

FIRST NATIONAL

FINANCIAL CORPORATION



Report to Shareholders

Period Ended September 30, 2024

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FINANCIAL CORPORATION



Fellow Shareholders:

First National's performance for the three months ended September 30, 2024 is summarized below.

- Mortgages Under Administration increased 6% to a record \$150.6 billion from \$141.9 billion at September 20, 2023
- Revenue decreased 1% to \$560.4 from \$562.9 million a year ago
- Pre-FMV Income, a non-GAAP measure, was \$75.3 million, 21% lower than a year ago
- Net income was \$36.4 million (\$0.59 cents per share) compared to \$83.6 million (\$1.38 per share)
- Common share dividends paid or declared were \$36.7 million (payout ratio of 104%) compared to \$36.0 million (payout ratio of 44%) a year ago

Profitability reflected the effects of a challenging marketplace on mortgage originations and operating leverage and higher investments in direct securitization which benefits income in future periods. In the quarter, single family residential mortgage originations (including renewals) of \$6.7 billion were 20% below last year's levels, while commercial originations (including renewals) of \$2.7 billion were 17% lower.

Increase in Common Share Dividend

In issuing third quarter results, the Board of Directors announced an increase in the Company's monthly dividend to an annualized rate of \$2.50 per common share from \$2.45 per share annualized, effective with the payment on December 13, 2024, for shareholders of record November 29, 2024.

Special Dividend

The Board of Directors also announced a special dividend of \$0.50 per common share to be paid on December 13, 2024 to shareholders of record on November 29, 2024. This payment reflects the Board's determination that First National has generated excess capital in the past year and that the capital needed for near-term growth can be generated from current operations.

Looking Forward

With recent action by the Bank of Canada to reduce interest rates, First National experienced a 50% increase in single family residential mortgage commitments in the third quarter which should translate into new fundings in upcoming periods. Commercial mortgage originations are also expected to benefit from ongoing demand for insured financing within the multi-unit property sector. Please see the outlook in our MD&A for more information.

First National is well prepared to execute its business plan and is confident that its strong relationships with mortgage brokers, diverse funding sources, the value inherent in its mortgage renewal book and income and cash from its \$44 billion portfolio of mortgages pledged under securitization and \$104 billion servicing portfolio will serve it well in the future.

Yours sincerely,

Stephen Smith
Executive Chairman

Jason Ellis
President and Chief Executive Officer

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 October 29, 2024. This discussion should be read in conjunction with the unaudited interim condensed consolidated financial statements and accompanying notes of First National Financial Corporation (the "Company" or "Corporation" or "First National") as at and for the three months ended September 30, 2024. The unaudited interim condensed 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 Income" 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 more than \$150 billion in mortgages under administration ("MUA"), First National is one of Canada's largest non-bank originators and underwriters of mortgages and is among the top three lenders in market share in the mortgage broker distribution channel.

Third Quarter 2024 Results Summary

First National's performance in the third quarter of 2024 met management's expectations. Mortgages Under Administration (MUA) surpassed \$150 billion, despite a 19% decline in total mortgage originations, including renewals, compared to the prior year. Core operating profitability, measured by Pre-FMV Income⁽¹⁾, decreased by 21% from the third quarter of 2023 reflecting several factors including the impact of lower single-family origination volumes on placement fees; lower originations in third party underwriting and fulfillment processing services which affected mortgage servicing revenue and higher other operating expenses. Earnings were also affected by more direct securitization which delays the recognition of income to future periods.

The following summarizes performance of the Company's significant metrics:

- MUA grew to \$150.6 billion at September 30, 2024 from \$141.9 billion at September 30, 2023, an increase of 6%; growth from June 30, 2024, when MUA was \$148.2 billion, was 6% on an annualized basis.
- Total single-family mortgage origination, including renewals, was \$6.7 billion in the third quarter of 2024 compared to \$8.3 billion in 2023. The Company attributes the 20% decrease to increased competition in the mortgage broker distribution channel. In the past 12 months bank lenders in the channel offered discounted rates and large broker incentives. Commercial segment origination, including renewals, of \$2.7 billion was 17% lower than the \$3.3 billion originated in the 2023 third quarter primarily as a result of timing related to funding insured multi-unit mortgages and lower conventional mortgage activity. Year to date growth in commercial mortgage origination of 17% continued to be fueled by demand for high-quality insured multi-unit mortgage products. Total combined origination of \$9.4 billion was lower by 19% compared to a year ago.
- Revenue for the third quarter of 2024 decreased approximately 1% to \$560.4 million from \$562.9 million in the third quarter of 2023 largely reflecting changing interest rates. In 2024, monetary policy led to interest rate cuts. The related decline in bond yields resulted in the realization of about \$25.6 million of losses related to the Company's residential commitment hedging program. In the third quarter of 2023, bond yields increased, and the Company recorded gains of \$18.4 million. Without these changes, revenue grew by 8%, supported by higher revenue from a growing securitization portfolio and higher coupon rates.
- Income before income taxes was \$49.7 million in the third quarter of 2024 compared to \$113.8 million in the third quarter of 2023. The decrease included the effect of changing capital market conditions in both years. Excluding gains and losses related to financial instruments, earnings before income taxes and gains and losses on financial instruments ("Pre-FMV Income" ⁽¹⁾) for the third quarter 2024 decreased by 21% to \$75.3 million from \$95.5 million in the 2023 comparative quarter. This change was largely the result of lower single-family origination which negatively affected both placement fees and mortgage servicing revenue related to third-party underwriting services. Lower volumes reduced the Company's operating leverage in both departments compared to the prior year's quarter. The Company also invested more heavily in its direct securitization programs which delayed the recognition of revenue to future periods in contrast to the comparative quarter. Higher operating costs, particularly related to technology, further reduced earnings by about \$4.9 million.

The Company's Board of Directors announced an increase in First National's regular monthly common share dividend to an annualized rate of \$2.50 per share from \$2.45 per share effective with the dividend payable on December 13, 2024 and a special common share dividend in the amount of \$0.50 per share, payable on December 13, 2024, to shareholders of record on November 29, 2024. This special payment reflects the Board's determination that the Company has generated excess capital in the past year and that the capital needed for near-term growth can be generated from current operations.

(1) This non-IFRS measure adjusts income before income taxes by eliminating the impact of changes in fair value by adding back losses on the valuation of financial instruments (except those on mortgage investments) and deducting gains on the valuation of financial instruments (except those on mortgage investments). See Key Performance Indicators section in this MD&A.

Selected Quarterly Information

Quarterly Results of First National Financial Corporation

(\$000s, except per share amounts)

	Revenue	Net Income for the Period	Pre-FMV Income for the Period ⁽¹⁾	Net Income per Common Share	Total Assets
2024					
Third quarter	\$560,386	\$36,409	\$75,254	\$0.59	\$50,460,286
Second quarter	\$538,450	\$54,070	\$77,498	\$0.93	\$50,093,796
First quarter	\$518,045	\$49,892	\$62,745	\$0.82	\$45,765,958
2023					
Fourth quarter	\$503,441	\$44,245	\$77,125	\$0.72	\$45,957,399
Third quarter	\$562,861	\$83,630	\$95,456	\$1.38	\$45,176,543
Second quarter	\$525,897	\$89,194	\$89,854	\$1.47	\$46,417,841
First quarter	\$432,086	\$35,738	\$59,748	\$0.58	\$44,268,705
2022					
Fourth quarter	\$414,785	\$42,669	\$59,492	\$0.70	\$43,763,672

Reconciliation of Quarterly Determination of Pre-FMV Income

(\$000s, except per share amounts)

	Income before income tax for the Period	Add/ deduct Realized and unrealized losses (gains)	Deduct (losses), add gains related to mortgage investments	Pre-FMV Income for the Period ⁽¹⁾
2024				
Third quarter	\$49,689	\$25,565	\$—	\$75,254
Second quarter	\$73,490	\$4,008	\$—	\$77,498
First quarter	\$67,892	(\$5,147)	\$—	\$62,745
2023				
Fourth quarter	\$59,895	\$16,894	\$336	\$77,125
Third quarter	\$113,830	(\$18,435)	\$61	\$95,456
Second quarter	\$121,544	(\$31,690)	\$—	\$89,854
First quarter	\$48,638	\$11,110	\$—	\$59,748
2022				
Fourth quarter	\$58,269	\$1,353	(\$130)	\$59,492

- (1) This non-IFRS measure adjusts income before income taxes by eliminating the impact of changes in fair value by adding back losses on the valuation of financial instruments (except those on mortgage investments) and deducting gains on the valuation of financial instruments (except those on mortgage investments). See Key Performance Indicators section in this MD&A.

