2021
Management Discussion & Analysis

Local banking means more.

PROSPERA
CREDIT UNION

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Management Discussion & Analysis

Prospera Credit Union (Prospera) is pleased to provide an overview of our 2021 financial and operational results.

This past year was marked by the challenges of navigating through multiple climate crises, on top of a second year of COVID-19 that would again test everyone's resilience. Through it all, we are very proud of the support we were able to provide our members, their families, and our local communities. With perseverance and fortitude, we made significant progress as we advanced our work of building a stronger credit union to better serve our members.

This Management Discussion and Analysis (MD&A) enables members to assess Prospera's financial condition and results of operations for the 2021 fiscal year. It should be read in conjunction with our December 31, 2021 Audited Consolidated Financial Statements (Financial Statements), prepared in accordance with International Financial Reporting Standards (IFRS). All amounts in the MD&A are expressed in Canadian dollars. The MD&A commentary includes information available up to and including March 10, 2022, which is the date Prospera's Board of Directors approved the Financial Statements.

Corporate Overview

As a credit union with deep roots in British Columbia, we are proud to be woven into the fabric of our local communities – in times of challenge, recovery, and prosperity. A community-based, purpose-driven organization, Prospera delivers financial services to more than 117,000 members across BC through a network of 26 branch locations, our Member Service Centre, and a number of different mobile and digital channels. Together, we are a cooperative that measures our success by the financial success of our members.

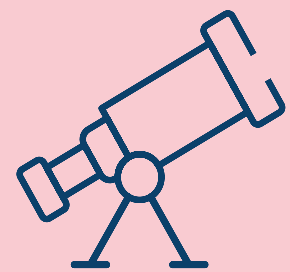
Our primary lines of business include Personal Banking, Business Banking (including Leasing), and Wealth Planning. Deposits are insured by the Credit Union Deposit Insurance Corporation (CUDIC) of BC. Our corporate office is located on the traditional territories of the Semiahmoo, Katzie, Kwikwetlem, Kwantlen, Qayqayt, and Tsawwassen First Nations in Surrey, BC.

At Prospera, our mandate is clear: we exist to serve our members. Moreover, our vision and mission are at the heart of everything we do and guide all of our collective actions.

Our vision

Together we'll help build ...

- vibrant healthy communities
- thriving local enterprise
- financially empowered people



Our mission

To be a catalyst for the prosperity and aspirations of enterprising local businesses and all the people that make them great, through excellence in deep member insights leading to tailored solutions, enabled and empowered employees, and personalized digital experiences.

Financial Performance Highlights

Operating income
$38.0 million

Deposits
$5.8 billion

Net interest income
$142.6 million

Assets under management
$8.7 billion

Loans & leases receivable
$5.5 billion

Members' equity
$382.5 million

Return on equity
6.1%

Capital ratio
(including system capital)
14.1%

Efficiency ratio 81.6%

Community investment
$0.7 million

Foundation
$0.5 million

Return on average assets
0.33%

Business highlights

Members

You can now visit any of our 26 branches – from Vancouver through the Fraser Valley and to the Okanagan – to complete the most common transactions.

Three branches and our Corporate office now display our new brand and logo, with civic approvals in process and many more coming soon.

+117,000 members

+103,000 Personal Banking members

+14,000 Business Banking members

+16,000 Wealth Planning clients

+4,000 Leasing customers

Member Service Centre

+175,000 calls

+21,000 emails

Regular attention provided to different enterprising local businesses throughout the year and particularly during Small Business Month.

You can now access new digital banking features that include viewing credit card balances and transactions, banking system alerts, and access to void cheques in online banking.

Employees

Designated a Great Place to Work® for the second year in a row.

Launched an employee-led Diversity Council.

Launched our new employer brand, Team Local.

TEAM LOCAL

THE HUB

Improved collaboration and seamless communication by moving all employees onto one Office 365 environment and launching a new intranet.

Launched new organizational values, including:

- Cultivate trusting relationships
- Empower and enable others
- Lead with curiosity
- Embrace change and execute with purpose
- Thrive as One Team

Community

Through the Foundation and our direct credit union community programs, we donated

+$1 million

to our local communities in 2021.

Prospera contributed an additional $500,000 to the Prospera Foundation, now one of the largest credit union endowments in Canada with more than **$10 million in assets.**

Line of business overview

Business Banking and Leasing

Business Banking at Prospera supports 14,000 local business owners and includes three divisions: Local Business, Core Commercial, and Real Estate Development. In 2021, all three divisions had very strong results. This was achieved by an unwavering focus on people, programs, and relationships supporting existing and new enterprising local businesses with net portfolio growth of approximately $310 million or 20%.

Funding more than 1,500 vehicle and equipment leases

2021 highlights included:

- Streamlining our lending and credit processes, enabling a quicker turnaround and a much better member experience.
- Significantly increasing our local business lending limits, allowing us to meet more of our members' needs.
- Reducing the average time to open a new business account from two days to only 30 minutes using our new software; similarly, time to fund small business loans has decreased from two days to two hours!
- Funding multiple new construction developments, providing new housing for hundreds of families in our communities.
- Ending the year with total assets of more than $1.8 billion in business lending.

With Prospera's merger, they now have additional lending capacity to support my business, including offering higher loan limits that have allowed us to grow our business and finance larger construction projects. I'm grateful for their partnership and responsiveness to my business needs.

Bhupinder Johal
CEO, Metro-Van Construction Group

Leasing

WS Leasing Ltd., Prospera's Auto Leasing Division, gives us a national presence in consumer and commercial vehicle, equipment, and fleet leasing across Canada. Overall, this division finished the year with strong results, particularly over the second half, despite the lowest auto inventories in decades. Mercado Capital Corporation is our is our business equipment leasing division that has customers across the country.

2021 highlights included:

- Funding more than 1,500 vehicle and equipment leases.
- Ending the year with a lease portfolio approaching $250 million.

Personal Banking

Our Personal Banking team serves more than 100,000 members from 26 branch locations and provides a wide range of banking and lending solutions. In 2021, a core priority was to ensure that all members could be served across all locations with their most commonly requested transactions, a key commitment arising from the 2020 merger. This goal was accomplished before the end of the year, allowing members to conduct day-to-day banking at any branch, regardless of where the account was opened. The most common transactions include bill payments, withdrawals, deposits, transfers between accounts, opening accounts, online banking set up, and more.

