MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management's discussion and analysis ("MD&A") of financial condition and results of operations is prepared as of February 23, 2016. This discussion should be read in conjunction with the audited consolidated financial statements and accompanying notes of First National Financial Corporation (the "Company" or "Corporation" or "First National") as at and for the year ended December 31, 2015. The audited consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS").

This MD&A contains forward-looking information. Please see "Forward-Looking Information" for a discussion of the risks, uncertainties and assumptions relating to these statements. The selected financial information and discussion below also refer to certain measures to assist in assessing financial performance. These other measures such as "Pre-FMV EBITDA" and "After tax Pre-FMV Dividend Payout Ratio" should not be construed as alternatives to net income or loss or other comparable measures determined in accordance with IFRS as an indicator of performance or as a measure of liquidity and cash flow. These measures do not have standard meanings prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers.

Unless otherwise noted, tabular amounts are in thousands of Canadian dollars.

Additional information relating to the Company is available in First National Financial Corporation's profile on the System for Electronic Data Analysis and Retrieval ("SEDAR") website at www.sedar.com.

General Description of the Company

First National Financial Corporation is the parent company of First National Financial LP ("FNFLP"), a Canadian-based originator, underwriter and servicer of predominantly prime residential (single-family and multi-unit) and commercial mortgages. With over $93 billion in mortgages under administration ("MUA"), First National is Canada's largest non-bank originator and underwriter of mortgages and is among the top three in market share in the mortgage broker distribution channel.

In 2013, First National consolidated its interest in First National Mortgage Investment Fund (the "Fund"), which it launched in late 2012. Although the Company only owns about 18% of the units issued by the Fund, because of its status as sole seller to the Fund and its rights as promoter, the application of IFRS suggests that First National exercises control over the Fund. The Fund was created to obtain economic exposure to a diversified portfolio of primarily commercial mezzanine mortgages. Through the Fund's consolidation, the Company has effectively taken on a portfolio of about $47 million (December 31, 2014 - $55 million) of mortgages. Because of the Company's small proportionate interest in the Fund's units, it has also recorded a $33 million (December 31, 2014 - $39 million) non-controlling interest in equity which offsets these assets.

2015 Results Summary

The Company is pleased with 2015 results. Single-family origination increased 3% compared to 2014 to a new annual record in spite of weakness in Alberta and Saskatchewan's economies. New commercial origination was very strong and increased by 19%. These volumes and consistent renewal rates enabled the Company to grow its MUA and build the value of its portfolio of securitized mortgages.

- MUA grew to $93.8 billion at December 31, 2015 from $85.9 billion at December 31, 2014, an increase of 9%; the growth from September 30, 2015, when MUA was $92.6 billion, represented an annualized increase of 5%;
- The Canadian single-family real estate market performed steadily in 2015 despite the oil-related slowdown evident in western Canada. Even with a decrease in origination of 11% out of its Calgary office, the Company increased national new single-family mortgage origination by 3% to $12.9 billion in 2015 from $12.5 billion in 2014. The commercial segment had a very strong year as volumes increased by 19%, from $3.7 billion in 2014 to over $4.4 billion in 2015. Together, overall origination for 2015 increased by 7% year over year;
- The Company also took advantage of opportunities in the year to renew $4.3 billion of single-family mortgages. In 2014, the Company renewed $3.4 billion of single-family mortgages. The growth is attributable to more mortgages up for renewal than in the prior year and slightly higher retention rates. For the commercial segment, renewals decreased to $0.9 billion from $1.3 billion as more borrowers elected to refinance with the Company at increased mortgage values on maturity. While this reduced renewal production, this trend was reflected in the higher new origination volumes noted above;
- Revenue for 2015 increased to $915.3 million from $803.1 million in 2014. The 14% increase is attributable to higher revenues from the Company's underwriting and fulfillment business offset by losses on financial instruments which decreased revenue by $17.2 million year over year. Placement fee revenue and Interest revenue – securitized mortgages also grew as the Company increased the volume of mortgages placed with institutions and its portfolio of securitized mortgages;
- Income before income taxes for the year increased by 6% from $140.3 million in 2014 to $148.7 million in 2015. The increase was achieved despite large changes in the capital markets, which negatively affected the Company's interest rate hedges and mortgages held at fair value in both years. The Company recorded losses of $52.1 million on financial instruments in 2015 in contrast to smaller losses on financial instruments of $34.9 million in 2014. The net change in losses on financial instruments between 2015 and 2014 decreased income before income taxes between the quarters by $17.2 million.
- Without the impact of gains and losses on financial instruments, the Company's earnings before income taxes, depreciation and amortization ("Pre-FMV EBITDA[1]") for 2015 increased by almost 15%, from $183.1 million in 2014 to $209.9 million in 2015. The increase was due primarily to increased earnings from securitization and the transition to profitability in the new underwriting and fulfilment processing services business.

The Company was very pleased with these results as the year progressed. In October 2015, announced that its Board of Directors approved an increase in the dividend on its common shares. Effective with the dividend paid on December 15, 2015, the annual dividend rate was increased from $1.50 per share to $1.55 per share, an increase of 3.3%.

Outstanding Securities of the Corporation

At December 31, 2015 and February 23, 2016, the Corporation had 59,967,429 common shares, 4,000,000 Class A preference shares, Series 1 and 175,000 April 2020 notes outstanding.

Selected Quarterly Information

Quarterly Results of First National Financial Corporation

($000s, except per share amounts)

	Revenue	Net Income (Loss) for the period	Pre-FMV EBITDA for the period (1)	Net Income (Loss) per Common Share	Total Assets
2015					
Fourth Quarter	$250,008	$41,084	$58,527	$0.66	$27,926,732
Third Quarter	$246,641	$29,308	$60,955	$0.46	$27,624,359
Second Quarter	$251,206	$42,538	$52,012	$0.68	$27,585,945
First Quarter	$167,460	($3,499)	$38,439	($0.09)	$26,638,048
2014					
Fourth Quarter	$198,254	$17,856	$43,229	$0.27	$25,953,914
Third Quarter	$230,552	$35,331	$50,121	$0.56	$25,077,361
Second Quarter	$201,596	$28,217	$48,392	$0.44	$23,902,513
First Quarter	$172,705	$23,061	$41,388	$0.35	$21,683,307

(1) This non-IFRS measure adjusts income before income taxes by adding back expenses for amortization of intangible and capital assets but it also eliminates the impact of changes in fair value by adding back losses on the valuation of financial instruments and deducting gains on the valuation of financial instruments.

With First National's large portfolio of mortgages pledged under securitization, quarterly revenue is driven primarily by the gross interest earned on the mortgages pledged under securitization. Servicing revenue will also change as the third-party portfolio of mortgages grows or contracts. The gross interest on the mortgage portfolio is dependent both on the size of the portfolio of mortgages pledged under securitization as well as weighted average mortgage rates. Although mortgage rates have declined recently, the Company has steadily increased MUA and its portfolio of securitized mortgages over the last 24 months. Net income is partially dependent on conditions in the debt markets, which affect the value of gains and losses on financial instruments arising from the Company's interest rate hedging program. Accordingly, the movement of this measurement between quarters is related to factors external to the Company's core business (primarily conditions in the bond markets). By removing this volatility and analyzing Pre-FMV EBITDA, management believes a more appropriate measurement of the Company's performance can be assessed.

Generally, in the last eight quarters, the Company has grown its origination volumes in order to build its servicing portfolio and to enable it to securitize larger amounts of mortgages in the NHA-MBS market. This longer-term strategy has been successful and Pre-FMV EBITDA grew steadily to over $209 million in 2015. Despite continued success in growing MUA and mortgage origination volume, tightening mortgage spreads over the past 5 years has reduced relative profitability of mortgages pledged for securitization and deferred placements fees. The table above shows a trend of growing income reflecting typical Canadian seasonality: slower first and fourth quarters and stronger mid-year quarters. In the first quarter of 2015, the surprise cut in the Bank of Canada's overnight rate on January 21, 2015, had a large, unfavourable effect on the Company's net income. Although the Company recorded growth in origination volumes and grew its MUA, the first quarter of 2015 featured large net losses on the fair value of financial instruments as bond yields fell. In the third and fourth quarters of 2015, the Company achieved the highest quarterly levels of Pre-FMV EBITDA since the Company began tracking this measure in 2012 due to a combination of steady origination and contributions from its third party underwriting and fulfillment services business.