With First National's large portfolio of mortgages under administration, quarterly revenue is driven primarily by servicing income and the gross interest earned on mortgages pledged under securitization. The gross interest on the mortgage portfolio is dependent both on the size of the portfolio of mortgages pledged under securitization, as well as mortgage rates. Recently MUA has increased, and revenue followed. Net income is partially dependent on conditions in bond 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. By removing this volatility and analyzing Pre-FMV Income, management believes a more appropriate measurement of the Company's performance can be assessed.

In the past eight quarters, the Company experienced a relatively volatile economic environment. 2022 began with a positive economic outlook: there was a surplus of liquidity for investment in financial assets and origination volumes remained strong. However, late in the 2022 first quarter, risks associated with inflation became evident as wages and prices increased across the economy and companies competed for employees. The Bank of Canada moved quickly and continuously beginning on March 2, 2022, in an attempt to stem inflation. Short-term interest rates rose by 425 basis points between March 2022 and January 2023 to their highest level since 2011. While spreads on new mortgage originations widened somewhat, the Company faced the headwinds of a slowing housing market, and strong competition for customers such that it earned comparatively lower Pre-FMV Income ⁽¹⁾. 2023 featured a return to a more stable housing environment: mortgage rates stabilized, and consumer confidence returned. In general, despite two more increases from the Bank of Canada, there was a sequential improvement in mortgage origination volumes between the first and third quarters of 2023. The fourth quarter was softer as economic indicators turned more negative. The resulting operational efficiency from solid origination levels and the record MUA, translated to higher Pre-FMV Income⁽¹⁾. 2024 began with increased competition, particularly in the mortgage broker distribution channel which negatively affected origination and reduced the Company's operational leverage.

Outstanding Securities of the Corporation

At September 30, 2024 and October 29, 2024, the Corporation had outstanding: 59,967,429 common shares; 2,984,835 Class A preference shares, Series 1; 1,015,165 Class A preference shares, Series 2; 200,000 November 2024 senior unsecured notes; 200,000 November 2025 senior unsecured notes; 200,000 September 2026 unsecured notes; and 200,000 November 2027 senior unsecured notes.

Selected Annual Financial Information and Reconciliation to Pre-FMV Income⁽¹⁾

(\$000s, except per share amounts)

	2023	2022	2021
For the Year Ended December 31,			
Income Statement Highlights			
Revenue	2,024,285	1,574,293	1,394,606
Interest expense – securitized mortgages	(1,119,475)	(739,295)	(630,279)
Brokerage fees	(139,199)	(173,290)	(201,786)
Salaries, interest and other operating expenses	(421,704)	(392,626)	(298,720)
Add (deduct): realized and unrealized losses (gains) on financial instruments	(22,121)	(59,610)	(5,815)
Add (deduct): unrealized gains (losses) regarding mortgage investments	397	(710)	(730)
Pre-FMV Income ⁽¹⁾	322,183	208,762	257,276
Add (deduct): realized and unrealized gains (losses) on financial instruments excluding those on mortgage investments	21,785	60,320	6,545
Provision for income taxes	(91,100)	(71,350)	(69,260)
Net income	252,807	197,732	194,561
Common share dividends declared	189,397	141,423	210,885
Per Share Highlights			
Net income per common share	4.15	3.25	3.20
Dividends per common share	3.16	2.36	3.52
At Year End			
Balance Sheet Highlights			
Total assets	45,957,399	43,763,672	42,274,158
Total long-term financial liabilities	598,745	399,222	398,888

Note:

- (1) Pre-FMV Income is not a recognized earnings measure under IFRS and does not have a standardized meaning prescribed by IFRS. Therefore, Pre-FMV Income may not be comparable to similar measures presented by other issuers. Investors are cautioned that Pre-FMV Income 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 the residential and commercial mortgage markets 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 a leading non-bank mortgage lender. 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 business processes and service to mortgage brokers and borrowers; and maintaining a conservative risk profile. An important element of the Company's strategy is its direct relationship with mortgage borrowers. The Company is considered 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;
- Raising capital for operations; 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, create longer-term value from servicing rights, renewals and growth in the customer base for marketing initiatives. As at September 30, 2024, MUA totalled \$150.6 billion, up from \$141.9 billion at September 30, 2023, an increase of 6%. The growth of MUA in the third quarter of 2024 was also 6% on an annualized basis.

Growth in Origination of Mortgages

Direct Origination by the Company

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. Increased origination satisfies demand from institutional customers and produces volume for the Company's own securitization programs. In the third quarter of 2024, the Company's single-family origination decreased by 20% compared to 2023's third quarter. The Company believes this is the result of increased competition. The commercial segment continued to perform well despite changing market conditions. Total commercial volumes were \$2.7 billion in the quarter compared to \$3.3 billion in the third quarter of 2023, a decrease of 17%. On a combined basis, overall origination in third quarter 2024 was about 19% lower than the 2023 third quarter.

Third-Party Mortgage Underwriting and Fulfilment Processing Services

In 2015, the Company launched its third-party underwriting and fulfilment processing services business with a large Canadian Schedule I bank ("Bank"). This business is designed to adjudicate mortgages originated by the Bank through the single-family residential mortgage broker channel. 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. 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 late 2019 and 2023, the Company entered into similar agreements with two other Canadian banks.

Excalibur Mortgage Products

The Company originates alternative single-family (“Excalibur”) mortgage products. Alternative lending describes single-family residential mortgages that are originated using broader underwriting criteria than those applied in originating prime mortgages. These mortgages generally have higher interest rates than prime mortgages. First National’s relationships with mortgage brokers and its underwriting systems allow for cost effective origination of significant volumes. The product is originated primarily for placement with institutional investors, but beginning in April 2019, the Company finalized an agreement with a bank-sponsored securitization conduit to fund a portion of Excalibur origination. In early 2020, an agreement was reached with another bank-sponsored conduit to provide additional funding for this product. Excalibur was rolled out gradually, beginning in Ontario. Currently the program originates the majority of its mortgages in Ontario with a growing presence in Western Canada.

Raising Capital for Operations

Bank Credit Facility

The Company’s \$1.5 billion revolving line of credit with a syndicate of banks enables it to fund the large amounts of mortgages accumulated for securitization. In the second quarter of 2024, the Company extended the term of the facility by another year to mature in March 2029. The facility bears interest at floating rates. The Company has elected to undertake this debt for a number of reasons: (1) the facility provides the amount of debt required 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 senior unsecured notes, which are fully drawn during their term; (3) the five-year remaining term 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 1, 2024, 200,000 new Series 5 notes were issued at a coupon of 6.261% for a three-year 7-month term maturing November 1, 2027. These notes add to the Company’s 2023 issuance of 200,000 7.293% Series 4 senior unsecured notes, 2020’s issuance of 200,000 2.961% Series 3 senior unsecured notes and 2019’s issuance of 200,000 3.582% Series 2 senior unsecured notes. The net proceeds of these issuances, after broker commissions, were invested in FNFLP. On settlement, the proceeds were used to pay down a portion of the indebtedness under the bank credit facility. The Company’s medium-term debt capital now stands at approximately \$800 million. The notes issued in April 2024 provide the Company with liquidity to fund the 2019 issued notes which mature on November 25, 2024.