In 2021, our local branch network experienced significant changes as we started to rebrand and ensure each location was best positioned to conveniently serve our members. In April, we opened the White Rock branch, our first newly branded, full-service location. In June, we relocated the Austin branch to a new location in Burquitlam, adjacent to rapid transit. With overlapping service areas, we amalgamated the Willowbrook Langley branch with the Clayton Heights and Langley City local branches. In the Okanagan, renovations commenced on the Kelowna Mission Park branch. Finally, in 2021 a new microsite was launched for members, Local Banking Means More, to communicate new member benefits and features.

2021 highlights included:

- Full capability to serve all members with their most commonly requested transactions at any of our 26 branches.
- Originating $485 million in new mortgages for 1,900 members and an additional refinancing or renewal of a further $860 million in mortgages for 3,300 members across the Lower Mainland through to the Okanagan.

> **In these days of unrest and increasing difficulties in negotiating the simplest of contracts, it is an absolute joy to work with people such as Prospera. Your whole team was involved in the support and efforts to get my grandchildren their first home. I am not only greatly relieved, but proud to think of you all as truly our financial family!**
>
> Anne Hails, a 17-year member

Member Service Centre

In 2021, our two Member Service Centres provided a wide range of banking and lending solutions. Due to the impacts of the pandemic, both centres continued to provide their services remotely, while maintaining a positive and safe member experience. A significant achievement in 2021 was aligning the two call centres onto one unified server, which resulted in improved reporting and providing the foundation for our upcoming single banking platform integration, and a unified member experience through both call centres.

2021 highlights included:

- Further enhancing the security of member accounts with the launch of two-factor authentication.
- Triaging support to members affected by natural disasters in the fall.
- Enhancing remote support for members through increased staffing and enhanced functionality.

All employees were migrated onto one Office 365 environment, enabling seamless communication across our organization dramatically improving our ability to collaborate and serve our members more efficiently in a hybrid work environment.

Wealth Planning

Prospera's dedicated team of wealth management professionals provide expert advice to help clients plan for their future. Their core services include financial planning, estate planning, tax planning, income protection and investment management. In 2021, a key focus was to bring greater resources and more focused investment options and planning services to our wealth members. This includes expanding the number of advisors licenced under the Investment Industry Regulatory Organization of Canada (IIROC) platform, which offers more client-focused investment options and relationships.

2021 highlights included:

- Expanding our Wealth team to 21 certified financial planners.
- Serving more than 16,000 members who have an active wealth product.
- Finishing 2021 with nearly $1.9 billion in wealth assets under management on behalf of our members.

Corporate

Our corporate division encompasses several departments, including Business Technology Solutions, Communications, Centralized Services, Credit, the Enterprise Project Management Office, Facilities, Finance and Business Intelligence, Governance, Internal Audit, Legal Affairs, Marketing, People Experience, Risk, and Treasury.

Each of these areas contributes in an important way to delivering products and services to our members, and all of these teams worked exceptionally hard this past year on core integration activities on top of their day-to-day responsibilities. Among other things, this included harmonizing our human resource information system, moving all employees onto one benefits plan, re-engineering our internal audit function, strengthening our cybersecurity capabilities, and implementing a new recovery team to aid in the aftermath of the multiple climate related crises this past year. In addition, all employees were migrated onto one Office 365 environment, enabling seamless communication across our organization, dramatically improving our ability to collaborate and serve our members more efficiently in a hybrid work environment.

> **Although, we've only known our advisor for a relatively short time, we feel we have a solid relationship. We trust the advice we're given and appreciate the way our advisor is able to clearly explain things to us.**
>
> Esther & Richard Wheeler

2021 Operating Results

Our second year of operations as a merged entity was characterized by perseverance and progress. We advanced initiatives to build a stronger credit union to serve our members within an unprecedented and complex operating environment, resulting from the continued COVID-19 pandemic and multiple climate crises in the communities we serve.

Despite the many twists and turns this past year, overall financial results were quite strong. Operating income of $38.0 million was up 9.5% from our inaugural year and net income of $23.6 million was similarly strong, up nearly 5%. Notwithstanding the significant investments made as part of integration, operating efficiency continued to trend in the right direction as we continued to unlock further synergies from harmonizing our operations. While assets under management declined from $9.2 billion to $8.7 billion in 2021, most of this reflects an intentional run-off of excess liquidity during the year. Overall, these solid financial returns have added to a strong capital base and will enable Prospera to continue to make important investments in the business on behalf of our members.

The following chart details the comparative financial and industry metrics.

Financial Metrics		2021		2020	% ▲	
Operating income	$	$38.01 M	$	$34.70 M	9.5%	▲
Net income	$	$23.61 M	$	$22.51 M	4.9%	▲
Assets under management	$	$8.75 B	$	$9.15 B	-4.4%	▼
Total assets	$	$6.72 B	$	$7.36 B	-8.6%	▼
Total loans	$	$5.29 B	$	$5.37 B	-1.5%	▼
Total leases	$	$248.24 M	$	$278.62 M	-10.9%	▼
Total deposits	$	$5.85 B	$	$6.09 B	-4.1%	▼

Industry Metrics	2021	2020	% ▲	
Capital ratio	14.1%	14.8%	-4.7%	▼
Return on average assets	0.33%	0.30%	10.0%	▲
Return on equity	6.1%	6.1%	0.0%	–
Operating efficiency	81.6%	82.3%	-0.9%	▼
Liquidity	19.4%	26.6%	-27.1%	▼