Selected Annual Financial Information and Reconciliation to Pre-FMV EBITDA

($000s, except per share amounts)

	2015	2014	2013
For the Year ended December 31, Income Statement Highlights			
Revenue	915,315	803,107	776,508
Interest expense – securitized mortgages	(488,659)	(434,726)	(323,236)
Brokerage fees	(107,045)	(77,105)	(84,420)
Salaries, interest and other operating expenses	(161,821)	(143,062)	(127,404)
Add (deduct): realized and unrealized (gains) losses on financial instruments	52,143	34,916	(43,866)
Pre-FMV EBITDA[(1)]	209,933	183,130	197,582
Amortization of capital assets	(4,114)	(2,909)	(2,374)
Amortization of intangible assets	(5,000)	(5,000)	(5,563)
Add (deduct): realized and unrealized gains (losses) on financial instruments	(52,143)	(34,916)	43,866
Provision for income taxes	(39,245)	(35,840)	(61,410)
Net income	109,431	104,465	172,101
Dividends declared	95,101	93,602	90,294
Per Share Highlights			
Net income per common share	1.71	1.62	2.75
Dividends per common share	1.51	1.48	1.38
At Year End Balance Sheet Highlights Total assets	27,926,732	25,953,914	20,569,217
Total long-term financial liabilities	174,420	176,418	179,195

Notes:

(1) Pre-FMV EBITDA is not a recognized earnings measure under IFRS and does not have a standardized meaning prescribed by IFRS. Therefore, Pre-FMV EBITDA may not be comparable to similar measures presented by other issuers. Investors are cautioned that Pre-FMV EBITDA should not be construed as an alternative to net income or loss determined in accordance with IFRS as an indicator of the Company's performance or as an alternative to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows.

Vision and Strategy

The Company provides mortgage financing solutions to virtually the entire mortgage market in Canada. By offering a full range of mortgage products, with a focus on customer service and superior technology, the Company believes that it is the leading non-bank mortgage lender in the industry. Growth has been achieved while maintaining a relatively conservative risk profile. The Company intends to continue leveraging these strengths to lead the "non-bank" mortgage lending industry in Canada, while appropriately managing risk.

The Company's strategy is built on four cornerstones: providing a full range of mortgage solutions for Canadian single family and commercial customers; growing assets under administration; employing technology to enhance service to mortgage brokers and borrowers, lower costs and rationalize business processes; and maintaining a conservative risk profile. An important element of the Company's strategy is its direct relationship with the mortgage borrower. Although the Company places most of its originations with third parties, FNFLP is perceived by most of its borrowers as the mortgage lender. This is a critical distinction. It allows the Company to communicate with each borrower directly throughout the term of the related mortgage. Through this relationship, the Company can negotiate new transactions and pursue marketing initiatives. Management believes this strategy will provide long-term profitability and sustainable brand recognition for the Company.

Key Performance Drivers

The Company's success is driven by the following factors:

- Growth in the portfolio of mortgages under administration;
- Growth in the origination of mortgages;
- Lowering the costs of operations through the innovation of systems and technology; and
- Employing innovative securitization transactions to minimize funding costs.

Growth in Portfolio of Mortgages under Administration

Management considers the growth in MUA to be a key element of the Company's performance. The portfolio grows in two ways: through mortgages originated by the Company and through third-party mortgage servicing contracts. Mortgage originations not only drive revenues from placement and interest from securitized mortgages, but perhaps more importantly, longer-term value from servicing fees, mortgage administration fees, renewals and the growth of the customer base for marketing initiatives. As at December 31, 2015, MUA totalled $93.8 billion, up from $85.9 billion at December 30, 2014, an increase of 9%. This compares to $92.6 billion at September 30, 2015, representing an annualized increase of 5%.

Growth in Origination of Mortgages

The origination of mortgages not only drives the growth of MUA as described above, but leverages the Company's origination platform, which has a large fixed-cost component. As more mortgages are originated, the marginal costs of underwriting decrease. By growing origination, not only can the Company satisfy demand from its institutional customers, but it can also produce volume for its own securitization programs. Despite a decrease in origination of 11% out of its Calgary office, the Company exceeded the record origination experienced in 2014 by 3%. The commercial segment had a very strong year as volumes increased by 19%, from $3.7 billion in 2014 to $4.4 billion in 2015. Together, overall origination for 2015 increased by 7% year over year.

Mortgage Underwriting and Fulfillment Processing Services

Early in the third quarter of 2014, the Company entered into an agreement with a large Canadian schedule I bank ("Bank") to provide underwriting and fulfillment processing services for mortgages originated by the Bank through the single-family residential mortgage broker channel. Under the strategic agreement, First National employs a customized software solution based on its industry leading MERLIN technology to accept mortgage applications from the Bank in the mortgage broker channel and underwrite these mortgages in accordance with the Bank's underwriting guidelines. The Bank funds all the mortgages underwritten under the agreement and retains full responsibility for mortgage servicing and the client relationship. The new business was launched in Ontario in early 2015, western Canada in April 2015, and finally in Quebec in July 2015. Management considers the agreement a way to leverage the capabilities and strengths of First National in the mortgage broker channel and add some diversity to the Company's service offerings. In the third quarter of 2015, this business transitioned to profitability as volumes of mortgages underwritten increased with the summer season and operations normalized.

Lowering Costs of Operations

Innovations in Systems and Technology

The Company has always used technology to provide for efficient and effective operations. This is particularly true for its MERLIN underwriting system, Canada's only web-based, real-time broker information system. By creating a paperless, 24/7 commitment management platform for mortgage brokers, the Company is now ranked among the top three lenders by market share in the broker channel. This has translated into increased single-family origination volumes and higher closing ratios (the percentage of mortgage commitments the Company issues that actually become closed mortgages).

Bank Credit Facility

The Company uses a $1 billion revolving line of credit with a syndicate of banks. This facility enables the Company to fund the increasing amount of mortgages accumulated for securitization. The entire facility is floating rate and has a five-year term. The Company has elected to undertake this debt for a number of reasons: (1) the transaction increases the amount of debt available to fund mortgages originated for securitization purposes; (2) the debt is revolving and can be used and repaid as the Company requires, providing more flexibility than the Senior Unsecured Notes, which are fully drawn during their term; (3) the five-year term extension gives the Company a committed facility for the medium term; and (4) the cost of borrowing reflects the Company's BBB issuer rating.

Note Issuance

On April 6, 2015, the Company issued 175,000 4.01% Series 1 Senior Unsecured Notes due April 9, 2020 pursuant to a private placement under an offering memorandum. The net proceeds of the offering, after broker commissions, of $174.3 million were invested in FNFLP. On settlement, the proceeds were used to repay a portion of the outstanding amount drawn on the bank credit facility. On May 7, 2015, the Company drew on the bank credit facility to repay the maturing 5.07% $175 million debenture. Effectively the new note issuance has replaced the funding provided by the maturing debenture. Unlike the debenture which was secured on a pari passu basis with the bank syndicate, the newly issued notes are unsecured and can be invested in FNFLP such that the amount will qualify as "net worth" which allows the Company to increase the amount of NHA MBS it can issue under CMHC guidelines. Accordingly, the Company considers these funds to represent a source of capital to fund the upfront investment required by its securitization program. The 5.07% debenture was used primarily to fund mortgages in the holding period prior to securitization.