Preferred Share Issuance

Effective April 1, 2021, pursuant to the original prospectus, the Company reset the annual dividend rate on its outstanding Class A Series 1 preference shares to 2.895% for a five-year term to March 31, 2026. After the exercise of shareholder conversion rights in March 2021, there were 2,984,835 Class A Series 1 shares outstanding and 1,015,165 Class A Series 2 outstanding. The Series 2 shares bear a floating rate dividend calculated quarterly based on the 90-day T-Bill rate. Both the Series 1 and Series 2 shares pay quarterly dividends, subject to Board of Directors approval, and are redeemable at the discretion of the Company such that after each five-year term ending on March 31, the Company can choose to extend the shares for another five-year term at a fixed spread (2.07%) over the relevant index (five-year Government of Canada bond yield for any Series 1 shares or the 90-day T-Bill rate for any Series 2 shares). While investors in these shares have an option on each five-year anniversary to convert their Series 1 preference shares into Series 2 preference shares (and vice versa), there is no provision of redemption rights to these shareholders. As such, the Company considers these shares to represent a permanent source of capital.

Employing Securitization Transactions to Minimize Funding Costs

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

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 Canada Mortgage Bonds (“CMB”) program. Issuer status provides the Company with direct and independent access to reliable and low-cost funding. Insured mortgage spreads can be illustrated by comparing insured posted five-year fixed single-family mortgage rates to a similar term five-year Government of Canada bond as listed in the table below.

Period	Period end Five-Year Insured Mortgage Spread by Quarter
Q4 2022	1.48%
Q1 2023	1.62%
Q2 2023	1.65%
Q3 2023	1.59%
Q4 2023	2.07%
Q1 2024	1.46%
Q2 2024	1.38%
Q3 2024	1.65%

Generally, when this spread is wider, the Company can earn higher returns from its securitization activities, although credit spreads and program fees observed in mortgage securitization markets also affect profitability. In 2022 and through 2023, spreads widened in response to the Bank of Canada’s (“BoC”) interest rate policy announcements and an increase in general economic uncertainty. To start 2024, spreads tightened as renewed competition in the mortgage broker market took mortgage rates lower. More recently with 0.75% of aggregate overnight rate cuts by the BoC, mortgage spreads have widened as mortgage rates did not decrease as quickly as bond rates. In the third quarter of 2024, the Company originated and renewed approximately \$3.8 billion of single-family and multi-unit residential mortgages for securitization purposes.

The Company is subject to various regulations put in place by CMHC. These rules include the amount of CMHC guarantees issued which are required to issue a pool. Currently there is a tiered NHA-MBS guarantee fee pricing structure, such that any guarantees issued to one issuer over \$9.0 billion of issuance have a higher price. The tiered limit of \$9.0 billion remains unchanged for 2024. In July 2022, CMHC issued new rules related to the allocation of NHA-MBS guarantee fees between “lenders” and “aggregators”. These rules commenced in the latter part of 2023 through a transition period. CMHC indicated in 2023 that these rules may be subject to further clarification. While these rules have not yet impacted the Company’s ability to place mortgages with its existing institutional customers, the rules will have an ongoing impact on the amount of NHA MBS that issuers can create.

Canada Mortgage Bonds Program

The CMB program is an initiative where Canada Housing Trust (“CHT”) issues securities to investors in the form of semi-annual interest-yielding 5 and 10-year bonds. As a seller into the CMB, the Company is able to make direct sales of NHA MBS into the program. 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. Because of the effectiveness of the CMB, many institutions have indicated their desire to participate. As a result, CHT 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. CMHC has indicated there may be modifications which may reduce the amounts which the Company’s can sell into 10-year CMB. After the federal government reviewed the CMB program in 2023, it announced in September 2023 that the annual limit for Canada Mortgage Bonds would increase to \$60 billion from \$40 billion such that the \$20 billion increase is dedicated to multi-family pools. At the same time, CMHC increased available NHA MBS guarantees from \$150 billion to \$170 billion for 2024 to mirror the additional CMB capacity.

Key Performance Indicators

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

- Earnings before income taxes and losses and gains on financial instruments, with the exception of any losses or gains related to mortgage investments ("Pre-FMV Income"⁽¹⁾); and
- Dividend payout ratio.

Beginning in 2020, the Company presented Pre-FMV Income⁽¹⁾ as a key performance indicator. This non-IFRS measure adjusts the Company's earnings by excluding gains and losses related to the fair value of financial instruments. Pre-FMV Income is not recognized under IFRS. However, management believes that Pre-FMV Income is a useful measure that provides investors with an indication of income normalized for capital-market fluctuations. Pre-FMV Income 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 Income may differ from other issuers and, accordingly, Pre-FMV Income may not be comparable to measures used by other issuers.

	Quarter ended		Nine months ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
For the Period				
Revenue	560,386	562,861	1,616,881	1,520,844
Income before income taxes	49,689	113,830	191,071	284,012
Pre-FMV Income ⁽¹⁾	75,254	95,456	215,497	245,058
At Period End				
Total assets	50,460,286	45,176,543	50,460,286	45,176,543
Mortgages under administration	150,568,194	141,915,465	150,568,194	141,915,465

- (1) This non-IFRS measure adjusts income before income taxes by eliminating the impact of changes in fair value by adding back losses on the valuation of financial instruments (except those on mortgage investments) and deducting gains on the valuation of financial instruments (except those on mortgage investments).

Since going public in 2006, First National has been considered a high-yielding, dividend-paying company. With a large MUA that generates continuing income and cash flow and a business model that is designed to make efficient use of capital, the Company has been able to pay distributions to its shareholders that 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 paid out as dividends. Similar to the performance measurement for earnings, the Company also calculates the dividend payout ratio on a basis using after-tax Pre-FMV Income.

Determination of Common Share Dividend Payout Ratio

	Quarter Ended		Nine months Ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
For the Period	(\$000s)			
Net income attributable to common shareholders	35,426	82,666	137,414	205,710
Total dividends paid or declared on common shares	36,730	35,980	110,190	107,941
Total common share dividend payout ratio	104%	44%	80%	52%
After-tax Pre-FMV dividend payout ratio ⁽¹⁾	68%	52%	71%	61%

Note:

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

For the quarter ended September 30, 2024, the total common share payout ratio was 104% compared to 44% for the quarter ended September 30, 2023. However, in both years, the Company recorded gains and losses on changes in fair value of financial instruments. Gains and losses are recorded in the period in which the prices on Government of Canada bonds change; however, the offsetting economic impact is generally reflected in narrower or wider spreads in the future once the mortgages have been pledged for securitization. Accordingly, management does not consider such gains and losses to affect its dividend payment policy in the short term. If the gains and losses on financial instruments in the two quarters are excluded from the above calculations, the regular dividend payout ratio for the third quarter of 2024 would have been 68% compared to 52% in the 2023 quarter.

The Company also paid \$1.0 million of dividends on its preferred shares in the third quarter of 2024 which was the same amount paid in the 2023 quarter.

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. In general, originations are allocated from one funding source to another depending on different criteria, including type of mortgage and securitization limits, with an overall consideration related to maintaining diversified funding sources. The Company retains servicing rights on virtually all the mortgages it originates. This provides the Company with servicing fees to complement revenue earned through originations. For the quarter ended September 30, 2024, origination volume decreased to \$9.4 billion from \$11.6 billion, or about 19% compared to the 2023 quarter.

Securitization

The Company securitizes a portion of its origination through various vehicles, including NHA-MBS, CMB and asset-backed commercial paper (“ABCP”). Although these transactions legally 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 \$9.4 billion of originations in the third quarter of 2024, \$3.8 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 placed. 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 \$9.4 billion of originations in the third quarter of 2024, \$5.4 billion was placed with institutional investors.