Operating income

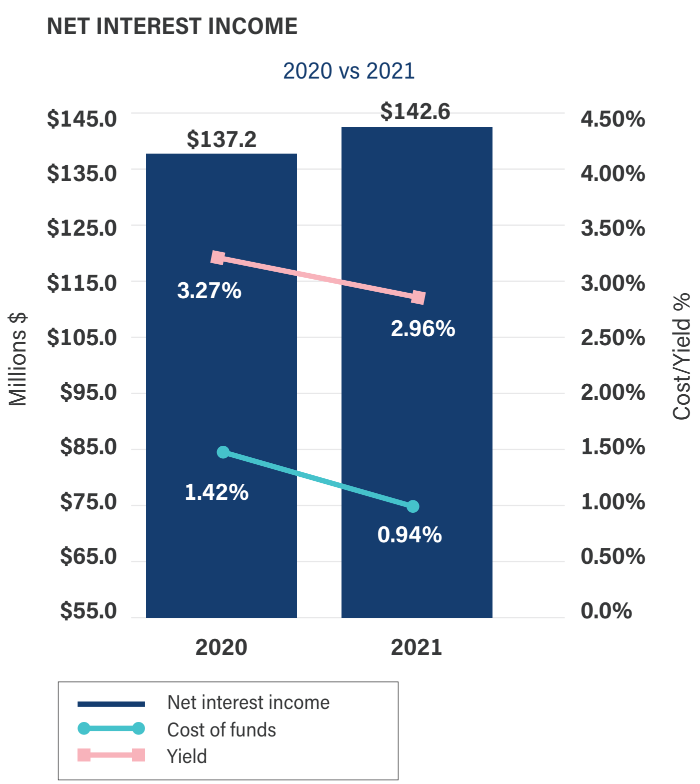
Operating income is defined as income excluding taxes, contributions to the Foundation, one-time integration expenses, and unrealized gains and losses on financial investments. It measures the net operating results of our primary business operations.

Our operating income was $38.0 million in 2021, compared to $34.7 million in 2020, an increase of 9.5% over the previous year. In 2021, our second year as a newly merged organization, we launched our new strategy, a new brand, and new organizational values all designed to better serve our members. During the year, we expanded our wealth offerings to deliver enhanced options and capabilities for our members, resulting in strong growth and earnings. We also saw significant growth and success in Business Banking as we were able to help more members with their financial needs. In Personal Banking, overall lending balances declined slightly as we saw significant refinancing activity, reflective of a very active housing market and many members taking advantage of locking in historically low rates. Throughout the year, costs remained well managed, albeit with significant investments made in advancing our integration activities, expanding and refreshing our branch network, enhancing our IT infrastructure and cybersecurity capabilities, and rolling out our new brand – **Local banking means more**. Notwithstanding some of the challenges inherent in our operating environment, credit losses were quite low for the year, and we also saw a reversal of our expected credit loss provision, which is discussed further below. All in all, we are quite pleased with these operating results, which provide a good foundation for the year ahead.

Net income

Net income in 2021 was $23.6 million, up from $22.5 million in 2020. A continued focus on managing costs and identification of areas with potential for enhanced earnings allowed us to perform favourably in 2021. Additionally, the execution of key integration activities enabled us to realize synergies, which also had a positive impact on net income in 2021.

Further analysis and discussions on the key components of net income are outlined below.



The largest component of our operating income is net interest income. This is driven by volume, mix and yield.

While the yield declined from 3.27% to 2.96%, net interest income increased to $142.6 million, up from $137.2 million in 2020. The change in net interest income reflects a historically low interest rate environment as both lending rates and interest earned on deposits were relatively low throughout the year. This was offset by our mix of business with greater growth in higher yielding business banking. It also reflects refinancing activity in residential mortgages, which gets recorded as part of net interest income. As rates are expected to rise, we continue to see significant movement in the portfolio from variable to fixed rate products, with many members taking advantage of the lower interest rates as they renew mortgages.

Impairment losses on loans, leases receivable, investments and other assets

In assessing our loans and leases receivable portfolios for evidence of impairment, we considered various factors: bankruptcy, default, payment delinquency, and declines in the value of mortgage security or other collateral and additional economic considerations. Individual loans or leases may be found to be impaired due to specific factors. For loans assessed as impaired, we continue to hold substantial security, which serves to protect against loss. In addition, evaluations of the overall portfolios of mortgages, loans, vehicle leases and equipment leases occur regularly to quantify losses that might arise from broader factors. We are proactive in the management of delinquency and other credit concerns to ensure that credit losses are kept as low as possible.

During the year, we reported recoveries on impairment of financial assets, which reflects a reversal of the expected credit loss provision more than off-setting modest write-offs experienced in the year.

In determining the expected credit loss (ECL) provision, management considers future macroeconomic and industry-specific trends. The ECL provision is extensively reviewed on a quarterly basis by credit union management. ECL provision reversals totaling $2.6 million were recorded in 2021, reflecting an improved outlook of the macroeconomic environment.

We also recorded impairments on other assets of $0.5 million in 2021, $2.0 million lower than in 2020. The reduction reflects a significant shortage of used vehicles in the market, thereby inflating the value of vehicles taken into inventory.

Net fee and commission income

Net fee and commission income was $20.8 million, an increase of $1.2 million over 2020 results.

Wealth management revenues grew to $14.1 million, an increase of $2.1 million from $12.0 million in 2020. This reflects continued growth in our wealth management portfolio, which increased by $239 million to $1.9 billion. In 2021, we successfully integrated our two legacy trading platforms and continued to convert assets from the Mutual Fund Dealers Association platform to the Investment Industry Regulatory Organization of Canada, which offers expanded product offerings to members.

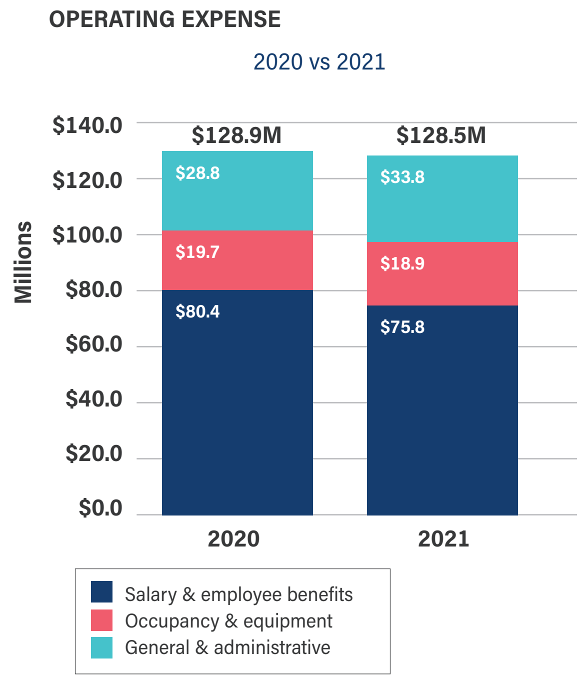
Increases in fee and commission income were partially offset by a decrease in creditor insurance income. This reflects the small decline in the Personal Banking portfolio as well as creditor claims experience. Fee income from bad debt recoveries also declined in 2021, largely within the equipment leasing portfolio. With reduced equipment leasing volumes, we experienced lower defaults than in 2020, and as a result, lower bad debt recoveries.