Employing Securitization Transactions to Minimize Funding Costs

Approval as both an Issuer of NHA-MBS and Seller to the Canada Mortgage Bonds Program

The Company has been involved in the issuance of NHA-MBS since 1995. In December 2007, the Company was approved by Canada Mortgage and Housing Corporation ("CMHC") as an issuer of NHA-MBS and as a seller into the CMB program. Issuer status has provided the Company with a funding source that it can access independently. Perhaps more importantly, seller status for the CMB gives the Company direct access to the CMB. Generally, the demand for high-quality fixed and floating rate investments increased significantly with the economic turmoil in 2009. This demand has continued into 2015 and allowed the Company to issue almost $6.4 billion of mortgages through the NHA-MBS and CMB programs during the year. In August 2013, CMHC announced that it would be limiting the amount of guarantees it would issue on NHA-MBS pools created for sale to the "market". CMHC indicated that the amount of guarantees it was providing for such market pools (generally any pool not sold to the Canada Housing Trust ("CHT") for the CMB) was growing significantly. In order to better control the absolute amount of risk that it takes on in this respect, CMHC has implemented policies to allocate the amount of guarantees to issuers. The current amount being allocated to First National is approximately the amount that the Company used in 2015. These rules are similar to the CMB allocation rules described below, which have been in place since 2008 and are subject to change each year.

Mortgage spreads can be illustrated by comparing posted five-year fixed single-family mortgage rates to a similar-term Government of Canada bond as listed in the table below.

Period	Average five year Mortgage Spread for the Period
2006	1.12%
2007	1.50%
2008	2.68%
2009	1.76%
2010	1.75%
2011	1.76%
2012	1.92%
2013	1.75%
2014	1.57%
2015	1.87%

The table shows an average spread of 1.12% in 2006. With the credit crisis, this spread ballooned to as high as 3.46% in 2008. Between 2009 and 2011, liquidity issues at financial institutions diminished and the competition for mortgages increased such that spreads remained consistently higher than pre-crisis levels. In mid-2011, the United States credit rating was downgraded and interest rates fell significantly, accounting for wider mortgage spreads in 2012 which tightened again in 2013. In 2014, more competitive pressures took mortgage rates lower and compressed mortgage spreads to 2007 levels. To begin 2015, mortgage spreads quickly widened as a slowdown in economic growth and the Bank of Canada rate cut have reduced bond yields dramatically. This trend continued through to the end of the year as economic indicators continued to decline such that as at December 31, 2015, the spread widened to 1.87%. While funding spreads have also moved out, spreads are wide enough to support the Company's securitization program. In 2015, the Company originated and renewed for securitization purposes approximately $6.7 billion of single-family mortgages and $1.7 billion of multi-unit residential mortgages in order to take advantage of these spreads. In 2015, the Company securitized through NHA-MBS approximately $2.0 billion of floating rate single-family mortgages, $3.7 billion of fixed rate single-family mortgages and $0.6 billion of fixed rate multi-unit residential mortgages.

Canada Mortgage Bonds Program

The CMB program is an initiative sponsored by CMHC whereby the CHT issues securities to investors in the form of semi-annual interest-yielding five- and 10-year bonds. Pursuant to the Company's approval as a seller into the CMB, the Company is able to make direct sales into the program. Because of the similarities to a traditional Government of Canada bond (both have five- and 10-year non-amortizing terms and a federal government guarantee), the CMB trades in the capital markets at a modest premium to the yields on Government of Canada bonds. The ability to sell into the CMB has given the Company access to lower costs of funds on both single-family and multi-family mortgage securitizations. The Company also enjoys demand for mortgages from investment dealers who sell directly into the CMB. Because of the effectiveness of the CMB, there have been requests from approved CMB sellers for larger issuances. CHT has indicated that it will not unduly increase the size of its issuances and has created guidelines through CMHC that limit the amount that can be sold by each seller into the CMB each quarter. The Company is subject to these limitations.

Key Performance Indicators

The principal indicators used to measure the Company's performance are:

- Earnings before income taxes, depreciation and amortization, and losses and gains on financial instruments ("Pre-FMV EBITDA" (1)) ; and

- Dividend payout ratio.

Pre-FMV EBITDA is not a recognized measure under IFRS. However, management believes that Pre-FMV EBITDA is a useful measure that provides investors with an indication of income normalized for capital market fluctuations and prior to capital expenditures. Pre-FMV EBITDA should not be construed as an alternative to net income determined in accordance with IFRS or to cash flows from operating, investing and financing activities. The Company's method of calculating Pre-FMV EBITDA may differ from other issuers and, accordingly, Pre-FMV EBITDA may not be comparable to measures used by other issuers.

	Quarter ended		**Year ended**	
	December 31, 2015	**December 31, 2014**	**December 31, 2015**	**December 31, 2014**
For the Period		**($ 000's)**		
Revenue	250,008	198,254	915,315	803,107
Income before income taxes	56,384	23,206	148,676	140,305
Pre-FMV EBITDA (1)	58,527	43,229	209,933	183,130
At Period end				
Total assets	27,926,732	25,953,914	27,926,732	25,953,914
Mortgages under administration	93,829,513	85,889,561	93,829,513	85,889,561

Note:

(1) This non-IFRS measure adjusts income before income taxes by adding back expenses for amortization of intangible and capital assets but it also eliminates the impact of changes in fair value by adding back losses on the valuation of financial instruments and deducting gains on the valuation of financial instruments.

Since going public in 2006, First National has been considered a high-yielding dividend paying company. Over this period, the Company has paid almost $800 million of dividends/distributions to common shareholders/ unitholders. With a large MUA which generates continuing income and cash flow and a business model which is designed to make efficient use of capital, the Company has been able to pay distributions to its shareholders which represent a relatively large ratio of its earnings. The Company calculates the dividend payout ratio as dividends declared on common shares over net income attributable to common shareholders. This measure is useful to shareholders as it indicates the percentage of earnings which have been paid out in dividends. Similar to the performance measure for earnings, the Company also calculates the dividend payout ratio on a basis using after tax Pre-FMV EBITDA.

Determination of Common Share Dividend Payout Ratio

	Quarter ended		Year ended	
	December 31, 2015	**December 31, 2014**	**December 30, 2015**	**December 31, 2014**
For the Period	**($ 000's)**			
Net income attributable to common shareholders	39,387	16,018	102,468	97,060
Dividends paid or declared on common shares	22,988	22,488	90,451	88,952
Common Share Dividend Payout Ratio	58%	140%	88%	92%
After tax Pre-FMV Dividend Payout Ratio (1)	59%	76%	64%	72%

Note:

(1) This non-IFRS measure adjusts the net income used in the calculation of the dividend payout ratio to after tax Pre-FMV earnings so as to eliminate the impact of changes in fair value by adding back losses on the valuation of financial instruments and deducting gains on the valuation of financial instruments. The Company uses its aggregate effective tax rate to tax affect the impact of the valuation of financial instruments on this ratio.

For the year ended December 31, 2015, the common share payout ratio was 88% compared to 92% in 2014. In both 2015 and 2014, the Company recorded large losses on account of the fair value of financial instruments. These amounts are largely recorded in a period in which yields on Government of Canada bond yields changed; however, the offsetting economic impact is reflected in wider spreads on the mortgages pledged for securitization and will be generally realized in net interest margin over the terms of the mortgages. If the gains and losses on financial instruments in both years are excluded from the above calculations, the dividend payout ratio for 2015 would have been 64% compared to 72% in 2014.

The Company also paid $4.65 million of dividends on its preferred shares in 2015 and 2014.

Revenues and Funding Sources

Mortgage Origination

The Company derives a significant amount of its revenue from mortgage origination activities. Most mortgages originated are funded either by placement with institutional investors or through securitization conduits, in each case with retained servicing. Depending upon market conditions, either an institutional placement or a securitization conduit may be the most cost-effective means for the Company to fund individual mortgages. In general, originations are allocated from one funding source to another depending on market conditions and strategic considerations related to maintaining diversified funding sources. The Company retains servicing rights on virtually all of the mortgages it originates, which provide the Company with servicing fees to complement revenue earned through originations. For the year ended December 31, 2015, new origination volume increased from $16.2 billion to $17.3 billion, or about 7%, compared to 2014.