For all institutional placements, 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 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 two mortgage originators 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 are included in “Mortgage servicing income” in the consolidated statement of 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		Nine months Ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	(\$ millions)			
Mortgage Originations by Segment				
Single-family residential	6,685	8,311	16,314	20,048
Multi-unit and commercial	2,743	3,293	10,810	9,202
Total origination and renewals	9,428	11,604	27,124	29,250
Mortgage Originations by Funding Source				
Institutional investors	5,397	7,609	15,234	18,949
NHA-MBS/CMB/ABCP securitization	3,763	3,656	11,239	9,571
Internal Company resources	268	339	651	730
Total	9,428	11,604	27,124	29,250
Mortgages under Administration				
Single-family residential	95,373	94,554	95,373	94,554
Multi-unit residential and commercial	55,195	47,361	55,195	47,361
Total	150,568	141,915	150,568	141,915

Total mortgage origination volume was lower in the third quarter of 2024 compared to the comparative 2023 quarter. This reflected a 20% decrease in single-family volumes and a 17% decrease in commercial segment volumes year over year. Management believes the decrease in the single-family segment was due to increased competition in the mortgage broker distribution channel. In the past 12 months, two of the largest lenders in the channel have offered discounted rates and larger broker incentives to attract market share. The housing market across Canada performed well, although it is still somewhat muted compared to the 10 year trend. The Company's MERLIN technology continued to support its mortgage origination platform allowing First National to underwrite efficiently across the country. In the commercial segment, where the Company's expertise in underwriting multi-unit mortgages is a fundamental competency, 2024 volumes reflected continuing demand for insured mortgages. This success was offset by lower conventional mortgage activity as higher interest rates affected real estate valuations. Origination for direct securitization into NHA-MBS, CMB and ABCP programs remained a large part of the Company's strategy, with about \$3.8 billion of volume in the third quarter of 2024.

Net Interest – Securitized Mortgages

Comparing the quarter ended September 30, 2024, to the quarter ended September 30, 2023, "net interest – securitized mortgages" ("NIM") increased by about 4% to \$60.2 million from \$57.7 million. The portfolio of mortgages pledged under securitization grew 14% from \$38.9 billion at September 30, 2023 to \$44.4 billion at September 30, 2024. This reflected growth of 17% in the multi-unit residential program portfolio and 13% in single-family programs. Commercial segment earnings were up by \$3.3 million and grew with the larger portfolio and an increase in margin largely related to the success of the Company's insured construction mortgage program. Residential segment NIM was lower by \$0.8 million year over year as a result of tighter spreads. This was partially due to the current competitive environment, but also the result of the accounting related to the Company's interest rate management program for single-family mortgage commitments. The Company records gains and losses on such hedges in its current earnings while earning wider or narrower securitization NIM over the term of the related mortgages. Generally speaking, when the Company records gains on the hedges, there is a narrower securitization NIM on the related mortgages. The reverse is true when

there are losses. In each of the past three years, the Company recorded gains on these hedging instruments such that the mortgages securitized have comparatively narrower securitization spreads. Effectively, some of the spread otherwise earned on such transactions was recorded as an upfront gain on financial instruments as opposed to securitization NIM over the mortgage term. While difficult to calculate precisely, management believes this phenomenon reduced comparative NIM in the current quarter by about \$2 million. The residential segment was favorably affected by the Excalibur securitization program as it continued to perform with almost no realized loan-loss experience.

Placement Fees

Placement fee revenue decreased by 25% to \$57.1 million from \$75.8 million in the comparative quarter. The decrease was the result of a lower placement activity which decreased by 29% between the quarters and a shift in the mix of mortgages that make up placement volume. In the 2024 quarter, new residential origination decreased and was replaced with an increase in renewed residential mortgages. Generally, per-unit fees for renewed mortgages are markedly lower than those on new residential origination. However in the 2024 third quarter, per unit pricing of renewals placed increased as the Company transacted more placements on a “capital markets basis”. As bond yields decreased during the period between origination and placement, these transactions had a positive impact on profitability. Altogether, including prime mortgages, Excalibur and mortgage renewals, residential per-unit fees were higher by about 7% year over year.

Gains on Deferred Placement Fees

Gains on deferred placement fees revenue decreased 59% to \$2.9 million from \$7.0 million. These gains related primarily to multi-unit residential mortgages originated and sold to institutional investors where volumes decreased by 29% from the third quarter of 2023. Due to a more competitive environment and steepening yield curve, spreads in this business were tighter in the 2024 quarter than in 2023.

Mortgage Servicing Income

Mortgage servicing income decreased 7% to \$66.1 million from \$71.1 million. This decrease reflected lower revenues from the Company’s third-party underwriting business as the mortgage market was more competitive for our customers in 2024 compared to 2023. The decrease was partially offset by higher revenues related to MUA including administrative fees. In general, the elements of this revenue that relate to MUA were 2% higher year over year.

Mortgage Investment Income

Mortgage investment income decreased 3% to \$40.9 million from \$42.3 million. The decrease was due primarily to a smaller mortgage investment portfolio. In order to manage the Company’s efficient use of equity, it reduced the amount of commercial bridge lending by placing more of this product with its institutional customers. This decision reduced the mortgage loan and investment portfolio by about \$50 million but also reduced the amount of interest revenue generated by these mortgages. In general mortgage rates on mortgages accumulated for securitization are lower year over year as with the recent BoC rate cuts, mortgage rates have come down from comparative rates in 2023.

Realized and Unrealized Gains (Losses) on Financial Instruments

This financial statement line item consists of three primary components: (1) gains and losses related to the Company's economic hedging of single-family commitments, (2) gains and losses related to holding a portfolio of mortgage and loan investments at fair value, and (3) gains and losses on interest rate swaps used to mitigate interest rate risk on its CMB activity. The Company has elected to document hedging relationships for virtually all of the multi-residential commitments and mortgages it originates for its own securitization programs. It has also done the same for funded single-family mortgages and the swaps used in its ABCP programs. This has reduced the volatility of gains and losses on financial instruments otherwise recorded in the Company's regular earnings, as gains and losses on hedged items are generally deferred and amortized into income over the term of the related mortgages. The Company does not document a hedging relationship for accounting purposes related to its interest mitigation program on its single-family mortgage commitments. The Company believes, given the optional nature of these commitments, it is difficult to establish a valid hedging relationship. For financial reporting purposes, this means that there will still be gains and losses on financial instruments, but these should be limited to those on the bonds sold short used to mitigate such risk. The following table summarizes these gains and losses by category in the periods indicated:

Summary of Realized and Unrealized Gains (Losses) on Financial Instruments	Quarter Ended		Nine months Ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	(\$000s)			
Gains (losses) on short bonds used for the economic hedging program	(27,598)	20,271	(24,666)	44,501
Gains (losses) on mortgages held at fair value	—	61	—	61
Gains (losses) on interest rate swaps	2,033	(1,897)	240	(5,547)
Net gains (losses) on financial instruments	(25,565)	18,435	24,426	39,015

2023 began with an environment in which bond yields fell as economic sentiment turned softer; however by midyear the BoC once again increased its overnight rates to counter a stubborn inflationary economy. This resulted in increases in both short and long-term interest rates. Accordingly, the Company recorded gains on its short bonds used to economically hedge single-family mortgage commitments. 2024 began with a more volatile environment in which bond yields first fell but then rose as inflation indicators remained elevated and the central bank delayed possible overnight rate cuts. Then in early June 2024, the BoC began cutting rates and the bond market followed with yields decreasing significantly. Lower yields meant the Company recorded significant losses on the short bonds it uses to economically hedge single-family mortgage commitments.

Brokerage Fees Expense

Brokerage fees expense decreased 35% to \$29.9 million from \$46.0 million. This reflected a 38% year-over-year decrease in origination volumes of single-family mortgages for institutional investors offset by higher per-unit broker fees. 2024 continued to be a very competitive period for mortgages in the broker channel and incentives for broker increased such that year over year, per-unit broker fees were higher by about 3%.

Salaries and Benefits Expense

Salaries and benefits expense increased 7% to \$53.2 million from \$49.9 million. The primary increase in these expenses related to headcount growth of 9% (1,745 employees at September 30, 2024, compared to 1,603 at September 30, 2023). Some of the headcount growth pertains to staffing for the Company's new third-party underwriting customer. The Company's annual merit increase also led to increased employee costs. Incentive-driven commercial underwriting compensation was lower year over year by \$1.4 million on lower production volume. Management salaries were paid to the two senior executives (co-founders) who together control about 71% 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") in 2006.

