1, 2018, Desjardins Group and a partnership comprised of five provincial credit unions (the Centrals) and The CUMIS Group entered into an agreement to combine their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments L.P. This transaction led to the creation of Aviso Wealth, a wealth management company held in equal shares by Desjardins Group and the partnership between the Centrals and The CUMIS Group. Additional information concerning these transactions is found in "Impact of significant transactions", on page 13.

Wealth Management and Life and Health Insurance – Segment results

(in millions of dollars)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[(1)]	June 30, 2018[(1)]	September 30, 2017	**September 30, 2018[(1)]**	September 30, 2017
Net interest income	**$ 1**	$ 1	$ 1	**$ 3**	$ 1
Net premiums	**1,209**	1,190	1,078	**3,542**	3,318
Other operating income[(2)]	**397**	512	368	**1,331**	1,111
Operating income[(2)]	**1,607**	1,703	1,447	**4,876**	4,430
Investment income (loss)[(2)]	**(240)**	250	(385)	**165**	569
Total income	**1,367**	1,953	1,062	**5,041**	4,999
Provision for (recovery of) credit losses	**(1)**	(4)	-	**(5)**	-
Claims, benefits, annuities and changes in insurance contract liabilities	**573**	993	357	**2,407**	2,720
Non-interest expense	**572**	577	564	**1,772**	1,721
Income taxes on surplus earnings	**49**	56	20	**156**	105
Net surplus earnings for the period	**$ 174**	$ 331	$ 121	**$ 711**	$ 453
Specific item, net of income taxes					
Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.	**-**	(129)	-	**(129)**	-
Adjusted net surplus earnings for the period[(2)]	**$ 174**	$ 202	$ 121	**$ 582**	$ 453
Of which:					
Group's share	**$ 174**	$ 331	$ 121	**$ 711**	$ 452
Non-controlling interests' share	**-**	-	-	**-**	1
Indicators					
Net sales of savings products	**$ 2,146**	$ 1,299	$ 1,896	**$ 6,935**	$ 6,475
Insurance sales	**75**	94	100	**251**	428
Group insurance premiums	**828**	821	827	**2,479**	2,415
Individual insurance premiums	**220**	213	206	**645**	616
Annuity premiums	**161**	156	45	**418**	287
Segregated fund receipts	**413**	474	417	**1,555**	1,269

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and for the three-month period ended June 30, 2018 takes into account standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies" to the Interim Consolidated Financial Statements.

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

COMPARISON OF THE THIRD QUARTERS OF 2018 AND 2017 – WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

- **Net surplus earnings of $174 million,** up $53 million, or 43.8%, primarily as a result of:
  - More favourable claims experience.
  - Higher income as a result of growth in assets under management.

- **Operating income of $1,607 million,** up $160 million, or 11.1%, basically due to the following:
  - Increase of $131 million in premiums, with annuities accounting for $116 million, and individual insurance for $14 million.
  - Other operating income totalled $397 million, up $29 million, or 7.9%.
    - Higher income as a result of growth in assets under management.
    - Offset by the decline in income following the transaction involving Qtrade Canada Inc.

- **Loss totalling $240 million, presented under "Investment income (loss)",** compared to a loss of $385 million recognized in the comparative quarter.
  - Smaller loss primarily due to changes 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.
    - Changes for the most part due to fluctuations in the fair value of the bond portfolio, mainly as a result of a smaller increase in market interest rates than in the comparative quarter in 2017.

- **Total income of $1,367 million,** up $305 million, or 28.7%.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of $573 million,** up $216 million, or 60.5%, essentially due to the following:
  - Increase of $244 million in actuarial liabilities under "Insurance contract liabilities", which includes the effect of the increase in the fair value of matched investments.
  - However, more favourable claims experience mitigated the increase in actuarial liabilities.

- **Non-interest expense of $572 million,** up $8 million, or 1.4%, chiefly as a result of the following:
  - Increase in expense related to assets under management.
  - However, the transaction involving Qtrade Canada Inc. led to a decrease in expense.

COMPARISON OF THE FIRST NINE MONTHS OF 2018 AND 2017 – WEALTH MANAGEMENT AND LIFE AND HEALTH INSURANCE

- **Net surplus earnings of $711 million,** up $258 million, or 57.0%, and adjusted net surplus earnings of $582 million, up $129 million, or 28.5%, mainly as a result of:
  - Higher gains on the disposal of securities and real estate investments in 2018.
  - More favourable claims experience.
  - Higher income on account of growth in assets under management.

- **Operating income of $4,876 million,** up $446 million, or 10.1%, primarily due to the following:
  - Increase of $224 million in premiums, with annuities accounting for $131 million, group insurance for $64 million, and individual insurance for $29 million.
  - Other operating income totalled $1,331 million, up $220 million, or 19.8%.
    - Gain related to the transaction involving Qtrade Canada Inc. and the interest in Northwest & Ethical Investments L.P.
    - Higher income as a result of growth in assets under management.

- **Investment income of $165 million,** down $404 million, or 71.0%.
  - Decrease primarily due to changes in the fair value of assets backing liabilities related to life and health insurance operations.
    - Offset by the change in actuarial liabilities leading to lower 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 bond portfolio as a result of higher interest rates.
  - Mitigated by higher gains on the disposal of securities and real estate investments.

- **Total income of $5,041 million,** up $42 million, or 0.8%.

- **Expenses related to claims, benefits, annuities and changes in insurance contract liabilities of $2,407 million,** down $313 million, or 11.5%, essentially due to the following:
  - Decrease of $322 million in actuarial liabilities under "Insurance contract liabilities", which included the effect of the decrease in the fair value of matched investments. The more favourable claims experience of products helped to reduce actuarial liabilities.
  - Offset by the increase in benefits and actuarial liabilities as a result of growth in operations.

- **Non-interest expense of $1,772 million,** up $51 million, or 3.0%, chiefly as a result of:
  - Increase in expense related to assets under management.
  - However, the transaction involving Qtrade Canada Inc. led to a decrease in expense.

Property and Casualty Insurance

The Property and Casualty Insurance segment offers insurance products allowing Desjardins Group members and clients to protect themselves against disasters. It includes the operations of Desjardins General Insurance Group Inc. and its subsidiaries. Its products are distributed through P&C 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, as well as online and via applications for mobile devices.

On July 1, 2017, Desjardins Group completed the sale of two of its subsidiaries, namely Western Financial Group Inc. and Western Life Assurance Company. Additional information concerning these transactions is found under “Impact of significant transactions” on page 13.

Property and Casualty Insurance – Segment results

(in millions of dollars and as a percentage)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018(1)	June 30, 2018(1)	September 30, 2017	**September 30, 2018(1)**	September 30, 2017
Net interest income	**$ -**	$ -	$ -	**$ -**	$ 1
Net premiums	**1,120**	1,073	967	**3,252**	2,913
Other operating income (loss)(2)	**(34)**	(61)	230	**(116)**	236
Operating income(2)	**1,086**	1,012	1,197	**3,136**	3,150
Investment income(2)	**79**	58	9	**227**	129
Total income	**1,165**	1,070	1,206	**3,363**	3,279
Claims, benefits, annuities and changes in insurance contract liabilities	**803**	734	643	**2,352**	1,956
Non-interest expense	**271**	280	205	**828**	850
Income taxes on surplus earnings	**21**	4	40	**35**	75
Net surplus earnings for the period	**$ 70**	$ 52	$ 318	**$ 148**	$ 398
Specific item, net of income taxes					
Gain net of expenses related to the sale of Western Financial Group Inc. and Western Life Assurance Company(3)	**-**	-	(255)	**-**	(241)
Adjusted net surplus earnings for the period(2)	**$ 70**	$ 52	$ 63	**$ 148**	$ 157
Of which:					
Group’s share	**$ 57**	$ 41	$ 303	**$ 115**	$ 365
Non-controlling interests’ share	**13**	11	15	**33**	33
Indicators					
Gross written premiums	**$ 1,363**	$ 1,335	$ 1,207	**$ 3,714**	$ 3,460
Loss ratio(2)	**75.5%**	70.1%	73.0%	**75.0%**	70.4%
Current year loss ratio(2)	**80.0**	78.6	80.5	**80.6**	80.1
Loss ratio related to catastrophes and major events(2)	**3.5**	8.4	2.0	**4.3**	2.9
Ratio of favourable changes in prior-year claims(2)	**(8.0)**	(16.9)	(9.5)	**(9.9)**	(12.6)
Expense ratio(2)	**24.0**	25.5	24.3	**25.1**	25.9
Combined ratio(2)	**99.5**	95.6	97.3	**100.1**	96.3

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and for the three-month period ended June 30, 2018 takes into account standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.
(2) See "Basis of presentation of financial information".
(3) The difference compared to the data presented in the table for the adjusted surplus earnings of the Federation before dividends to member caisses is related to intersegment transaction expenses.

COMPARISON OF THE THIRD QUARTERS OF 2018 AND 2017 – PROPERTY AND CASUALTY INSURANCE

- **Net surplus earnings of $70 million,** down $248 million, and adjusted net surplus earnings up $7 million, or 11.1%, essentially due to:
  - Increase in investment income.
  - Offset, in part, by higher claims experience than in the comparative quarter of 2017, particularly due to one catastrophe as well as favourable changes in prior year claims, which were lower than in the comparative quarter.

- **Operating income of $1,086 million,** down $111 million, or 9.3%.

- **Net premiums of $1,120 million,** up $153 million, or 15.8%, essentially due to:
  - Increase of $100 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm’s Canadian operations, mainly due to the change in the rate of cession stipulated in the treaty, which provides for the scaling down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Increase attributable to the larger number of policies issued as a result of multiple growth initiatives across all market segments and regions.

- **Loss totalling $34 million, presented under “Other operating income (loss)”,** while income was recorded for the comparative quarter of 2017, resulting in a difference of $264 million, mainly because of the gain on the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017 and recorded in the comparative quarter.

- **Investment income of $79 million,** up $70 million, mainly as a result of:
  - Higher dividend income than in the comparative quarter in 2017, particularly due to income reinvestment, including prior period adjustments.
  - Smaller reduction in the fair value of matched bonds than in third quarter 2017, mainly on account of a smaller increase in market interest rates than in the comparative quarter. It should be remembered that this reduction in the value of bonds was offset by a similar reduction in the cost of claims because of a matching strategy.

- **Total income of $1,165 million,** down $41 million, or 3.4%.

- **Cost of claims totalling $803 million,** up $160 million, or 24.9%, mainly as a result of:
  - Business growth leading to a higher cost of claims.
  - Increase due to the reinsurance treaty signed as part of the acquisition of State Farm’s Canadian operations, which provides for the cession, scaled down over a five-year period, of the premiums and claims arising from new business and renewals after the acquisition date.
  - Loss ratio of 75.5% for the period ended September 30, 2018, compared to 73.0% for the corresponding period in 2017:
    - Higher ratio attributable to the greater impact of catastrophes and major events than in the comparative quarter in 2017, 3.5% vs. 2.0%. The third quarter of 2018 was affected by a catastrophe in September, namely damage caused by high winds and tornados mainly in the Ottawa and Gatineau regions. In the corresponding quarter of 2017, two major events had been noted, but no catastrophes.
    - Less positive developments than in third quarter 2017 concerning prior year claims, (8.0)% vs. (9.5)%.

- **Non-interest expense of $271 million,** up $66 million, or 32.2%, mainly as a result of an increase in expense partly due to the effect of the previously mentioned reinsurance treaty on the expense covered by it and because of business growth.

COMPARISON OF THE FIRST NINE MONTHS OF 2018 AND 2017 – PROPERTY AND CASUALTY INSURANCE

- **Net surplus earnings of $148 million,** down $250 million, and adjusted net surplus earnings down $9 million, or 5.7%, essentially due to:
  - Impact resulting from the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.
  - Higher claims experience than in the first nine months of 2017.
  - Offset by the increase in investment income.

- **Operating income of $3,136 million,** down $14 million, or 0.4%.

- **Net premiums of $3,252 million,** up $339 million, or 11.6%, primarily as a result of:
  - Increase of $258 million in net premiums subject to the reinsurance treaty signed as part of the acquisition of State Farm’s Canadian operations, mainly due to the change in the rate of cession stipulated in the treaty, which provides for the scaling 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 the decrease in net premiums following the sale of Western Life Assurance Company on July 1, 2017.

- **Loss totalling $116 million, presented under “Other operating income (loss)”,** while income was recognized for the comparative period of 2017, resulting in a difference of $352 million, mainly because of:
  - Gain on the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017 and recognized in the comparative period.
  - Decline in commission income following the sale of Western Financial Group Inc.

- **Investment income of $227 million,** up $98 million, primarily as a result of:
  - Higher dividend income than in the first nine months of 2017, particularly due to income reinvestment, including prior period adjustments.
  - Net gains, which were higher than those recognized for the same period in 2017, on the disposal of funds and common shares related to the rebalancing of certain portfolios.

- **Total income of $3,363 million,** up $84 million, or 2.6%.

- **Cost of claims totalling $2,352 million,** up $396 million, or 20.2%, essentially due to:
  - Business growth leading to a higher cost of claims.
  - Increase resulting from 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.
  - P&C insurers’ loss ratio of 75.0% for the nine-month period ended September 30, 2018, compared to 70.4% for the corresponding period in 2017.
    - Higher ratio primarily attributable to the less favourable change than in the first nine months of 2017 concerning prior year claims, (9.9)% vs. (12.6)%, mainly in automobile insurance.
    - Greater impact of catastrophes and major events than in the first nine months of 2017, 4.3% compared to 2.9%.

- **Non-interest expense of $828 million,** down $22 million, or 2.6%, mainly as a result of:
  - Decrease in expense due to the sale of Western Financial Group Inc. and Western Life Assurance Company completed on July 1, 2017.
  - Offset by increase in expense partly due to the effect of the previously mentioned reinsurance treaty on the expenses covered by it and because of business growth.

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 treasury activities and financial intermediation between the caisses' liquidity surpluses or needs, as well as orientation and organizational activities for Desjardins Group. This category also includes the operations of Desjardins Capital Inc. It further includes Desjardins Technology Group Inc., which encompasses all of Desjardins Group's IT operations. In addition to various adjustments required to prepare the Interim Consolidated Financial Statements, this category also contains intersegment balance eliminations.

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.

Treasury and Other Support to Desjardins Group Entities

(in millions of dollars)	For the three-month periods ended			For the nine-month periods ended	
	September 30, 2018[1]	June 30, 2018[1]	September 30, 2017	**September 30, 2018[1]**	September 30, 2017
Treasury activities	**$ 8**	$ 20	$ 31	**$ 51**	$ 90
Derivatives activities associated with hedging activities	**25**	(1)	49	**29**	79
Other[2]	**(50)**	(9)	(14)	**(66)**	(40)
Net surplus earnings (deficit) for the period	**$ (17)**	$ 10	$ 66	**$ 14**	$ 129
Of which:					
Group's share	**$ (17)**	$ 10	$ 66	**$ 14**	$ 129

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 and for the three-month period ended June 30, 2018 takes into account standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.

(2) Includes support function activities, various adjustments required to prepare the Interim Consolidated Financial Statements, and intersegment balance eliminations.

COMPARISON OF THE THIRD QUARTERS OF 2018 AND 2017 – CONTRIBUTION TO SURPLUS EARNINGS OF TREASURY AND OTHER SUPPORT TO DESJARDINS GROUP ENTITIES CATEGORY

- **Net deficit of $17 million,** compared to net surplus earnings of $66 million for the third quarter of 2017.
- **Treasury activities of $8 million,** compared to a contribution of $31 million to surplus earnings in 2017.
  - 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.
  - Lower trading income.
- **Activities related to derivatives associated with hedging activities of $25 million,** compared to surplus earnings of $49 million for the corresponding period in 2017.
  - Less favourable fluctuation in the fair value of swaps in 2018 because of an increase in interest rates that was not as high as in the same period in 2017.
- **Other activities recorded a $50 million deficit,** compared to an $14 million deficit in 2017.
  - Other activities affected, in 2018 and 2017, 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. They also included contributions from the *$100 Million Fund* and amounts paid out under the Desjardins Member Advantages program.

COMPARISON OF THE FIRST NINE MONTHS OF 2018 AND 2017 – CONTRIBUTION TO SURPLUS EARNINGS OF TREASURY AND OTHER SUPPORT TO DESJARDINS GROUP ENTITIES CATEGORY

- **Net surplus earnings of $14 million,** compared to $129 million for the first nine months of 2017.
- **Treasury activities of $51 million,** compared to a contribution of $90 million to surplus earnings in 2017.
  - Lower trading income.
- **Activities related to derivatives associated with hedging activities amounting to $29 million,** compared to surplus earnings of $79 million for the first nine months of 2017.
  - Less favourable fluctuation in the fair value of swaps in 2018 because of an increase in interest rates that was not as high as in the same period in 2017.
- **Other activities recorded a $66 million deficit,** compared to a $40 million deficit in 2017.
  - Other activities affected, in 2018 and 2017, 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. They also included contributions from the *$100 Million Fund* and amounts paid out under the Desjardins Member Advantages program.

SUMMARY OF INTERIM RESULTS

The table below presents a summary of data related to the results for the Federation's most recent eight quarters:

Results of the most recent eight quarters

(in millions of dollars)	2018			2017				2016
	Q3[(1)]	Q2[(1)]	Q1[(1)]	Q4	Q3	Q2	Q1	Q4
Net interest income	**$ 382**	$ 353	$ 368	$ 357	$ 364	$ 344	$ 339	$ 331
Net premiums	**2,288**	2,225	2,164	2,034	2,007	2,099	2,006	1,857
Other operating income[(2)]								
Assessments	**97**	99	99	94	93	91	99	98
Service agreements	**179**	186	184	179	187	194	167	174
Lending fees and credit card service revenues	**172**	164	186	182	154	153	171	151
Brokerage and investment fund services	**235**	239	271	261	241	307	278	281
Management and custodial service fees	**135**	128	127	131	109	111	106	108
Foreign exchange income	**15**	21	27	22	16	21	18	20
Other	**52**	163	70	(78)	330	47	63	(13)
Operating income[(2)]	**3,555**	3,578	3,496	3,182	3,501	3,367	3,247	3,007
Investment income (loss)[(2)]								
Net investment income (loss)	**(213)**	299	126	924	(316)	734	425	(1,062)
Overlay approach adjustment for insurance operations financial instruments	**76**	20	169	N/A	N/A	N/A	N/A	N/A
	(137)	319	295	924	(316)	734	425	(1,062)
Total income	**3,418**	3,897	3,791	4,106	3,185	4,101	3,672	1,945
Provision for credit losses	**73**	63	89	74	72	59	73	48
Claims, benefits, annuities and changes in insurance contract liabilities	**1,380**	1,727	1,656	2,120	1,000	1,922	1,753	(104)
Non-interest expense	**1,598**	1,568	1,628	1,651	1,433	1,605	1,550	1,560
Income taxes on surplus earnings	**68**	75	59	80	89	100	67	27
Surplus earnings before dividends to member caisses	**299**	464	359	181	591	415	229	414
Dividends to member caisses, net of income tax recovery	**-**	-	-	44	-	-	-	18
Net surplus earnings for the period after dividends to member caisses	**$ 299**	$ 464	$ 359	$ 137	$ 591	$ 415	$ 229	$ 396
Of which:								
Group's share	**$ 286**	$ 453	$ 350	$ 128	$ 576	$ 401	$ 224	$ 370
Non-controlling interests' share	**13**	11	9	9	15	14	5	26

(1) The information presented for the three-month periods ended September 30, 2018, June 30, 2018 and March 31, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.

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

Quarterly income, expenses and surplus earnings before dividends to member caisses fluctuate based on certain trends, including seasonal variations and changes in general economic conditions and capital market conditions. The results of the third quarter of 2017 were affected by the sale of Western Financial Group Inc. and Western Life Assurance Company, completed on July 1, 2017, while the results of the second quarter of 2018 were affected by the transaction involving Qtrade Canada Inc. and the interest in the associate Northwest & Ethical Investments L.P., completed on April 1, 2018. Additional information concerning these transactions is found under "Impact of significant transactions" on page 13. For more information about quarterly trends, see pages 42 and 43 of the 2017 annual MD&A.