Securitization

The Company securitizes a portion of its origination through various vehicles, including NHA-MBS, CMB and Asset-backed Commercial Paper (“ABCP”). Although legally these transactions represent sales of mortgages, for accounting purposes they do not meet the requirements for sale recognition and instead are accounted for as secured financings. These mortgages remain as mortgage assets of the Company for the full term and are funded with securitization-related debt. Of the Company’s $22.5 billion of new originations and renewals for the year ended December 31, 2015, $8.4 billion was originated for its own securitization programs.

Placement Fees and Gain on Deferred Placement Fees

The Company recognizes revenue at the time that a mortgage is placed with an institutional investor. Cash amounts received in excess of the mortgage principal at the time of placement are recognized in revenue as “placement fees”. The present value of additional amounts expected to be received over the remaining life of the mortgage sold (excluding normal market-based servicing fees) is recorded as a “deferred placement fee”. A deferred placement fee arises when mortgages with spreads in excess of a base spread are sold. Normally the Company would earn an upfront cash placement fee, but investors prefer paying the Company over time as they earn net interest margin on such transactions. Upon the recognition of a deferred placement fee, the Company establishes a “deferred placement fee receivable” that is amortized as the fees are received by the Company. Of the Company's $22.5 billion of new originations and renewals in 2015, $13.5 billion was placed with institutional investors.

For all institutional placements and mortgages sold to institutional investors for the NHA-MBS market, the Company earns placement fees. Revenues based on these originations are equal to either (1) the present value of the excess spread, or (2) an origination fee based on the outstanding principal amount of the mortgage. This revenue is received in cash at the time of placement. In addition, under certain circumstances, additional revenue from institutional placements and NHA-MBS may be recognized as “gain on deferred placement fees” as described above.

Mortgage Servicing and Administration

The Company services virtually all mortgages generated through its mortgage origination activities on behalf of a wide range of institutional investors. Mortgage servicing and administration is a key component of the Company’s overall business strategy and a significant source of continuing income and cash flow. In addition to pure servicing revenues, fees related to mortgage administration are earned by the Company throughout the mortgage term. Another aspect of servicing is the administration of funds held in trust, including borrowers’ property tax escrows, reserve escrows and mortgage payments. As acknowledged in the Company’s agreements, any interest earned on these funds accrues to the Company as partial compensation for administration services provided. The Company has negotiated favourable interest rates on these funds with the chartered banks that maintain the deposit accounts, which has resulted in significant additional servicing revenue.

In addition to the interest income earned on securitized mortgages and deferred placement fees receivable, the Company also earns interest income on mortgage-related assets, including mortgages accumulated for sale or securitization, mortgage and loan investments and purchased mortgage servicing rights.

The Company provides underwriting and fulfilment processing services to a mortgage originator using the mortgage broker distribution channel. The Company earns a fee based on the dollar value of funded mortgages. These fees are recognized at the time a mortgage funds and is included in “Mortgage servicing income” in the consolidated statement of comprehensive income.

Results of Operations

The following table shows the volume of mortgages originated by First National and mortgages under administration for the periods indicated:

	Quarter ended		Year ended	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
	($ millions)			
Mortgage Originations by Segment				
New Single-family residential	2,921	2,860	12,880	12,525
New Multi-unit and commercial	1,266	1,195	4,420	3,701
Sub-total	4,187	4,055	17,300	16,226
Single-family residential renewals	1,246	823	4,287	3,365
Multi-unit and commercial renewals	321	328	923	1,306
Total origination and renewals	5,754	5,206	22,510	20,897
Mortgage Originations by Funding Source				
Institutional investors – new residential	2,224	1,434	8,350	6,323
Institutional investors – renew residential	436	372	1,827	1,700
Institutional investors – multi/commercial	856	1,091	3,327	3,343
NHA-MBS/ CMB/ ABCP securitization	2,122	2,095	8,433	8,942
Internal Company resources /CMBS	116	214	573	589
Total	5,754	5,206	22,510	20,897
Mortgages under Administration				
Single-family residential	73,312	66,992	73,312	66,992
Multi-unit residential and commercial	20,518	18,898	20,518	18,898
Total	93,830	85,890	93,830	85,890

Total new mortgage origination volumes increased in 2015 compared to 2014 by 7%. Single-family volumes increased by 3% and commercial segment volumes increased by 19% year over year as demand for housing and commercial real estate continued and the Company increased its share in the mortgage broker channel. The growth rate was mitigated by lower volumes originated from the Company's Calgary office. These volumes were lower by 11% year over year as the turmoil associated with the rapid decline in the price of oil slowed the housing market in Alberta and Saskatchewan. When combined with renewals, total production increased from $20.9 billion in 2014 to $22.5 billion in 2015, or by 8%. The low interest rate environment which existed for most of 2014 continued in 2015, highlighted by the Bank of Canada's two reductions to its overnight rate. Low mortgage rates, which stimulate increased real estate transactions, together with the Company's expertise in mortgage underwriting, drove higher origination volumes. Origination for direct securitization into NHA-MBS, CMB and ABCP programs remained a large part of the Company's strategy with volumes of $8.4 billion in 2015, lower than the $8.9 billion originated in the 2014 year. The Company used more institutional placements in 2015 as demand from investors increased and securitization markets exhibited increased volatility with the recent economic uncertainty.

Net Interest - Securitized Mortgages

Comparing the year ended December 31, 2015 to the year ended December 31, 2014, "net interest – securitized mortgages" increased by 14% to $132.2 million from $115.5 million. The increase was due to a larger portfolio of securitized mortgages together with wider weighted-average spreads on the portfolio year over year. The portfolio of mortgages funded through securitization increased by 10% from $22.3 billion as at December 31, 2014 to $24.5 billion as at December 31, 2015. Although mortgage spreads have only recently widened, in 2014 and 2015 the Company experienced large losses on account of the financial instruments. These losses primarily comprise losses on short bonds used by the Company for its hedging program. As described below, the typical offset to these losses is wider mortgage spreads, which the Company earns in net interest on securitized mortgages over their terms. The result of these wider spreads can now be seen in the Company's net interest – securitized mortgages revenue. Net interest is also affected by the amortization of deferred origination and other costs that are capitalized on securitized mortgages.

Placement Fees

Placement fee revenue increased by 30% to $165.7 million from $127.1 million in 2014. New residential origination volume for institutional customers, excluding renewals, increased from $6.32 billion in 2014 to $8.35 billion in 2015 or by 32%. The year-over-year change was also affected by renewal related placement fees and commercial segment fees, both of which grew but not as much as fees related to new single-family origination.

Gains on Deferred Placement Fees

Gains on deferred placement fees revenue increased 6% to $11.1 million from $10.5 million. The gains relate to multi-unit residential mortgages originated and sold to institutional NHA-MBS issuers. Although volumes for these transactions decreased by 8% from 2014 to 2015, spreads on these transactions widened so that the Company realized higher per unit gains.

Mortgage Servicing Income

Mortgage servicing income increased 26% to $117.1 million from $93.1 million. This increase was due to revenue earned on the new underwriting and fulfillment processing services business which the Company launched in January 2015. Without this revenue, mortgage servicing income grew at a rate lower than the MUA growth of 9% as a result of the decline in the average per unit servicing fee. The decline is a consequence of lower fees charged to some of the largest residential investors which commenced in late 2013.

Mortgage Investment Income

Mortgage investment income decreased 8% to $52.8 million from $57.1 million. A portion of the decrease relates to a $2.5 million provision for loan loss on its portfolio of mortgage and loan investments which the Company has determined is required on four non-performing commercial mortgages. In 2014, the Company did not accrue any provision for loss. The decrease is also due to the Company's securitization program. As the Company elects to securitize, it funds mortgages accumulated for securitization and earns the mortgage interest rate income in the warehousing period prior to securitization. Generally mortgage rates have fallen between 2014 and 2015. Prevailing interest rates on five year closed mortgages were about 3.50% in mid-2014 compared to 2.65% in mid-2015. This decreases revenue on such mortgages. The decrease has been offset partially by greater revenue on the Company's performing mortgage and loan investments which have grown by over $15 million between December 2014 and 2015.