Interest Expense

Interest expense increased 2% to \$47.5 million from \$46.4 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 investor or funding with a securitization vehicle. The Company used its \$1.5 billion syndicated bank line together with repurchase agreements to fund mortgages during this period. The overall interest expense increased from 2023 because of higher usage of repurchase agreements to fund the larger balances of mortgages accumulated for securitization. Interest expense also includes the cost of carry related to the Company’s economic hedging program.

Other Operating Expenses

Other operating expenses increased by 30% to \$21.4 million from \$16.5 million primarily due to higher information technology costs including higher depreciation related to investments in computer hardware and software.

Income before Income Taxes and Pre-FMV Income⁽¹⁾

Income before income taxes decreased 56% to \$49.7 million from \$113.8 million in third quarter 2023. This decrease was partially the result of changing capital markets. The Company’s results include gains and losses on financial instruments used to economically hedge residential mortgage commitments. As described previously in this MD&A, the Company recorded \$25.6 million of losses on financial instruments (excluding gains related to mortgage investments) in the 2024 quarter. Comparatively, in the 2023 quarter, the Company recorded \$18.4 million of gains on financial instruments (excluding losses related to mortgage investments). The change in these values accounted for a \$44.0 million decrease in comparative income before income taxes. Pre-FMV Income⁽¹⁾, which excludes these changes, decreased by 21% to \$75.3 million from \$95.5 million. This change was largely the result of lower single-family origination which negatively affected both placement fees and mortgage servicing revenue related to the third-party underwriting business. Lower volumes reduced the Company’s operating leverage in both departments compared to the prior year's quarter. The Company also invested more heavily in its direct securitization programs which delayed the recognition of revenue to future periods in contrast to the comparative quarter. Higher operating costs particularly related to technology further reduced earnings by \$4.9 million.

Income Tax Expense

The provision for taxes decreased by 56% to \$13.3 million from \$30.2 million. The provision decreased proportionately with net income before income taxes.

Other Comprehensive Income

For the commercial segment, the Company hedges the interest rate risk associated with insured multi-residential mortgages. This hedging begins on commitment and ends when the Company either securitizes the mortgage or places the mortgage with an institutional investor. As the Company determined that these cash flow hedges were effective, the Company recorded \$54.3 million of pre-tax net losses on such hedges in OCI in the third quarter of 2024. In the quarter, the Company amortized a portion of the gains and losses in accumulated OCI into regular earnings in the amount of \$5.2 million. The remaining OCI amount will be amortized into net income in future periods.

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	
	(\$000s except percent amounts)			
For the Quarter Ended	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
Originations and renewals	6,686,336	8,311,410	2,743,309	3,292,302
Percentage change	(20%)		(17%)	
Revenue	394,173	413,373	166,213	149,488
Percentage change	(5%)		11%	
Income before income taxes	21,044	77,954	28,645	35,876
Percentage change	(73%)		(20%)	
As at	September 30, 2024	December 31, 2023	September 30, 2024	December 31, 2023
Identifiable assets	33,124,574	30,362,969	17,305,936	15,564,654
Mortgages under administration	95,373,574	94,545,641	55,194,620	49,001,325

Residential Segment

Residential origination volumes including renewals decreased by 20% between the third quarters of 2023 and 2024 while residential revenues decreased by 5%. Revenue was lower partly due to the impact of gains and losses on financial instruments. Excluding the impact of these revenues, revenue increased by 6%, largely due to higher interest revenue on its securitized portfolio which resulted from the higher interest rate environment over the past two years. Net income before tax was also affected by fair value-related revenues. Without the impact of these revenues, net income before tax decreased to \$46.6 million in the 2024 quarter from \$59.6 million in the 2023 quarter, or 22%. This change was largely the result of lower single-family origination which negatively affected both placement fees and mortgage servicing revenue related to the third-party underwriting business. Lower volumes reduced the Company's operating leverage in both departments compared to the prior year's quarter. Income was also negatively affected by shorter term placement volumes which reduced per-unit fees. Identifiable assets increased from December 31, 2023 as the Company's mortgages pledged under securitization increased by about \$3.0 billion while mortgages accumulated for securitization decreased by \$0.5 billion.

Commercial Segment

Third quarter 2024 commercial revenues were higher compared to those in the 2023 quarter by 11% but segment income before income taxes decreased by 20% year over year. Revenue increased on 17% growth in the Company's securitized mortgage portfolio. The decrease in income reflected higher direct securitization by the Company. By securitizing directly, the company does not earn significant revenue in the period of origination but incurs the cost of origination through higher incentive-based compensation to the employees involved in commercial origination. Identifiable assets increased from December 31, 2023, as the Company increased its portfolio of securitized mortgages by about \$1.9 billion and decreased its commercial hedging assets by \$0.2 billion.

Liquidity and Capital Resources

The Company's fundamental liquidity strategy has been to originate and invest in prime Canadian mortgages. Management's belief has always been that these mortgages are attractive to investors and should always be well bid and highly liquid. This strategy proved effective during the turmoil experienced in 2007 through 2009, and once again at the onset of the Covid-19 pandemic, when capital markets were disrupted and the demand for high-quality assets increased. As the Company's results in those years demonstrated, First National was able to attract 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 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 financial institutions for total credit of \$1.5 billion. This facility was extended for a year in April 2024 and now matures in March 2029. As at September 30, 2024, the Company had entered into repurchase transactions with financial institutions to borrow \$1.0 billion related to \$1.0 billion of mortgages held in "mortgages accumulated for sale or securitization" on the balance sheet.

At September 30, 2024, outstanding bank indebtedness was \$999.5 million (December 31, 2023 - \$1,083.0 million). This debt was used to fund a portion of mortgages accumulated for sale or securitization totalling \$1,115.8 million (December 31, 2023 - \$1,026.9 million). At September 30, 2024, the Company's other interest-yielding assets included: (1) deferred placement fees receivable of \$73.7 million (December 31, 2023 - \$73.9 million) and (2) mortgage and loan investments of \$145.2 million (December 31, 2023 - \$270.9 million). The Company considers the portion of bank indebtedness and the senior unsecured notes that fund assets other than mortgages accumulated for sale or securitization a proxy for true leverage. This leverage increased between December 31, 2023, and September 30, 2024, and now stands at \$682.1 million (December 31, 2023 - \$654.8 million). This represents a debt-to-equity ratio of approximately 0.92:1. This ratio increased from the ratio of 0.89:1 as at December 31, 2023. In general, an increase in this ratio is a result of losses related to the Company's hedging activities which reduce levels of equity.

The Company funds a 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 by the Company. On specified days, 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 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 6 to 18-month terms, to bridge existing borrowers in the interim period before traditional term financing can be provided. The banking syndicate has provided credit facilities to partially fund these investments. The Company's mortgage and loan investments also includes a portfolio of single-family mortgages not eligible for securitization. These arise when minor imperfections are discovered on mortgages otherwise originated for securitization. The portfolio comprises largely prime insured mortgages. To the extent these mortgages are financed by bank borrowings, as they repay, the cash 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 longer-term assets.

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 September 30, 2024, the investment in cash collateral was \$169.5 million (December 31, 2023 - \$151.6 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 September 30, 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.

