VersaBank

Interim Consolidated Financial Statements
January 31, 2020
(Unaudited)

VERSABANK

Consolidated Balance Sheets
(Unaudited)

(thousands of Canadian dollars)

As at	January 31 2020	October 31 2019	January 31 2019
Assets			
Cash	$ 134,253	$ 139,145	$ 95,203
Securities	-	10,061	9,990
Loans, net of allowance for credit losses (note 4)	1,668,720	1,594,288	1,603,185
Other assets (note 5)	51,792	41,887	37,900
	$ 1,854,765	$ 1,785,381	$ 1,746,278
Liabilities and Shareholders' Equity			
Deposits	$ 1,454,979	$ 1,399,889	$ 1,371,123
Subordinated notes payable (note 6 and 13)	4,883	4,881	9,859
Securitization liabilities (note 7)	33,388	33,366	33,490
Other liabilities (note 8)	117,281	107,082	104,096
	1,610,531	1,545,218	1,518,568
Shareholders' equity:			
Share capital (note 9)	182,094	182,094	182,094
Retained earnings	62,140	58,069	45,616
	244,234	240,163	227,710
	$ 1,854,765	$ 1,785,381	$ 1,746,278

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

VERSABANK

Consolidated Statements of Comprehensive Income

(Unaudited)

(thousands of Canadian dollars, except per share amounts)

	for the three months ended	
	January 31 2020	January 31 2019
Interest income:		
Loans	$ 21,274	$ 21,130
Securities	892	829
	22,166	21,959
Interest expense:		
Deposits and other	8,482	8,302
Subordinated notes	127	217
	8,609	8,519
Net interest income	13,557	13,440
Non-interest income	25	19
Total revenue	13,582	13,459
Provision (recovery) for credit losses (note 4)	(208)	(289)
	13,790	13,748
Non-interest expenses:		
Salaries and benefits	3,939	3,905
General and administrative	2,171	2,402
Premises and equipment	595	647
	6,705	6,954
Income before income taxes	7,085	6,794
Tax provision (note 10)	1,944	1,862
Net income and comprehensive income	$ 5,141	$ 4,932
Basic and diluted income per common share (note 11)	$ 0.22	$ 0.21
Weighted average number of common shares outstanding	21,123,559	21,123,559

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

VERSABANK

Consolidated Statements of Changes in Shareholders' Equity
(Unaudited)

(thousands of Canadian dollars)	for the three months ended January 31 2020	January 31 2019
Common shares (note 9):		
Balance, beginning and end of the period	$ 152,612	$ 152,612
Preferred shares (note 9):		
Series 1 preferred shares		
Balance, beginning and end of the period	$ 13,647	$ 13,647
Series 3 preferred shares		
Balance, beginning and end of the period	$ 15,690	$ 15,690
Contributed surplus:		
Balance, beginning and end of the period	$ 145	$ 145
Total share capital	$ 182,094	$ 182,094
Retained earnings:		
Balance, beginning of the period	$ 58,069	$ 41,473
Impact of adopting IFRS 9	-	78
Net income	5,141	4,932
Dividends paid on common and preferred shares	(1,070)	(867)
Balance, end of the period	$ 62,140	$ 45,616
Total shareholders' equity	$ 244,234	$ 227,710

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

VERSABANK

Consolidated Statements of Cash Flows

(Unaudited)

(thousands of Canadian dollars)	for the three months ended	
	January 31 2020	January 31 2019
Cash provided by (used in):		
Operations:		
Net income	$ 5,141	$ 4,932
Adjustments to determine net cash flows:		
Items not involving cash:		
Provision (recovery) for credit losses	(208)	(289)
Income tax provision	1,944	1,862
Interest income	(22,166)	(21,959)
Interest expense	8,609	8,519
Amortization	286	180
Interest received	21,346	26,539
Interest paid	(10,691)	(10,982)
Change in operating assets and liabilities:		
Loans	(73,336)	23,658
Deposits	57,164	(63,607)
Change in other assets and liabilities	(1,224)	(2,104)
	(13,135)	(33,251)
Investing:		
Proceeds from sale and maturity of securities	10,000	-
Purchase of property and equipment	(36)	(158)
	9,964	(158)
Financing:		
Dividends paid	(1,070)	(867)
Repayment of lease obligations	(90)	-
Income taxes paid	(561)	(302)
	(1,721)	(1,169)
Change in cash	(4,892)	(34,578)
Cash, beginning of the period	139,145	129,781
Cash, end of the period	$ 134,253	$ 95,203