Realized and Unrealized Gains (Losses) on Financial Instruments

For First National, this financial statement line item typically consists of two components: (1) gains and losses related to the Company's economic hedging activities, and (2) gains and losses related to holding term assets derived using discounted cash flow methodology. Much like the short bonds that the Company uses for hedging, the term assets are affected by changes in credit markets and Government of Canada bond yields (which form the risk-free benchmarks used to price the Company's deferred placement fees receivable, and mortgages designated as held for trading). The following table summarizes these gains and losses by category in the periods indicated:

	Quarter ended		Year ended	
Summary of realized and unrealized gains (losses) on financial instruments	**December 31, 2015**	**December 31, 2014**	**December 31, 2015**	**December 31, 2014**
	($ 000's)			
Losses on short bonds used for the economic hedging program	(734)	(16,550)	(35,076)	(41,486)
Gains (losses) on mortgages held at fair value	1,050	(1,447)	18,642	15,733
Losses on interest rate swaps	(13)	(173)	(36,457)	(9,396)
Gains on deferred placement fees receivable	16	226	724	307
Other gains (losses)	11	(44)	24	(74)
Total losses on financial instruments	330	(17,988)	(52,143)	(34,916)

For 2015, negative economic news during the year meant 5-year bond yields decreased by about 0.60% in the year. 2014 also featured poor global economic sentiment and 5-year bond yields also fell by about 0.60%. For the Company, this meant the value of holding short bond positions as a hedge against its mortgages pending securitization decreased in both 2015 and 2014. Accordingly, the Company recorded significant net losses related to the valuation of these financial instruments in 2015 and 2014.

The Company uses short Government of Canada bonds (including CHT-issued bonds) together with repurchase agreements to create forward interest rate contracts to hedge the interest rate risk associated with fixed rate mortgages originated for its own securitization programs. For accounting purposes, these do not qualify as interest rate hedges as the bonds used are not derivatives but cash-based financial instruments. These gains or losses are recorded in the period in which the bond yields change; however, the offsetting economic gains or losses are not recorded in the same period. Instead, the resulting economic gain (or loss) will be reflected primarily in wider or narrower spreads on the mortgages pledged for securitization and will be realized in net interest margin over the terms of the mortgages and the related debts. In 2015, the Company recorded losses on these hedges of $35.1 million (2014 – $41.5 million). While these losses decreased the net income earned in 2015, the gross spread on the related portfolio of securitized mortgages going forward will be proportionally wider as the Company issues securitization-related debt at lower relative interest rates than it would have prior to the movement in bond yields. In order to adequately hedge its interest rate exposure, the Company had more than $740 million of bonds sold short as at December 31, 2015.

The portion of the Company's mortgages which is held at fair value (primarily those funded through ABCP), was affected positively by the change in bond yields; however, these gains were offset by the widening of mortgage funding credit spreads experienced which negatively impacted these mortgages to a greater extent in 2015 than in the prior year such that these mortgages gained only $18.6 million of value (2014 - $15.7 million). The valuation of interest rate swaps, which were used to manage the interest rate exposure from fixed-rate mortgages in the ABCP portfolio, was negatively affected in both years by lower bond yields such that unrealized losses of $36.5 million (2014 - $9.4 million) were recorded.

Brokerage Fees Expense

Brokerage fees expense increased 39% to $107.0 million from $77.1 million. This increase is explained almost entirely by higher origination volumes of single-family mortgages for institutional investors, which increased by 32%. The expense also increased because of higher per unit broker fees and the costs of portfolio insurance, which both increased between 2% and 3% from 2014.

Salaries and Benefits Expense

Salaries and benefits expense increased 25% to $84.8 million from $67.6 million. The increase is due primarily to an increase in headcount and higher employee costs associated with the new third party underwriting business. The Company hired 117 employees during the fourth quarter of 2014 and the first half of 2015 for this business. Accordingly, the Company had about $8.8 million of direct salary-related expenses for this division in 2015 compared to $0.9 million in 2014. The increase is also the result of higher employee costs associated with commercial segment origination. The Company compensates its commercial sales staff with commissions based on the profitability of originated mortgages. Commercial origination, excluding renewals, increased by 19% from 2014 and the related compensation to sales staff increased by $3.1 million year over year. As at December 31, 2015, the Company had 915 employees, compared to 770 as at December 31, 2014. The growth in head count, excluding employees working in the third-party underwriting and fulfillment services business, was 7%. This growth largely reflected the need to meet the administrative demand associated with increased MUA, which grew by 9% year over year. Management salaries were paid to the two senior executives (Co-founders) who together control about 77% of the Company’s common shares. The current period expense is a result of the compensation arrangement executed on the closing of the initial public offering (“IPO”).

Interest Expense

Interest expense decreased 1% to $35.9 million from $36.3 million. As discussed in the “Liquidity and Capital Resources” section of this analysis, the Company warehouses a portion of the mortgages it originates prior to settlement with the ultimate investor or funding with a securitization vehicle. The Company used the senior unsecured note together with a $1 billion credit facility with a syndicate of banks and 30-day repurchase facilities to fund the mortgages during this period. The overall interest expense has decreased from the prior period due to falling interest rates as the prime lending rate of most banks was lowered from 3.0% to 2.70% during the year as a result of the cuts made by the Bank of Canada during 2015.

Other Operating and Amortization of Intangibles Expenses

Other operating and amortization of intangibles expenses increased 7% to $50.2 million from $47.1 million. The amortization of intangible assets recognized on the IPO was $5.0 million in each of 2015 and 2014. Other operating expenses increased by $4.3 million related to the costs of running the new third party underwriting department which launched in 2015. These expenses and general growth in operating costs associated with a larger MUA were offset by $3.6 million of lower hedge costs. These are costs the Company incurs to operate its economic hedging program. The costs are lower as a consequence of lower bond yields which generally decrease the costs of carrying the instruments used in the program.

Income before Income Taxes and Pre-FMV EBITDA

Income before income taxes increased 6% to $148.7 million from $140.3 million. There was an increase despite changes in the capital markets, which negatively affected the Company's interest rate hedges and the carrying values of certain mortgage assets in both 2015 and 2014. Income before income taxes was comparatively lower in 2015 than 2014 by $17.2 million because of the unfavourable change in losses on financial instruments. Pre-FMV EBITDA, which eliminates the impact of gains and losses on financial instruments, increased 15% to $209.9 million from $183.1 million. The increase was due primarily to: 1) the Company's decision to place more of its origination with institutional customers; and 2) the transition to profitability in its new underwriting and fulfillment services business. The Company earned more placement fees which translated to increased earnings as there is a fixed cost of operating the origination departments. With respect to the new third party underwriting services business, the third quarter confirmed the successful implementation of the Company's business model. With strong seasonal origination for this business in the third and fourth quarter of 2015, the Company surpassed break even volumes and the division contributed earnings to overall corporate profitability. In 2014, the start-up losses related to this business represented drag on the Company's consolidated earnings.

Provision for Income Taxes

The provision for taxes increased by 9% to $39.2 million from $35.8 million. The provision is higher due to the higher income earned in 2015 compared to the income recorded in 2014.