Fee and commission expense reduced slightly in 2021 by $0.3 million. The net reduction reflects lower loan and lease receivable fees, which declined by $0.2 million, reflective of the slight decline in the lending and leasing portfolios. With continued pandemic restrictions, we saw a decrease of $0.1 million in ATM and point-of-sale transaction fees under member service fee expense.

Net gains on financial instruments at fair value through profit and loss (FVTPL) and other income

During the year, we recognized realized losses of $2.0 million on investments, compared to realized gains of $3.8 million in 2020. In addition, we recorded unrealized losses on financial instruments of $5.8 million, compared to unrealized gains of $6.0 million the prior year. These amounts largely reflect the fair value adjustments associated with changes in underlying interest rates throughout the year.

Operating expenses



Overall, operating costs remained well managed throughout the year, decreasing slightly from 2020. Key components are described below.

Salary and employee benefit expense decreased by $4.6 million in 2021, reflective of continued synergies, maintaining certain vacancies throughout the year and a reduction in restructuring costs. These savings were partially offset by recruitment costs and general wage increases associated with a highly competitive labour market.

Occupancy and equipment expense decreased by 3.8% to $18.9 million in 2021. This was primarily due to the one-time accelerated depreciation of certain equipment and signage in 2020. These reduced expenses were offset slightly against operating expenses incurred establishing our new branch locations in Burquitlam and New Westminster.

General and administrative expense increased by $5.0 million to $33.8 million in 2021. The largest component of this increase reflects the development and launch of the new Prospera brand and ongoing efforts to support various lines of business totaling $2.4 million. In addition, CUDIC premiums increased by 101% or $2.3 million due to higher premium assessment rates. These costs also reflect continued investment in our digital IT infrastructure of $0.7 million, partially offset by a reduction in other administrative expense of $0.4 million.

As part of our ongoing commitment to support our local communities, these costs also include a $500,000 donation to the Prospera Foundation in 2021.

Income taxes

Although income levels in 2021 were higher than in 2020, tax expense came in lower due to a lower effective tax rate. The effective tax rate for 2021 was 19.8% compared to 20.9% in 2020. The primary driver behind this reduction reflects the applicable tax rate that is applied to integration related expenses, which were significantly higher in the prior year. Deferred taxes are calculated on temporary differences under the liability method using tax rates expected to apply when the liability is settled, or when the asset is realized.

Supporting our business members

> **Prospera is more than a credit union, they're our partner in community and we are truly blessed to be able to do what we do, and we couldn't have done it without our partners!**

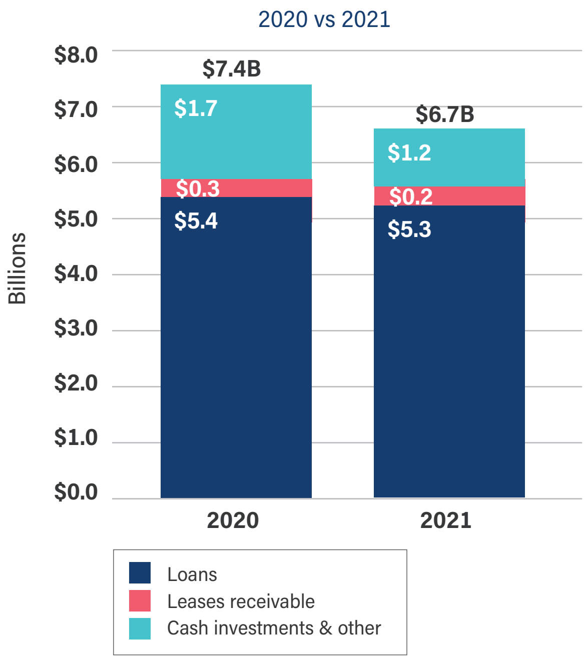
Alison Silgardo
CEO, Seniors Services Society of BC

Balance sheet

Asset and liability portfolios

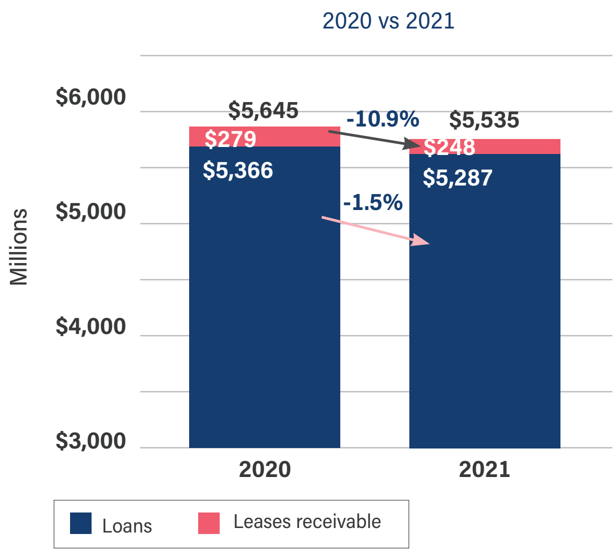
On book assets declined from $7.4 billion to $6.7 billion in 2021 with most of the decline reflective of holding lower cash and near-term investments as we attempted to reduce excess liquidity.