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

1. Reporting entity:

VersaBank (the "Bank") operates as a Schedule I bank under the *Bank Act (Canada)* and is regulated by the Office of the Superintendent of Financial Institutions ("OSFI"). The Bank, whose shares trade on the Toronto Stock Exchange, provides commercial lending services to select niche markets in Canada.

The Bank is incorporated and domiciled in Canada, and maintains its registered office at Suite 2002, 140 Fullarton Street, London, Ontario, Canada, N6A 5P2.

2. Basis of preparation:

a) Statement of compliance:

These interim Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board (IASB) and have been prepared in accordance with International Accounting Standard ("IAS") 34 – *Interim Financial Reporting* and do not include all of the information required for full annual financial statements. These interim Consolidated Financial Statements should be read in conjunction with the Bank's audited Consolidated Financial Statements for the year ended October 31, 2019.

The interim Consolidated Financial Statements for the three months ended January 31, 2020 and 2019 were approved by the Audit Committee of the Board of Directors on February 24, 2020.

b) Basis of measurement:

These interim Consolidated Financial Statements have been prepared on the historical cost basis except for securities that are designated as fair value through other comprehensive income which are measured at fair value in the Consolidated Balance Sheets.

c) Functional and presentation currency:

These interim Consolidated Financial Statements are presented in Canadian dollars which is the Bank's functional currency.

d) Use of estimates and judgments:

In preparing these interim Consolidated Financial Statements, management has exercised judgment and developed estimates in applying accounting policies and generating reported amounts of assets and liabilities at the date of the financial statements and income and expenses during the reporting periods. Areas where significant judgement was applied include the business model applied for the classification and measurement of financial instruments, assessing significant changes in credit risk on financial assets and in the selection of relevant forward looking information in assessing the Bank's allowance for losses on its financial assets. Estimates are applied in the determination of the allowance for losses on financial assets and the measurement of deferred income taxes. It is reasonably possible, on the basis of existing knowledge, that actual results may vary from that expected in the generation of these estimates. This could result in material adjustments to the carrying amounts of assets and/or liabilities affected in the future.

Estimates and their underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are applied prospectively once they are recognized.

3. Significant accounting policies and future accounting changes:

The accounting policies applied by the Bank in these interim Consolidated Financial Statements are the same as those applied by the Bank as at and for the year ended October 31, 2019 and are detailed in Note 3 of the Bank's 2019 audited Consolidated Financial Statements, except for changes to accounting policies resulting from the adoption of IFRS 16 (*Leases*) noted below.

There have been a number of standards and amendments that have been issued by the IASB that are not effective for the Bank's fiscal year end of October 31, 2020 and therefore have not been applied in preparing these interim consolidated financial statements.

Leases (IFRS 16)

Effective November 1, 2019, the Bank adopted IFRS 16, which sets out prescribed methodology related to the recognition, measurement, presentation and disclosure of operational leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all major leases. IFRS 16 supersedes previous accounting standards for leases, including IAS 17, *Leases* and IFRIC 4 – *Determining whether an arrangement contains a lease.* As a result of adopting IFRS 16, the Bank recognized an increase to both assets and liabilities on the Consolidated Balance Sheet, as well as a decrease in rent expense, with a corresponding increase in amortization expense (due to depreciation of the right-of-use assets) and an increase in finance costs (due to accretion of the lease obligation).