Operating Segment Review

The Company aggregates its business from two segments for financial reporting purposes: (i) Residential (which includes single-family residential mortgages); and (ii) Commercial (which includes multi-unit residential and commercial mortgages), as summarized below:

Operating Business Segments				
	Residential		Commercial	
	($000's except percent amounts)			
Quarter ended	**December 31, 2015**	**December 31, 2014**	**December 31, 2015**	**December 31, 2014**
Originations and renewals	17,167,524	15,889,345	5,343,080	5,007,918
Percentage change	*8.0%*		*6.7%*	
Revenue	706,040	608,471	209,275	194,636
Percentage change	*16.0%*		*7.5%*	
Income before income taxes	100,455	95,631	48,221	44,674
Percentage change	*5.0%*		*7.9%*	
Period ended	**December 31, 2015**	**December 31, 2014**	**December 31, 2015**	**December 31, 2014**
Identifiable assets	22,276,053	21,112,421	5,620,903	4,811,717
Mortgages under administration	73,311,858	66,991,706	20,517,771	18,897,855

Residential Segment

Overall residential origination including renewals increased by 8% between 2015 and 2014 while residential revenues increased by about 16%. Part of the change in revenue is due to the change in gains and losses on financial instruments. Excluding these changes, revenue increased by 19% as the Company's new third party underwriting and fulfillment began producing revenue in 2015. The increase in normalized revenue also includes growth in gross revenue from the securitization program. The net change in gains and losses on financial instruments of $22 million also affected net income before income taxes. Without the impact of this fair value change, net income before income taxes for the residential segment would have increased by 22% year over year, indicative of revenue growth and increased profitability from the Company's renewal pipeline. Together with the profits earned by the third party underwriting services business, income grew faster than revenue. Identifiable assets increased from December 31, 2014, as the Company added about $1.7 billion of net single-family mortgages to mortgages pledged under securitization. This increase was offset by a decrease of almost $600 billion of government bonds purchased under resale agreements for hedging purposes as the Company elected to place more of its origination with institutional customers and accordingly, reduced its short bond position.

Commercial Segment

2015 commercial revenues increased by about 8% from 2014, but increased by 5% if the impact of changes in gains and losses on the fair value of financial instruments are excluded. This difference is due largely to the provision for loss of $2.5 million which reduced mortgage investment income and falling interest rates which reduced gross securitization interest, mortgage interest earned on mortgages on the balance sheet and interest earned on funds held in trust. Although higher net revenue from the securitized mortgage portfolio in the Company's commercial segment and better spreads on deferred placement fees contributed to increase profits, without fair value amounts, net income before tax decreased by 3% year over year. This is the result of the provision for loss and more origination being securitized by the Company directly. This increases salary costs to in-house sales staff but produces very little profit in the year of securitization. Identifiable assets increased since December 31, 2014, as the Company added about $500 million of net commercial mortgages to mortgages pledged under securitization and increased the amount of government bonds purchased for hedging purposes by about $200 million.

Liquidity and Capital Resources

The Company's fundamental liquidity strategy has been to invest in prime Canadian mortgages. Management's belief has always been that these mortgages are considered "AAA" by investors and will always be well bid and highly liquid. This strategy proved effective during the turmoil experienced in 2007 through 2009, when capital markets retreated and only the highest-quality assets were bid. As the Company's results in those years demonstrated, First National had little trouble finding investors to purchase its mortgage origination at profitable margins. Originating prime mortgages also allows the Company to securitize in the capital markets; however, this activity requires significant cash resources to purchase and hold mortgages prior to arranging for term debt through the securitization markets. For this purpose, the Company uses the combination of the $175 million unsecured notes and the Company's revolving bank credit facility. This aggregate indebtedness is typically used to fund: (1) mortgages accumulated for sale or securitization, (2) the origination costs associated with securitization, and (3) mortgage and loan investments. The Company has a credit facility with a syndicate of eleven financial institutions for a total credit of $1 billion. This facility was extended in May 2015 for a five-year term maturing in May 2020. Bank indebtedness may also include borrowings obtained through overdraft facilities. At December 31, 2015, the Company entered into repurchase transactions with financial institutions to borrow $806 million related to $822 million of mortgages held in "mortgages accumulated for sale or securitization" on the balance sheet.

At December 31, 2015, outstanding bank indebtedness (excluding bank indebtedness at the Fund level) was $576.9 million (December 31, 2014 - $601.9 million). Together with the unsecured notes of $175 million (December 31, 2014 – debenture of $175 million), this "combined debt" was used to fund $675.3 million (December 31, 2014 - $690.2 million) of mortgages accumulated for sale or securitization. At December 31, 2015, the Company's other interest-yielding assets included: (1) deferred placement fees receivable of $38.2 million (December 31, 2014 – $34.6 million) and (2) mortgage and loan investments of $246.0 million (December 31, 2014 - $230.4 million). The difference between "combined debt" and the mortgages accumulated for sale or securitization funded by it, which the Company considers a proxy for true leverage, has increased between December 31, 2014 and December 31, 2015, and now stands at $76.0 million (December 31, 2014 – $86.7 million). This represents a debt-to-equity ratio of approximately 0.18 to 1, which the Company believes is conservative. This ratio decreased from December 31, 2014 when it was 0.21 to 1 as, generally, the Company reinvested retained earnings to reduce debt.

The Company funds a large portion of its mortgage originations for institutional placement on the same day as the advance of the related mortgage. The remaining originations are funded by the Company on behalf of institutional investors or pending securitization on the day of the advance of the mortgage. On specified days, sometimes daily, the Company aggregates all mortgages warehoused to date for an institutional investor and transacts a settlement with that institutional investor. A similar process occurs prior to arranging for term funding through securitization. The Company uses a portion of the committed credit facility with the banking syndicate to fund the mortgages during this warehouse period. The credit facility is designed to be able to fund the highest balance of warehoused mortgages in a month and is normally only partially drawn.

The Company also invests in short-term mortgages, usually for six- to 18-month terms, to bridge existing borrowers in the interim period between long-term financing solutions. The banking syndicate has provided credit facilities to partially fund these investments. As these investments return cash, it will be used to pay down this bank indebtedness. The syndicate has also provided credit to finance a portion of the Company's deferred placement fees receivable and the origination costs associated with securitization as well as other miscellaneous longer-term financing needs.

The Company uses ABCP as an efficient source of funding primarily for short term insured mortgages. In the May 2013 federal budget, the government announced it was going to take steps to limit the securitization of government insured mortgages to CMHC sponsored programs. As ABCP is not sponsored by CMHC, such a limitation would impact the Company. Almost two years after the announcement, legislation was passed and detailed transition information was published. With the change in the federal government, the legislation was reconfirmed in February 2016 with some delayed application dates. Generally, the regulations make mortgage default insurance invalid for single-family mortgages sold to non-CMHC sponsored securitizations after June 30, 2016. Accordingly, existing single-family mortgages in ABCP conduits as at June 30, 2016 can be funded by ABCP until their maturity, not to exceed 5 years. There is still discussion in the industry concerning the legislation; however if implemented as currently described, the new legislation would mean that the Company must find other funding sources for the insured mortgages it has historically funded with ABCP. The Company is considering various alternatives including whole loan sales and selling short term NHA-MBS pools to ABCP conduits. The Company may also adjust its renewal offering to provide incentives to borrowers to select five year terms as opposed to shorter terms. These alternatives may not be as economical to the Company as ABCP. A portion of the Company’s capital has been employed to support its ABCP and NHA-MBS programs, primarily to provide credit enhancements as required by rating agencies. The most significant portion of cash collateral is the investment made on behalf of the Company’s ABCP programs. As at December 31, 2015, the investment in cash collateral was $29.2 million (December 31, 2014 - $19.0 million).

The Company’s Board of Directors has elected to pay dividends, when declared, on a monthly basis on the outstanding common shares and on a quarterly basis on the outstanding preference shares. For purposes of the enhanced dividend tax credit rules contained in the *Income Tax Act* (Canada) and any corresponding provincial and territorial tax legislation, all dividends (and deemed dividends) paid by the Company to Canadian residents on both common and preference shares after December 31, 2010, are designated as "eligible dividends". Unless stated otherwise, all dividends (and deemed dividends) paid by the Company hereafter are designated as "eligible dividends" for the purposes of such rules. For the preference shares, the Company has elected to pay any tax under Part VI.1 of the *Income Tax Act*, such that corporate holders of the shares will not be required to pay tax under Part VI.1 of the *Income Tax Act* on dividends received on such shares.