Financial Instruments and Risk Management

The Company records mortgages accumulated for sale and a portion of 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 income. The mortgages accumulated for sale are held for very short periods, and any change in value due to changing interest rates is the obligation of the ultimate institutional investor. Accordingly, the Company believes there will be little, if any, effect on its income related to the change in fair value of these mortgages. The majority of mortgages in mortgage and loan investments are uninsured commercial segment bridge loans. These are primarily floating rate loans that have mortgage terms of 18 months or less. As the mortgages do not conform to conventional mortgage lending, there are few active quoted markets available to determine the fair value of these assets. The Company estimates fair value based upon: benchmark interest rates, credit spreads for similar products, creditworthiness and status of the borrower, valuation of the underlying real property, payment history, and other conditions specific to the rationale for the loan. Any favourable or unfavourable amounts will be recorded in the statement of 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. The Company designates hedging relationships such that the results of any effective hedging does not affect the Company's statement of income. See previous discussion in this MD&A under "Realized and Unrealized Gains (Losses) on Financial Instruments". As at September 30, 2024, the Company had \$1.5 billion 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 to be sold to the Company's other securitization vehicles. As at September 30, 2024, the Company had entered into \$0.8 billion of notional value forward bond sales for this segment. The Company is also a party to two interest rate swaps that economically hedge the interest rate exposure related to certain CMB transactions in which the Company has replacement obligations. As at September 30, 2024, the aggregate value of these swaps which mature in September 2025 and September 2026, was a \$3.9 million liability. During the third quarter of 2024, the Company recorded a gain of \$2.0 million related to these swaps.

As described above, the Company employs various strategies to reduce interest rate risk. In the normal course of business, the Company also takes on 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 ultimate date of placement or securitization. If credit spreads widen during this holding period, this is unfavourable for the Company. It means that the Company cannot fund the mortgages originated with a funding source as effectively as originally intended. Despite entering into effective interest rate hedges, the Company's exposure to credit spreads will remain. This risk is inherent in the Company's business model and the Company believes it cannot be economically hedged. As at September 30, 2024, the Company had various exposures to changing credit spreads. In particular, in mortgages accumulated for sale or securitization, there were approximately \$2.1 billion of mortgages that were susceptible to some degree of changing credit spreads.

Capital Expenditures

A significant portion of First National's business model is the origination and placement or securitization of financial assets. Generally, placement activities do not require any capital investment. Securitization transactions may require the investment of 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. The business requires capital expenditures on technology (both software and hardware), leasehold improvements, and office furniture. During the quarter, the Company purchased new computer equipment and software and made leasehold improvements. In the long term, the Company expects capital expenditures on fixed assets will be approximately \$10 million annually.

Summary of Contractual Obligations

The Company's long-term obligations include leases of premises with terms up to 15 years for its 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.

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, 2023. The policies that 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 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 assumes there is virtually no prepayment on multi-unit residential fixed-rate mortgages as most prepayments earn the Company a prepayment fee which offsets any impairment to retained interests.

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 method of determining the assumptions underlying the estimates used for the quarter ended September 30, 2024, are consistent with those used for the year ended December 31, 2023, and the quarters ended March 31, 2024, June 30, 2024, and September 30, 2023.

The Company elects to treat certain of its financial assets and liabilities, including mortgages accumulated for sale, a portion of 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. A portion of the bonds sold short are designated as an effective hedge, and

accordingly, a portion of the change in the short bonds' fair value may be recorded in Other Comprehensive Income or deferred against hedge assets. This accounting has reduced the volatility in earnings as changes in the value on short bonds have been matched to the recognition of the change in value of the hedged mortgages. 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 the assets listed above are subject to Company estimates. The most significant would be implicit in the valuation of mortgage and loan investments that are recorded at FVTPL. These are generally non-homogeneous mortgages where it is difficult to find independent valuation comparatives. The Company uses information in its underwriting files, regional real estate information and other internal measures to determine the fair value of these assets.

As a mortgage lender, the Company invests in uninsured mortgages. When it funds these mortgages through securitization debt, it continues to be liable for any credit losses. The key inputs in the measurement of any expected credit loss ("ECL") include probability of default, loss given default and forecast of future economic conditions, which involves significant judgment. Upon application of IFRS 9 with respect to impairment, there has been no impact on the Company's earnings. Because of the high proportion of government-insured mortgages in its securitized portfolio and the low historical loss rates on the uninsured mortgages on which the Company lends, credit losses are typically low compared to its securitization portfolio. In the third quarter of 2024, the Company recorded a recovery on its provision for credit loss of \$0.5 million.

Disclosure Controls and Internal Control 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.

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.

No changes were made in the Company's internal controls over financial reporting during the quarter ended September 30, 2024, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ESG

The Company issued its initial Public Accountability Statement in the fall of 2021. In November 2023, it issued an updated report which explores First National's approach to sustainability and provides environmental, social and governance disclosure that has been reviewed and approved by the Board of Directors. It complements the Management Information Circular, Annual Information Form, Management Discussion and Analysis and Annual Report, all of which offer information about the financial position, priorities, responsibilities and commitments of the consolidated operations of First National.

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 including third-party servicing customers, reliance on independent mortgage brokers, changes in interest rates, repurchase obligations and breach of representations and warranties on mortgage sales, risk of servicer termination including the impact of trigger events on cash collateral and retained interests, reliance on multi-unit residential and commercial mortgages, general economic conditions, legislation and government regulation (including regulations imposed by the Department of Finance and CMHC and the policies set by and for mortgage default insurance companies), potential for losses on uninsured mortgages, 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, unfavourable litigation, and environmental liability. In addition, there are risks associated with the structure of the Company, including: those related to the dependence on FNFLP, leverage and restrictive covenants, dividends that are not guaranteed and could fluctuate with the Company's performance, restrictions on potential growth, the market price of the Company's shares, statutory remedies, control of the Company, and contractual restrictions. The Company is subject to Canadian federal and provincial income and commodity tax laws and pays such taxes as it determines are compliant with such legislation. Among the risks of all potential tax matters, there is a risk that tax legislation changes are detrimental to the Company or that Canadian tax authorities interpret tax legislation differently than the Company's filing positions. 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. The total of one investor's activities with the Company accounted for approximately 8.5% of the Company's total revenues in 2023. Rate hikes by the Bank of Canada in 2022 and 2023 raised short-term interest rates by 475 basis points. In that same period mortgage rates for 5-year term mortgages have increased by approximately 300 basis points and bank prime lending rates rose by 475 basis points with the last increase occurring in early July 2023. Despite recent interest rate decreases, higher borrowing rates will directly affect consumers across the country. Management believes these changes may impact the Company negatively in future periods. Losses related to these risks could be material. 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 in the “Risk and Uncertainties Affecting the Business” section. In evaluating this information, the reader should specifically consider various factors, including the risks outlined in the “Risk and Uncertainties Affecting the Business” section, that 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 October 29, 2024, 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

The third quarter of 2024 unfolded much as the Company expected. In general, management believes that the housing activity and prices are relatively stable with some regional outperformance observed in Alberta and Quebec. The Company believes lower single-family origination is primarily the result of increased competition particularly in the mortgage broker distribution channel. In the third quarter, the Company continued to build its MUA and its portfolio of mortgages pledged under securitization. It will benefit from both MUA and the securitized portfolio in the future: earning income from mortgage administration, net securitization margin and improving its position to capture increased renewal opportunities.

In the short term, the Company now expects increased year over year single-family origination in the next two quarters. With the Bank of Canada cutting overnight rates by 0.75% between June and September and a further reduction of 0.50% on October 23, 2024, not only are mortgage rates lower but the fear of a rising rate environment has been allayed somewhat. Management believes this backdrop may provide confidence to borrowers who have remained on the sidelines. In fact, single-family mortgage commitments issued in the third quarter were approximately 50% higher than those issued during the same quarter last year. Given this growth in mortgage commitments, management expects fourth quarter origination volumes to exceed those from the same quarter last year. For its commercial segment, the Company anticipates steady new origination volumes as government incentives support the creation of multi-unit housing. These initiatives, including the recent increase of the Canada Mortgage Bonds program from \$40 to \$60 billion, not only enhanced the level of financing available for multi-unit mortgages, but also removed uncertainties about such programs in the future. These developments have created a reliable and stable source of funds for the Company to originate CMHC insured multi-unit mortgages. However, given the increased certainty of these programs, other lenders have become more aggressive and mortgage spreads are narrowing from the levels originated in 2023 and those to start 2024 as the Company competes for qualifying mortgages. In both business segments, management is confident that First National will remain a competitive lender in the marketplace.