BALANCE SHEET REVIEW

BALANCE SHEET MANAGEMENT

Consolidated Balance Sheets

(in millions of dollars and as a percentage)	As at September 30, 2018[1]		As at December 31, 2017	
Assets				
Cash and deposits with financial institutions	**$ 2,488**	**1.6%**	$ 1,731	1.2%
Securities	**52,058**	**32.5**	46,904	32.2
Securities borrowed or purchased under reverse repurchase agreements	**11,856**	**7.4**	9,377	6.4
Net loans and acceptances	**61,972**	**38.7**	58,715	40.3
Segregated fund net assets	**13,964**	**8.7**	13,379	9.2
Derivative financial instruments	**4,274**	**2.7**	3,772	2.6
Other assets	**13,633**	**8.4**	11,862	8.1
Total assets	**$ 160,245**	**100.0%**	$ 145,740	100.0%
Liabilities and equity				
Deposits	**$ 57,798**	**36.1%**	$ 52,149	35.8%
Commitments related to securities sold short	**11,199**	**7.0**	9,112	6.3
Commitments related to securities lent or sold under repurchase agreements	**13,182**	**8.2**	10,062	6.9
Derivative financial instruments	**4,262**	**2.7**	3,677	2.5
Insurance contract liabilities	**28,681**	**17.9**	28,300	19.4
Segregated fund net liabilities	**13,931**	**8.7**	13,354	9.2
Other liabilities	**12,966**	**8.1**	11,679	7.9
Subordinated notes	**1,343**	**0.8**	1,388	1.0
Equity	**16,883**	**10.5**	16,019	11.0
Total liabilities and equity	**$ 160,245**	**100.0%**	$ 145,740	100.0%

(1) The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

Total assets

As at September 30, 2018, the Federation’s total assets stood at $160.2 billion, up $14.5 billion, or 10.0%, since December 31, 2017. This growth was due in large part to securities, including those borrowed or purchased under reverse repurchase agreements, as well as net loans and acceptances.

Cash and deposits with financial institutions, and securities

As at September 30, 2018, the Federation’s cash and deposits with financial institutions amounted to $2.5 billion, an increase of $757 million, or 43.7%, since December 31, 2017. Securities, including securities borrowed or purchased under reverse repurchase agreements, totalled $63.9 billion as at September 30, 2018, for an increase of $7.6 billion, or 13.6%, since the end of 2017. The increase was due to growth in market activities and deposits.

Loans and clients’ liability under acceptances

As at September 30, 2018, the Federation’s outstanding loan portfolio, including acceptances, net of the allowance for credit losses, was $62.0 billion, an increase of $3.3 billion, or 5.5%, since December 31, 2017. Growth in consumer, credit card and other personal loans outstanding, and in business and government loans, which accounted for 30.9% and 61.9%, respectively, of the Federation’s total portfolio, was largely responsible for the increase.

Consumer, credit card and other personal loans outstanding, which totalled $19.3 billion as at September 30, 2018, were up by $1.7 billion, or 10.0%, since December 31, 2017, while business and government loans, which reached a volume of $38.7 billion as at that date, increased by $1.6 billion, or 4.4%, over the period. The Federation’s outstanding residential mortgages, which totalled $4.5 billion as at September 30, 2018, were up $194 million, or 4.5%, since December 31, 2017.

Loans and acceptances

(in millions of dollars and as a percentage)	As at September 30, 2018[1]			As at December 31, 2017		
Residential mortgages	**$**	**4,517**	**7.2%**	$	4,323	7.3%
Consumer, credit card and other personal loans		**19,293**	**30.9**		17,547	29.8
Business and government		**38,669**	**61.9**		37,043	62.9
		62,479	**100.0%**		58,913	100.0%
Allowance for credit losses		**(507)**			(198)	
Total loans and acceptances by borrower category	**$**	**61,972**		$	58,715	
Loans guaranteed or insured[2]	**$**	**4,869**		$	5,609	

[1] The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies", to the Interim Consolidated Financial Statements.
[2] Loans fully or partially guaranteed or insured by a public or private insurer or a government.

Credit quality

Information about the quality of the Federation's loan portfolio is presented in the "Risk management" section on page 35 of this MD&A.

Deposits

The Federation's outstanding deposits rose to $57.8 billion as at September 30, 2018, up $5.6 billion, or 10.8%, since December 31, 2017, largely as a result of growth in business and government deposits, which accounted for 78.6% of the total deposit portfolio. In fact, these deposits were up $4.5 billion, or 10.9%, since the end of 2017, to total $45.4 billion for third quarter 2018. This increase was due in particular to the various securities, including commercial paper and covered bonds, issued on U.S., Canadian and European markets, which supported the growth in Desjardins Group's funding requirements.

Deposits

(in millions of dollars and as a percentage)	As at September 30, 2018			As at December 31, 2017		
Individuals	**$**	**4,194**	**7.3%**	$	4,353	8.3%
Business and government		**45,426**	**78.6**		40,963	78.6
Deposit-taking institutions		**8,178**	**14.1**		6,833	13.1
Total deposits	**$**	**57,798**	**100.0%**	$	52,149	100.0%

Deposits from deposit-taking institutions totalled $8.2 billion as at September 30, 2018, up $1.3 billion, or 19.7%, since December 31, 2017. Deposits from individuals were down $159 million, or 3.7%, during the same period to total $4.2 billion as at September 30, 2018.

Insurance contract liabilities

The Federation's insurance contract liabilities stood at $28.7 billion as at September 30, 2018, up $381 million, or 1.3%, since December 31, 2017.

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

Equity

Equity totalled $16.9 billion as at September 30, 2018, up $864 million, or 5.4%, since the prior year-end. Net surplus earnings after dividends to member caisses, totalling $1.1 billion for the first nine months of 2018, were a source of this growth. In addition, the Federation issued F capital shares for proceeds of $124 million, net of issuance expenses, as well as F capital shares having a value of $142 million for the payment of interest when the holder has elected to receive remuneration in the form of F capital shares. Remuneration of $247 million on capital shares and the impact of changes in accounting policies in the amount of $214 million reduced equity.

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

CAPITAL MANAGEMENT

Capital management is crucial to the financial management of Desjardins Group, 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. Additional information on the Integrated Capital Management Framework can be found in the "Capital management" section of the Federation's 2017 annual MD&A.

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 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 Tier 1A capital ratio 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 the Federation's subsidiaries. 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 (the MCT Guideline) issued by the AMF. The property and casualty insurance subsidiaries under federal jurisdiction must comply with the OSFI's Minimum Capital Test Guideline for federally regulated property and casualty insurance companies. Developments in these guidelines are presented in the "Changes in the regulatory environment" section 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 CARLI guideline.

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. Additional information in this regard can be found in the Federation's 2017 annual MD&A on pages 47 and 48. 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.

On December 7, 2017, the BCBS issued a discussion paper on the regulatory treatment of sovereign exposures. Comments on the topic could be sent to the BCBS until March 9, 2018. The BCBS did not obtain a consensus in order to make changes to the treatment of exposures to sovereign risk.

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 anticipated implementation of the new threshold before January 1, 2022 is left at the discretion of the regulators. For its part, 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 since the second quarter of 2018. The OSFI also released a discussion paper on July 16 detailing the OSFI's preliminary views and the implementation timetable for the recent Basel III reforms in Canada. The AMF has not yet expressed its intentions in this regard.

On March 22, 2018, the BCBS issued a consultative document entitled "Revisions to the minimum capital requirements for market risk", which addresses certain issues raised following the publication on January 14, 2016 of the revised version of the minimum capital requirements for market risk. The consultative document includes proposed changes aimed, in particular, at increasing the risk sensitivity of the standardized approach and recalibrating risk weights for interest risk, equity risk and foreign exchange risk. It also proposes changes to the "Simplified alternative to the standardised approach to market risk capital requirements" issued on June 29, 2017. On December 7, 2017, the BCBS had announced that financial institutions should present information using the standardized approach as of January 1, 2022.

Compliance with requirements

As at September 30, 2018, the Tier 1A, Tier 1 and total capital ratios, calculated in accordance with Basel III requirements, all stood at 17.0%. The leverage ratio was 7.7%.

The Federation and its subsidiaries that are subject to minimum regulatory capital requirements were in compliance with said requirements as at September 30, 2018.

Regulatory capital

The following tables present the Federation's main capital components, regulatory capital, risk-weighted assets, capital ratios, and movements in capital during the period.

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]	• General 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 entities[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' CET 1 and AT1 ratios, for financial services cooperatives regulated by the AMF.
(2) The non-controlling interests balance 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) Represents 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 Tier 1A capital. The net non-deducted balance will be subject to risk-weighting at a rate of 250%.

Regulatory capital and capital ratios

(in millions of dollars and as a percentage)	As at September 30, 2018[1]	As at December 31, 2017
Tier 1A capital		
Federation's capital shares	**$ 4,767**	$ 4,501
Other capital shares	**4,031**	4,036
Reserves	**620**	540
Undistributed surplus earnings	**6,563**	5,655
Eligible accumulated other comprehensive income	**140**	456
Deductions[2][3]	**(5,883)**	(6,026)
Total Tier 1A capital	**10,238**	9,162
Non-controlling interests	**-**	13
Deductions[2]	**-**	(13)
Total Tier 1B capital	**-**	-
Total Tier 1 capital	**10,238**	9,162
Tier 2 capital		
Subordinated notes subject to phase-out	**809**	1,032
General allowance	**296**	126
Non-controlling interests	**-**	-
Deductions[2]	**(1,105)**	(1,158)
Total Tier 2 capital	**-**	-
Total regulatory capital (Tiers 1 and 2)	**$ 10,238**	$ 9,162
Ratios and leverage ratio exposure		
Tier 1A capital ratio[4]	**17.0%**	17.5%
Tier 1 capital ratio[4]	**17.0**	17.5
Total capital ratio[4]	**17.0**	17.5
Leverage ratio[5]	**7.7**	7.9
Leverage ratio exposure	**$ 132,507**	$ 115,915

(1) The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

(2) 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.

(3) Deductions from Tier 1A are comprised of regulatory adjustments ($2,279 million, $2,152 million in 2017), for which cross-investments ($1,816 million, $1,634 million in 2017), significant investments ($3,076 million, $3,137 million in 2017), and items that could not be deducted from Tiers 1B and 2 because of insufficient capital in these tiers ($528 million, $737 million in 2017).

(4) As prescribed by the guideline, the capital ratios are expressed as a percentage of regulatory capital to risk-weighted assets.

(5) The leverage ratio is calculated according to the guideline 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 exposure, and 4) off-balance sheet exposures.

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 measures 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 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 are still in progress with the AMF.

On December 21, 2017, the Federation filed a new short form prospectus and obtained a receipt to issue F capital shares for a maximum of $125 million during the 12 months following the date of the receipt. This new issue started on January 23, 2018. During the first nine months of 2018, the Federation issued F capital shares for proceeds of $124 million, net of issuance expenses. In addition, the Federation issued F capital shares having a value of $142 million for payment of interest when the holder has elected to receive remuneration in F capital shares.

In addition, on March 24, 2018, the distribution of net income of $60 million to member caisses with regard to G capital shares was approved at the Annual General Meeting of Desjardins Group.

As at September 30, 2018, the Tier 1A capital ratio was down 51 basis points compared to December 31, 2017. Growth in surplus earnings and reserves was offset by an increase in risk-weighted assets, the switch to IFRS 9 and the decrease in accumulated other comprehensive income.

Change in regulatory capital
For the nine-month period ended

(in millions of dollars)	September 30, 2018
Tier 1A capital	
Balance at beginning of period	**$ 9,162**
Increase in reserves and undistributed surplus earnings(1)	**988**
Eligible accumulated other comprehensive income	**(316)**
Federation's capital shares	**266**
Other capital shares	**(5)**
Deductions	**143**
Balance at end of period	**10,238**
Tier 1B capital	
Balance at beginning of period	**-**
Non-controlling interests	**(13)**
Deductions	**13**
Balance at end of period	**-**
Total Tier 1 capital	**10,238**
Tier 2 capital	
Balance at beginning of period	**-**
Senior notes subject to phase-out	**(223)**
General allowance	**170**
Deductions	**53**
Balance at end of period	**-**
Total capital	**$ 10,238**

(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 approval to use the Standardized Approach for calculating operational risk as of June 30, 2017. On June 29, 2018, the Federation obtained the AMF's approval to use market risk internal models for trading portfolios while continuing to use the Standardized Approach for foreign exchange risk and commodity risk in the banking portfolio as of September 30, 2018.

As indicated in the table below, risk-weighted assets totalled $60.3 billion as at September 30, 2018. Of this amount, $46.8 billion was for credit risk, $5.1 billion for market risk and $8.6 billion for operational risk. As at December 31, 2017, risk-weighted assets stood at $52.4 billion.

Risk-weighted assets

	Internal Ratings-Based Approach		Standardized Approach		Total as at September 30, 2018				Total as at December 31, 2017
(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	$ -	$ -	$ 6,686	$ -	$ 6,686	$ -	$ -	-%	$ 21
Financial institutions	-	-	40,853	8,200	40,853	8,200	656	20.1	7,601
Businesses	-	-	15,276	14,897	15,276	14,897	1,192	97.5	12,989
Securitizations	-	-	5	68	5	68	5	1,360.0	75
Shares	-	-	200	289	200	289	23	144.5	241
SMEs similar to other retail client exposures	-	-	2,107	1,615	2,107	1,615	129	76.6	1,288
Mortgages	2,159	285	438	153	2,597	438	35	16.9	329
Other retail client exposures (excluding SMEs)	6,891	3,720	922	697	7,813	4,417	353	56.5	3,207
Qualifying revolving retail client exposures	30,815	8,407	-	-	30,815	8,407	673	27.3	8,110
Subtotal - Credit risk other than counterparty risk	39,865	12,412	66,487	25,919	106,352	38,331	3,066	36.0	33,861
Counterparty risk									
Sovereign borrowers	-	-	35	-	35	-	-	-	-
Financial institutions	-	-	1,978	396	1,978	396	33	20.0	343
Businesses	-	-	9	9	9	9	1	100.0	4
Trading portfolio	-	-	1,209	343	1,209	343	27	28.4	374
Credit valuation adjustment (CVA) charge	-	-	-	-	-	1,068	85	-	910
Additional requirements for banking and trading portfolio	-	-	-	-	162	3	-	-	1
Subtotal - Counterparty risk	-	-	3,231	748	3,393	1,819	146	53.6	1,632
Other assets(3)	-	-	-	-	17,341	5,929	474	34.2	6,340
Scaling factor(4)	-	745	-	-	-	745	60	-	677
Total credit risk	39,865	13,157	69,718	26,667	127,086	46,824	3,746	36.8	42,510
Market risk									
Value at Risk (VaR) and Stressed VaR (SVaR)	-	2,788	-	-	-	2,788	223	-	N/A(6)
Additional requirements for risks	-	1,798	-	-	-	1,798	144	-	N/A(6)
Additional requirements for other risks(5)	-	-	-	488	-	488	39	-	N/A(6)
Total market risk(6)	-	4,586	-	488	-	5,074	406	-	1,965
Operational risk	-	-	-	8,577	-	8,577	686	-	8,143
Total risk-weighted assets before threshold	39,865	17,743	69,718	35,732	127,086	60,475	4,838	-	52,618
Risk-weighted assets after the transitional provisions for the CVA charge(7)									
RWA for Tier 1A capital	-	-	-	-	-	60,261	4,821	-	52,364
RWA for Tier 1 capital	-	-	-	-	-	60,293	4,823	-	52,409
RWA for total capital	-	-	-	-	-	60,325	4,826	-	52,445
Total risk-weighted assets	$ 39,865	$ 17,743	$ 69,718	$ 35,732	$ 127,086	$ 60,261	$ 4,821	-%	$ 52,364

(1) Net exposure, after credit risk mitigation (net of loss allowance for expected credit losses on credit-impaired loans other than for retail clients (except for credit card loans) under the Standardized Approach but not under the Internal Ratings-Based Approach in accordance with the AMF guideline).

(2) The capital requirement is 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 related to 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 currency risk, commodities risk and options risk calculated using the Standardized Approach.

(6) Internal models have been used since third quarter 2018 to calculate the market risk of trading portfolios instead of the Standardized Approach used for previous periods. Prior-period data have not been restated and were reported according to a different segmentation.

(7) The scaling factors used since January 1, 2014 to account for the requirements for the CVA charge are being phased in to calculate the Tier 1A, Tier 1 and total capital ratios, which are 80%, 83% and 86%, respectively, in 2018 (72%, 77% and 81% in 2017). They will reach 100% for each capital tier by 2019.

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. Additional information can be found in the "Off-balance sheet arrangements" section of the Federation's 2017 annual MD&A.

Assets under management and under administration

As at September 30, 2018, the Federation administered, for the account of caisse members and its clients, assets worth $404.1 billion, for a decrease of $15.9 billion, or 3.8%, following the transaction involving Qtrade Canada Inc., as described in the section "Significant events in 2018". The financial assets entrusted to the Federation as wealth manager totalled $67.9 billion as at September 30, 2018, up $1.3 billion, or 1.9%, since December 31, 2017.

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 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.

Structured entities

In the normal course of operations, the Federation enters into various financial transactions with structured entities 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 controls 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 Annual Consolidated Financial Statements provides more information on structured entities.

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 Annual Consolidated Financial Statements provides more information about the securitization of the Federation's loans.

RISK MANAGEMENT

RISK MANAGEMENT

Desjardins Group's objective in risk management is to optimize the risk-return trade-off, in accordance with its risk appetite, 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.

The Federation is exposed to different types of risk in its normal course of operations, including credit risk, market risk, liquidity risk, operational risk, insurance risk, strategic risk, reputational risk, risk related to pension plans, environmental risk and risk related to the regulatory and legal environment.

Risk management is a function covering all Desjardins Group operations, including those of the Federation. As a result, the description of risk management that follows is a description for Desjardins Group. 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 stability 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 culture in which each of its business segments, employees and managers is responsible for risk management.

In the first nine months of fiscal 2018, Desjardins Group's governance structure, frameworks and practices for risk management, and the nature and description of the risks to which the Federation is exposed (including operational risk, insurance risk, strategic risk, reputational risk, risk related to pension plans, environmental risk and risk related to the regulatory and legal environment) did not change significantly from those described on pages 56 to 85 of the Federation's 2017 annual MD&A. In addition to these types of risk, other risk factors, which are not under Desjardins Group's control (including the Federation's control) could have an impact on its future results. These principal risks and emerging risks, as well as other risk factors, did not change significantly from those described on pages 53 to 55 of the Federation's 2017 annual MD&A.

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, including through its loans to member caisses. It is also exposed through various other commitments, including letters of credit, transactions involving derivative financial instruments and securities transactions.

Quality of loan portfolio

On January 1, 2018, the Federation adopted IFRS 9, “Financial Instruments”, which replaces IAS 39, “Financial Instruments: Recognition and Measurement”. Contrary to the approach used by IAS 39, which was based on an “Incurred Loss” impairment model, IFRS 9 uses an “Expected Credit Loss” model. The IFRS 9 impairment model is therefore more forward-looking in nature. For more information, refer to Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

As at September 30, 2018, according to Note 5, “Loans and allowance for credit losses”, to the Interim Consolidated Financial Statements, the allowance for credit losses totalled $507 million, up $309 million compared to December 31, 2017. This increase was due mainly to growth in outstandings, the revision of economic scenarios, and the migration of borrowers to higher risk ratings. The adoption of IFRS 9 as at January 1, 2018 made the allowance for credit losses more volatile.

Gross credit-impaired loans outstanding are now considered Stage 3 loans of the impairment model. The ratio of gross credit-impaired loans, as a percentage of the total gross loans and acceptances portfolio, was 0.36% for the third quarter of 2018, compared to 0.14% as at December 31, 2017. This increase was due to the fact that under IFRS 9, all default loans are now considered credit-impaired unless the detrimental impact on the estimated future cash flows is considered negligible. The allowance for credit losses on credit-impaired loans totalled $101 million as at September 30, 2018, resulting in a provisioning rate for credit-impaired loans of 45.5%.