The Bank's accounting policy under IFRS 16 is set out below:

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease arrangement based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Bank recognizes a right-of-use asset and a lease obligation at the lease commencement date. The right-of-use asset is initially measured based on the initial amount of the lease obligation adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset and/or the site on which it is located, less any lease incentives received. The assets are depreciated to the earlier of the end of useful life of the right-of-use asset or the lease term using the straight-line method as this methodology most closely reflects the expected pattern of consumption of the associated future economic benefits. The lease term includes periods covered by an option to extend if there is reasonable certainty that the Bank will exercise that option. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease obligation.

The lease obligation is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the incremental borrowing rate that is a function of the asset type or class and the credit quality of the borrower. Generally, the Bank will use its incremental borrowing rate as the discount rate. Variable lease payments that do not depend on an index or rate are not included in the measurement of the lease obligation.

The lease obligation is measured at amortized cost using the effective interest rate method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank’s estimate of the amount expected to be payable under a residual value guarantee, or if the Bank changes its assessment of whether it will exercise a purchase, extension or termination option.

When the lease obligation is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or the remeasured amount is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

Impact of adoption of IFRS 16

Effective November 1, 2019, the Bank adopted IFRS 16 using the modified retrospective approach and accordingly the information presented for Fiscal 2019 has not been restated. It remains as previously reported under IAS 17 and related interpretations.

Prior to the adoption of IFRS 16 the Bank’s total minimum operating lease commitments as at October 31, 2019 were $6.8 million. On initial application, the Bank has elected to record right-of-use assets based on the corresponding lease obligations. Right-of-use assets and lease obligations of $3.3 million were recorded as of November 1, 2019, with no net impact on retained earnings. When measuring its lease liabilities, the Bank discounted lease payments at its incremental borrowing rate, applicable to the asset class(es) at November 1, 2019. The weighted-average rate applied is 4.4%.

The Bank elected to apply the practical expedient to account for leases for which the lease term ends within 12 months of the date of initial application as short-term leases.

The following table reconciles the Bank’s operating lease commitments at October 31, 2019, as previously disclosed in the Bank’s 2019 audited Consolidated Financial Statements, to the lease obligations recognized on initial application of IFRS 16 at November 1, 2019:

(thousands of Canadian dollars)	
Operating lease commitments as at October 31, 2019	$ 6,808
Discounted using the incremental borrowing rate as at November 1, 2019	5,557
Non-lease components included within operating lease commitments	(2,268)
Recognition exemption for short term leases	(35)
Lease obligations recognized as at November 1, 2019	$ 3,254

4. Loans:

a) Summary of loans and allowance for credit losses:

(thousands of Canadian dollars)	January 31 2020	October 31 2019	January 31 2019
Commercial real estate	$ 526,375	$ 509,564	$ 568,331
Non-commercial real estate	38,099	44,608	60,328
Corporate and public sector	38,227	40,670	48,845
Structured finance	1,061,207	994,842	921,303
	1,663,908	1,589,684	1,598,807
Allowance for credit losses	(1,911)	(2,119)	(2,364)
Accrued interest	6,723	6,723	6,742
Total loans, net of allowance for credit losses	$ 1,668,720	$ 1,594,288	$ 1,603,185

The following table provides a summary of loan amounts, ECL allowance amounts, and expected loss ("EL") rates by lending asset category:

	As at January 31, 2020				As at January 31, 2019			
(thousands of Canadian dollars)	**Stage 1**	**Stage 2**	**Stage 3**	**Total**	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Commercial real estate	$ 467,145	$ 52,886	$ 6,344	**$ 526,375**	$ 501,370	$ 48,037	$ 18,924	**$ 568,331**
ECL allowance	1,286	236	-	**1,522**	1,187	269	-	**1,456**
EL %	0.28%	0.45%	0.00%	**0.29%**	0.24%	0.56%	-	**0.26%**
Non-commercial real estate	$ 38,099	$ -	$ -	**$ 38,099**	$ 60,328	$ -	$ -	**$ 60,328**
ECL allowance	82	-	-	**82**	133	-	-	**133**
EL %	0.22%	0.00%	0.00%	**0.22%**	0.22%	-	-	**0.22%**
Corporate and public sector	$ 38,227	$ -	$ -	**$ 38,227**	$ 48,218	$ -	$ 627	**$ 48,845**
ECL allowance	31	-	-	**31**	64	-	400	**464**
EL %	0.08%	0.00%	0.00%	**0.08%**	0.13%	-	63.80%	**0.95%**
Structured finance	$ 1,058,886	$ 2,231	$ 90	**$ 1,061,207**	$ 918,817	$ 2,486	$ -	**$ 921,303**
ECL allowance	276	-	-	**276**	310	1	-	**311**
EL %	0.03%	0.00%	0.00%	**0.03%**	0.03%	0.04%	0.00%	**0.03%**
Loans	$ 1,602,357	$ 55,117	$ 6,434	**$ 1,663,908**	$ 1,528,733	$ 50,523	$ 19,551	**$ 1,598,807**
Total ECL allowance	1,675	236	-	**1,911**	1,694	270	400	**2,364**
Total EL %	0.10%	0.43%	0.00%	**0.11%**	0.11%	0.53%	2.05%	**0.15%**

The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the three months ended January 31, 2020:

(thousands of Canadian dollars)	Stage 1	Stage 2	Stage 3	Total
Commercial real estate				
Balance at beginning of period	$ 1,557	$ 209	$ -	1,766
Transfer in (out) to Stage 1	5	(5)	-	-
Transfer in (out) to Stage 2	(13)	13	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(320)	19	-	(301)
Loan originations	66	-	-	66
Derecognitions and maturities	(9)	-	-	(9)
Provision for (recovery of) credit losses	(271)	27	-	(244)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 1,286**	**$ 236**	**$ -**	**1,522**
Non-commercial real estate				
Balance at beginning of period	$ 86	$ -	$ -	86
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(10)	-	-	(10)
Loan originations	8	-	-	8
Derecognitions and maturities	(2)	-	-	(2)
Provision for (recovery of) credit losses	(4)	-	-	(4)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 82**	**$ -**	**$ -**	**82**
Corporate and public sector				
Balance at beginning of period	$ 38	$ -	$ -	38
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(7)	-	-	(7)
Loan originations	-	-	-	-
Derecognitions and maturities	-	-	-	-
Provision for (recovery of) credit losses	(7)	-	-	(7)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 31**	**$ -**	**$ -**	**31**
Structured finance				
Balance at beginning of period	$ 229	$ -	$ -	229
Transfer in (out) to Stage 1	17	(17)	-	-
Transfer in (out) to Stage 2	(34)	34	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(2,585)	(7)	-	(2,592)
Loan originations	3,008	-	-	3,008
Derecognitions and maturities	(359)	(10)	-	(369)
Provision for (recovery of) credit losses	47	-	-	47
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 276**	**$ -**	**$ -**	**276**
Total balance at end of period	**$ 1,675**	**$ 236**	**$ -**	**1,911**

The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the three months ended January 31, 2019:

(thousands of Canadian dollars)	Stage 1	Stage 2	Stage 3	Total
Commercial real estate				
Balance at beginning of period	$ 1,257	$ 348	$ -	1,605
Transfer in (out) to Stage 1	(1)	1	-	-
Transfer in (out) to Stage 2	21	(101)	80	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(94)	22	(80)	(152)
Loan originations	59	-	-	59
Derecognitions and maturities	(55)	(1)	-	(56)
Provision for (recovery of) credit losses	(70)	(79)	-	(149)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 1,187**	**$ 269**	**$ -**	**1,456**
Non-commercial real estate				
Balance at beginning of period	$ 151	$ -	$ -	151
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(18)	-	-	(18)
Loan originations	-	-	-	-
Derecognitions and maturities	-	-	-	-
Provision for (recovery of) credit losses	(18)	-	-	(18)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 133**	**$ -**	**$ -**	**133**
Corporate and public sector				
Balance at beginning of period	$ 81	$ -	$ 400	481
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(19)	-	-	(19)
Loan originations	2	-	-	2
Derecognitions and maturities	-	-	-	-
Provision for (recovery of) credit losses	(17)	-	-	(17)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 64**	**$ -**	**$ 400**	**464**
Structured finance				
Balance at beginning of period	$ 415	$ 1	$ -	416
Transfer in (out) to Stage 1	(36)	36	-	-
Transfer in (out) to Stage 2	19	(19)	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(1,203)	(5)	-	(1,208)
Loan originations	1,469	-	-	1,469
Derecognitions and maturities	(354)	(12)	-	(366)
Provision for (recovery of) credit losses	(105)	-	-	(105)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	**$ 310**	**$ 1**	**$ -**	**311**
Total balance at end of period	**$ 1,694**	**$ 270**	**$ 400**	**2,364**