TOTAL ASSETS



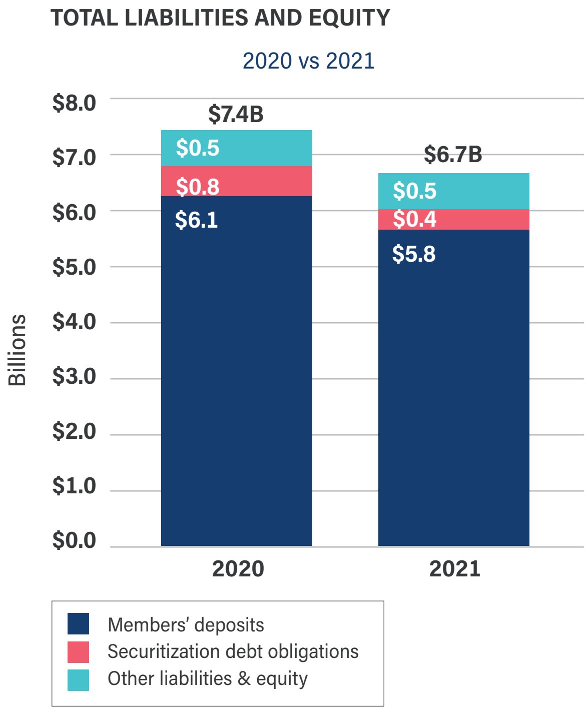
- Total assets ended at $6.7 billion, a decline of $0.7 billion over 2020.
- The reduction is comprised of reductions in cash, investments, and other assets of $0.5 billion, loans of $78.9 million, and leases receivable of $30.4 million.

ASSET PORTFOLIO
LOANS & LEASES RECEIVABLE



- Overall loan balances decreased by $78.9 million or 1.5% during 2021. The decline in loans reflects a decrease in Personal Banking lending and an increase in the business lending portfolio. The Personal Banking portfolio ended the year at $3.5 billion, with a net decrease of $383.8 million, compared to December 2020. Despite a high volume of new loan originations, Personal Banking loan balances experienced a record level of rate refinancing in line with housing sales activity and historically low interest rates. This decline was offset by a notable increase in Business Banking lending during the year. The Business Banking portfolio ended the year at $1.8 billion, with a net increase of $310.0 million compared to December 2020.
- Leases receivable decreased $30.4 million or 10.9% from 2020. The vehicle portfolio of $198.0 million in leases receivables was down by $5.0 million in 2021. The automotive and equipment sectors faced significant inventory challenges in 2021, due to chip shortages, and other supply chain disruptions

related to COVID-19. While automotive balances were down slightly year over year, activity in the second half was quite strong and we are positioned for good growth as supply chain challenges get resolved. Within equipment leasing, we continue to take a more cautious approach, focused on supporting existing member relationships as we consider the economic risks associated with the current operating environment.



- In 2021 members' deposits decreased by 4.1% to $5.8 billion. This was driven by an intentional and managed reduction in large institutional deposits in 2021 in an attempt to runoff our excess liquidity positions.

To maintain diverse funding sources, we routinely securitize loans and leases to raise additional funds at competitive rates.

- Securitization and debt obligations decreased by $421.8 million in 2021. With excess liquidity, we limited the use of securitization in 2021. This decrease is comprised of $403.4 million and $18.4 million in loan and lease securitizations, respectively.

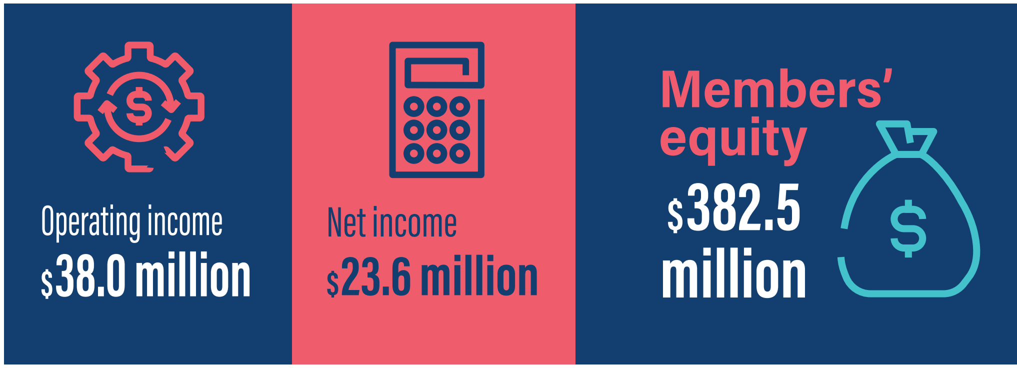
- There were no borrowings at the end of 2021. Due to excess liquidity, stability in deposit balances and small declines in lending balances, borrowings were not required during 2021.

The non-financial asset and liability categories are a much smaller component of the consolidated statement of financial position when compared with member accounts. These balances reflect the assets and liabilities used in the credit union's operations, along with certain income tax and pension-related balances. The balances in these asset and liability accounts saw modest changes from 2020, in keeping with ongoing business activity. Pension and income tax-related asset and liability balances have fluctuated, largely due to changes in rates. The retirement benefit obligation and income tax payable were recorded as $28.5 million and $7.5 million compared to $37.1 million and $5.0 million in 2020.

Members' equity

Members' equity is comprised of retained earnings, contributed surplus, and accumulated other comprehensive loss, and grew to $382.5 million at the end of 2021. Within members' equity, the increase in retained earnings represents net income for the year of $23.6 million. Contributed surplus of $130.9 million was created as part of the IFRS 3 business combination accounting for the merger and is also included in members' equity.