The following tables present gross credit-impaired loans by Federation borrower category and the change in the gross credit-impaired loan balance.

Gross credit-impaired loans[1] by borrower category

(in millions of dollars and as a percentage)	As at September 30, 2018[2]					As at December 31, 2017	
	Gross carrying amount			Allowance for credit losses on credit-impaired loans	Net credit-impaired loans	Gross impaired loans	Net impaired loans
	Gross loans and acceptances	Gross credit-impaired loans					
Residential mortgages	$ 4,517	$ 9	0.20%	$ -	$ 9	$ 8	$ 3
Consumer, credit card and other personal loans	19,293	195	1.01	96	99	72	49
Business and government	38,669	18	0.05	5	13	4	-
Total loans	**$ 62,479**	**$ 222**	**0.36%**	**$ 101**	**$ 121**	$ 84	$ 52

[1] Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.
[2] The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

Change in gross credit-impaired loans[1]

(in millions of dollars)	For the three-month periods ended			For the nine-month period ended	
	September 30, 2018[2]	June 30, 2018[2]	September 30, 2017	September 30, 2018[2]	September 30, 2017
Gross impaired loans at the beginning of the period under IAS 39	**N/A**	N/A	$ 76	**$ 84**	$ 95
Impact of adopting IFRS 9 as at January 1, 2018	**N/A**	N/A	N/A	**125**	N/A
Gross credit-impaired loans at the beginning of the last period under IFRS 9	**$ 208**	$ 209	N/A	**209**	N/A
Gross credit-impaired loans since the last period	**149**	218	108	**482**	332
Loans returned to unimpaired status	**(133)**	(60)	(48)	**(226)**	(168)
Write-offs and recoveries	**(61)**	(79)	(67)	**(208)**	(210)
Other changes	**59**	(80)	5	**(35)**	25
Gross credit-impaired loans at the end of the period	**$ 222**	$ 208	$ 74	**$ 222**	$ 74

[1] Further to the adoption of IFRS 9 on January 1, 2018, all loans included in Stage 3 of the impairment model are considered to be credit-impaired. The criteria for considering a loan to be impaired were different under IAS 39. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.
[2] The information presented for the three-month and nine-month periods ended September 30, 2018 and the three-month period ended June 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.

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.

A large proportion of Desjardins Group's 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. 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 U.S.

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 period of time at a given confidence level. A Monte Carlo VaR is calculated daily on the trading portfolios, using a 99% confidence level and a holding horizon of one day. It is therefore reasonable to expect a loss exceeding the VaR figure once every 100 days. The calculation of VaR is based on historical data for a one-year interval.

In addition to aggregate VaR, Desjardins Group 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, aggregate SVaR takes into account the historical data for a crisis period of one year from September 2008.

The table below presents the aggregate VaR and the aggregate SVaR of 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.

VaR by risk category (Trading portfolio)

(in millions of dollars)	**For the quarter ended September 30, 2018**				For the quarters ended June 30, 2018		September 30, 2017	
	As at September 30, 2018	**Average**	**High**	**Low**	As at June 30, 2018	Average	As at September 30, 2017	Average
Equities	**$ 0.2**	**$ 0.4**	**$ 1.0**	**$ 0.2**	$ 0.4	$ 0.4	$ 0.4	$ 0.4
Foreign exchange	**0.6**	**0.7**	**1.2**	**0.3**	0.9	0.4	0.1	0.4
Interest rate	**5.1**	**4.6**	**6.0**	**3.6**	4.6	4.6	2.0	2.5
Specific interest rate risk(1)	**6.5**	**7.3**	**9.7**	**5.6**	7.1	7.0	4.7	5.1
Diversification effect(2)	**(7.3)**	**(8.2)**	**N/A(3)**	**N/A(3)**	(8.3)	(7.7)	(5.1)	(5.8)
Aggregate VaR	**$ 5.1**	**$ 4.8**	**$ 6.0**	**$ 3.9**	$ 4.7	$ 4.7	$ 2.1	$ 2.6
Aggregate SVaR	**$ 12.1**	**$ 14.9**	**$ 21.6**	**$ 11.3**	$ 17.4	$ 18.4	$ 12.3	$ 11.3

(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 specific risk from general market risk. This approach consists of creating a sub-portfolio that contains the positions involving the specific risk of an 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) Represents the risk reduction related to diversification, namely the difference between the sum of the VaRs 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 $4.8 million for the quarter ended September 30, 2018, which was stable compared to the quarter ended June 30, 2018. The average of the aggregate SVaR was $14.9 million for the quarter ended September 30, 2018, down $3.5 million compared to the quarter ended June 30, 2018. It should be noted that there has been no change in the model or assumptions over the periods presented.

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 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, 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 interval of 99%.

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

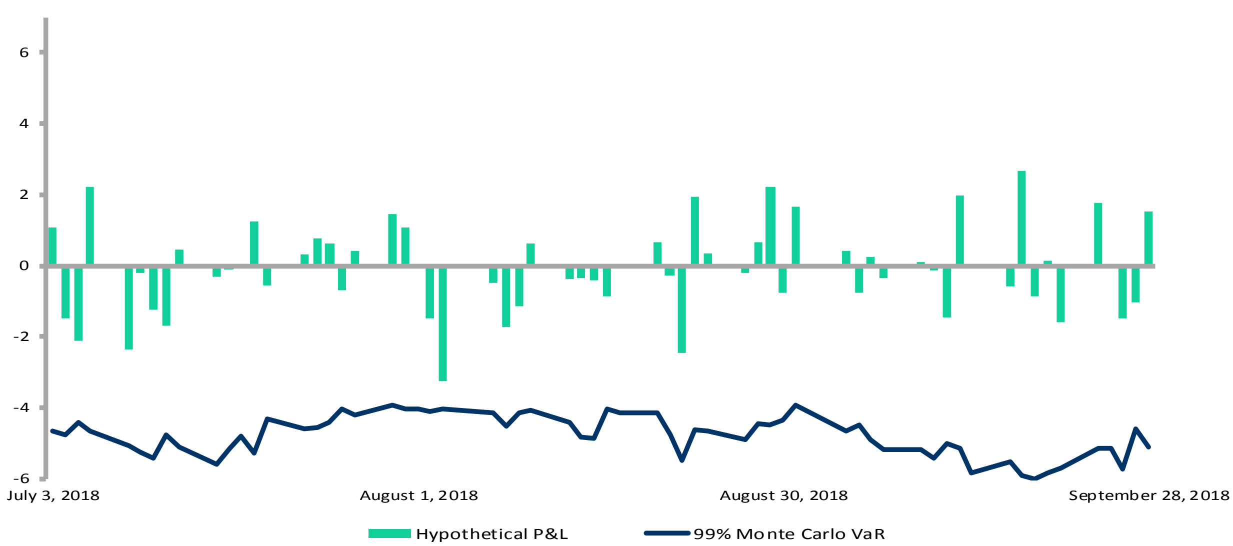
Back testing

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 the hypothetical P&L related to these activities. During the third quarter of 2018, there was no exception with regard to hypothetical P&L.

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 and 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 quarters 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/Liability Committee (ALCO) 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.

The table below 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 on insurance activities is presented in Note 1 of this table.

Interest rate sensitivity (before income taxes)(1)

(in millions of dollars)	**As at September 30, 2018**		As at June 30, 2018		As at September 30, 2017	
	Net interest income(2)	**Economic value of equity(3)**	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	**$ (6)**	**$ 132**	$ (21)	$ 113	$ (1)	$ (9)
Impact of a 100-basis-point decrease in interest rates(4)	**4**	**(136)**	19	(116)	9	9

(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 $220 million decrease in the economic value of equity before taxes as at September 30, 2018, and in a $254 million and $217 million decrease as at June 30, 2018 and September 30, 2017, respectively. A 100-basis-point decrease in interest rates would result in a $236 million increase in the economic value of equity before taxes as at September 30, 2018, and in a $229 million and $196 million increase as at June 30, 2018 and September 30, 2017, respectively.
(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 foreign exchange forward 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.

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 funding, 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 has 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, as presented under "Sources of financing". 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. It should be noted that the enactment date of the regulatory requirements concerning the NSFR was recently postponed until January 1, 2020, and Desjardins Group intends to comply with this ratio once it has 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 120.0% for the quarter ended September 30, 2018, compared to 119.8% 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 crisis scenarios.

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 both the programs used as well as the staggering of contractual maturities, allows it to maintain high regulatory liquidity ratios while ensuring their stability. Total deposits, including wholesale funding, presented on the Consolidated Balance Sheets amounted to $57.8 billion as at September 30, 2018, up $5.6 billion since December 31, 2017. Additional information on deposits is presented in the "Balance sheet management" section 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, and these strategies are regulated by policies. In the first nine months of 2018, 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 as follows:

Main financing programs
As at September 30, 2018

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

The following table represents remaining terms to maturity of wholesale funding.

Remaining contractual terms to maturity of wholesale funding

(in millions of dollars)	As at September 30, 2018								As at December 31, 2017
	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	$ 2,512	$ 864	$ 14	$ 2	$ 3,392	$ -	$ -	$ 3,392	$ 2,802
Commercial paper	6,500	2,714	775	2,166	12,155	-	-	12,155	9,276
Medium-term notes	-	1,250	-	983	2,233	2,636	6,075	10,944	11,030
Mortgage loan securitization	-	483	318	788	1,589	1,336	6,833	9,758	9,164
Covered bonds	-	-	1,500	-	1,500	1,498	2,619	5,617	4,517
Subordinated notes	-	-	-	-	-	844	499	1,343	1,388
Total	$ 9,012	$ 5,311	$ 2,607	$ 3,939	$ 20,869	$ 6,314	$ 16,026	$ 43,209	$ 38,177
Including:									
Secured	$ -	$ 483	$ 1,818	$ 788	$ 3,089	$ 3,678	$ 9,951	$ 16,718	$ 15,069
Unsecured	9,012	4,828	789	3,151	17,780	2,636	6,075	26,491	23,108

The 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 $5.0 billion compared to December 31, 2017, mainly because of an increase in commercial paper and covered bonds.

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

Wholesale funding by currency

(in millions of dollars and as a percentage)	As at September 30, 2018		As at December 31, 2017	
Canadian dollars	$ 20,579	47.7%	$ 18,345	48.1%
U.S. dollars	13,762	31.8	12,105	31.7
Other	8,868	20.5	7,727	20.2
	$ 43,209	100.0%	$ 38,177	100.0%

The Federation also participated in new issues under the NHA Mortgage-Backed Securities Program for a total amount of $1.9 billion in the first nine months of 2018. During the same period, the Federation also made an issue of covered bonds totalling 750 million euros on the European market, and an issue of 1.0 billion euros under its multi-currency medium-term note program. In addition, the Federation made two issues for a total of $1.1 billion under its Canadian medium-term note program.

Outstanding notes issued under the Federation's medium-term financing programs amounted to $26.3 billion as at September 30, 2018, compared to $24.7 billion as at December 31, 2017. 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 $1.3 billion as at September 30, 2018, compared to $1.4 billion as at December 31, 2017. Furthermore, to round out its financing and increase its capital base, in the first nine months of 2018, the Federation issued F capital shares for proceeds of $124 million, net of issuance fees, as well as F capital shares having a value of $142 million for the payment of interest when the holder has elected to receive remuneration in the form of 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 the first nine months of 2018, the credit ratings and outlooks assigned to Desjardins Group's securities remained unchanged and were affirmed by the rating agencies Moody's, Standard & Poor's (S&P), DBRS and Fitch.

After the publication, on April 18, 2018, of the Department of Finance Canada's final version of regulations to implement the main features of the Bank Recapitalization (Bail-in) Regime and of the OSFI's final version of its guideline on Total Loss Absorbing Capacity (TLAC), DBRS, Moody's and S&P issued press releases with several decisions concerning the credit ratings of Canadian domestic systemically important banks (D-SIB). Given that the Bail-in Regime is not applicable to AMF-regulated Desjardins Group, it was not mentioned in DBRS's, Moody's and S&P's press releases.

The ratings outlooks for Desjardins Group from S&P and Fitch are stable, but DBRS's and Moody's outlooks are negative. DBRS's and Moody's assignment of a negative ratings outlook to Desjardins Group can be explained by the uncertainty about the application of a Bail-in Regime for Desjardins. However, Moody's ratings outlook for Desjardins Capital Inc. is stable.

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

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 that 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 more credit rating agencies.

Contractual maturities of on-balance sheet items and off-balance sheet commitments

The following table 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 for 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 amounts 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.

Note 15, "Insurance contract liabilities", to the Annual Consolidated Financial Statements provides additional information on the contractual maturities of actuarial liabilities and provisions for claims and adjustment expenses.

Residual contractual maturities of on-balance sheet items and off-balance sheet commitments

As at September 30, 2018[1]

(in millions of dollars)	Less than 1 month	1 to 3 months	3 to 6 months	6 to 9 months	9 to 12 months	1 to 2 years	2 to 5 years	Over 5 years	No stated maturity	Total
Assets										
Cash and deposits with financial institutions	$ 2,016	$ 356	$ 7	$ -	$ -	$ -	$ -	$ -	$ 109	$ 2,488
Securities										
Securities at fair value through profit or loss[2]	403	681	539	1,103	1,205	2,974	10,315	17,043	4,680	38,943
Securities at fair value through other comprehensive income[2]	2,120	422	209	694	299	1,104	3,811	2,681	43	11,383
Securities at amortized cost[2]	1,315	97	85	148	51	2	4	30	-	1,732
Securities borrowed or purchased under reverse repurchase agreements	11,422	434	-	-	-	-	-	-	-	11,856
Loans										
Residential mortgages[3]	21	43	44	112	131	820	2,029	1,306	11	4,517
Consumer, credit card and other personal loans[3]	42	73	158	205	269	1,057	5,078	5,239	7,172	19,293
Business and government[3]	6,572	1,731	1,640	1,538	1,279	5,889	10,105	3,567	6,097	38,418
Allowance for credit losses	-	-	-	-	-	-	-	-	(507)	(507)
Segregated fund net assets	-	-	-	-	-	-	-	-	13,964	13,964
Clients' liability under acceptances	176	74	-	1	-	-	-	-	-	251
Premiums receivable	181	61	13	3	-	-	-	-	2,133	2,391
Derivative financial instruments	152	122	117	196	130	905	2,474	169	9	4,274
Amounts receivable from clients, brokers and financial institutions	3,000	1	-	-	-	-	-	-	41	3,042
Reinsurance assets	37	73	72	64	61	192	356	1,072	105	2,032
Investment property	-	-	-	-	-	-	-	-	934	934
Property, plant and equipment	-	-	-	-	-	-	-	-	787	787
Goodwill	-	-	-	-	-	-	-	-	121	121
Intangible assets	-	-	-	-	-	-	-	-	468	468
Deferred tax assets	-	-	-	-	-	-	-	-	758	758
Other assets	834	124	98	37	22	14	39	5	1,927	3,100
Total assets	$ 28,291	$ 4,292	$ 2,982	$ 4,101	$ 3,447	$ 12,957	$ 34,211	$ 31,112	$ 38,852	$ 160,245

See page 45 for footnotes.

Residual contractual maturities of on-balance sheet items and off-balance sheet commitments (continued)
As at September 30, 2018[(1)]

(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[(4)]	$ 21	$ 53	$ 80	$ 86	$ 87	$ 322	$ 551	$ 6	$ 2,988	$ 4,194
Business and government[(4)]	9,673	5,408	2,651	1,843	2,138	5,500	13,213	2,052	2,948	45,426
Deposit-taking institutions[(4)]	570	191	278	314	102	660	1,938	9	4,116	8,178
Acceptances	176	74	-	1	-	-	-	-	-	251
Commitments related to securities sold short[(5)]	190	234	213	52	169	1,919	2,306	6,111	5	11,199
Commitments related to securities lent or sold under repurchase agreements	13,182	-	-	-	-	-	-	-	-	13,182
Derivative financial instruments	167	111	130	203	134	834	2,390	283	10	4,262
Amounts payable to clients, brokers and financial institutions	4,544	3	-	-	-	-	-	-	2,006	6,553
Insurance contract liabilities	429	773	933	819	792	1,880	4,189	16,313	2,553	28,681
Segregated fund net liabilities	-	-	-	-	-	-	-	-	13,931	13,931
Net defined benefit plan liabilities	-	-	-	-	-	-	-	-	1,360	1,360
Deferred tax liabilities	-	-	-	-	-	-	-	-	230	230
Other liabilities	1,773	191	215	262	27	65	78	51	1,910	4,572
Subordinated notes	-	-	-	-	-	844	-	499	-	1,343
Total equity	-	-	-	-	-	-	-	-	16,883	16,883
Total liabilities and equity	$ 30,725	$ 7,038	$ 4,500	$ 3,580	$ 3,449	$ 12,024	$ 24,665	$ 25,324	$ 48,940	$ 160,245
Off-balance sheet commitments										
Credit commitments[(6)]	$ 4,114	$ 202	$ 239	$ 727	$ 975	$ 2,427	$ 7,792	$ 636	$ 89,242	$ 106,354
Indemnification commitments related to securities lending	-	-	-	-	-	-	-	-	2,228	2,228
Commitments under lease contracts	4	8	11	11	11	38	96	193	-	372
Documentary letters of credit	-	1	-	-	-	-	-	-	-	1
Guarantees and standby letters of credit	43	235	81	63	198	6	17	75	106	824
Credit default swaps	-	-	-	-	-	-	-	349	-	349

See page 45 for footnotes.

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
Assets										
Cash and deposits with financial institutions	$ 1,343	$ 378	$ -	$ -	$ -	$ -	$ -	$ -	$ 10	$ 1,731
Securities										
Securities at fair value through profit or loss(2)	45	541	1,152	835	2,112	2,195	7,181	15,881	1,712	31,654
Available-for-sale securities(2)	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(3)	39	49	227	93	120	505	1,934	1,350	6	4,323
Consumer, credit card and other personal loans(3)	41	84	196	209	273	1,128	4,473	4,472	6,671	17,547
Business and government(3)	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	-	-	-	-	-	-	41	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	$ 11,278	$ 28,970	$ 28,858	$ 38,768	$ 145,740

See page 45 for footnotes.

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(4)	$ 42	$ 75	$ 122	$ 72	$ 76	$ 237	$ 526	$ 3	$ 3,200	$ 4,353
Business and government(4)	9,246	3,768	1,703	1,653	2,134	5,383	12,019	1,602	3,455	40,963
Deposit-taking institutions(4)	685	192	279	186	200	687	1,840	6	2,758	6,833
Acceptances	31	-	-	-	-	-	-	-	-	31
Commitments related to securities sold short(5)	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(6)	$ 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

(1) The information presented as at September 30, 2018 takes into account the standards and amendments adopted on January 1, 2018. The comparative data have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements.
(2) Equity securities are classified under “No stated maturity”.
(3) Amounts repayable on demand are classified under “No stated maturity”.
(4) Deposits payable on demand or after notice are considered as having "No stated maturity".
(5) Amounts are presented by remaining contractual maturity of the underlying security.
(6) 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.

ADDITIONAL INFORMATION RELATED TO CERTAIN RISK EXPOSURES

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

Asset-backed securities

(in millions of dollars)	As at September 30, 2018		As at December 31, 2017	
	Notional amounts	**Fair value**	Notional amounts	Fair value
Financial asset-backed and mortgage-backed securities[1]	**$ 145**	**$ 145**	$ 146	$ 148

[1] None of the securities held is directly backed by subprime residential mortgage loans. Following the adoption of IFRS 9 as at January 1, 2018, these securities are presented under “Securities at fair value through profit or loss” and “Securities at fair value through other comprehensive income” on the Consolidated Balance Sheets. As at December 31, 2017, they were presented under "Securities at fair value through profit or loss" and “Available-for-sale securities”.

Derivative financial instruments

(in millions of dollars)	As at September 30, 2018			As at December 31, 2017		
	Notional amounts	**Positive value**	**Negative value**	Notional amounts	Positive value	Negative value
Credit default swaps[1]	**$ 349**	**$ 7**	**$ -**	$ 616	$ 13	$ 2
Total return swaps[2]	**116**	**-**	**1**	86	-	1

[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.