First National is well prepared to execute its business plan. The Company expects to enjoy the value of its continued goodwill with broker partners earned over the last 35+ years. With diverse relationships over an array of institutional investors and solid securitization markets, the Company has access to consistent and reliable sources of funding.

The Company is confident that its strong relationships with mortgage brokers and diverse funding sources will continue to set First National apart from its competition. The Company will continue to generate income and cash flow from its \$44 billion portfolio of mortgages pledged under securitization and \$104 billion servicing portfolio and focus on the value inherent in its significant single-family renewal book.

First National Financial Corporation

Interim condensed consolidated financial statements
[Unaudited]
Third quarter 2024

First National Financial Corporation

Interim condensed consolidated statements of financial position

[Unaudited – in thousands of Canadian dollars]


As at

	September 30, 2024 \$	December 31, 2023 \$
Assets		
Restricted cash <i>[note 3]</i>	792,493	550,842
Cash held as collateral for securitization <i>[note 3]</i>	169,536	151,557
Accounts receivable and sundry	160,931	133,264
Mortgages accumulated for sale or securitization <i>[note 5]</i>	2,109,978	2,583,634
Mortgages pledged under securitization <i>[note 3]</i>	44,392,673	39,427,192
Deferred placement fees receivable <i>[note 4]</i>	73,660	73,904
Mortgage and loan investments <i>[note 6]</i>	145,237	270,921
Income taxes recoverable	16,157	—
Securities purchased under resale agreements	2,493,196	2,653,376
Other assets <i>[note 7]</i>	106,425	112,709
Total assets	50,460,286	45,957,399
Liabilities and equity		
Liabilities		
Bank indebtedness <i>[note 9]</i>	999,529	1,083,000
Obligations related to securities and mortgages sold under repurchase agreements	975,300	1,524,192
Accounts payable and accrued liabilities	297,751	285,344
Securities sold short	2,496,871	2,649,249
Debt related to securitized mortgages <i>[note 10]</i>	43,985,222	38,880,798
Senior unsecured notes	798,425	598,745
Income taxes payable	—	47,408
Deferred income tax liabilities	166,000	150,900
Total liabilities	49,719,098	45,219,636
Equity attributable to shareholders		
Common shares <i>[note 11]</i>	122,671	122,671
Preferred shares <i>[note 11]</i>	97,394	97,394
Retained earnings	505,023	477,799
Accumulated other comprehensive income	16,100	39,899
Total equity	741,188	737,763
Total liabilities and equity	50,460,286	45,957,399

See accompanying notes

On behalf of the Board:


Robert Mitchell


Robert Pearce

First National Financial Corporation

Interim condensed consolidated statements of income

[Unaudited – in thousands of Canadian dollars]

	Three months ended		Nine months ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	\$	\$	\$	\$
Revenue				
Interest revenue – securitized mortgages	418,898	348,034	1,180,040	973,913
Interest expense – securitized mortgages	(358,712)	(290,333)	(1,012,079)	(815,335)
Net interest – securitized mortgages	60,186	57,701	167,961	158,578
Placement fees	57,127	75,797	147,669	193,795
Gains on deferred placement fees <i>[note 4]</i>	2,877	7,037	12,856	20,419
Mortgage investment income	40,918	42,238	107,887	101,481
Mortgage servicing income	66,131	71,320	192,855	192,221
Realized and unrealized gains (losses) on financial instruments <i>[note 12]</i>	(25,565)	18,435	(24,426)	39,015
	201,674	272,528	604,802	705,509
Expenses				
Brokerage fees	29,874	45,963	64,188	114,118
Salaries and benefits	53,195	49,884	169,565	148,933
Interest	47,494	46,374	119,092	107,682
Other operating	21,422	16,477	60,886	50,764
	151,985	158,698	413,731	421,497
Income before income taxes	49,689	113,830	191,071	284,012
Income tax expense	13,280	30,200	50,700	75,450
Net income for the period	36,409	83,630	140,371	208,562
Earnings per share				
Basic <i>[note 11]</i>	0.59	1.38	2.29	3.43

See accompanying notes

First National Financial Corporation

Interim condensed consolidated statements of comprehensive income

[Unaudited – in thousands of Canadian dollars]

	Three months ended		Nine months ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	\$	\$	\$	\$
Net income for the period	36,409	83,630	140,371	208,562
Other comprehensive income (loss) items that subsequently may be reclassified to income				
Net gains (losses) from change in fair value of cash flow hedges	(54,311)	14,804	(33,327)	29,762
Reclassification of net losses (gains) to income	5,192	(13,831)	1,028	(21,133)
	(49,119)	973	(32,299)	8,629
Income tax recovery (expense)	13,000	(300)	8,500	(2,300)
Total other comprehensive income (loss)	(36,119)	673	(23,799)	6,329
Total comprehensive income for the period	290	84,303	116,572	214,891

See accompanying notes

First National Financial Corporation

Interim condensed consolidated statements of changes in equity

[Unaudited – in thousands of Canadian dollars]

	Common shares	Preferred shares	Retained earnings	Accumulated other comprehensive income	Total equity
	\$	\$	\$	\$	\$
Balance as at January 1, 2024	122,671	97,394	477,799	39,899	737,763
Net income	—	—	140,371	—	140,371
Other comprehensive loss	—	—	—	(23,799)	(23,799)
Dividends paid or declared	—	—	(113,147)	—	(113,147)
Balance as at September 30, 2024	122,671	97,394	505,023	16,100	741,188

	Common shares	Preferred shares	Retained earnings	Accumulated other comprehensive income	Total equity
	\$	\$	\$	\$	\$
Balance as at January 1, 2023	122,671	97,394	418,244	60,671	698,980
Net income	—	—	208,562	—	208,562
Other comprehensive income	—	—	—	6,329	6,329
Dividends paid or declared	—	—	(110,793)	—	(110,793)
Balance as at September 30, 2023	122,671	97,394	516,013	67,000	803,078

See accompanying notes

First National Financial Corporation

Interim condensed consolidated statements of cash flows

[Unaudited – in thousands of Canadian dollars]

	Three months ended		Nine months ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	\$	\$	\$	\$
Operating activities				
Net income for the period	36,409	83,630	140,371	208,562
Add (deduct) items				
Provision for deferred income taxes	7,400	8,400	23,600	14,100
Non-cash portion of gains on deferred placement fees	(2,632)	(6,814)	(12,196)	(19,849)
Decrease (increase) in restricted cash	(52,748)	258,804	(241,651)	(28,492)
Net investment in mortgages pledged under securitization	(2,543,786)	(493,183)	(4,894,269)	(1,612,930)
Net increase in debt related to securitized mortgages	2,559,978	229,567	5,033,212	1,547,912
Securities purchased under resale agreements, net	1,188,700	1,748,129	160,180	806,520
Securities sold short, net	(1,280,325)	(1,724,046)	(162,683)	(741,373)
Amortization of deferred placement fees receivable	4,217	3,836	12,440	11,243
Amortization of property, plant and equipment	4,222	3,872	12,666	11,617
Unrealized losses (gains) on financial instruments	40,116	(17,185)	(25,691)	(47,122)
	(38,449)	95,010	45,979	150,188
Net change in non-cash working capital balances related to operations	1,067,885	(325,281)	403,347	(489,081)
Cash provided by (used in) operating activities	1,029,436	(230,271)	449,326	(338,893)
Investing activities				
Additions to property, plant and equipment	(2,086)	(1,666)	(6,382)	(4,138)
Repayment of (investment in) cash held as collateral for securitization	(18,036)	7,011	(17,979)	923
Investment in mortgage and loan investments	(233,202)	(310,995)	(526,874)	(714,484)
Repayment of mortgage and loan investments	282,731	358,907	652,558	709,626
Cash provided by (used in) investing activities	29,407	53,257	101,323	(8,073)
Financing activities				
Dividends paid	(37,716)	(36,940)	(113,168)	(110,714)
Obligations related to securities and mortgages sold under repurchase agreements	(699,947)	50,415	(548,892)	142,332
Repayment of lease liabilities	(1,397)	(1,407)	(4,190)	(4,221)
Issuance of senior unsecured notes	—	199,088	199,072	199,088
Cash provided by (used in) financing activities	(739,060)	211,156	(467,178)	226,485
Net decrease (increase) in bank indebtedness during the period	319,783	34,142	83,471	(120,481)
Bank indebtedness, beginning of period	(1,319,312)	(1,220,491)	(1,083,000)	(1,065,868)
Bank indebtedness, end of period	(999,529)	(1,186,349)	(999,529)	(1,186,349)
Supplemental cash flow information				
Interest received	477,801	402,195	1,335,428	1,115,865
Interest paid	365,097	268,727	1,015,306	764,523
Income taxes paid	1,444	6,480	90,537	8,144

See accompanying notes

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

1. General organization and business of First National Financial Corporation

First National Financial Corporation [the “Corporation” or “Company”] 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 \$150 billion in mortgages under administration as at September 30, 2024, FNFLP is a significant participant in the mortgage broker distribution channel.