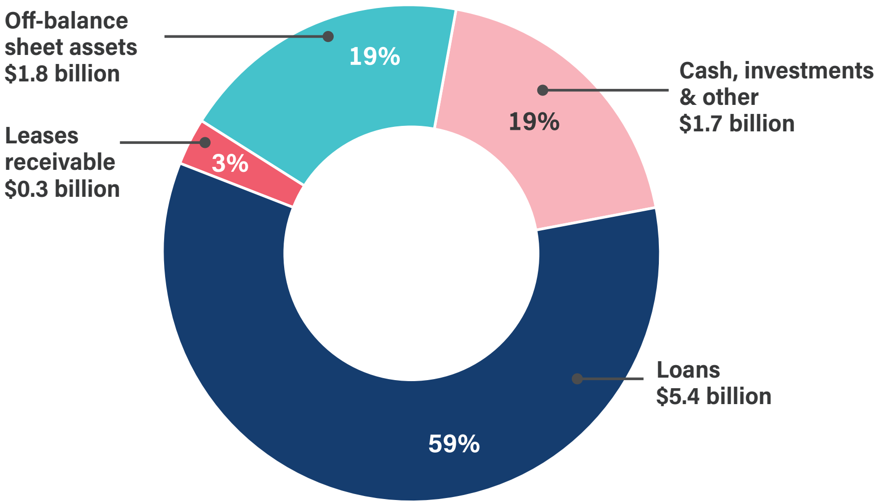
Comprehensive income for 2021 was $32.8 million in the year, compared to $17.3 million in 2020. This represents net income of $23.6 million combined with net actuarial gains of $11.0 million on our defined benefit plans, offset by a deferred tax recovery of $1.8 million in 2021.



Assets under management

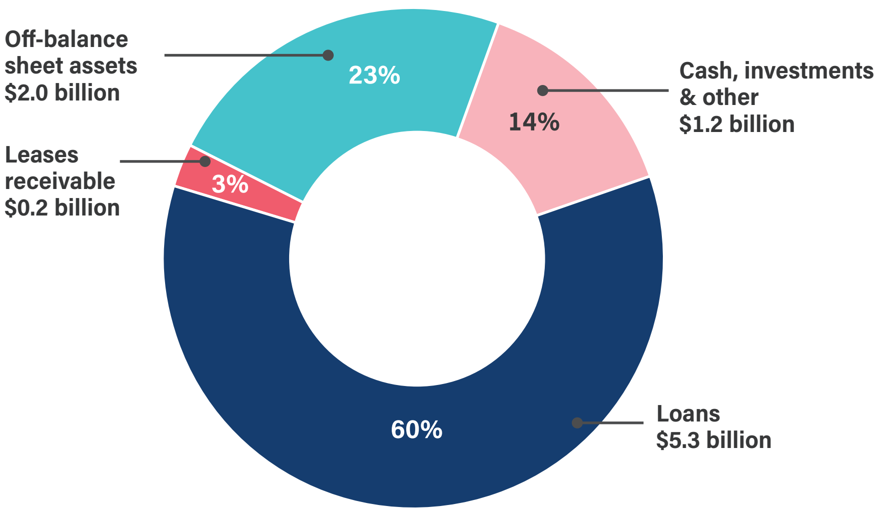
ASSETS UNDER MANAGEMENT - $9.2 BILLION

2020



ASSETS UNDER MANAGEMENT - $8.7 BILLION

2021



Assets under management
$8.7 billion

At December 31, 2021, we held $8.7 billion of assets under management, a decrease of 4.4% from 2020. The proportionate share of off-balance sheet assets to total assets under administration increased from 19.6% to 23.1%.

At December 31, 2021, **off-balance sheet assets under administration** were $2.0 billion, an increase of $228.6 million from $1.8 billion in 2020.

The largest component of off-balance sheet assets under administration is member investment products. At December 31, 2021, the total value of member investment products under management was $1.86 billion ($1.62 billion in 2020). These increases reflect strong net sales in wealth management along with capital market appreciation.

For customers with self-directed retirement accounts, we act as administrator for a fee. Self-directed RRSP funds under administration were $4.6 million, down from $9.0 million in 2020. The reduction in self-directed RRSPs is primarily a result of customers moving their investments into our managed wealth line of business.

Throughout 2021, we also acted as facilitator for the Canada Emergency Business Account (CEBA) loans program. This was in support of a federal relief program for businesses to gain access to interest-free loans during the pandemic. We reported a balance of $62.9 million within 2,071 CEBA loans in 2021.

Periodically, other financial institutions are invited to participate in the funding of large-dollar loans that are originated by Prospera. These syndicated loans are administered for a fee, and totaled $93.4 million, down from $112.2 million in 2020.

Managing business risks

Prospera effectively manages risks in a disciplined and proactive approach that allows the organization to capitalize on opportunities in a way that aligns with its risk appetite. This balanced approach gives strong consideration to each of our many stakeholders, including our members, employees, regulators, service providers, and the broader community.

The enterprise risk management (ERM) framework enables the board to set the types and amount of risk Prospera is willing to take in pursuit of our strategic objectives. It's guided by foundational risk management principles, including regular monitoring and reporting such as consideration for changes in the market, products, and best practices. Please see the Governance Report for more information on this approach.

Prospera follows the three lines of defense model. The first line (risk owners): Operational employees who understand and correctly carry out their roles and responsibilities; second line (oversight function): Independent oversight employees that monitor risk and compliance among operational employees; and third line (independent assurance): Internal audit and the board who regularly review business operations and oversight functions to confirm they are performing at appropriate levels for risk tolerance and regulatory compliance.

Within Prospera, an ERM Committee, led by our Chief Risk Officer and made up of senior executives, is responsible for overseeing, managing, and reporting to the board on compliance with our risk management policies, risk appetite, and risk tolerances. Furthermore, a Management Credit Committee, also led by our Chief Risk Officer and made up of senior executives, provides oversight of the lending portfolio. The Risk, Investment and Loan Committee, through delegated accountability from the board, ensures governance and oversight for adherence to our board-approved ERM framework, and is responsible for reviewing and monitoring adherence to the ERM framework, so that we are effectively managing and controlling risk.

Supporting our business members

Prospera understands the fact that running a business is not an easy thing, so they want to help you out in any area they possibly can!

José Latchinian
Owner, José & Co. Custom Jewellers

Capital and Balance Sheet management

Balance sheet management

As an important part of our overall risk management strategy, we ensure that sufficient and appropriate capital is available to protect against both expected and unexpected events and support ongoing sustainable growth. A strong capital position offers protection in the face of risk and preserves the security of customer deposits. Strong and sufficient capital allows the credit union to pursue new initiatives and expand services to members. We also determine the amount of capital required to support operating divisions and ensure that it is used in the most efficient and effective manner. We regularly monitor and complete quarterly portfolio stress testing to ensure capital can support our operating plans.