Leveraged finance loans and subprime loans

(in millions of dollars)	As at September 30, 2018	As at December 31, 2017
Leveraged finance loans[1]	**$ 109**	$ 149
Alt-A mortgage loans[2]	**18**	19
Subprime residential mortgage loans[3]	**2**	1

[1] Leveraged finance loans are defined as loans to large corporations and finance companies whose credit rating is between BB+ and D, and whose level of indebtedness is very high compared to other companies in the same industry.
[2] Alt-A mortgage loans 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] Subprime residential mortgage 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.

ADDITIONAL INFORMATION

CONTROLS AND PROCEDURES

During the interim period ended September 30, 2018, the Federation did not make any changes to its internal control over financial reporting that have materially affected, or may materially affect, its operations. On January 1, 2018, the adoption of IFRS 9, “Financial Instruments”, IFRS 15, “Revenue from Contracts with Customers”, and the amendments to IFRS 4, “Insurance Contracts”, did not have a significant impact on internal control over financial reporting. The parties involved and their responsibilities regarding internal control are described on page 86 of the 2017 annual MD&A.

RELATED PARTY DISCLOSURES

In the normal course of operations, 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 carries out transactions with other Desjardins Group entities, which are primarily caisses.

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. These policies and procedures have not changed significantly since December 31, 2017.

Additional information on related party transactions is provided in Note 33, “Related party disclosures”, to the Annual Consolidated Financial Statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

A description of the accounting policies used by the Federation is essential to understanding the Annual and Interim Consolidated Financial Statements. The significant accounting policies are described in Note 2, “Basis of presentation and significant accounting policies”, to the Federation’s Annual Consolidated Financial Statements on pages 109 to 124 of the 2017 Annual Report, except for the amendments described in Note 2, “Basis of presentation and significant accounting policies”, to the Interim Consolidated Financial Statements as a result of the adoption of IFRS 9, “Financial Instruments”, IFRS 15, “Revenue from Contracts with Customers”, and the amendments to IFRS 4, “Insurance Contracts”, on January 1, 2018.

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. Explanations of the significant accounting policies that have required management to make difficult, subjective or complex judgments, often about matters that are inherently uncertain, are provided on pages 87 to 91 of the 2017 annual MD&A as well in Note 2, “Basis of presentation and significant accounting policies”, and Note 5, “Loans and allowance for credit losses”, to these Interim Consolidated Financial Statements.

No material change was made to these judgments, estimates, assumptions and accounting policies during the first nine months of 2018, except for the changes regarding the accounting standards adopted on January 1, 2018.

FUTURE ACCOUNTING CHANGES

Accounting standards issued by the IASB but not yet effective for the Federation are presented in Note 2, “Basis of presentation and significant accounting policies”, to the Federation's Annual Consolidated Financial Statements, on pages 124 to 126 of the 2017 Annual Report. Additional information is also presented under “Future accounting changes” on pages 91 to 95 of the 2017 annual MD&A. Since then, the IASB has issued the following changes:

Conceptual Framework for Financial Reporting

In March 2018, the IAS issued the “Conceptual Framework for Financial Reporting”, which replaces the existing “Conceptual Framework for Financial Reporting”. The “Conceptual Framework for Financial Reporting” includes new concepts, updates definitions and recognition criteria for assets and liabilities, and clarifies certain key concepts. The Federation is currently assessing the impact of adopting this new framework, which will be effective for annual periods beginning on or after January 1, 2020.

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Consolidated Balance Sheets

(unaudited)

(in millions of Canadian dollars)	Notes	As at September 30, 2018[(1)]	As at December 31, 2017
ASSETS			
Cash and deposits with financial institutions		**$ 2,488**	$ 1,731
Securities			
Securities at fair value through profit or loss		**38,943**	31,654
Available-for-sale securities		**N/A**	15,250
Securities at fair value through other comprehensive income		**11,383**	N/A
Securities at amortized cost		**1,732**	N/A
		52,058	46,904
Securities borrowed or purchased under reverse repurchase agreements		**11,856**	9,377
Loans	5		
Residential mortgages		**4,517**	4,323
Consumer, credit card and other personal loans		**19,293**	17,547
Business and government		**38,418**	37,012
		62,228	58,882
Allowance for credit losses	5	**(507)**	(198)
		61,721	58,684
Segregated fund net assets		**13,964**	13,379
Other assets			
Clients' liability under acceptances		**251**	31
Premiums receivable		**2,391**	2,098
Derivative financial instruments		**4,274**	3,772
Amounts receivable from clients, brokers and financial institutions		**3,042**	1,563
Reinsurance assets		**2,032**	2,202
Investment property		**934**	817
Property, plant and equipment		**787**	780
Goodwill		**121**	121
Intangible assets		**468**	466
Deferred tax assets		**758**	746
Other		**3,100**	2,188
Assets of the disposal group held to be transferred		**-**	881
		18,158	15,665
TOTAL ASSETS		**$ 160,245**	$ 145,740
LIABILITIES AND EQUITY			
LIABILITIES			
Deposits	7		
Individuals		**$ 4,194**	$ 4,353
Business and government		**45,426**	40,963
Deposit-taking institutions		**8,178**	6,833
		57,798	52,149
Other liabilities			
Acceptances		**251**	31
Commitments related to securities sold short		**11,199**	9,112
Commitments related to securities lent or sold under repurchase agreements		**13,182**	10,062
Derivative financial instruments		**4,262**	3,677
Amounts payable to clients, brokers and financial institutions		**6,553**	4,247
Insurance contract liabilities		**28,681**	28,300
Segregated fund net liabilities		**13,931**	13,354
Net defined benefit plan liabilities		**1,360**	1,741
Deferred tax liabilities		**230**	204
Other		**4,572**	4,794
Liabilities of the disposal group held to be transferred		**-**	662
		84,221	76,184
Subordinated notes		**1,343**	1,388
TOTAL LIABILITIES		**143,362**	129,721
EQUITY			
Capital stock	9	**8,798**	8,537
Undistributed surplus earnings		**6,574**	5,674
Accumulated other comprehensive income	10	**130**	458
Reserves		**620**	540
Equity – Group's share		**16,122**	15,209
Non-controlling interests		**761**	810
TOTAL EQUITY		**16,883**	16,019
TOTAL LIABILITIES AND EQUITY		**$ 160,245**	$ 145,740

(1) The information presented as at September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Condensed Interim Consolidated Financial Statements.

On behalf of the Board of Directors of the *Fédération des caisses Desjardins du Québec*,

Guy Cormier
Chair of the Board

Serge Rousseau
Vice-Chair of the Board

Consolidated Statements of Income

(unaudited)

(in millions of Canadian dollars)	Notes	For the three-month periods ended September 30 2018[(1)]	2017	For the nine-month periods ended September 30 2018[(1)]	2017
INTEREST INCOME					
Loans		**$ 681**	$ 537	**$ 1,874**	$ 1,511
Securities		**59**	46	**167**	144
		740	583	**2,041**	1,655
INTEREST EXPENSE					
Deposits		**335**	199	**868**	551
Subordinated notes and other		**23**	20	**70**	57
		358	219	**938**	608
NET INTEREST INCOME	12	**382**	364	**1,103**	1,047
NET PREMIUMS		**2,288**	2,007	**6,677**	6,112
OTHER INCOME					
Assessments		**97**	93	**295**	283
Service agreements		**179**	187	**549**	548
Lending fees and credit card service revenues		**172**	154	**522**	478
Brokerage and investment fund services		**235**	241	**745**	826
Management and custodial service fees		**135**	109	**390**	326
Net investment income (loss)	12	**(213)**	(316)	**212**	843
Overlay approach adjustment for insurance operations financial assets		**76**	N/A	**265**	N/A
Foreign exchange income		**15**	16	**63**	55
Other		**52**	330	**285**	440
		748	814	**3,326**	3,799
TOTAL INCOME		**3,418**	3,185	**11,106**	10,958
PROVISION FOR CREDIT LOSSES	5	**73**	72	**225**	204
CLAIMS, BENEFITS, ANNUITIES AND CHANGES IN INSURANCE CONTRACT LIABILITIES		**1,380**	1,000	**4,763**	4,675
NON-INTEREST EXPENSE					
Remuneration and other payments		**140**	135	**423**	403
Salaries and fringe benefits		**539**	511	**1,698**	1,707
Premises, equipment and furniture, including depreciation		**126**	127	**361**	365
Service agreements and outsourcing		**76**	64	**245**	207
Communications		**49**	51	**163**	176
Other		**668**	545	**1,904**	1,730
		1,598	1,433	**4,794**	4,588
OPERATING SURPLUS EARNINGS		**367**	680	**1,324**	1,491
Income taxes on surplus earnings		**68**	89	**202**	256
NET SURPLUS EARNINGS FOR THE PERIOD AFTER DIVIDENDS TO MEMBER CAISSES		**$ 299**	$ 591	**$ 1,122**	$ 1,235
of which:					
Group's share		**$ 286**	$ 576	**$ 1,089**	$ 1,201
Non-controlling interests' share		**13**	15	**33**	34

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Condensed Interim Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income
(unaudited)

(in millions of Canadian dollars)	For the three-month periods ended September 30 2018[(1)]	2017	For the nine-month periods ended September 30 2018[(1)]	2017
Net surplus earnings for the period after dividends to member caisses	**$ 299**	$ 591	**$ 1,122**	$ 1,235
Other comprehensive income, net of income taxes				
Items that will not be reclassified subsequently to the Consolidated Statements of Income				
Remeasurement of net defined benefit plan liabilities	**105**	221	**297**	86
Share of associates and joint ventures accounted for using the equity method	**1**	2	**2**	1
	106	223	**299**	87
Items that will be reclassified subsequently to the Consolidated Statements of Income				
Net change in unrealized gains and losses on available-for-sale securities				
Net unrealized gains (losses)	**N/A**	(35)	**N/A**	113
Reclassification of net gains to the Consolidated Statements of Income	**N/A**	(17)	**N/A**	(148)
	N/A	(52)	**N/A**	(35)
Net change in unrealized gains and losses on debt securities classified as at fair value through other comprehensive income				
Net unrealized losses	**(55)**	N/A	**(87)**	N/A
Reclassification of net losses to the Consolidated Statements of Income	**8**	N/A	**13**	N/A
	(47)	N/A	**(74)**	N/A
Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets				
Net unrealized losses	**(60)**	N/A	**(83)**	N/A
Reclassification of net (gains) losses to the Consolidated Statements of Income	**1**	N/A	**(131)**	N/A
	(59)	N/A	**(214)**	N/A
Net change in cash flow hedges				
Net gains (losses) on derivative financial instruments designated as cash flow hedges	**(7)**	-	**(15)**	2
Reclassification to the Consolidated Statements of Income of net gains on derivative financial instruments designated as cash flow hedges	**(1)**	(1)	**(3)**	(4)
	(8)	(1)	**(18)**	(2)
Net unrealized exchange losses on the translation of a net investment in a foreign operation, net of hedging transactions	**-**	(1)	**-**	(1)
	(114)	(54)	**(306)**	(38)
Total other comprehensive income, net of income taxes	**(8)**	169	**(7)**	49
COMPREHENSIVE INCOME FOR THE PERIOD	**$ 291**	$ 760	**$ 1,115**	$ 1,284
of which:				
Group's share	**$ 282**	$ 741	**$ 1,091**	$ 1,246
Non-controlling interests' share	**9**	19	**24**	38

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Condensed Interim Consolidated Financial Statements.

Income taxes on other comprehensive income

The tax expense (recovery) related to each component of other comprehensive income for the period is presented in the following table.

(in millions of Canadian dollars)	For the three-month periods ended September 30 2018[(1)]	2017	For the nine-month periods ended September 30 2018[(1)]	2017
Item that will not be reclassified subsequently to the Consolidated Statements of income				
Remeasurement of net defined benefit plan liabilities	**$ 38**	$ 80	**$ 107**	$ 32
	38	80	**107**	32
Items that will be reclassified subsequently to the Consolidated Statements of Income				
Net change in unrealized gains and losses on available-for-sale securities				
Net unrealized gains (losses)	**N/A**	(16)	**N/A**	18
Reclassification of net gains to the Consolidated Statements of Income	**N/A**	(4)	**N/A**	(29)
	N/A	(20)	**N/A**	(11)
Net change in unrealized gains and losses on debt securities classified as at fair value through other comprehensive income				
Net unrealized losses	**(20)**	N/A	**(31)**	N/A
Reclassification of net losses to the Consolidated Statements of Income	**5**	N/A	**6**	N/A
	(15)	N/A	**(25)**	N/A
Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets				
Net unrealized losses	**(20)**	N/A	**(31)**	N/A
Reclassification of net (gains) losses to the Consolidated Statements of Income	**3**	N/A	**(20)**	N/A
	(17)	N/A	**(51)**	N/A
Net change in cash flow hedges				
Net gains (losses) on derivative financial instruments designated as cash flow hedges	**(2)**	-	**(8)**	1
Reclassification to the Consolidated Statements of Income of net gains on derivative financial instruments designated as cash flow hedges	**(1)**	(1)	**(1)**	(2)
	(3)	(1)	**(9)**	(1)
	(35)	(21)	**(85)**	(12)
Total income tax expense	**$ 3**	$ 59	**$ 22**	$ 20

(1) The information presented for the three-month and nine-month periods ended September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

Consolidated Statements of Changes in Equity

For the nine-month periods ended September 30
(unaudited)

(in millions of Canadian dollars)	Note	Capital stock (Note 9)	Undistributed surplus earnings	Accumulated other comprehensive income (Note 10)	Reserves			Equity - Group's share	Non-controlling interests	Total equity
					Stabilization reserve	General and other reserves	Total reserves			
BALANCE AS AT DECEMBER 31, 2017		**$ 8,537**	**$ 5,674**	**$ 458**	**$ 467**	**$ 73**	**$ 540**	**$ 15,209**	**$ 810**	**$ 16,019**
Impact of changes in accounting policies	2	**-**	**34**	**(35)**	**-**	**(213)**	**(213)**	**(214)**	**-**	**(214)**
OPENING BALANCE AS AT JANUARY 1, 2018[(1)]		**8,537**	**5,708**	**423**	**467**	**(140)**	**327**	**14,995**	**810**	**15,805**
Net surplus earnings for the period after dividends to member caisses		**-**	**1,089**	**-**	**-**	**-**	**-**	**1,089**	**33**	**1,122**
Other comprehensive income for the period		**-**	**295**	**(293)**	**-**	**-**	**-**	**2**	**(9)**	**(7)**
Comprehensive income for the period		**-**	**1,384**	**(293)**	**-**	**-**	**-**	**1,091**	**24**	**1,115**
Issuance of F capital shares		**267**	**-**	**-**	**-**	**-**	**-**	**267**	**-**	**267**
F capital share issuance costs		**(1)**	**-**	**-**	**-**	**-**	**-**	**(1)**	**-**	**(1)**
Other net change in capital stock		**(5)**	**3**	**-**	**-**	**-**	**-**	**(2)**	**-**	**(2)**
Remuneration on capital shares		**-**	**(247)**	**-**	**-**	**-**	**-**	**(247)**	**-**	**(247)**
Redemption of share capital		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(11)**	**(11)**
Dividends		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(28)**	**(28)**
Transfer from undistributed surplus earnings (to reserves)		**-**	**(293)**	**-**	**96**	**197**	**293**	**-**	**-**	**-**
Transactions related to buy-out options		**-**	**30**	**-**	**-**	**-**	**-**	**30**	**(19)**	**11**
Buy-out of non-controlling interests		**-**	**(13)**	**-**	**-**	**-**	**-**	**(13)**	**(15)**	**(28)**
Other		**-**	**2**	**-**	**-**	**-**	**-**	**2**	**-**	**2**
BALANCE AS AT SEPTEMBER 30, 2018[(1)]		**$ 8,798**	**$ 6,574**	**$ 130**	**$ 563**	**$ 57**	**$ 620**	**$ 16,122**	**$ 761**	**$ 16,883**
BALANCE AS AT DECEMBER 31, 2016		$ 8,066	$ 4,781	$ 393	$ 436	$ 88	$ 524	$ 13,764	$ 916	$ 14,680
Net surplus earnings for the period after dividends to member caisses		-	1,201	-	-	-	-	1,201	34	1,235
Other comprehensive income for the period		-	86	(41)	-	-	-	45	4	49
Comprehensive income for the period		-	1,287	(41)	-	-	-	1,246	38	1,284
Issuance of F capital shares		354	-	-	-	-	-	354	-	354
F capital share issuance costs		(1)	-	-	-	-	-	(1)	-	(1)
Other net change in capital stock		97	-	-	-	-	-	97	(97)	-
Remuneration on capital shares		-	(167)	-	-	-	-	(167)	-	(167)
Redemption of share capital		-	-	-	-	-	-	-	(8)	(8)
Dividends		-	-	-	-	-	-	-	(30)	(30)
Transfer from undistributed surplus earnings (to reserves)		-	(115)	-	31	84	115	-	-	-
Transactions related to put options		-	6	-	-	-	-	6	(3)	3
Other		-	1	-	-	-	-	1	(2)	(1)
BALANCE AS AT SEPTEMBER 30, 2017		$ 8,516	$ 5,793	$ 352	$ 467	$ 172	$ 639	$ 15,300	$ 814	$ 16,114

(1) The information presented for the nine-month period ended September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, “Basis of presentation and significant accounting policies”.

The accompanying notes are an integral part of the Condensed Interim Consolidated Financial Statements.

Consolidated Statements of Cash Flows

(unaudited)

(in millions of Canadian dollars)	For the nine-month periods ended September 30 2018[(1)]	2017
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES		
Operating surplus earnings	**$ 1,324**	$ 1,491
Non-cash adjustments:		
Depreciation of property, plant and equipment and investment property, and amortization of intangible assets	**141**	143
Net change in insurance contract liabilities	**381**	455
Provision for credit losses	**225**	204
Net realized losses on securities classified as at fair value through other comprehensive income	**19**	N/A
Net realized gains on available-for-sale securities	**N/A**	(182)
Overlay approach adjustment for insurance operations financial assets	**(265)**	N/A
Impairment on available-for-sale securities recognized in profit or loss	**N/A**	5
Other	**(64)**	137
Change in operating assets and liabilities:		
Securities at fair value through profit or loss	**(3,911)**	(2,964)
Securities borrowed or purchased under reverse repurchase agreements	**(2,480)**	(3,044)
Loans	**(3,556)**	(3,936)
Derivative financial instruments, net amount	**56**	1,151
Net amounts receivable from and payable to clients, brokers and financial institutions	**772**	599
Deposits	**5,649**	6,360
Commitments related to securities sold short	**2,087**	2,053
Commitments related to securities lent or sold under repurchase agreements	**3,119**	(448)
Other	**(736)**	(833)
Payment of the contingent consideration	**(250)**	(243)
Income taxes paid on surplus earnings	**(154)**	(229)
Payment of dividends to member caisses	**(60)**	-
	2,297	719
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES		
Purchase of debt securities and subordinated notes from third parties on the market	**(46)**	(21)
Issuance of F capital shares	**124**	229
F capital share issuance costs	**(1)**	(1)
Other net change in capital stock	**(2)**	-
Remuneration on capital shares	**(105)**	(42)
Redemption of share capital	**(11)**	(8)
Dividends paid	**(28)**	(30)
Buy-out of non-controlling interests	**(28)**	-
Transactions related to put options and buy-out options	**(63)**	(14)
	(160)	113
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES		
Purchase of available-for-sale securities	**N/A**	(37,210)
Proceeds from disposals of available-for-sale securities	**N/A**	13,968
Proceeds from maturities of available-for-sale securities	**N/A**	22,253
Purchase of securities at fair value through other comprehensive income and at amortized cost	**(49,106)**	N/A
Proceeds from disposals of securities at fair value through other comprehensive income and at amortized cost	**6,635**	N/A
Proceeds from maturities of securities at fair value through other comprehensive income and at amortized cost	**41,233**	N/A
Acquisitions of property, plant and equipment, intangible assets and investment property	**(141)**	(193)
Subsidiary disposal, net of cash and cash equivalents sold	**-**	684
Payment of the contingent consideration recognized at acquisition date	**(27)**	(23)
	(1,406)	(521)
Net increase in cash and cash equivalents	**731**	311
Cash and cash equivalents at beginning of period	**1,757**	1,212
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$ 2,488**	$ 1,523
Supplemental information on cash flows from (used in) operating activities		
Interest paid	**$ 890**	$ 821
Interest and dividends received	**2,760**	2,358

(1) The information presented for the nine-month period ended September 30, 2018 reflects the standards and amendments adopted on January 1, 2018. Comparative figures have not been restated. For more information, see Note 2, "Basis of presentation and significant accounting policies".