The Bank holds security against the majority of its loans in the form of either mortgage interests over property, other registered securities over assets, guarantees and holdbacks on loan and lease receivables (see note 8).

b) Impaired loans:

At January 31, 2020, impaired loans were $6.4 million (October 31, 2019 - $6.3 million).

5. Other assets:

(thousands of Canadian dollars)	January 31 2020	October 31 2019	January 31 2019
Accounts receivable	$ 1,443	$ 437	$ 555
Funds held for securitization liabilities	22,309	17,073	6,298
Prepaid expenses and other	7,226	4,840	5,951
Property and equipment	7,765	7,911	8,368
Right-of-use assets	3,150	-	-
Deferred income tax asset	9,899	11,626	16,728
	$ 51,792	$ 41,887	$ 37,900

6. Subordinated notes payable:

(thousands of Canadian dollars)	January 31 2020	October 31 2019	January 31 2019
Ten year term, unsecured, non-viability contingent capital compliant, subordinated note payable, principal amount of $5.0 million, effective interest rate of 10.41%, maturing March 2029.	$ 4,883	$ 4,881	$ -
Ten year term, unsecured, callable subordinated note payable, principal amount of $10.0 million, effective interest rate of 8.77%, redeemed March 2019.	$ -	$ -	$ 9,859
	$ 4,883	$ 4,881	$ 9,859

In March 2019, the Bank redeemed the $10.0 million subordinate note payable. In the same month the Bank completed a private placement of non-viability contingent capital (“NVCC”) compliant note payable in the principal amount of $5.0 million, of which $500,000 was issued to a related party (see note 13). Issue costs associated with the private placements were $125,000.

7. Securitization liabilities:

Securitization liabilities include amounts payable to counterparties for cash received upon initiation of securitization transactions, accrued interest on amounts payable to counterparties, and the unamortized balance of deferred costs and discounts which arose upon initiation of the securitization transactions.

The amounts payable to counterparties bear interest at rates ranging from 3.55% - 3.95% and mature in 2020. Securitized residential insured mortgages and other assets are pledged as collateral for these liabilities.

8. Other liabilities:

(thousands of Canadian dollars)	January 31 2020	October 31 2019	January 31 2019
Accounts payable and other	$ 2,570	$ 3,983	$ 1,959
Lease obligations	3,164	-	-
Cash collateral and amounts held in escrow	6,291	6,098	5,467
Holdbacks payable on loan and lease receivables	105,256	97,001	96,670
	$ 117,281	$ 107,082	$ 104,096

9. Share capital:

a) Common shares:

At January 31, 2020, there were 21,123,559 (October 31, 2019 – 21,123,559) common shares outstanding.

b) Preferred shares:

At January 31, 2020, there were 1,461,460 (October 31, 2019 – 1,461,460) Series 1 preferred shares and 1,681,320 (October 31, 2019 – 1,681,320) Series 3 preferred shares outstanding. These shares are Basel III compliant, non-cumulative rate reset preferred shares which include NVCC provisions. As a result, these shares qualify as Additional Tier 1 Capital (see note 14).

c) Stock options:

At January 31, 2020, there were 42,017 common share stock options outstanding (October 31, 2019 – 42,934).

10. Tax provision:

Tax provision for the three months ended January 31, 2020 was $1.9 million (January 31, 2019 - $1.9 million). The Bank's statutory federal and provincial income tax rate is approximately 27% (2019 – 27%). The effective rate is affected by certain items not being taxable or deductible for income tax purposes.