Financial Instruments and Risk Management

The Company has elected to treat deferred placement fees receivable, certain mortgages pledged under securitization that have been funded with ABCP and NHA-MBS debt and several mortgages within mortgage and loan investments, as financial assets measured at “fair value through profit or loss” such that changes in market value are recorded in the consolidated statement of comprehensive income. Effectively, these assets are treated much like bonds earning the Company a coupon at the discount rates used by the Company. The discount rates used represent the interest rate associated with a risk-free bond of the same duration plus a premium for the risk/uncertainty of the asset’s residual cash flows. As rates in the bond market change, the carrying values of these assets will change. These changes may be significant (favourable and unfavourable) from quarter to quarter. The Company enters into fixed-for-float swaps to manage the interest rate exposure of fixed mortgages sold to ABCP conduits. These instruments will also be treated as fair value through profit or loss. While the Company has attempted to exactly match the principal balances of the fixed mortgages over the next five-year period to the notional swap values for the same period, there will be differences in these amounts. Any favourable or unfavourable amounts will be recorded in the consolidated statement of comprehensive income each quarter.

The Company believes its hedging policies are suitably designed such that the interest rate risk of holding mortgages prior to securitization is mitigated. From an accounting perspective, any gains or losses on these instruments are recorded in the current period, as the Company’s economic hedging strategy does not qualify as hedging for accounting purposes. The Company uses synthetic bond forwards (consisting of bonds sold short and bonds purchased under resale agreements) to manage interest rate exposure between the time a mortgage rate is committed to the borrower and the time the mortgage is transferred to the securitization vehicle and the matched term debt is arranged. As interest rates change, the value of these short bonds will vary inversely with the value of the related mortgages. As interest rates increase, a gain will be recorded on the bonds, which should be offset by a tighter interest rate spread between the interest rates on mortgages and the securitization debt. This spread will be earned over the term of the related mortgages. For single-family mortgages, primarily mortgages for the Company's own securitization programs, only some of the mortgage commitments issued by the Company eventually fund. The Company must assign a probability of funding to each mortgage in the pipeline and estimate how that probability changes as mortgages move through the various stages of the pipeline. The amount that is actually hedged is the expected value of mortgages funding within the next 120 days (120 days being the standard maximum rate hold period available for the mortgages). As at December 31, 2015, the Company had $413 million of notional forward bond positions related to its single-family programs. For multi-unit residential and commercial mortgages, the Company assumes all mortgages committed will fund and hedges each mortgage individually. This includes mortgages committed for the CMB program as well as mortgages for transfer to the Company's other securitization vehicles. As at December 31, 2015, the Company had entered into $332 million of notional value forward bond sales for this segment. The total net value of realized and unrealized gains and losses on account of all notional hedges pertaining to the period January 1, 2015 to December 31, 2015 was a $35.1 million loss. This amount has been included in revenue in the statement of comprehensive income.

The Company is party to two interest rate swaps that economically hedge the interest rate exposure related to certain mortgages held on the balance sheet that the Company has originated as replacement assets for its CMB activities. As at December 31, 2015, the aggregate notional value of these swaps was $26.8 million. During the year the value of these swaps did not change significantly. The swaps mature between December 2016 and June 2021.

As described above, the Company employs various strategies to reduce interest rate risk. In the normal course of business, the Company takes some credit spread risk. This is the risk that the credit spread at which a mortgage is originated changes between the date of commitment of that mortgage and the date of sale or securitization. This can be illustrated by the Company's experience with commercial mortgages originated for the CMBS market in the spring of 2007. These mortgages were originated at credit spreads designed to be profitable to the Company when sold to a bank-sponsored CMBS conduit. Unfortunately for the Company, when these mortgages funded, the CMBS market had shut down. The alternative to this channel was more expensive as credit spreads elsewhere in the marketplace for this type of mortgage had widened. The Company adjusted for market-suggested increases in credit spreads in 2007 and 2008, adjusting the value of the mortgages downward. In 2009, the economic environment remained weak but did not worsen from what it was at the end of 2008. Overall credit spreads stopped widening such that the Company applied the same spreads to these mortgages and the Company did not record any additional unrealized losses or gains related to credit spread movement. Despite entering into effective economic interest rate hedges, the Company's exposure to credit spreads remained. This risk is inherent in the Company's business model and cannot be economically hedged.

The same exposure to risk is inherent in the Company's securitization through ABCP. The Company is exposed to the risk that 30-day ABCP rates are greater than 30-day BA rates. Prior to the financial crisis, the Company considered this a low risk given the quality of the assets securitized, the amount of credit enhancements provided by the Company and the strong covenant of the bank-sponsored conduits with which the Company transacted. In 2008, 30-day ABCP traded at approximately 1.10 percentage points over BAs; but by the end of March 2011 and continuing until the current period, it was priced at a discount to BAs. At the same time the Company has leveraged on changing credit spreads. The success of this approach has been demonstrated through the increase in volume and profitability of the NHA-MBS program and significant increases in gains on deferred placement fees from the sale of prime insured mortgages. As at December 31, 2015, the Company had various exposures to changing credit spreads. In particular, in mortgages accumulated for sale or securitization, there were almost $1.5 billion of mortgages that are susceptible to some degree of changing credit spreads.

Capital Expenditures

A significant portion of First National's business model consists of the origination and placement or securitization of financial assets. Generally, placement activities do not require much capital investment as the Company acts primarily in the capacity of a broker. On the other hand, the undertaking of securitization transactions may require significant amounts of the Company's own capital. This capital is provided in the form of cash collateral, credit enhancements, and the upfront funding of broker fees and other origination costs. These are described more fully in the "Liquidity and Capital Resources" section above. For fixed assets, the business requires capital expenditures on technology (both software and hardware), leasehold improvements and office furniture. During the year ended December 31, 2015, the Company purchased new computers and office and communications equipment. In the long term, the Company expects capital expenditures on fixed assets will be approximately $4.0 million annually.

Summary of Contractual Obligations

The Company's long-term obligations include five- to 10-year premises leases for its six offices across Canada, and its obligations for the ongoing servicing of mortgages sold to securitization conduits and mortgages related to purchased servicing rights. The Company sells its mortgages to securitization conduits on a fully-serviced basis, and is responsible for the collection of the principal and interest payments on behalf of the conduits, including the management and collection of mortgages in arrears.

		Payments Due By Period			
	Total	0-1 Years	1-3 Years	4-5 Years	After 5 Years
			($000's)		
Lease Obligations	21,232	6,192	11,511	2,920	609

Critical Accounting Policies and Estimates

The Company prepares its financial statements in accordance with IFRS, which requires management to make estimates, judgments and assumptions that management believes are reasonable based upon the information available. These estimates, judgments and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates on historical experience and other assumptions that it believes to be reasonable under the circumstances. Management also evaluates its estimates on an ongoing basis. The significant accounting policies of First National are described in Note 2 to the Company's annual consolidated financial statements as at December 31, 2015. The policies which First National believes are the most critical to aid in fully understanding and evaluating its reported financial results include the determination of the gains on deferred placement fees and the impact of fair value accounting on financial instruments.

The Company uses estimates in valuing its gain or loss on the sale of its mortgages placed with institutions earning a deferred placement fee. Under IFRS, valuing a gain on deferred placement fees requires the use of estimates to determine the fair value of the retained interest (derived from the present value of expected future cash flows) in the mortgages. These retained interests are reflected on the Company's balance sheet as deferred placement fees receivable. The key assumptions used in the valuation of gains on deferred placement fees are prepayment rates and the discount rate used to present value future expected cash flows. The annual rate of unscheduled principal payments is determined by reviewing portfolio prepayment experience on a monthly basis. The Company uses different rates for its various programs, which average approximately 11% for single-family mortgages. The Company assumes there is virtually no prepayment on multi-unit residential fixed rate mortgages.

On a quarterly basis, the Company reviews the estimates used to ensure their appropriateness and monitors the performance statistics of the relevant mortgage portfolios to adjust and improve these estimates. The estimates used reflect the expected performance of the mortgage portfolio over the lives of the mortgages. The assumptions underlying the estimates used for the year ended December 31, 2015 continue to be consistent with those used for the year ended December 31, 2014 and the quarters ended September 30, June 30 and March 31, 2015.