The accompanying notes are an integral part of the Condensed Interim Consolidated Financial Statements.

Notes to the Condensed Interim Consolidated Financial Statements
(unaudited)

NOTE 1 – INFORMATION ON THE *FÉDÉRATION DES CAISSES DESJARDINS DU QUÉBEC*

Nature of operations

The *Fédération des caisses Desjardins du Québec* (the Federation) is the cooperative entity responsible for assuming orientation, framework, coordination and development activities for Desjardins Group. The role of the Federation is also to protect the interests of Desjardins Group members. It provides its member caisses with a variety of services, including certain technical, financial, and administrative services. The member caisses exercise a collective power over the Federation, and each of them has a significant influence on the Federation.

In addition, the Federation is the parent company of several financial services subsidiaries. The address of its head office is 100 Des Commandeurs Street, Lévis, Quebec, Canada.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

Statement of compliance

Pursuant to the *Act Respecting Financial Services Cooperatives*, these unaudited Condensed Interim Consolidated Financial Statements (the Interim 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), more specifically in accordance with International Accounting Standard (IAS) 34, "Interim Financial Reporting", and the accounting requirements of the *Autorité des marchés financiers* (AMF) in Quebec, which do not differ from IFRS. Certain comparative figures have been reclassified to conform with the presentation of the Interim Consolidated Financial Statements for the current period. These reclassifications had no impact on the Federation's profit or loss or total assets and liabilities.

These Interim Consolidated Financial Statements should be read in conjunction with the audited Annual Consolidated Financial Statements (the Annual Consolidated Financial Statements) for the year ended December 31, 2017, and the shaded areas of section 4.0, "Risk management", of the related Management's Discussion and Analysis, which are an integral part of the Annual Consolidated Financial Statements. All accounting policies were applied as described in Note 2, "Basis of presentation and significant accounting policies", to the Annual Consolidated Financial Statements, except for the changes described in the "Changes in accounting policies" section of this note.

These Interim Consolidated Financial Statements were approved by the Board of Directors of the Federation on November 13, 2018.

Presentation and functional currency

These Interim Consolidated Financial Statements are expressed in Canadian dollars, which is also the functional currency of the Federation. Dollar amounts presented in the tables of the Notes to the Interim Consolidated Financial Statements are in millions of dollars, unless otherwise stated.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

CHANGES IN ACCOUNTING POLICIES

On January 1, 2018, the Federation adopted IFRS 9, “Financial Instruments”, IFRS 15, “Revenue from Contracts with Customers”, and the amendments to IFRS 4, “Insurance Contracts”.

IFRS 9 replaces IAS 39, “Financial Instruments: Recognition and Measurement”, and gives rise to new requirements for the classification and measurement of financial assets and liabilities and the impairment of financial instruments, as well as requirements for hedge accounting. 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.

The amendments to IFRS 4 are designed to address the concerns of insurers and their representative bodies about the different effective dates of IFRS 9 and IFRS 17, “Insurance Contracts”. These 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 could apply, to financial assets that are eligible and designated in accordance with certain specific criteria.

IFRS 15 introduces a single, comprehensive revenue recognition model for all contracts with customers other than those that are within the scope of other standards, such as financial instruments, insurance contracts and leases. The core principle of this standard is that revenue recognition should depict the transfer of control over a good or a service in an amount that reflects the consideration received or expected to be received in exchange for such good or service.

The significant accounting policies set out below arise from the adoption of these new standards and amendments and are applicable retrospectively as of January 1, 2018 without restatement of comparative periods. Consequently, the information presented for fiscal 2017 is in accordance with the accounting policies described in the Annual Consolidated Financial Statements for the year ended December 31, 2017.

a) Financial assets and liabilities

Financial assets and liabilities are recognized on the date the Federation becomes a party to their contractual provisions, namely the date of acquisition or issuance of the financial instrument. Regular-way purchases and sales of financial assets are recognized on a trade-date basis.

Classification and measurement

The classification of financial assets and liabilities in the classes defined in the financial instrument standard is presented in Note 3, “Carrying amount of financial instruments”.

Financial assets are classified based on their contractual cash flow characteristics and the business model under which they are held.

Contractual cash flow characteristics

In order to meet the cash flow characteristics criterion for purposes of classifying a financial asset, the cash flows from this asset must be solely payments of principal and interest on the principal amount outstanding. Principal is generally the fair value of the financial asset at initial recognition. Interest consists mainly of consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time, but it may also include consideration for other basic lending risks and costs, such as liquidity risk and administrative costs, as well as a certain profit margin.

Business models

The Federation’s business models are determined in a manner that reflects how groups of financial assets are managed to achieve a particular business objective. The business models refer to how the Federation manages its financial assets in order to generate cash flows. They therefore reflect whether cash flows will result from collecting contractual cash flows, selling financial assets or both. Determining business models requires the use of judgment and is based on all relevant evidence that is available to the Federation at the date of the assessment.

The Federation’s business models are defined as follows:

- Held to collect contractual cash flows: The objective of holding financial assets is achieved by collecting contractual cash flows.
- Held to collect contractual cash flows and sell: The objective is achieved by both collecting contractual cash flows and selling financial assets.
- Other business models: The objective is not consistent with any of the above-mentioned business models.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The classification and measurement of financial assets can be summarized as follows:

<table>
<tr><th colspan="2" rowspan="2">Classes</th><th rowspan="2">Categories</th><th colspan="2">Recognition</th></tr>
<tr><th>Initial</th><th>Subsequent</th></tr>
<tr><td rowspan="5">Financial assets</td><td rowspan="2">At fair value through profit or loss (i)</td><td>Classified as at fair value through profit or loss (ii)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td>Designated as at fair value through profit or loss (iii)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td rowspan="2">At fair value through other comprehensive income (iv)</td><td>Classified as at fair value through other comprehensive income (v)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td>Designated as at fair value through other comprehensive income (vi)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td colspan="2">Amortized cost (vii)</td><td>Fair value</td><td>Amortized cost</td></tr>
</table>

(i) Financial assets included in the “At fair value through profit or loss” class comprise financial assets “Classified as at fair value through profit or loss” and “Designated as at fair value through profit or loss”. Therefore:

- Changes in fair value of financial assets included in this class are recorded under “Net investment income (loss)” in the Consolidated Statements of Income.

- Interest income – calculated using the effective interest method – and dividend income from securities included in the “At fair value through profit or loss” class of the Personal and Business Services segment and the Other category are recognized under “Interest income – Securities” and, for the other segments, such income is mainly recognized under “Net investment income (loss)”. Interest income from derivative financial instruments is recognized under “Net investment income (loss)”.

(ii) Financial assets “Classified as at fair value through profit or loss” include the following:

- Debt instruments that are managed for trading purposes or on a fair value basis or do not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.

- Equity instruments.

- Derivative financial instruments.

Certain financial assets “Classified as at fair value through profit or loss” are designated for the overlay approach. For more information, see the “Application of the overlay approach to insurance operations financial assets” section of this note.

(iii) Financial assets “Designated as at fair value through profit or loss” are debt securities designated as such by management upon initial recognition, on an instrument-by-instrument basis. Management may make this irrevocable designation if doing so eliminates or significantly reduces a measurement or recognition inconsistency for the financial asset.

The Federation’s financial assets included in this measurement category comprise mainly securities (debt instruments) that back the life and health insurance actuarial liabilities and the property and casualty insurance provisions for claims.

(iv) Financial assets included in the “At fair value through other comprehensive income” class comprise financial assets “Classified as at fair value through other comprehensive income” and “Designated as at fair value through other comprehensive income”. Therefore:

- Changes in fair value of financial assets included in this class, except for changes related to the loss allowance for expected credit losses and exchange gains and losses on financial assets “Classified as at fair value through other comprehensive income”, are recorded in the Consolidated Statements of Comprehensive Income as net unrealized gains and losses. For financial assets “Classified as at fair value through other comprehensive income”, gains and losses are reclassified to the Consolidated Statements of Income when the asset is derecognized, while for financial assets “Designated as at fair value through other comprehensive income”, gains and losses are never reclassified subsequently to the Consolidated Statements of Income and are reclassified immediately to undistributed surplus earnings.

- Premiums and discounts on the purchase of financial assets “At fair value through other comprehensive income” are amortized over the life of the securities using the effective interest method and recognized under “Interest income – Securities” for the Personal and Business Services segment and the Other category. For the other segments, they are mainly recognized under “Net investment income (loss)”.

(v) Financial assets “Classified as at fair value through other comprehensive income” include debt instruments that are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

(vi) Financial assets "Designated as at fair value through other comprehensive income" include equity securities for which an irrevocable election was made, on an instrument-by-instrument basis. Financial assets included in this measurement category comprise investments in private companies that are held on a long-term basis.

(vii) Securities included in the "Amortized cost" class are financial assets that are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal or interest.

Securities included in this class are initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they are measured at amortized cost using the effective interest method. Income recognized on securities included in the "Amortized cost" class is presented under "Interest income – Loans" in the Consolidated Statements of Income when it is recognized by the Personal and Business Services segment and the Other category. For the other segments, it is recognized mainly under "Net investment income (loss)".

Financial assets are not reclassified following their initial recognition, except when the business model for managing those financial assets is changed.

Application of the overlay approach to insurance operations financial assets

The Federation elected to designate certain eligible financial assets for the overlay approach to reduce the volatility in profit or loss arising from the different effective dates of IFRS 9, "Financial Instruments", and IFRS 17, "Insurance Contracts". To be eligible, a financial asset must meet the following criteria:

- It is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety applying IAS 39, "Financial Instruments: Recognition and Measurement".
- It is held in respect of an activity connected with contracts within the scope of IFRS 4.

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 if the Federation had continued to apply IAS 39. As a result, 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. In determining the amount that would have been reported in the Consolidated Statements of Income if IAS 39 had been applied, the Federation considers gains (losses) on sales of securities, foreign currency fair value hedge accounting for equity instruments as well as impairment losses on equity instruments using accounting policies required by IAS 39.

Reclassifications are presented under "Overlay approach adjustment for insurance operations financial assets" in the Consolidated Statements of Income and under "Net change in unrealized gains and losses related to the overlay approach adjustment for insurance operations financial assets" in the Consolidated Statements of Comprehensive Income. The overlay approach may be used for the years beginning before January 1, 2021 or until the adoption of IFRS 17, if earlier.

Financial liabilities are classified based on their characteristics and the intention of management upon their issuance.

The classification and measurement of financial liabilities can be summarized as follows:

<table>
<tr><th colspan="2" rowspan="2">Classes</th><th rowspan="2">Categories</th><th colspan="2">Recognition</th></tr>
<tr><th>Initial</th><th>Subsequent</th></tr>
<tr><td rowspan="3">Financial liabilities</td><td rowspan="2">At fair value through profit or loss (i)</td><td>Classified as at fair value through profit or loss (ii)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td>Designated as at fair value through profit or loss (iii)</td><td>Fair value</td><td>Fair value</td></tr>
<tr><td colspan="2">Amortized cost (iv)</td><td>Fair value</td><td>Amortized cost</td></tr>
</table>

(i) Financial liabilities included in the "At fair value through profit or loss" class comprise financial liabilities "Classified as at fair value through profit or loss" and "Designated as at fair value through profit or loss". Therefore:

- Changes in fair value of financial liabilities included in this class are recorded under "Net investment income (loss)" in the Consolidated Statements of Income, except for financial liabilities designated as at fair value, for which the change in fair value that is attributable to the Federation's own credit risk is recognized in other comprehensive income with no subsequent reclassification to profit or loss.
- Interest expense related to financial liabilities included in the "At fair value through profit or loss" class is recognized under "Net investment income (loss)".

(ii) Financial liabilities "Classified as at fair value through profit or loss" are securities held for trading and include debt securities issued with the intention to repurchase them in the near term and securities that are part of a portfolio of securities that are managed together and for which there is evidence of an actual pattern of short-term profit-taking, such as "Commitments related to securities sold short". Derivative financial instruments are also classified as "Held for trading".

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

(iii) Financial liabilities "Designated as at fair value through profit or loss" are designated as such by management upon initial recognition, on an instrument-by-instrument basis, and are essentially debt securities. Management may make this irrevocable designation if doing so eliminates or significantly reduces a measurement or recognition inconsistency for the financial liability, if a group of financial liabilities is managed and its performance is evaluated on a fair value basis, or if the liabilities are hybrid financial liabilities containing at least one embedded derivative that would otherwise be separated from the host contract and recognized separately.

The Federation held no financial liabilities classified in this measurement category at the reporting date.

(iv) Financial liabilities that are not in the "At fair value through profit or loss" class are included in the "Amortized cost" class.

Financial liabilities included in this class are initially recognized at fair value in the Consolidated Balance Sheets and, at subsequent reporting dates, they are measured at amortized cost using the effective interest method. Interest expense on securities included in the "Amortized cost" class is recognized under "Interest expense" in the Consolidated Statements of Income for the Personal and Business Services segment and the Other category. Interest expense for the other segments is recognized mainly under "Net investment income (loss)" in the Consolidated Statements of Income.

b) Impairment of financial instruments

At each reporting date, the Federation recognizes a loss allowance for expected credit losses for debt instruments classified as at amortized cost or as at fair value through other comprehensive income, as well as certain off-balance sheet items, namely loan commitments and financial guarantees. This allowance is estimated based on an impairment model that comprises three 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 instruments considered as credit impaired, a loss allowance amounting to the lifetime expected credit losses continues to be recognized.

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

Determination of significant increases in credit risk

To determine whether, at the reporting date, credit risk has significantly increased since initial recognition, the Federation bases its assessment on the change in default risk over the expected life of the financial instrument, which requires significant judgment.

To this end, the Federation compares the probability of default (PD) of the financial instrument at the reporting date with its PD at the date of initial recognition. In addition, it considers reasonable and supportable information indicating a significant increase in credit risk since initial recognition, including qualitative information and information about future economic conditions to the extent that it affects the assessment of the instrument's PD. The criteria used to determine a significant increase in credit risk are mainly based on a relative change combined with an absolute change in the PD and vary depending on the type of clients. All instruments that are more than 30 days past due are transferred to Stage 2 of the impairment model.

Definition of default and credit-impaired financial asset

The definition of default used in the impairment model corresponds to the definition used for internal credit risk management purposes and for regulatory purposes. It considers relevant quantitative and qualitative factors. In particular, a loan is in default when contractual payments are over 90 days past due. A financial asset is considered credit-impaired when it is in default, unless the detrimental impact on estimated future cash flows is considered insignificant.

Measurement of the loss allowance for expected credit losses

The loss allowance for expected credit losses reflects an unbiased amount, based on a probability-weighted present value of cash flow shortfalls, and takes into account reasonable and supportable information about past events, current conditions and forecasts of future economic conditions. Generally, the loss allowance for expected credit losses represents the present value of the difference between cash flows that are due, or the amount of the commitment that may be used under the terms and conditions of the contract, and total cash flows that the Federation expects to receive. For credit-impaired financial assets, expected credit losses are calculated based on the difference between the gross carrying amount of the asset and estimated cash flows.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The measurement of the loss allowance for expected credit losses is estimated for each exposure at the reporting date and is based on multiplying the three credit risk parameters, namely PD, loss given default (LGD) and exposure at default (EAD). The result of this multiplication is then discounted using the effective interest rate. The parameters are estimated using an appropriate segmentation that considers common credit risk characteristics. For financial instruments in Stage 1 of the impairment model, credit risk parameters are projected over a maximum horizon of 12 months, while for those in Stage 2 or Stage 3, they are projected over the remaining life of the instrument.

The loss allowance for expected credit losses also considers information about future economic conditions. To incorporate forward-looking information relevant to the determination of significant increases in credit risk and the measurement of the loss allowance for expected credit losses, the Federation uses the econometric models for credit risk projection. These models estimate the impact of macroeconomic variables on the various credit risk parameters. The Federation uses three scenarios (base, upside and downside) to determine the loss allowance for expected credit losses and assigns to each scenario a probability of occurrence. The Federation may also make adjustments to take into account the relevant information that affects the measurement of the loss allowance and that has not been incorporated into the credit risk parameters. Incorporating forward-looking information is based on a set of assumptions and methodologies specific to credit risk and economic projections and therefore requires a high degree of judgment.

For credit-impaired financial assets that are individually material, measuring the loss allowance for expected credit losses does not require using credit risk parameters. It is instead based on an extensive review of the borrower’s situation and the realization of collateral held. The measurement represents a probability-weighted present value, calculated using the effective interest rate, of cash flow shortfalls that takes into consideration the impact of various scenarios that may materialize and information about future economic conditions.

Expected life

The expected life of most financial instruments is equal to the maximum contractual term during which the Federation is exposed to credit risk, including extension options that may be exercised solely by the borrower. The exception to this rule concerns revolving exposures, which consist of personal and business lines of credit and credit card loans. Their life is estimated as being the period over which there is exposure to credit risk but for which expected credit losses would not be mitigated by normal credit risk management actions.

Recognition of the loss allowance for expected credit losses

The loss allowance for expected credit losses on loans is recorded under “Allowance for credit losses” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income.

The loss allowance for expected credit losses on loan commitments and financial guarantees is recorded under “Other liabilities – Other” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income.

The loss allowance for expected credit losses on securities at “Amortized cost” is recorded against “Securities – Securities at amortized cost” in the Consolidated Balance Sheets and under “Provision for credit losses” in the Consolidated Statements of Income. The loss allowance for expected credit losses on securities “Classified as at fair value through other comprehensive income” is recognized under “Net unrealized losses on debt securities classified as at fair value through other comprehensive income” in the Consolidated Statements of Comprehensive Income and under “Provision for credit losses” in the Consolidated Statements of Income.

Foreclosed assets

Assets foreclosed to settle credit-impaired loans are recognized on the date of the foreclosure at their fair value less costs to sell. Any difference between the carrying amount of the loan and the fair value recorded for the foreclosed assets is recognized under “Provision for credit losses”.

Loan write-off

A loan is written off, in whole or in part, when recovery is no longer reasonably expected, which is when all attempts at restructuring or collection have been made and, based on an assessment of the file in its entirety, there are no other means to recover the loan. When a loan is written off completely, any subsequent payments are recorded under “Provision for credit losses” in the Consolidated Statements of Income. Credit card balances are written off completely when no payment has been received at the end of a period of 180 days. These balances could however still be subject to enforcement activity.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

c) Derivative financial instruments and hedging activities

Hybrid financial instruments

When a hybrid contract contains a host that is an asset within the scope of IFRS 9, the entire hybrid contract is classified and recognized based on the characteristics of the hybrid contract.

An embedded derivative is separated from the host and accounted for separately as a derivative when the host is not an asset within the scope of IFRS 9 and the following conditions are met: (a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the hybrid contract is not measured at fair value with changes in fair value recognized in the Consolidated Statements of Income.

The Federation does not hold any hybrid financial instruments containing a host that is not an asset within the scope of IFRS 9.

d) Revenue recognition

Revenue is recognized when the Federation has transferred control of a good or service. In addition to the items mentioned in section a), "Financial assets and liabilities", the specific recognition criteria that follow must also be met before revenue can be recognized.

Net interest income

Interest income and expense are mainly earned or incurred by the Personal and Business Services segment and the Other category. They are recognized using the effective interest method for all financial instruments measured at amortized cost, for interest-bearing financial assets "Classified as at fair value through other comprehensive income" and for financial instruments included in the "At fair value through profit or loss" class.

The effective interest method is used in the calculation of the amortized cost of a financial asset or liability and in the allocation of interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of a financial asset or to the amortized cost of a financial liability.