11. Income per common share:

(thousands of Canadian dollars)

	for the three months ended	
	January 31 2020	January 31 2019
Net income	$ 5,141	$ 4,932
Less: dividends on preferred shares	(542)	(550)
	4,599	4,382
Average number of common shares outstanding	21,123,559	21,123,559
Income per common share:	$ 0.22	$ 0.21

The Series 1 and Series 3 NVCC preferred shares are contingently issuable shares and do not have a dilutive impact.

12. Commitments and contingencies:

The amount of credit related commitments represents the maximum amount of additional credit that the Bank could be obligated to extend.

(thousands of Canadian dollars)

	January 31 2020	October 31 2019	January 31 2019
Loan commitments	$ 263,696	$ 261,366	$ 184,591
Letters of credit	48,464	48,074	39,066
	$ 312,160	$ 309,440	$ 223,657

13. Related party transactions:

The Bank's Board of Directors and Senior Executive Officers represent key management personnel and are related parties. At January 31, 2020, amounts due from these related parties totalled $1.4 million (October 31, 2019 - $1.4 million). The interest rates charged on these loans are similar to those charged in an arms-length transaction. Interest income earned on the above loans for the three months ended January 31, 2020 was $13,000 (January 31, 2019 - $8,000). All loans issued to key management personnel were current as at January 31, 2020 and 2019.

In March 2019, the Bank issued a $500,000 subordinated note payable to key management personnel which bears interest at a rate of 10% and matures in March 2029 (note 6).

14. Capital management:

a) Overview:

The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence as well as to support future development of the business. The impact of the level of capital on shareholders' return is an important consideration and the Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater leverage and the advantages and security afforded by a more robust capital position.

OSFI sets and monitors capital requirements for the Bank. Capital is managed in accordance with policies and plans that are regularly reviewed and approved by the Board of Directors and take into account forecasted capital requirements and financial market conditions.

The goal is to maintain adequate regulatory capital for the Bank to be considered well capitalized, protect consumer deposits and provide capacity to support organic growth as well as to capitalize on strategic opportunities that do not otherwise require accessing the public capital markets, all the while providing a satisfactory return to shareholders. The Bank's regulatory capital is comprised of share capital, retained earnings and unrealized gains and losses on fair value through other comprehensive income securities (Common Equity Tier 1 capital), preferred shares (Additional Tier 1 capital) and the qualifying amount of subordinated notes (Tier 2 capital).

The Bank monitors its capital adequacy and related capital ratios on a daily basis and has policies setting internal maximum and minimum amounts for its capital ratios. These capital ratios consist of the leverage ratio and the risk-based capital ratios.

During the period ended January 31, 2020, there were no material changes in the Bank's management of capital.

b) Risk-Based Capital Ratios:

The Basel Committee on Banking Supervision has published the Basel III rules on capital adequacy and liquidity ("Basel III").

OSFI requires that all Canadian banks must comply with the Basel III standards on an "all-in" basis for the purpose of determining their risk-based capital ratios. Required minimum regulatory capital ratios are a 7.0% Common Equity Tier 1 ("CET1") capital ratio and an 8.5% Tier 1 capital ratio and 10.5% total capital ratio, all of which include a 2.50% capital conservation buffer.

OSFI also requires banks to measure capital adequacy in accordance with guidelines for determining risk adjusted capital and risk-weighted assets including off-balance sheet credit instruments as specified in the Basel III regulations. Based on the deemed credit risk for each type of asset, assets held by the Bank are assigned a weighting ranging between 0% to 150% to determine the Bank's risk weighted equivalent assets and its risk-based capital ratios.