The Company has elected to treat its financial assets and liabilities, including deferred placement fees receivable, specific mortgages pledged under securitization, some mortgage and loan investments and bonds sold short, at fair value through profit or loss. Essentially, this policy requires the Company to record changes in the fair value of these instruments in the current period's earnings. The Company's assets and liabilities are such that the Company must use valuation techniques based on assumptions that are not fully supported by observable market prices or rates in most cases. Much like the valuation of deferred placement fees receivable described above, the Company's method of determining the fair value of its securitized mortgages has a significant impact on earnings. The Company uses different prepayment rates for its various programs, which average approximately 10% for single-family mortgages. The Company assumes there is virtually no prepayment on multi-unit residential fixed rate mortgages. Actual prepayment experience has been consistent with these assumptions. The Company has also assumed discount rates based on Government of Canada bond yields plus a spread that the Company believes would enable a third party to purchase the mortgages and make a normal profit margin for the risk involved.

Future Accounting Changes

In July 2014, the IASB issued the final version of IFRS 9 – Financial Instrument, replacing IAS 39 and all previous versions of IFRS 9. This final version of IFRS 9 includes a logical model for classification and measurement, a single, forward-looking 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. Under this standard, financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. The accounting model for financial liabilities is largely unchanged from IAS 39 except for the presentation of the impact of own credit risk on financial liabilities which will be recognized in OCI, rather than in profit and loss as under IAS 39. The new general hedge accounting principles under IFRS 9 are aimed to align hedge accounting more closely with risk management. This new standard does not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness; however it is expected to provide more hedging strategies that are used for risk management to qualify for hedge accounting and introduce more judgment to assess the effectiveness of a hedging relationship.

IFRS 9 is mandatorily effective for annual periods beginning on or after January 1, 2018. The Company is in process of evaluating the impact of IFRS 9 on the Company's financial statements.

In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, replacing IAS 11 - Construction Contracts, IAS 18 - Revenue, IFRIC 13 - Customer Loyalty Programs, IFRIC 15 - Agreements for the Construction of Real Estate, IFRIC 18 - Transfer of Assets from Customers, and SIC 31 Revenue – Barter Transactions Involving Advertising Services. The standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step revenue recognition process to determine the nature, amount, timing and uncertainty of revenue and cash flows from the contracts with customers.

IFRS 15 is effective for fiscal years ending on or after December 31, 2018. The Company intends to adopt IFRS 15 in its financial statements for the annual period beginning on January 1, 2018 and is currently analyzing the impact on the Company's financial statements.

In January 2016, the IASB issued IFRS 16 - *Leases*, replacing IAS 17 - *Leases*. IFRS 16 requires lessees to recognize assets and liabilities for most leases instead of previous categories of finance leases, which are reported on the balance sheet, or operating leases, which are disclosed only in the notes to the financial statements, under IAS 17. IFRS 16 is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted for companies that also adopt IFRS 15. The Company is currently assessing the impact of this standard on the Company's consolidated financial statements.

Disclosure Controls and Internal Controls over Financial Reporting

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company in reports filed under Canadian securities laws is recorded, processed, summarized and reported within the time periods specified under those laws, and include controls and procedures that are designed to ensure that information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

As of December 31, 2015, management evaluated, under the supervision of and with the participation of the Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company's disclosure controls and procedures. Based on this evaluation, management concluded that the Company's disclosure controls and procedures, as defined by National Instrument 52-109, *Certification of Disclosure in Issuers' Annual and Interim Filings*, were effective as of December 31, 2015.

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with reporting standards; however, because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis.

Management evaluated, under the supervision of and with the participation of the Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company's internal control over financial reporting based on the criteria set forth in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") and, based on that evaluation, concluded that the Company's internal control over financial reporting was effective as of December 31, 2015 and that no material weaknesses have been identified in the Company's internal control over financial reporting as of December 31, 2015. No changes were made in the Company's internal controls over financial reporting during the year ended December 31, 2015 that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

Risks and Uncertainties Affecting the Business

The business, financial condition and results of operations of the Company are subject to a number of risks and uncertainties, and are affected by a number of factors outside the control of management of the Company. In addition to the risks addressed elsewhere in this discussion and the financial statements, these risks include: ability to sustain performance and growth, reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers, changes in interest rates, repurchase obligations and breach of representations and warranties on mortgage sales, risk of servicer termination events and trigger events on cash collateral and retained interests, reliance on multi-unit residential and commercial mortgages, general economic conditions, legislation and government regulation (including the policies set for mortgage default insurance companies), competition, reliance on mortgage insurers, reliance on key personnel and the ability to attract and retain employees and executives, conduct and compensation of independent mortgage brokers, failure or unavailability of computer and data processing systems and software, insufficient insurance coverage, change in or loss of ratings, impact of natural disasters and other events, and environmental liability. In addition, risks associated with the structure of the Company include those related to the dependence on FNFLP, leverage and restrictive covenants, dividends which are not guaranteed and could fluctuate with FNFLP's performance, restrictions on potential growth, the market price of the Company's shares, statutory remedies, control of the Company and contractual restrictions, and income tax matters. Risk and risk exposure are managed through a combination of insurance, a system of internal controls and sound operating practices. The Company's key business model is to originate primarily prime mortgages and find funding through various channels to earn ongoing servicing or spread income. For the single-family residential segment, the Company relies on independent mortgage brokers for origination and several large institutional investors for sources of funding. These relationships are critical to the Company's success. For a more complete discussion of the risks affecting the Company, reference should be made to the Company's Annual Information Form.

Forward-Looking Information

Forward-looking information is included in this MD&A. In some cases, forward-looking information can be identified by the use of terms such as ''may'', ''will'', ''should'', ''expect'', ''plan'', ''anticipate'', ''believe'', ''intend'', ''estimate'', ''predict'', ''potential'', ''continue'' or other similar expressions concerning matters that are not historical facts. Forward-looking information may relate to management's future outlook and anticipated events or results, and may include statements or information regarding the future financial position, business strategy and strategic goals, product development activities, projected costs and capital expenditures, financial results, risk management strategies, hedging activities, geographic expansion, licensing plans, taxes and other plans and objectives of or involving the Company. Particularly, information regarding growth objectives, any increase in mortgages under administration, future use of securitization vehicles, industry trends and future revenues is forward-looking information. Forward-looking information is based on certain factors and assumptions regarding, among other things, interest rate changes and responses to such changes, the demand for institutionally placed and securitized mortgages, the status of the applicable regulatory regime, and the use of mortgage brokers for single-family residential mortgages. This forward-looking information should not be read as providing guarantees of future performance or results, and will not necessarily be an accurate indication of whether or not, or the times by which, those results will be achieved. While management considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect. Forward-looking information is subject to certain factors, including risks and uncertainties, which could cause actual results to differ materially from what management currently expects. These factors include reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers, and changes in interest rates as outlined under ''Risk and Uncertainties Affecting the Business''. In evaluating this information, the reader should specifically consider various factors, including the risks outlined under ''Risk and Uncertainties Affecting the Business'', which may cause actual events or results to differ materially from any forward-looking information. The forward-looking information contained in this discussion represents management's expectations as of February 23, 2016, and is subject to change after such date. However, management and the Company disclaim any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as required under applicable securities regulations.

Outlook

Management is very pleased with both the MUA and origination growth in 2015. With higher origination levels and renewal volume, the Company was able to increase the volume it placed with institutional investors, and only reduce slightly the amount it retained for its securitization activities. Management is particularly pleased with the results from its underwriting and fulfillment processing services business which transitioned to profitability in the third quarter thanks to strong seasonal volumes and the execution of its business plan.

Looking forward, the Company expects the low interest rate environment, which was reinforced with January and July 2015 Bank of Canada rate cuts, to continue into 2016. Low rates will keep mortgage affordability at favourable levels and mitigate refinancing risk. The Company will focus on the significant value of renewal opportunities and its partnerships with institutional customers in order to maximize profitability. Management expects the Company to continue to generate cash flow from its $25 billion portfolio of mortgages pledged under securitization and $69 billion servicing portfolio that will maximize financial performance. First National also expects the underwriting and fulfillment processing services business to continue to add to earnings as mortgages processed increase in response to the Company's superior service levels to the mortgage broker distribution channel.