For financial assets that are not considered credit-impaired (Stages 1 and 2), interest income is calculated on the gross carrying amount of the financial instrument. For credit-impaired financial assets (Stage 3), interest income is calculated by applying the effective interest rate to the amortized cost of the asset, which corresponds to the gross carrying amount less the loss allowance for expected credit losses.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

IMPACT OF CHANGES IN ACCOUNTING POLICIES

The retrospective impact of applying IFRS 9, IFRS 15 and amendments to IFRS 4 have been recognized in the opening balances of the Consolidated Balance Sheet as at January 1, 2018.

The following table presents the impact of adopting these standards and amendments on the Federation's Consolidated Balance Sheet as at January 1, 2018.

	Balance as at December 31, 2017	IFRS 9	IFRS 15	IFRS 4	Opening balance as at January 1, 2018
ASSETS					
Cash and deposits with financial institutions	$ 1,731	$ -	$ -	$ -	**$ 1,731**
Securities	46,904	-	-	-	**46,904**
Securities borrowed or purchased under reverse repurchase agreements	9,377	-	-	-	**9,377**
Loans	58,882	-	-	-	**58,882**
Allowance for credit losses	(198)	(295)	-	-	**(493)**
Segregated fund net assets	13,379	-	-	-	**13,379**
Other assets	15,665	77	46	-	**15,788**
TOTAL ASSETS	$ 145,740	$ (218)	$ 46	$ -	**$ 145,568**
LIABILITIES AND EQUITY					
LIABILITIES					
Deposits	$ 52,149	$ -	$ -	$ -	**$ 52,149**
Other liabilities	76,184	(6)	48	-	**76,226**
Subordinated notes	1,388	-	-	-	**1,388**
TOTAL LIABILITIES	129,721	(6)	48	-	**129,763**
EQUITY					
Capital stock	8,537	-	-	-	**8,537**
Undistributed surplus earnings	5,674	410	-	(376)	**5,708**
Accumulated other comprehensive income	458	(411)	-	376	**423**
Reserves	540	(211)	(2)	-	**327**
Equity – Group's share	15,209	(212)	(2)	-	**14,995**
Non-controlling interests	810	-	-	-	**810**
TOTAL EQUITY	16,019	(212)	(2)	-	**15,805**
TOTAL LIABILITIES AND EQUITY	$ 145,740	$ (218)	$ 46	$ -	**$ 145,568**

The following table presents additional information on the impact of adopting these standards and amendments on the Federation's "Equity – Federation's share" as at January 1, 2018.

	Group's share
Undistributed surplus earnings	
Balance as at December 31, 2017	**$ 5,674**
Adoption of the IFRS 9 measurement categories	**412**
Net unrealized gains related to the overlay approach adjustment for insurance operations financial assets	**(376)**
Recognition of expected credit losses on financial instruments	**(2)**
Opening balance as at January 1, 2018	**$ 5,708**
Accumulated other comprehensive income	
Balance as at December 31, 2017	**$ 458**
Adoption of the IFRS 9 measurement categories	**(412)**
Recognition of expected credit losses on debt securities at fair value through other comprehensive income	**1**
Net unrealized gains related to the overlay approach adjustment for insurance operations financial assets	**376**
Opening balance as at January 1, 2018	**$ 423**
Reserves	
Balance as at December 31, 2017	**$ 540**
Recognition of expected credit losses on financial instruments	**(211)**
Impact of the adoption of IFRS 15	**(2)**
Opening balance as at January 1, 2018	**$ 327**

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The following table presents the impact of adopting IFRS 9 on the classification and measurement of financial instruments as at January 1, 2018.

	Notes	Measurement category under IAS 39	Measurement category under IFRS 9	Carrying amount under IAS 39 as at December 31, 2017	Carrying amount under IFRS 9 as at January 1, 2018
Financial assets					
Cash and deposits with financial institutions	**(1)**	At fair value through profit or loss – held for trading	Amortized cost	**$ 23**	**$ 23**
		At fair value through profit or loss – designated as at fair value through profit or loss	Designated as at fair value through profit or loss	**298**	**298**
		Available for sale	Classified as at fair value through other comprehensive income	**639**	**639**
		Loans and receivables	Amortized cost	**771**	**771**
Securities					
Debt instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	**13,271**	**13,271**
		At fair value through profit or loss – designated as at fair value through profit or loss	Designated as at fair value through profit or loss	**16,665**	**16,665**
	(2)	At fair value through profit or loss – designated as at fair value through profit or loss	Classified as at fair value through profit or loss	**6**	**6**
	(3)	Available for sale	Classified as at fair value through profit or loss	**23**	**23**
		Available for sale	Classified as at fair value through other comprehensive income	**10,860**	**10,860**
	(4)	Available for sale	Amortized cost	**1,090**	**1,090**
Equity instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	**41**	**41**
	(5)	At fair value through profit or loss – designated as at fair value through profit or loss	Classified as at fair value through profit or loss	**1,671**	**1,671**
	(6)	Available for sale	Classified as at fair value through profit or loss	**3,275**	**3,275**
	(7)	Available for sale	Designated as at fair value through other comprehensive income	**2**	**2**
Securities borrowed or purchased under reverse repurchase agreements		Loans and receivables	Amortized cost	**$ 9,377**	**$ 9,377**

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The following table presents the impact of adopting IFRS 9 on the classification and measurement of financial instruments as at January 1, 2018 *(continued)*.

	Notes	Measurement category under IAS 39	Measurement category under IFRS 9	Carrying amount under IAS 39 as at December 31, 2017	Carrying amount under IFRS 9 as at January 1, 2018
Financial assets *(continued)*					
Loans		Loans and receivables	Amortized cost	$ 58,684	$ 58,389
Other financial assets					
Clients' liability under acceptances		Loans and receivables	Amortized cost	31	31
Premiums receivable		Loans and receivables	Amortized cost	2,098	2,098
Derivative financial instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	3,772	3,772
Amounts receivable from clients, brokers and financial institutions		Loans and receivables	Amortized cost	1,563	1,563
Other		Loans and receivables	Amortized cost	1,013	1,013
Total financial assets				$ 125,173	$ 124,878
Financial liabilities					
Deposits		Financial liabilities at amortized cost	Amortized cost	$ 52,149	$ 52,149
Other financial liabilities					
Acceptances		Financial liabilities at amortized cost	Amortized cost	31	31
Commitments related to securities sold short		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	9,112	9,112
Commitments related to securities lent or sold under repurchase agreements		Financial liabilities at amortized cost	Amortized cost	10,062	10,062
Derivative financial instruments		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	3,677	3,677
Amounts payable to clients, brokers and financial institutions		Financial liabilities at amortized cost	Amortized cost	4,247	4,247
Other		Financial liabilities at amortized cost	Amortized cost	2,638	2,638
		At fair value through profit or loss – held for trading	Classified as at fair value through profit or loss	452	452
Subordinated notes		Financial liabilities at amortized cost	Amortized cost	1,388	1,388
Total financial liabilities				$ 83,756	$ 83,756

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

(1) Certain items in cash and deposits with financial institutions were classified as “Held for trading” under IAS 39 as at December 31, 2017. As at January 1, 2018, the Federation classified these debt instruments as at “Amortized cost” under IFRS 9 as they are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest. All these securities matured or were sold during the first quarter of 2018. The effective interest rate on these debt instruments ranged from 0.59% and 1.73% as at January 1, 2018, and interest income recognized on these securities following the adoption of IFRS 9 was insignificant.

(2) These debt instruments were classified as “Designated as at fair value through profit or loss” under IAS 39 as at December 31, 2017. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as the contractual terms of these financial assets give rise to cash flows that are not solely payments of principal and interest on the principal amount outstanding.

(3) These debt instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, these debt instruments were “Classified as at fair value through profit or loss” under IFRS 9 because they are held within a business model whose objective is achieved by selling financial assets or because they do not meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest.

(4) These debt instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, the Federation classified them as at “Amortized cost” under IFRS 9 as they are held within a business model whose objective is achieved by collecting contractual cash flows and meet the criteria of the contractual cash flow test performed to determine whether cash flows are solely payments of principal and interest. The fair value of the securities still held as at September 30, 2018 was $45 million. If these securities had not been reclassified to be measured at “Amortized cost” under IFRS 9 as at January 1, 2018, an insignificant loss would have been recognized in the Consolidated Statements of Comprehensive Income for the three-month period ended September 30, 2018 and an insignificant loss would have been recognized for the nine-month period ended September 30, 2018.

(5) These equity instruments were classified as “Designated as at fair value through profit or loss” under IAS 39 as at December 31, 2017. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as, under IFRS 9, all investments in equity instruments other than those designated as at fair value through other comprehensive income have to be included in this measurement category.

(6) These equity instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, they were “Classified as at fair value through profit or loss” as, under IFRS 9, all investments in equity instruments other than those designated as at fair value through other comprehensive income have to be included in this measurement category.

(7) These equity instruments were classified as “Available for sale” under IAS 39 as at December 31, 2017. They were recognized at fair value and changes in fair value were recognized in the Consolidated Statements of Comprehensive Income. As at January 1, 2018, these instruments, which consist of an investment in a private company that will be held on a long-term basis, were irrevocably “Designated as at fair value through other comprehensive income”. Gains and losses on these instruments will therefore never be reclassified subsequently to the Consolidated Statements of Income.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The following table reconciles the carrying amounts of financial instruments recognized under IAS 39 as at December 31, 2017 to the carrying amounts under IFRS 9 as at January 1, 2018.

	Carrying amount under IAS 39 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
Financial assets				
Classified as at fair value through profit or loss[1]				
Cash and deposits with financial institutions	$ 23	$ -	$ -	$ 23
To securities at amortized cost	-	(23)	-	(23)
	23	(23)	-	-
Securities				
Debt instruments	13,271	-	-	13,271
From securities designated as at fair value through profit or loss	-	6	-	6
From available-for-sale securities	-	23	-	23
Equity instruments	41	-	-	41
From securities designated as at fair value through profit or loss	-	1,671	-	1,671
From available-for-sale securities	-	3,275	-	3,275
	13,312	4,975	-	18,287
Derivative financial instruments	3,772	-	-	3,772
Total financial assets classified as at fair value through profit or loss	17,107	4,952	-	22,059
Designated as at fair value through profit or loss[2]				
Cash and deposits with financial institutions	298	-	-	298
Securities				
Debt instruments	16,671	-	-	16,671
To securities classified as at fair value through profit or loss	-	(6)	-	(6)
Equity instruments	1,671	-	-	1,671
To securities classified as at fair value through profit or loss	-	(1,671)	-	(1,671)
	18,342	(1,677)	-	16,665
Total financial assets designated as at fair value through profit or loss	18,640	(1,677)	-	16,963
Available for sale				
Cash and deposits with financial institutions	639	-	-	639
To securities classified as at fair value through other comprehensive income	-	(639)	-	(639)
	639	(639)	-	-
Securities				
Debt instruments	11,973	-	-	11,973
To securities classified as at fair value through profit or loss	-	(23)	-	(23)
To securities classified as at fair value through other comprehensive income	-	(10,860)	-	(10,860)
To securities at amortized cost	-	(1,090)	-	(1,090)
Equity instruments	3,277	-	-	3,277
To securities classified as at fair value through profit or loss	-	(3,275)	-	(3,275)
To securities designated as at fair value through other comprehensive income	-	(2)	-	(2)
	15,250	(15,250)	-	-
Total available-for-sale financial assets	$ 15,889	$ (15,889)	$ -	$ -

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The following table reconciles the carrying amounts of financial instruments recognized under IAS 39 as at December 31, 2017 to the carrying amounts under IFRS 9 as at January 1, 2018 (*continued*).

	Carrying amount under IAS 39 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
Financial assets *(continued)*				
Classified as at fair value through other comprehensive income				
Cash and deposits with financial institutions	$ -	$ -	$ -	$ -
From available-for-sale securities	-	639	-	639
	-	639	-	639
Securities				
Debt instruments	-	-	-	-
From available-for-sale securities	-	10,860	-	10,860
	-	10,860	-	10,860
Total financial assets classified as at fair value through other comprehensive income	-	11,499	-	11,499
Designated as at fair value through other comprehensive income				
Securities				
Equity instruments	-	-	-	-
From available-for-sale securities	-	2	-	2
Total financial assets designated as at fair value through other comprehensive income	-	2	-	2
Amortized cost(3)				
Cash and deposits with financial institutions	771	-	-	771
From securities held for trading	-	23	-	23
	771	23	-	794
Securities				
Debt instruments	-	-	-	-
From available-for-sale securities	-	1,090	-	1,090
	-	1,090	-	1,090
Securities borrowed or purchased under reverse repurchase agreements	9,377	-	-	9,377
Loans	58,684	-	(295)	58,389
Other financial assets	4,705	-	-	4,705
Total financial assets at amortized cost	$ 73,537	$ 1,113	$ (295)	$ 74,355

(1) For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the “At fair value through profit or loss – held for trading” category.
(2) For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the “At fair value through profit or loss – designated as at fair value through profit or loss” category.
(3) For the carrying amount under IAS 39 as at December 31, 2017, corresponds to the “Loans and receivables” category.

NOTE 2 – BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES (*continued*)

The following table reconciles allowances determined under IAS 39 and IAS 37, "Provisions, Contingent Liabilities and Contingent Assets", as at December 31, 2017 to the allowance determined using the IFRS 9 expected credit losses model as at January 1, 2018.

	Carrying amount under IAS 39 and IAS 37 as at December 31, 2017	Reclassification	Remeasurement	Carrying amount under IFRS 9 as at January 1, 2018
Allowance on financial assets at amortized cost				
Loans and receivables reclassified as at amortized cost	$ 198	$ -	$ 295	$ 493
	198	-	295	493
Allowance on securities at fair value through other comprehensive income				
Available-for-sale securities reclassified as at fair value through other comprehensive income	-	-	1	1
	-	-	1	1
Allowance on off-balance sheet items	40	-	(6)	34
Total allowances	$ 238	$ -	$ 290	$ 528

FUTURE ACCOUNTING CHANGES

Accounting standards issued by the IASB, but not yet effective as at December 31, 2017, are described in Note 2, "Basis of presentation and significant accounting policies", to the Annual Consolidated Financial Statements. The IASB has since issued the following amendments:

Conceptual Framework for Financial Reporting

In March 2018, the IASB issued the "Conceptual Framework for Financial Reporting", which replaces the current version of the conceptual framework. The "Conceptual Framework for Financial Reporting" includes new concepts, updates the definitions and recognition criteria for assets and liabilities and clarifies some key concepts. The Federation is currently assessing the impact of adopting this new framework, which will be effective for annual periods beginning on or after January 1, 2020.

NOTE 3 – CARRYING AMOUNT OF FINANCIAL INSTRUMENTS

CLASSIFICATION AND CARRYING AMOUNT OF FINANCIAL INSTRUMENTS

The following tables present the carrying amount of all financial assets and liabilities according to their classification in the classes defined in the financial instrument standards.

	At fair value through profit or loss		At fair value through other comprehensive income			
As at September 30, 2018	**Classified as at fair value through profit or loss**	**Designated as at fair value through profit or loss**	**Classified as at fair value through other comprehensive income[4]**	**Designated as at fair value through other comprehensive income**	**Amortized cost[4]**	**Total**
Financial assets[1]						
Cash and deposits with financial institutions	$ -	$ 366	$ 847	$ -	$ 1,275	$ 2,488
Securities	22,745	16,198	11,340	43	1,732	52,058
Securities borrowed or purchased under reverse repurchase agreements	-	-	-	-	11,856	11,856
Loans[2]	-	-	-	-	61,721	61,721
Other financial assets						
Clients' liability under acceptances	-	-	-	-	251	251
Premiums receivable	-	-	-	-	2,391	2,391
Derivative financial instruments[3]	4,274	-	-	-	-	4,274
Amounts receivable from clients, brokers and financial institutions	-	-	-	-	3,042	3,042
Other	15	-	-	-	1,444	1,459
Total financial assets	$ 27,034	$ 16,564	$ 12,187	$ 43	$ 83,712	$ 139,540
Financial liabilities						
Deposits	$ -	$ -	$ -	$ -	$ 57,798	$ 57,798
Other financial liabilities						
Acceptances	-	-	-	-	251	251
Commitments related to securities sold short	11,199	-	-	-	-	11,199
Commitments related to securities lent or sold under repurchase agreements	-	-	-	-	13,182	13,182
Derivative financial instruments[3]	4,262	-	-	-	-	4,262
Amounts payable to clients, brokers and financial institutions	-	-	-	-	6,553	6,553
Other	244	-	-	-	2,612	2,856
Subordinated notes	-	-	-	-	1,343	1,343
Total financial liabilities	$ 15,705	$ -	$ -	$ -	$ 81,739	$ 97,444

[1] An amount of $2,918 million corresponds to financial assets designated for the overlay approach.
[2] For more information, see Note 5, "Loans and allowance for credit losses".
[3] Include derivative financial instruments designated as hedging instruments amounting to $246 million in assets and $442 million in liabilities.
[4] As at September 30, 2018, the allowance for credit losses on securities at "Amortized cost" totalled $1 million, and the allowance for credit losses on securities "Classified as at fair value through other comprehensive income" totalled $2 million. Detailed information on the allowance for credit losses on loans is presented in Note 5, "Loans and allowance for credit losses".

During the nine-month period ended September 30, 2018, no financial instruments have been reclassified.

NOTE 3 – CARRYING AMOUNT OF FINANCIAL INSTRUMENTS *(continued)*

CLASSIFICATION AND CARRYING AMOUNT OF FINANCIAL INSTRUMENTS *(continued)*

	At fair value through profit or loss				
As at December 31, 2017	Held for trading	Designated as at fair value through profit or loss	Available for sale[(1)]	Loans and receivables, and financial liabilities at amortized cost	Total
Financial assets					
Cash and deposits with financial institutions	$ 23	$ 298	$ 639	$ 771	$ 1,731
Securities	13,312	18,342	15,250	-	46,904
Securities borrowed or purchased under reverse repurchase agreements	-	-	-	9,377	9,377
Loans[(2)]	-	-	-	58,684	58,684
Other financial assets					
Clients' liability under acceptances	-	-	-	31	31
Premiums receivable	-	-	-	2,098	2,098
Derivative financial instruments[(3)]	3,772	-	-	-	3,772
Amounts receivable from clients, brokers and financial institutions	-	-	-	1,563	1,563
Other	-	-	-	1,013	1,013
Total financial assets	$ 17,107	$ 18,640	$ 15,889	$ 73,537	$ 125,173
Financial liabilities					
Deposits	$ -	$ -	$ -	$ 52,149	$ 52,149
Other financial liabilities					
Acceptances	-	-	-	31	31
Commitments related to securities sold short	9,112	-	-	-	9,112
Commitments related to securities lent or sold under repurchase agreements	-	-	-	10,062	10,062
Derivative financial instruments[(3)]	3,677	-	-	-	3,677
Amounts payable to clients, brokers and financial institutions	-	-	-	4,247	4,247
Other	452	-	-	2,638	3,090
Subordinated notes	-	-	-	1,388	1,388
Total financial liabilities	$ 13,241	$ -	$ -	$ 70,515	$ 83,756

(1) During the year ended December 31, 2017, the Federation concluded that there was no objective evidence of material impairment.
(2) For more information, see Note 5, "Loans and allowance for credit losses".
(3) Include derivative financial instruments designated as hedging instruments amounting to $275 million in assets and $351 million in liabilities.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS

DETERMINATION OF THE FAIR VALUE OF FINANCIAL INSTRUMENTS

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 valuation 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 made 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.

For more information on the valuation techniques used to determine the fair value of the main financial instruments, refer to Note 2, “Basis of presentation and significant accounting policies”, to the Annual Consolidated Financial Statements.

Financial instruments whose fair value equals 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”.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of certain financial instruments measured at amortized cost does not equal fair value. These financial instruments are presented in the following table.

	As at September 30, 2018		As at December 31, 2017	
	Carrying amount	**Fair value**	Carrying amount	Fair value
Financial assets				
Securities	**$ 1,732**	**$ 1,732**	N/A	N/A
Loans	**61,721**	**61,559**	$ 58,684	$ 58,838
Financial liabilities				
Deposits	**57,798**	**57,686**	52,149	50,182
Subordinated notes	**1,343**	**1,400**	1,388	1,488

FAIR VALUE HIERARCHY

The fair value measurement of financial instruments is determined using the following three-level fair value hierarchy:

- Level 1 – Measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 – Valuation techniques based primarily on observable market data.
- Level 3 – Valuation techniques not based primarily on observable market data.