As a BC credit union, we must meet the capital requirements outlined in the *Financial Institutions Act* (FIA) of British Columbia and the related capital requirements regulation. This regulation specifies the minimum capital a credit union must maintain and how this capital is defined and measured. The calculation of the statutory capital requirement is based on BC Financial Services Authority's (BCFSA) assessment of the relative risk of the assets held by a credit union, thus establishing that more capital is to be held against riskier assets.

BCFSA uses three capital indicators in the assessment of credit union capital adequacy:

1. The FIA regulations require a credit union to have a capital ratio of at least 8.0% to operate without any statutory restrictions. A credit union operating below this limit will be subject to immediate statutory restrictions and may be considered non-viable by BCFSA.

2. BCFSA's supervisory target of 10.0% sits above the regulatory threshold and provides BCFSA with sufficient time to address any threats to the solvency of the credit union before it falls below the regulatory requirement.

3. Credit unions are expected to establish their own internal capital target ratio, which should be set above the supervisory target. This internal target is used as a base for corrective internal action before capital erodes below the supervisory target.

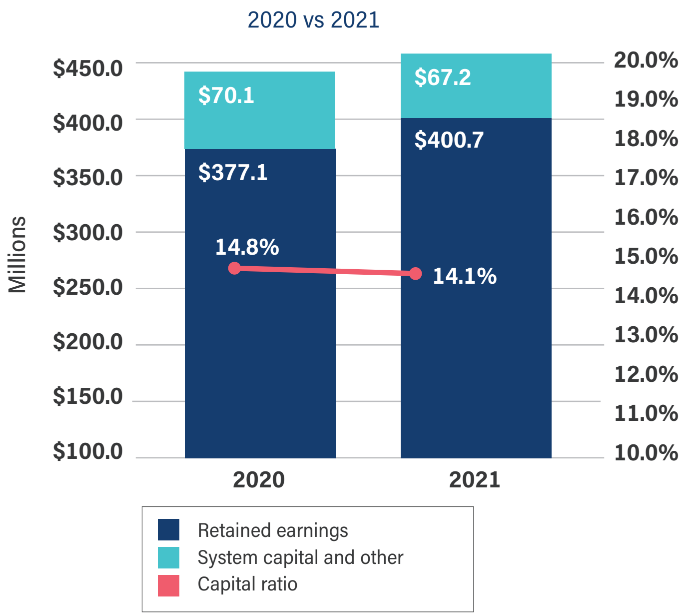
Prospera's capital policy requires an annual internal capital adequacy target to be established and maintained. For 2021, the internal capital adequacy target was 12.5%. We forecast the amount and composition of the balance sheet and expected levels of risk-adjusted assets and manage within these levels to remain sufficiently capitalized.

Prospera's main source of our capital is the retention of earnings. Our capital base also includes member shares and our proportionate share of system capital. System capital refers to the retained earnings of the centralized credit union organizations (CUDIC, Central 1 Credit Union and Stabilization Central Credit Union), which are owned by BC credit unions.

- As at December 31, 2021, Prospera's total capital base was $467.9 million compared with $447.2 million in 2020.
- Our capital adequacy ratio, including system capital, was 14.1% at December 31, 2021, compared to 14.8% in 2020. This exceeded regulatory requirements and the credit unions internal policy requirements.

Capital Ratio
(including system capital)
14.1%

CAPITAL



Overall capital levels increased in 2021 reflecting strong earnings. As outlined above, the capital ratio is impacted by the composition of asset portfolios and the associated underlying risk weightings. Although total loans declined slightly in 2021, the increase in our business portfolio with higher associated risk weightings drove up our risk weighted assets. As our risk weighted assets increased more than our capital, our capital ratio decreased from 14.8% to 14.1%. These results remain well above our internal threshold.

Liquidity

Liquidity is carefully managed to ensure that members' requirements are met at all times. By ensuring that sufficient, readily accessible or liquid assets are available, we're able to meet member demand for withdrawals and deposit redemptions, fund loans, leases and business operations, and protect the credit union against sudden, unforeseen cash needs.

As a BC credit union, Prospera must meet the liquidity requirements outlined in the FIA and the related liquidity requirement regulation. This regulation specifies the minimum liquid assets a credit union must maintain, and how liquidity is determined. The legislation requires that liquid assets representing at least 8.0% of deposit and debt obligations be held by a credit union. This liquidity ratio is regularly stress tested and is intended to ensure that liquidity is adequate in relation to the business being conducted.

- At December 31, 2021, Prospera's liquidity ratio was 19.4%, compared with 26.6% in 2020. An intentional runoff of excess liquidity combined with a small decrease in lending resulted in a decrease in the liquidity ratio in 2021.
- Liquidity levels exceeded both the regulatory and internal policy requirements.

Loans and lease securitization

Prospera regularly and routinely enters into transactions, whereby the credit union or a subsidiary securitizes (sells) consumer mortgage loans or leases receivable to third party investors. We do this to access cost-effective funding for additional growth and to manage liquidity risk, credit risk and interest rate risk. Securitization transactions have no impact on members who have a consumer mortgage or lease with the credit union.

During the year, we continued to participate in securitization programs to issue mortgage-backed securities included in the Canada Mortgage Bonds program. These conduits were established to reduce liquidity risk by further diversifying funding sources.

In 2021, Prospera had securitized consumer mortgage loans receivables of $45.2 million ($120.6 million in 2020) and securitized leases receivables of $7.0 million ($15.8 million in 2020).

Borrowing facilities

In addition to our borrowing facility with Central 1 Credit Union, Prospera maintains credit facilities with other major financial institutions. The credit union can draw on these facilities as required to finance operations. Our credit lines provide borrowing capacity of approximately 10.4% of credit union assets.

The credit union did not have any borrowings from credit facilities at December 31, 2021.

2022 Economic Outlook

The Canadian economy demonstrated its resiliency and strength in 2021 by growing rapidly from the abrupt economic losses of 2020. Despite the challenges of the resurgent COVID-19 Delta variant and continued supply chain constraints, gross domestic product (GDP) recovered to its pre-pandemic level by the end of 2021. As the Delta wave diminished, the economy continued its upward trajectory, and inflation, once considered transient, became persistent at levels not seen since the early 1990s.