The Bank's risk-based capital ratios are calculated as follows:

(thousands of Canadian dollars)	January 31 2020	October 31 2019
Common Equity Tier 1 (CET1) capital		
Directly issued qualifying common share capital	$ 152,757	$ 152,757
Retained earnings	62,140	58,069
CET1 before regulatory adjustments	214,897	210,826
Regulatory adjustments applied to CET1	(11,498)	(13,281)
Common Equity Tier 1 capital	$ 203,399	$ 197,545
Additional Tier 1 capital		
Directly issued qualifying Additional Tier 1 instruments	$ 29,337	$ 29,337
Total Tier 1 capital	$ 232,736	$ 226,882
Tier 2 capital		
Directly issued capital instruments	$ 5,000	$ 5,000
Tier 2 capital before regulatory adjustments	5,000	5,000
Regulatory adjustments applied to Tier 2	-	-
Total Tier 2 capital	$ 5,000	$ 5,000
Total regulatory capital	$ 237,736	$ 231,882
Total risk-weighted assets	$ 1,558,070	$ 1,501,435
Capital ratios		
CET1 ratio	13.05%	13.16%
Tier 1 capital ratio	14.94%	15.11%
Total capital ratio	15.26%	15.44%

c) Leverage Ratio:

The leverage ratio, which is prescribed under the Basel III Accord, is a supplementary measure to the risk-based capital requirements and is defined as the ratio of Tier 1 capital to the Bank's total exposures. The leverage ratio is calculated as follows:

(thousands of Canadian dollars)	January 31 2020	October 31 2019
On-balance sheet assets	$ 1,854,765	$ 1,785,381
Assets amounts deducted in determing the Basel III Tier 1 capital	(11,498)	(13,281)
Total on-balance sheet exposures	1,843,267	1,772,100
Off-balance sheet exposure at gross notional amount	$ 312,160	$ 309,440
Adjustments for conversion to credit equivalent amount	(192,338)	(190,023)
Off-balance sheet exposures	119,822	119,417
Tier 1 capital	232,736	226,882
Total exposures	1,963,089	1,891,517
Leverage ratio	11.86%	11.99%

The Bank was in compliance with the leverage ratio prescribed by OSFI throughout the periods presented.

15. Interest rate position:

The Bank is subject to interest rate risk which is the risk that a movement in interest rates could negatively impact net interest margin, net interest income and the economic value of assets, liabilities and shareholders' equity. The following table provides the duration difference between the Bank's assets and liabilities and the potential after-tax impact of a 100 basis point shift in interest rates on the Bank's earnings during a 12 month period as well as the potential after-tax impact of a 100 basis point shift in interest rates on the Bank's shareholders' equity over a 60 month period if no remedial actions are taken.

	January 31, 2020		October 31, 2019	
	Increase 100 bps	Decrease 100 bps	Increase 100 bps	Decrease 100 bps
Increase (decrease):				
Impact on projected net interest income during a 12 month period	$ 1,869	$ (1,857)	$ 1,621	$ (1,613)
Impact on reported equity during a 60 month period	$ (3,863)	$ 3,993	$ (3,669)	$ 3,780
Duration difference between assets and liabilities (months)	1.2		1.3	

16. Fair Value of Financial Instruments:

Fair values are based on management's best estimates of market conditions and valuation policies at a certain point in time. The estimates are subjective and involve particular assumptions and matters of judgment and as such, may not be reflective of future fair values. The Bank's loans and deposits lack an available market as they are not typically exchanged and, therefore, they are not necessarily representative of amounts realizable upon immediate settlement. See Note 21 to the October 31, 2019 audited Consolidated Financial Statements for more information on fair values.

	January 31, 2020		October 31, 2019	
(thousands of Canadian dollars)	Book Value	Fair Value	Book Value	Fair Value
Assets				
Cash and cash equivalents	$ 134,253	$ 134,253	$ 139,145	$ 139,145
Securities	-	-	10,061	10,061
Loans	1,668,720	1,672,300	1,594,288	1,593,277
Other financial assets	23,752	23,752	17,510	17,510
Liabilities				
Deposits	$ 1,454,979	$ 1,465,837	$ 1,399,889	$ 1,403,816
Subordinated notes payable	4,883	5,000	4,881	5,000
Securitization liabilities	33,388	33,574	33,366	33,469
Other financial liabilities	117,281	117,281	107,082	107,082

CORPORATE INFORMATION

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Retired, former Executive Director of the International Monetary Fund

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