Transfers between levels

Transfers between hierarchy levels for instruments measured at fair value are made at the reporting date.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

HIERARCHY OF FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE

The following tables present the hierarchy for financial instruments measured at fair value in the Consolidated Balance Sheets.

As at September 30, 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets				
Financial assets at fair value through profit or loss				
Cash and deposits with financial institutions	$ 49	$ 317	$ -	$ 366
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	10,352	1,099	-	11,451
Provincial governmental entities and municipal corporations in Canada	16,412	1,154	-	17,566
School or public corporations in Canada	14	85	-	99
Foreign public administrations	628	-	-	628
Other securities				
Financial institutions	30	873	56	959
Other issuers	-	2,798	762	3,560
Equity securities	3,408	634	638	4,680
	30,893	6,960	1,456	39,309
Derivative financial instruments				
Interest rate contracts	-	1,935	-	1,935
Foreign exchange contracts	-	335	-	335
Other contracts	-	2,004	-	2,004
	-	4,274	-	4,274
Other assets	-	-	15	15
Total financial assets at fair value through profit or loss	30,893	11,234	1,471	43,598
Financial assets at fair value through other comprehensive income				
Cash and deposits with financial institutions	179	668	-	847
Securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	2,021	580	-	2,601
Provincial governmental entities and municipal corporations in Canada	4,592	573	-	5,165
Foreign public administrations	8	-	-	8
Other securities				
Financial institutions	-	2,971	-	2,971
Other issuers	-	506	89	595
Equity securities	-	43	-	43
Total financial assets at fair value through other comprehensive income	6,800	5,341	89	12,230
Financial instruments of segregated funds	5,960	7,920	72	13,952
Total financial assets	$ 43,653	$ 24,495	$ 1,632	$ 69,780
Financial liabilities				
Financial liabilities at fair value through profit or loss				
Other liabilities				
Commitments related to securities sold short	$ 11,013	$ 186	$ -	$ 11,199
Other	-	-	244	244
	11,013	186	244	11,443
Derivative financial instruments				
Interest rate contracts	-	2,065	-	2,065
Foreign exchange contracts	-	277	-	277
Other contracts	-	1,920	-	1,920
	-	4,262	-	4,262
Total financial liabilities	$ 11,013	$ 4,448	$ 244	$ 15,705

NOTE 4 –FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

HIERARCHY OF FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE *(continued)*

As at December 31, 2017	Level 1	Level 2	Level 3	Total
Financial assets				
Financial assets at fair value through profit or loss				
Cash and deposits with financial institutions	$ 8	$ 313	$ -	$ 321
Securities at fair value through profit or loss				
Debt securities issued or guaranteed by				
Canadian governmental entities	7,620	1,247	-	8,867
Provincial governmental entities and municipal corporations in Canada	15,232	1,176	-	16,408
School or public corporations in Canada	14	94	-	108
Foreign public administrations	312	-	-	312
Other securities				
Financial institutions	29	800	58	887
Other issuers	-	2,497	867	3,364
Equity securities	1,236	236	236	1,708
	24,451	6,363	1,161	31,975
Derivative financial instruments				
Interest rate contracts	-	1,624	-	1,624
Foreign exchange contracts	-	390	-	390
Other contracts	-	1,758	-	1,758
	-	3,772	-	3,772
Total financial assets at fair value through profit or loss	24,451	10,135	1,161	35,747
Available-for-sale financial assets				
Cash and deposits with financial institutions	36	603	-	639
Available-for-sale securities				
Debt securities issued or guaranteed by				
Canadian governmental entities	1,821	573	-	2,394
Provincial governmental entities and municipal corporations in Canada	4,610	1,205	-	5,815
Foreign public administrations	7	28	-	35
Other securities				
Financial institutions	-	2,878	-	2,878
Other issuers	5	751	95	851
Equity securities	2,367	631	279	3,277
Total available-for-sale financial assets	8,846	6,669	374	15,889
Financial instruments of segregated funds	5,859	7,456	60	13,375
Total financial assets	$ 39,156	$ 24,260	$ 1,595	$ 65,011
Financial liabilities				
Financial liabilities held for trading				
Other liabilities				
Commitments related to securities sold short	$ 8,951	$ 161	$ -	$ 9,112
Other	-	-	452	452
	8,951	161	452	9,564
Derivative financial instruments				
Interest rate contracts	-	1,619	-	1,619
Foreign exchange contracts	-	365	-	365
Other contracts	-	1,693	-	1,693
	-	3,677	-	3,677
Total financial liabilities	$ 8,951	$ 3,838	$ 452	$ 13,241

During the nine-month period ended September 30, 2018 and the year ended December 31, 2017, no material transfers attributable to changes in the observability of market data were made between hierarchy levels for instruments measured at fair value.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3

Valuation process for financial instruments categorized within Level 3

The Federation has implemented various key controls and procedures to ensure that financial instruments categorized within Level 3 are appropriately and reliably measured. The financial governance framework provides for independent monitoring and segregation of duties in that respect. During the nine-month period ended September 30, 2018, no significant changes were made to the key controls and procedures as well as the valuation techniques for financial instruments categorized within Level 3. For more information on the valuation process for financial instruments categorized within Level 3, refer to Note 4, “Fair value of financial instruments”, to the Annual Consolidated Financial Statements.

Sensitivity of financial instruments categorized within Level 3

The Federation performs sensitivity analyses to measure the fair value of financial instruments categorized within Level 3. Changing unobservable inputs to one or more reasonably possible alternative assumptions does not significantly change the fair value of financial instruments categorized within Level 3.

Valuation techniques and inputs used to measure the fair value of financial instruments categorized within Level 3

During the nine-month period ended September 30, 2018, no changes were made to valuation techniques. Some changes were made to input value ranges used to determine fair value, but they did not result in material changes to the fair value of financial instruments categorized within Level 3.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3 *(continued)*

Changes in fair value of financial instruments categorized within Level 3

The following tables present the changes in fair value of financial instruments categorized within Level 3 of the hierarchy, namely financial instruments whose fair value is determined using valuation techniques not based mainly on observable market data.

For the nine-month period ended September 30, 2018	Balance as at December 31, 2017	Impact of changes in accounting policies (Note 2)	Balance as at January 1, 2018	Realized gains / losses recognized in profit or loss[1]	Unrealized gains / losses recognized in profit or loss[2]	Unrealized gains / losses recognized in other comprehensive income[3]	Transfers of instruments into (out of) Level 3	Purchases / Issuances / Other	Sales / Settlements / Other	Balance at end of period
Financial assets										
Financial assets at fair value through profit or loss										
Securities										
Other securities										
Financial institutions										
Mortgage bonds	$ 58	$ -	$ 58	$ -	$ (2)	$ -	$ -	$ -	$ -	$ 56
Other issuers										
Hedge funds	4	-	4	4	(1)	-	-	-	-	7
Asset-backed term notes	6	-	6	-	2	-	-	-	(3)	5
Mortgage bonds	857	-	857	-	(33)	-	-	-	(74)	750
Equity securities	236	279	515	-	9	-	-	123	(9)	638
Other assets	-	-	-	-	-	-	-	15	-	15
Total financial assets at fair value through profit or loss	**1,161**	**279**	**1,440**	**4**	**(25)**	**-**	**-**	**138**	**(86)**	**1,471**
Available-for-sale financial assets										
Securities										
Other securities										
Other issuers										
Mortgage bonds	95	(95)	-	-	-	-	-	-	-	-
Equity securities	279	(279)	-	-	-	-	-	-	-	-
Total available-for-sale financial assets	**374**	**(374)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Financial assets at fair value through other comprehensive income										
Securities										
Other securities										
Other issuers										
Mortgage bonds	-	95	95	-	-	(4)	-	-	(2)	89
Total financial assets at fair value through other comprehensive income	**-**	**95**	**95**	**-**	**-**	**(4)**	**-**	**-**	**(2)**	**89**
Financial instruments of segregated funds	60	-	60	(1)	2	-	-	81	(70)	72
Total financial assets	**$ 1,595**	**$ -**	**$ 1,595**	**$ 3**	**$ (23)**	**$ (4)**	**$ -**	**$ 219**	**$ (158)**	**$ 1,632**
Financial liabilities										
Financial liabilities at fair value through profit or loss										
Other liabilities – Other										
Financial liability related to put options	$ 64	$ -	$ 64	$ -	$ -	$ -	$ -	$ -	$ (64)	$ -
Financial liability related to the contingent consideration	388	-	388	-	133	-	-	-	(277)	244
Total financial liabilities	**$ 452**	**$ -**	**$ 452**	**$ -**	**$ 133**	**$ -**	**$ -**	**$ -**	**$ (341)**	**$ 244**

[1] Realized gains or losses on financial assets classified or designated as at fair value through profit or loss are presented under "Net investment income (loss)".
[2] Unrealized gains or losses on financial assets classified or designated as at fair value through profit or loss are presented under "Net investment income (loss)".
[3] Unrealized gains or losses on financial assets “Classified as at fair value through other comprehensive income” are recognized under “Net unrealized losses” on debt securities at fair value through other comprehensive income, while unrealized gains or losses on financial assets “Designated as at fair value through other comprehensive income” are recognized under “Net change in unrealized gains and losses on equity securities designated as at fair value through other comprehensive income” in the Consolidated Statements of Comprehensive Income.

NOTE 4 – FAIR VALUE OF FINANCIAL INSTRUMENTS *(continued)*

FAIR VALUE OF FINANCIAL INSTRUMENTS CATEGORIZED WITHIN LEVEL 3 *(continued)*

Changes in fair value of financial instruments categorized within Level 3 (*continued*)

For the nine-month period ended September 30, 2017	Balance at beginning of period	Realized gains / losses recognized in profit or loss[(1)]	Unrealized gains / losses recognized in profit or loss[(2)]	Unrealized gains / losses recognized in other comprehensive income[(3)]	Transfers of instruments into (out of) Level 3	Purchases / Issuances / Other	Sales / Settlements / Other	Balance at end of period
Financial assets								
Financial assets at fair value through profit or loss								
Securities								
Other securities								
Financial institutions								
Mortgage bonds	$ 60	$ -	$ (2)	$ -	$ -	$ -	$ -	$ 58
Other issuers								
Hedge funds	7	-	4	-	-	-	-	11
Asset-backed term notes	8	-	2	-	-	-	(3)	7
Mortgage bonds	981	-	(23)	-	-	-	(55)	903
Equity securities	97	(1)	8	-	-	130	(37)	197
Total financial assets at fair value through profit or loss	1,153	(1)	(11)	-	-	130	(95)	1,176
Available-for-sale financial assets								
Securities								
Other securities								
Other issuers								
Mortgage bonds	101	-	-	(3)	-	-	(2)	96
Equity securities	130	-	2	19	-	116	(4)	263
Total available-for-sale financial assets	231	-	2	16	-	116	(6)	359
Financial instruments of segregated funds	20	-	2	-	(4)	13	(3)	28
Total financial assets	$ 1,404	$ (1)	$ (7)	$ 16	$ (4)	$ 259	$ (104)	$ 1,563
Financial liabilities								
Financial liabilities held for trading								
Other liabilities – Other								
Financial liability related to put options	$ 68	$ -	$ 6	$ -	$ -	$ -	$ (12)	$ 62
Financial liability related to the contingent consideration	364	-	131	-	-	-	(266)	229
Total financial liabilities	$ 432	$ -	$ 137	$ -	$ -	$ -	$ (278)	$ 291

(1) Realized gains or losses on financial assets held for trading and designated as at fair value through profit or loss are presented under "Net investment income (loss)".
(2) Unrealized gains or losses on financial assets held for trading and designated as at fair value through profit or loss are presented under "Net investment income (loss)".
(3) Unrealized gains or losses on available-for-sale financial assets are recognized under "Net unrealized gains (losses)" on available-for-sale securities in the Consolidated Statements of Comprehensive Income.

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES

The information presented in the following tables has been prepared in accordance with IFRS 9 as at September 30, 2018 and in accordance with IAS 39 as at December 31, 2017. For more information, see Note 2, "Basis of presentation and significant accounting policies".

EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS

At each reporting date, loans and off-balance sheet items are classified based on their credit quality using their 12-month PD adjusted to take into consideration relevant forward-looking information over their lifetime. This is the PD used to determine whether credit risk has significantly increased since initial recognition or identify financial instruments in regulatory default.

The following tables present PD tranches in relation with risk levels for loans and off-balance sheet items.

Residential mortgages, consumer, credit card and other personal loans

Risk levels	PD tranches
Excellent	0.00% to 0.08%
Very low	0.09% to 0.33%
Low	0.34% to 2.09%
Moderate	2.10% to 7.32%
High	7.33% to 99.99%
Default	100.00%

Business and government

Risk levels	PD tranches
Investment grade	0.00% to 0.36%
Non-investment grade	0.37% to 4.50%
Under watch	4.51% to 99.99%
Default	100.00%

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS *(continued)*

The following tables present the gross carrying amount of loans and the exposure amount for off-balance sheet items for which the Federation estimates a loss allowance for expected credit losses, according to credit quality and the impairment model stage in which they are classified.

Loans

	Non-credit impaired		Credit-impaired	
As at September 30, 2018	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Residential mortgages				
Excellent	$ 1,124	$ -	$ -	$ 1,124
Very low	1,690	-	-	1,690
Low	1,492	9	-	1,501
Moderate	96	65	-	161
High	2	22	-	24
Default	-	8	9	17
Total gross residential mortgages	$ 4,404	$ 104	$ 9	$ 4,517
Allowance for credit losses	(4)	(1)	-	(5)
Total net residential mortgages	$ 4,400	$ 103	$ 9	$ 4,512
Consumer, credit card and other personal loans				
Excellent	$ 1,779	$ -	$ -	$ 1,779
Very low	4,009	-	-	4,009
Low	4,584	49	-	4,633
Moderate	6,000	1,229	-	7,229
High	30	1,418	-	1,448
Default	-	-	195	195
Total gross consumer, credit card and other personal loans	$ 16,402	$ 2,696	$ 195	$ 19,293
Allowance for credit losses	(100)	(285)	(96)	(481)
Total net consumer, credit card and other personal loans	$ 16,302	$ 2,411	$ 99	$ 18,812
Business and government loans(1)				
Investment grade	$ 34,801	$ -	$ -	$ 34,801
Non-investment grade	2,947	742	-	3,689
Under watch	35	126	-	161
Default	-	-	18	18
Total gross business and government loans	$ 37,783	$ 868	$ 18	$ 38,669
Allowance for credit losses	(8)	(8)	(5)	(21)
Total net business and government loans	$ 37,775	$ 860	$ 13	$ 38,648

(1) Including clients' liability under acceptances

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

EXPOSURE TO CREDIT RISK OF LOANS AND OFF-BALANCE SHEET ITEMS *(continued)*

Off-balance sheet items

	Non-credit impaired		Credit-impaired	
As at September 30, 2018	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Residential mortgages, consumer, credit card and other personal loans				
Excellent	$ 14,281	$ 1	$ -	$ 14,282
Very low	17,775	5	-	17,780
Low	3,532	97	-	3,629
Moderate	4,474	1,352	-	5,826
High	8	592	-	600
Default	-	-	20	20
Total gross off-balance sheet items	$ 40,070	$ 2,047	$ 20	$ 42,137
Allowance for credit losses	(21)	(15)	-	(36)
Total net off-balance sheet items	$ 40,049	$ 2,032	$ 20	$ 42,101
Business and government				
Investment grade	$ 60,767	$ -	$ -	$ 60,767
Non-investment grade	3,192	1,046	-	4,238
Under watch	15	21	-	36
Default	-	-	1	1
Total gross off-balance sheet items	$ 63,974	$ 1,067	$ 1	$ 65,042
Allowance for credit losses	-	-	-	-
Total net off-balance sheet items	$ 63,974	$ 1,067	$ 1	$ 65,042

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

ALLOWANCE FOR CREDIT LOSSES

The following table presents the changes in the balance of the allowance for expected credit losses on loans.

For the nine-month period ended September 30, 2018	Non-credit impaired Stage 1	Non-credit impaired Stage 2	Credit-impaired Stage 3	Allowance for credit losses
Residential mortgages				
Balance as at January 1, 2018	**$ 4**	**$ 1**	**$ 4**	**$ 9**
Provision for credit losses				
Transfers to[1]:				
Stage 1	**-**	**-**	**-**	**-**
Stage 2	**-**	**-**	**-**	**-**
Stage 3	**-**	**-**	**-**	**-**
Net remeasurement due to transfers[2]	**-**	**-**	**-**	**-**
Changes in model inputs[3]	**-**	**-**	**(4)**	**(4)**
New originations or acquisitions[4]	**-**	**-**	**-**	**-**
Derecognition and maturities[5]	**-**	**-**	**-**	**-**
Net drawdowns (repayments)[6]	**-**	**-**	**-**	**-**
	-	**-**	**(4)**	**(4)**
Write-offs and recoveries	**-**	**-**	**-**	**-**
Balance as at September 30, 2018	**$ 4**	**$ 1**	**$ -**	**$ 5**
Consumer, credit card and other personal loans				
Balance as at January 1, 2018	**$ 96**	**$ 304**	**$ 94**	**$ 494**
Provision for credit losses				
Transfers to[1]:				
Stage 1	**211**	**(201)**	**(10)**	**-**
Stage 2	**(32)**	**56**	**(24)**	**-**
Stage 3	**(1)**	**(25)**	**26**	**-**
Net remeasurement due to transfers[2]	**(103)**	**51**	**90**	**38**
Changes in model inputs[3]	**(68)**	**138**	**205**	**275**
New originations or acquisitions[4]	**62**	**131**	**-**	**193**
Derecognition and maturities[5]	**(26)**	**(141)**	**(120)**	**(287)**
Net drawdowns (repayments)[6]	**(18)**	**(13)**	**42**	**11**
	25	**(4)**	**209**	**230**
Write-offs and recoveries	**-**	**-**	**(207)**	**(207)**
Balance as at September 30, 2018	**$ 121**	**$ 300**	**$ 96**	**$ 517**
Business and government				
Balance as at January 1, 2018	**$ 7**	**$ 9**	**$ 8**	**$ 24**
Provision for credit losses				
Transfers to[1]:				
Stage 1	**6**	**(5)**	**(1)**	**-**
Stage 2	**(1)**	**2**	**(1)**	**-**
Stage 3	**-**	**-**	**-**	**-**
Net remeasurement due to transfers[2]	**(3)**	**1**	**2**	**-**
Changes in model inputs[3]	**(2)**	**2**	**1**	**1**
New originations or acquisitions[4]	**3**	**-**	**-**	**3**
Derecognition and maturities[5]	**(2)**	**-**	**(2)**	**(4)**
Net drawdowns (repayments)[6]	**-**	**(1)**	**(1)**	**(2)**
	1	**(1)**	**(2)**	**(2)**
Write-offs and recoveries	**-**	**-**	**(1)**	**(1)**
Balance as at September 30, 2018	**$ 8**	**$ 8**	**$ 5**	**$ 21**
Total balances as at September 30, 2018	**$ 133**	**$ 309**	**$ 101**	**$ 543**
Composed of:				
Loans	**$ 112**	**$ 294**	**$ 101**	**$ 507**
Off-balance sheet items[7]	**21**	**15**	**-**	**36**

[1] Represents transfers between stages before the remeasurement of expected credit losses.
[2] Represents the remeasurement of the loss allowance for expected credit losses resulting from transfers between stages.
[3] Represents the change in the allowance resulting from changes in credit risk parameters and other model inputs.
[4] Represents the increase in the allowance for new drawdowns or acquisitions during the period, including loans that were derecognized and for which a new asset was recognized following a modification of terms.
[5] Represents mainly the decrease in the allowance for fully repaid loans, including loans that were derecognized and for which a new asset was recognized following a modification of terms.
[6] Represents changes in the allowance attributable to drawdowns and repayments on outstanding loans.
[7] The allowance for credit losses on off-balance sheet items is presented under "Other liabilities – Other" in the Consolidated Balance Sheets.