The Omicron variant began spreading in Canada in the fourth quarter of 2021 and quickly led to record infections. While this variant is expected to be short-lived, it will put a damper on GDP in the first quarter of 2022. Despite the short-term impact the Omicron variant will have on GDP, the Bank of Canada (BoC) expects the economy to grow by 4% in 2022 and 3.5% in 2023. This growth projection is highly dependant on the trajectory of the COVID-19 virus.

Job growth in 2021 was robust and Canada entered 2022 near full employment. This trend was interrupted in January 2022 with the loss of 200,000 jobs due to increased Omicron restrictions. Despite this, strong employment gains are expected in the first quarter as the Omicron variant wanes and restrictions are eased. Canadian unemployment will decrease to 5.7% and BC unemployment to less than 5% by the end of 2022. BC's tight labour market will continue, leading to slower job creation in 2022, due to difficulty filling positions. This will be partially offset by continued strong inter-provincial migration.

Geopolitical concerns resulting from Russia's invasion of Ukraine and its associated humanitarian crisis heralds a renewed period of uncertainty of the sort that has disrupted supply throughout the pandemic. The negative human and economic impacts will be greatest for Ukraine itself, then Russia, followed by eastern and central Europe. In North America, trade and financial links with Russian and Ukraine are much smaller, and much of the impact in North America will come as a by-product of any slowing in European growth. Oil and natural gas prices will be higher even if Russian exports are not cut off, as will prices for wheat, fertilizers, and some metals.

This war on Europe's eastern border could temper central banks' plans to raise interest rates, although at this stage it would take a lot for the BoC to delay setting off on a path to higher borrowing costs. There has been significant growth in the economy since the beginning of the pandemic, yet the policy rate remains at an emergency setting. Upside risks to inflation in the near term, with some downside risks to growth as an offset, likely still leaves the BoC on their prior course, with rate hikes on the way on March 2, and 100 basis points or more for this year as a whole, with more to come in 2023.

In the BoC's January 26, 2022, policy announcement, the Bank noted that persistent supply constraints are feeding through to a broader range of goods prices and, combined with higher food and energy prices, are expected to keep Consumer Price Index (CPI) inflation close to 5% in the first half of 2022. As supply shortages diminish, inflation is expected to decline reasonably quickly to about 3% by the end of this year and then gradually ease. Although near-term inflation expectations are higher than in late 2022, inflation is expected to return to the 2% target in 2023.

The housing market is expected to continue to favour sellers in 2022, with continued strong demand and tight supply. The BC Real Estate Association (BCREA) expects prices to rise by 8.5% in 2022, with much of that gain occurring in the first half of the year, and by 2.7% in 2023. BCREA singled out Metro Vancouver, Victoria, and the Fraser Valley as markets for continued demand.

Reflecting continued strong economic growth, Government of Canada bond yields are expected to rise by the end of 2022. Mortgage rates will also continue to rise but at levels that will continue to support housing demand and continued aggressive pricing. As the BoC policy rate increases, prime lending rates, on which variable rate loans are based, will also rise.

The 2022 outlook faces several uncertainties, including the trajectory of the COVID-19 virus, the Russian invasion of Ukraine, supply chain constraints, and persistently high inflation. Despite these factors, there is significant optimism that the current Omicron variant will be short-lived, and that economic growth will recover quickly from its impact. Further, although the Russian invasion of Ukraine, supply chain challenges, and inflation continue to be of concern, their effects are expected to ease through 2022, with inflation returning to the 2% target by the end of 2023.

Glossary of Terms

Assets under administration are balance sheet assets and third-party investment assets that the credit union originates and manages in return for administration fees and/or commissions. Although third party assets are not recorded on the credit union's balance sheet, they represent expanded investment options for customers, while providing the credit union with a reliable revenue stream.

Balance sheet is a statement of position that reflects the assets, liabilities, and capital of the credit union at a particular point in time, and cumulative retained earnings.

Client is used in the wealth business for both members and non-members who have wealth assets with Prospera.

Compensation expense includes salary, benefits, employee training and development costs.

Comprehensive income includes the net income of the credit union, unrealized derivative income along with changes in pension obligations recorded in the consolidated statement of financial position.

Credit risk is the risk of loss resulting from a borrower's inability or unwillingness to repay a loan in conjunction with inadequate collateral or from a counterparty's inability to complete or fulfill financial obligations.

Customer is used when referring to relationships in the Leasing business, whether business-to-business (B2B) or end-user (lessee) relationships.

Fee and commission expense includes costs related to delivery of transactional account services and leasing services, ATM and *Interac*® Direct Payment transaction processing costs, cheque clearing costs, investment management costs, custodial and other loan processing fees.

Fee and commission income comprises various fees, service charges, penalties and other miscellaneous revenues that are earned but not part of net interest income.

General and administrative expense includes data processing, marketing and other costs of administration.

Interest rate risk represents the potential adverse impact that changes to market interest rates may have on the earnings and value of the credit union. It generally arises from differences between the term to maturity of investments, loans and leases receivable, and those of the credit union's sources of funding..

Liquidity risk refers to the risk of being unable to obtain funds at reasonable prices or within a reasonable time period to meet obligations as they come due.

Member is used when referring to those who have paid shares, e.g., Personal Banking and Business Banking members.

Members' equity comprises retained earnings, contributed surplus and other comprehensive income.

Net fee and commission income includes **fee and commission income** netted with **fee and commission expense.**

Net income is the sum of net interest income, net fee and commission income and other income less operating expenses and taxes.

Net interest income is the difference between financial income (interest earned on investments, loans and leases receivable) and financial expense (interest paid on members' deposits and other financing). It is the largest component of the credit union's income.

Occupancy and equipment expense includes premises rent, maintenance and other property-related costs.

Operating expenses consists of compensation expense, occupancy and equipment expense, and other general and administrative expense.

Operating income is defined as income excluding taxes, contributions to the Foundation, one-time integration expenses, and unrealized gains and losses on financial investments. It measures the net operating results of our primary business operations.

Operational risk refers to the risk of loss resulting from the failure or inadequacy of internal systems and processes, or from external events that may negatively impact the credit union. These risks are carefully managed under Prospera's enterprise risk management program.