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

KEY DATA AND ASSUMPTIONS

Determining the loss allowance for expected credit losses is based on a set of assumptions and methodologies specific to credit risk and changes in economic conditions. Significant judgment must therefore be exercised to determine the loss allowance for expected credit losses. The main items affecting its measurement as at September 30, 2018 are the following:

- Changes in the borrowers' credit risk rating (or probability of default).
- Incorporation of forward-looking information.
- Estimated life of revolving exposures.

Changes in the borrowers' credit risk rating or probability of default

The borrowers' credit risk rating is the foundation of the credit risk assessment model. The rating of a borrower is directly related to its estimated PD. Many variables are taken into consideration in credit risk assessment models. For more information about these models, see section 4.2, "Risk management", of the 2017 Annual Management's Discussion and Analysis. Changes in the borrowers' credit risk rating have an impact on determining significant increases in credit risk (as this is mainly based on the change in the borrower's PD) and measuring the loss allowance for expected credit losses.

Changes in the borrowers' credit risk rating may increase or decrease the loss allowance for expected credit losses. Generally, a deterioration in a borrower's credit risk rating gives rise to an increase in the loss allowance for expected credit losses, while an improvement in a borrower's credit risk rating results in a decrease in the loss allowance for expected credit losses.

Incorporation of forward-looking information

The Federation uses three different scenarios to determine the loss allowances for expected credit losses, namely a base scenario, an upside scenario and a downside scenario. Projections for each scenario are provided for a four-year horizon. The macroeconomic variables projected under each scenario and the related probability of occurrence have a significant impact on determining significant increases in credit risk and measuring the loss allowance for expected credit losses. The main variables used are gross domestic product, unemployment rate, the Consumer Price Index, housing prices and the corporate financing spread. The macroeconomic variable projection and the determination of the probabilities of occurrence are reviewed quarterly.

The incorporation of forward-looking information may increase or decrease the loss allowance for expected credit losses. Generally, an improvement in the outlook will give rise to a decrease in the loss allowance for expected credit losses, while a deterioration in the outlook will result in an increase in the loss allowance for expected credit losses.

Estimated life of revolving exposures

To determine the life of revolving exposures, the Federation determines the period over which there is exposure to credit risk but for which expected credit losses would not be mitigated by normal credit risk management actions, which considers the following:

- The period over which the Federation was exposed to credit risk on similar financial instruments.
- The length of time for related defaults to occur on similar financial instruments following a significant increase in credit risk.
- The credit risk management action that it expects to take once the credit risk on the financial instruments has increased.

The determination of the estimated life of revolving exposures has a significant impact on estimating the loss allowance for expected credit losses, mainly for revolving exposures in Stage 2 of the impairment model. Generally, an increase in the estimated life of revolving exposures gives rise to an increase in expected credit losses.

The comparative information presented in the following tables have been prepared in accordance with IAS 39.

NOTE 5 – LOANS AND ALLOWANCE FOR CREDIT LOSSES *(continued)*

LOANS, CREDIT-IMPAIRED LOANS[1] AND ALLOWANCE FOR CREDIT LOSSES

The following table presents the credit quality of loans.

As at December 31, 2017	Gross loans neither past due nor credit-impaired	Gross loans past due but not credit-impaired	Gross credit-impaired loans	Individual allowances	Collective allowance[2]	Net loans
Residential mortgages	$ 4,260	$ 55	$ 8	$ 5	$ 2	$ 4,316
Consumer, credit card and other personal loans	16,764	711	72	-	136	17,411
Business and government	36,986	22	4	4	51	36,957
	$ 58,010	$ 788	$ 84	$ 9	$ 189	$ 58,684

[1] Following the adoption of IFRS 9 as at January 1, 2018, all loans included in Stage 3 of the impairment model are considered credit-impaired. Under IAS 39, the criteria applied to determine whether a loan is credit-impaired were different.
[2] Includes the collective allowance on impaired loans of $23 million.

GROSS LOANS PAST DUE BUT NOT CREDIT-IMPAIRED

The following table presents the aging of gross loans that are past due but not credit-impaired.

As at December 31, 2017	1 to 29 days	30 to 59 days	60 to 89 days	90 days or more	Total
Residential mortgages	$ 43	$ 4	$ -	$ 8	$ 55
Consumer, credit card and other personal loans	559	104	48	-	711
Business and government	21	1	-	-	22
	$ 623	$ 109	$ 48	$ 8	$ 788

ALLOWANCE FOR CREDIT LOSSES

The following table presents the changes in the allowance for credit losses.

For the nine-month period ended September 30, 2017	Residential mortgages	Consumer, credit card and other personal loans	Business and government	Total
Balance at beginning of period	$ 3	$ 148	$ 87	$ 238
Provision for credit losses	-	210	(6)	204
Write-offs and recoveries	-	(210)	-	(210)
Balance at end of period	$ 3	$ 148	$ 81	$ 232
Composed of:				
Allowance for credit losses	$ 3	$ 134	$ 56	$ 193
Allowance on off-balance sheet items[1]	-	14	25	39

[1] The allowance on off-balance sheet items is presented under “Other liabilities – Other”.

NOTE 6 – INTERESTS IN OTHER ENTITIES

COVERED BONDS

Under its covered bond program, the Federation issues debt securities guaranteed by a pool of mortgage loans. A structured entity is in place to guarantee principal and interest payments owing to the holders of the covered bonds issued by the Federation. This entity is controlled by the Federation, and therefore included in its Consolidated Financial Statements. The Federation granted financing to the entity in order to facilitate the acquisition of these assets. The financing granted by the Federation may reach a maximum amount equal to the outstanding loans held by the structured entity for the purpose of guaranteeing the covered bonds issues. Under the terms and conditions of each of the issuance agreements, the Federation has limited access to the assets that are legally owned by the entity. These assets do not meet the recognition criteria neither for the structured entity nor for the Federation, and are therefore not recognized in their respective balance sheets. The covered bonds, amounting to $5,617 million as at September 30, 2018 ($4,517 million as at December 31, 2017), are presented under "Deposits – Business and government" in the Consolidated Balance Sheets.

NOTE 7 – DEPOSITS

Deposits consist of demand deposits (payable on demand), notice deposits (payable upon notice) and term deposits (payable on a fixed date). Demand deposits are interest-bearing or non-interest-bearing deposits, primarily accounts with chequing privileges, for which the Federation does not have the right to require notice prior to withdrawal. Notice deposits are interest-bearing deposits, primarily savings accounts, for which the Federation has the legal right to require notice prior to withdrawal. Term deposits are interest-bearing deposits, primarily fixed-term deposit accounts, guaranteed investment certificates or other similar instruments, with a term that generally varies from 1 day to 10 years and mature on a predetermined date.

The following table presents the breakdown of deposits.

	As at September 30, 2018				As at December 31, 2017			
	Payable on demand	**Payable upon notice**	**Payable on a fixed date**	**Total**	Payable on demand	Payable upon notice	Payable on a fixed date	Total
Individuals	**$ 2,967**	**$ 51**	**$ 1,176**	**$ 4,194**	$ 3,154	$ 50	$ 1,149	$ 4,353
Business and government	**2,944**	**-**	**42,482**	**45,426**	3,452	-	37,511	40,963
Deposit-taking institutions	**4,116**	**-**	**4,062**	**8,178**	2,757	-	4,076	6,833
	$ 10,027	**$ 51**	**$ 47,720**	**$ 57,798**	$ 9,363	$ 50	$ 42,736	$ 52,149

NOTE 8 – SIGNIFICANT TRANSACTIONS

On April 1, 2018, the Federation and a partnership comprised of five provincial credit union centrals (the Centrals) and The CUMIS Group completed an agreement to merge their investments in Credential Financial Inc., Qtrade Canada Inc. and Northwest & Ethical Investments LP. This transaction resulted in the creation of Aviso Wealth, a wealth management company, in which the Federation and the partnership formed by the Centrals and The CUMIS Group each hold a 50% interest.

The Federation's interest in Aviso Wealth, amounting to $332 million as at April 1, 2018, is an interest in a joint venture and is accounted for using the equity method in the Wealth Management and Life and Health Insurance segment.

The assets and liabilities transferred by the Federation at the time Aviso Wealth was created were as follows:

	As at April 1st, 2018
Assets disposed of	
Cash and deposits with financial institutions	**$ 14**
Securities at fair value through profit or loss	**82**
Amounts receivable from clients, brokers and financial institutions	**630**
Property, plant and equipment	**2**
Goodwill	**32**
Intangible assets	**61**
Deferred tax assets	**1**
Other assets	**96**
Total assets disposed of	**$ 918**
Liabilities disposed of	
Deferred tax liabilities	**$ 14**
Amounts payable to clients, brokers and financial institutions	**682**
Other liabilities	**22**
Total liabilities disposed of	**$ 718**

A gain of $132 million on this transaction was recognized under "Other income – Other" in the Consolidated Statement of Income for the nine-month period ended September 30, 2018.

The operations of the Qtrade Canada Inc. subsidiary and the interest in the Northwest & Ethical Investments LP associate were presented in the Wealth Management and Life and Health Insurance segment.

NOTE 9 – CAPITAL STOCK

ISSUANCE OF SHARES

During the nine-month period ended September 30, 2018, the Federation issued 12,433,692 F capital shares for a cash consideration of $124 million, which represents the gross proceeds of this issuance of $125 million less issue costs of $1 million. In addition, the Federation issued 14,208,755 F capital shares having a value of $142 million as interest payments when the holders elected to receive their remuneration in F capital shares.

REDEMPTION OF SHARES

During the nine-month period ended September 30, 2018, the Federation redeemed for cancellation all FED-7 capital shares for a cash consideration of $5 million.

NOTE 10 – ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table presents the main components of “Accumulated other comprehensive income” (net of taxes).

	As at September 30, 2018		As at December 31, 2017	
	Group's share	**Non-controlling interests' share**	Group's share	Non-controlling interests' share
Items that will be reclassified subsequently to the Consolidated Statements of Income				
Net unrealized gains on available-for-sale securities	**N/A**	**N/A**	$ 446	$ 21
Net unrealized losses on debt securities classified as at fair value through other comprehensive income[(1)]	**$ (35)**	**$ (2)**	N/A	N/A
Net unrealized gains related to the overlay approach for insurance operations financial assets	**174**	**10**	N/A	N/A
Net gains (losses) on derivative financial instruments designated as cash flow hedges	**(11)**	**-**	11	-
Net unrealized exchange gains on the translation of a net investment in a foreign operation, net of hedging transactions	**2**	**-**	1	-
Accumulated other comprehensive income	**$ 130**	**$ 8**	$ 458	$ 21

(1) Including an allowance for credit losses of $2 million on securities classified as at fair value through other comprehensive income.

NOTE 11 – CAPITAL MANAGEMENT

Capital management is a function covering all Desjardins Group operations, including those of the Federation. Accordingly, the description of the Federation's capital management and the manner in which it meets its capital management objectives are derived from the orientation followed for all Desjardins Group operations. The goal of capital management at Desjardins Group is to ensure that a sufficient level of high-quality capital is maintained for the following reasons: to have flexibility for its development, to maintain favourable credit ratings and to maintain the confidence of depositors and financial markets.

Since January 1, 2017, the Federation's capital ratios are calculated according to the guideline on adequacy of capital base standards applicable to financial services cooperatives (the guideline) issued by the AMF.

The minimum Tier 1A capital ratio that the Federation must maintain is 8.0%. In addition, its Tier 1 capital ratio and total capital ratio must be above 9.5% and 11.5%, respectively. For the leverage ratio, the minimum requirement is 3.0%.

As mentioned in Note 9, "Capital stock", the Federation issued F capital shares in 2018 for gross proceeds of $267 million, including $142 million as interest payments to holders who elected to receive their remuneration in capital shares.

As at September 30, 2018, the Federation was in compliance with the AMF's capital ratio and leverage ratio regulatory requirements.

The following table presents the Federation's regulatory capital balances, risk-weighted assets and capital ratios.

(in millions of dollars and as a percentage)	As at September 30, 2018	As at December 31, 2017
Capital		
Tier 1A capital	**$ 10,238**	$ 9,162
Tier 1 capital	**10,238**	9,162
Total capital	**10,238**	9,162
Risk-weighted assets for capital ratio calculation purposes(1)		
For Tier 1A capital	**60,261**	52,364
For Tier 1 capital	**60,293**	52,409
For total capital	**60,325**	52,445
Risk-weighted assets for total capital calculation purposes(1)		
Credit risk	**46,674**	42,336
Market risk	**5,074**	1,965
Operational risk	**8,577**	8,143
Total risk-weighted assets	**$ 60,325**	$ 52,444
Ratios and leverage ratio exposure		
Tier 1A capital	**17.0%**	17.5%
Tier 1 capital	**17.0**	17.5
Total capital	**17.0**	17.5
Leverage	**7.7**	7.9
Leverage ratio exposure	**$ 132,507**	$ 115,915

(1) Takes into account the requirements of the CVA charge that have been phased in since January 1, 2014 to calculate the Tier 1A, Tier 1 and total capital ratios, which are 80%, 83% and 86%, respectively. They will reach 100% for each category by 2019.

NOTE 12 – NET INTEREST INCOME AND NET INVESTMENT INCOME (LOSS)

The information presented in the following tables has been prepared in accordance with IFRS 9 for the three-month and nine-month periods ended September 30, 2018 and in accordance with IAS 39 for the three-month and nine-month periods ended September 30, 2017. For more information, see Note 2, "Basis of presentation and significant accounting policies".

NET INTEREST INCOME

The following table presents the breakdown of net interest income according to the classification of financial assets and liabilities.

2018	**For the three-month period ended September 30**	**For the nine-month period ended September 30**
Interest income on financial assets		
At amortized cost	**$ 688**	**$ 1,892**
At fair value through other comprehensive income	**43**	**122**
At fair value through profit or loss	**9**	**27**
	740	**2,041**
Interest expense on financial liabilities at amortized cost	**358**	**938**
	$ 382	**$ 1,103**

NET INVESTMENT INCOME (LOSS)

The following table presents the breakdown of investment income and loss according to the classification of financial assets and liabilities.

2018	**For the three-month period ended September 30**			**For the nine-month period ended September 30**		
	Interest income and expense	**Fair value gains (losses) and other**	**Total**	**Interest income and expense**	**Fair value gains (losses) and other**	**Total**
Net investment income (loss) on financial assets and liabilities						
Classified as at fair value through profit or loss	**$ 158**	**$ (122)**	**$ 36**	**$ 292**	**$ (179)**	**$ 113**
Designated as at fair value through profit or loss	**129**	**(447)**	**(318)**	**374**	**(559)**	**(185)**
Classified as at fair value through other comprehensive income	**35**	**(14)**	**21**	**101**	**(17)**	**84**
At amortized cost and other	**37**	**11**	**48**	**110**	**90**	**200**
	$ 359	**$ (572)**	**$ (213)**	**$ 877**	**$ (665)**	**$ 212**

The comparative information presented in the following tables have been prepared in accordance with IAS 39.

FINANCIAL INSTRUMENTS HELD FOR TRADING

The following table presents the impact of income from financial instruments held for trading on the Consolidated Statements of Income.

2017	For the three-month period ended September 30	For the nine-month period ended September 30
Income		
Net interest income	$ 9	$ 30
Net investment income (loss)	17	24
	$ 26	$ 54

FINANCIAL INSTRUMENTS DESIGNATED AS AT FAIR VALUE THROUGH PROFIT OR LOSS

The following table presents the impact of income from financial instruments designated as at fair value through profit or loss on the Consolidated Statements of Income.

2017	For the three-month period ended September 30	For the nine-month period ended September 30
Income		
Net interest income	$ 4	$ 10
Net investment income (loss)	(457)	328
	$ (453)	$ 338

Net income on available-for-sale securities of $66 million for the three-month period ended September 30, 2017 and $325 million for the nine-month period ended September 30, 2017 are included in profit or loss under "Net investment income (loss)" in the Consolidated Statements of Income.

NOTE 13 – SEGMENTED INFORMATION

RESULTS BY BUSINESS SEGMENT

The following tables provide a summary of the Federation’s financial results by business segment.

	Personal and Business Services		Wealth Management and Life and Health Insurance		Property and Casualty Insurance		Treasury and Other Support to Desjardins Group Entities		Consolidated	
For the three-month periods ended September 30	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017
Net interest income	**$ 286**	$ 278	**$ 1**	$ 1	**$ -**	$ -	**$ 95**	$ 85	**$ 382**	$ 364
Net premiums	**-**	-	**1,209**	1,078	**1,120**	967	**(41)**	(38)	**2,288**	2,007
Other income	**411**	388	**157**	(17)	**45**	239	**135**	204	**748**	814
Total income	**697**	666	**1,367**	1,062	**1,165**	1,206	**189**	251	**3,418**	3,185
Provision for credit losses	**74**	72	**(1)**	-	**-**	-	**-**	-	**73**	72
Claims, benefits, annuities and changes in insurance contract liabilities	**-**	-	**573**	357	**803**	643	**4**	-	**1,380**	1,000
Non-interest expense	**522**	477	**572**	564	**271**	205	**233**	187	**1,598**	1,433
Operating surplus earnings	**101**	117	**223**	141	**91**	358	**(48)**	64	**367**	680
Income taxes on surplus earnings	**29**	31	**49**	20	**21**	40	**(31)**	(2)	**68**	89
Net surplus earnings for the period after dividends to member caisses	**$ 72**	$ 86	**$ 174**	$ 121	**$ 70**	$ 318	**$ (17)**	$ 66	**$ 299**	$ 591
of which:										
Group’s share	**$ 72**	$ 86	**$ 174**	$ 121	**$ 57**	$ 303	**$ (17)**	$ 66	**$ 286**	$ 576
Non-controlling interests’ share	**-**	-	**-**	-	**13**	15	**-**	-	**13**	15

	Personal and Business Services		Wealth Management and Life and Health Insurance		Property and Casualty Insurance		Treasury and Other Support to Desjardins Group Entities		Consolidated	
For the nine-month periods ended September 30	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017
Net interest income	**$ 835**	$ 808	**$ 3**	$ 1	**$ -**	$ 1	**$ 265**	$ 237	**$ 1,103**	$ 1,047
Net premiums	**-**	-	**3,542**	3,318	**3,252**	2,913	**(117)**	(119)	**6,677**	6,112
Other income	**1,294**	1,203	**1,496**	1,680	**111**	365	**425**	551	**3,326**	3,799
Total income	**2,129**	2,011	**5,041**	4,999	**3,363**	3,279	**573**	669	**11,106**	10,958
Provision for credit losses	**230**	204	**(5)**	-	**-**	-	**-**	-	**225**	204
Claims, benefits, annuities and changes in insurance contract liabilities	**-**	-	**2,407**	2,720	**2,352**	1,956	**4**	(1)	**4,763**	4,675
Non-interest expense	**1,561**	1,460	**1,772**	1,721	**828**	850	**633**	557	**4,794**	4,588
Operating surplus earnings	**338**	347	**867**	558	**183**	473	**(64)**	113	**1,324**	1,491
Income taxes on surplus earnings	**89**	92	**156**	105	**35**	75	**(78)**	(16)	**202**	256
Net surplus earnings for the period after dividends to member caisses	**$ 249**	$ 255	**$ 711**	$ 453	**$ 148**	$ 398	**$ 14**	$ 129	**$ 1,122**	$ 1,235
of which:										
Group's share	**$ 249**	$ 255	**$ 711**	$ 452	**$ 115**	$ 365	**$ 14**	$ 129	**$ 1,089**	$ 1,201
Non-controlling interests' share	**-**	-	**-**	1	**33**	33	**-**	-	**33**	34

SEGMENT ASSETS

	Personal and Business Services	Wealth Management and Life and Health Insurance	Property and Casualty Insurance	Treasury and Other Support to Desjardins Group Entities	Consolidated
As at September 30, 2018	**$ 58,886**	**$ 43,621**	**$ 13,042**	**$ 44,696**	**$ 160,245**
As at December 31, 2017	$ 51,696	$ 42,005	$ 13,138	$ 38,901	$ 145,740

GENERAL INFORMATION

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