The Corporation is incorporated under the laws of the Province of Ontario, Canada and has its registered office and principal place of business located at 16 York Street, Toronto, Ontario. The Corporation’s common and preferred shares are listed on the Toronto Stock Exchange under the symbols FN, FN.PR.A and FN.PR.B, respectively.

2. Material accounting policy information

Basis of preparation

The interim condensed consolidated financial statements have been prepared in accordance with IAS 34 – *Interim Financial Reporting* under International Financial Reporting Standards [“IFRS”], as issued by the International Accounting Standards Board. The interim condensed consolidated financial statements have been prepared using the same accounting policies used in the preparation of the audited annual consolidated financial statements for the year ended December 31, 2023.

These interim condensed consolidated financial statements should be read in conjunction with the audited annual consolidated financial statements and are presented in Canadian dollars with all values rounded to the nearest thousand, except when otherwise indicated. The interim condensed consolidated financial statements were authorized for issue by the Board of Directors on October 29, 2024.

Estimates and use of judgement

Management has exercised judgement in the process of applying the Company’s accounting policies. Some of the Company’s accounting policies require subjective, complex judgements and estimates relating to matters that are inherently uncertain. The preparation of these interim condensed consolidated financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the interim condensed consolidated statements of financial position dates and the reported amounts of revenue and expenses during the reporting periods.

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

3. Mortgages pledged under securitization

The Company securitizes residential and commercial mortgages in order to raise debt to fund these mortgages. Most of these securitizations consist of the transfer of fixed and floating rate mortgages into securitization programs, such as ABCP, NHA-MBS, and CMB. In these securitizations, the Company transfers the assets to structured entities for cash, and incurs interest-bearing obligations typically matched to the term of the mortgages. These securitizations do not qualify for derecognition, although the structured entities and other securitization vehicles have no recourse to the Company's other assets for failure of the mortgages to make payments when due.

As part of the ABCP transactions, the Company provides cash collateral for credit enhancement purposes as required by the rating agencies. Credit exposure to securitized mortgages is generally limited to this cash collateral. The principal and interest payments on the securitized mortgages are paid to the Company by the structured entities monthly over the term of the mortgages. The full amount of the cash collateral is recorded as an asset and the Company anticipates full recovery of these amounts. NHA-MBS securitizations may also require cash collateral in some circumstances. As at September 30, 2024, the cash held as collateral for securitization was \$169,536 [December 31, 2023 – \$151,557].

The following table compares the carrying amount of mortgages pledged for securitization and the associated debt:

	September 30, 2024		December 31, 2023	
	Carrying amount of securitized mortgages \$	Carrying amount of associated liabilities \$	Carrying amount of securitized mortgages \$	Carrying amount of associated liabilities \$
Securitized mortgages	44,043,284	(44,273,319)	39,264,199	(39,300,233)
Capitalized amounts related to hedge accounting	97,019	(90,315)	(41,212)	(19,103)
Capitalized origination costs	252,370	—	204,205	—
Debt discounts	—	378,412	—	438,538
Add	44,392,673	(43,985,222)	39,427,192	(38,880,798)
Principal portion of payments held in restricted cash	698,332	—	473,080	—
	45,091,005	(43,985,222)	39,900,272	(38,880,798)

The principal portion of payments held in restricted cash represents payments on account of mortgages pledged under securitization which have been received at period end but have not been applied to reduce the associated debt. This cash is applied to pay down the debt in the month subsequent to collection. In order to compare the components of mortgages pledged under securitization-to-securitization debt, this amount is added to the carrying value of mortgages pledged under securitization in the above table.

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

Mortgages pledged under securitization are classified as amortized cost and are carried at par plus adjustment for unamortized origination costs and amounts related to hedge accounting.

The changes in capitalized origination costs for the three months ended September 30, 2024 are as follows:

	2024	2023
	\$	\$
Opening balance, June 30	224,107	204,616
Add new origination costs capitalized in the period	55,279	27,151
Less amortization in the period	(27,016)	(23,705)
Ending balance, September 30	252,370	208,062

The following table summarizes the mortgages pledged under securitization that are past due:

	September 30, 2024	December 31, 2023
	\$	\$
Arrears days		
31 to 60	7,638	4,683
61 to 90	2,541	3,692
Greater than 90	13,026	9,868
	23,205	18,243

Of the mortgages in arrears summarized above, 41 are uninsured and have a principal balance of \$20,809 as at September 30, 2024 [December 31, 2023 – 29 mortgages, \$16,985], while the remaining loans are insured. The Company's exposure to credit loss is limited to uninsured mortgages with principal balances totaling \$5,545,347 [December 31, 2023 – \$4,851,746], before consideration of the value of underlying collateral. The majority of the uninsured mortgages are conventional prime single-family mortgages, with loan to value ratios of 80% or less.

The Company has provided an allowance for expected credit losses of \$6,793 as of September 30, 2024 [December 31, 2023 – \$5,808] related to mortgages pledged under securitization.

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

4. Deferred placement fees receivable

The Company enters into transactions with institutional investors to sell primarily fixed rate mortgages in which placement fees are received over time as well as at the time of the mortgage placement. These mortgages are derecognized when substantially all of the risks and rewards of ownership are transferred and the Company has minimal exposure to the variability of future cash flows from these mortgages. The investors have no recourse to the Company's other assets for failure of mortgagors to make payments when due.

Deferred placement fees receivable is classified as amortized cost and has been calculated initially based on the present value of the anticipated future stream of cash flows. This determination assumes there will be no credit losses, commensurate with the credit quality of the investors. It is also assumed that there will be no prepayment for the commercial segment as borrowers cannot refinance for financial advantage without paying the Company a fee commensurate with the value of its investment in the mortgage. The effect of variations, if any, between actual experience and assumptions will be recorded in future consolidated statements of income but is expected to be minimal.

	Three months ended September 30, 2024		
	Residential	Commercial	Total
	\$	\$	\$
Mortgages placed with institutional investors	—	1,366,324	1,366,324
Gains on deferred placement fees recognized	—	2,877	2,877
Cash receipts on deferred placement fees received	76	5,134	5,210
	Three months ended September 30, 2023		
	Residential	Commercial	Total
	\$	\$	\$
Mortgages placed with institutional investors	—	1,913,152	1,913,152
Gains on deferred placement fees recognized	—	7,037	7,037
Cash receipts on deferred placement fees received	92	4,594	4,686

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

5. Mortgages accumulated for sale or securitization

Mortgages accumulated for sale or securitization consist of mortgages the Company has originated for its own securitization programs together with mortgages funded in advance of settlement with institutional investors.

Mortgages originated for the Company's own securitization programs are classified as amortized cost and are recorded at par plus adjustment for unamortized origination costs. Mortgages funded for placement with institutional investors are designated as FVTPL and are recorded at fair value. The fair values of mortgages classified as FVTPL approximate their carrying values as the time period between origination and sale is short. The following table summarizes the components of mortgages according to their classification:

	September 30, 2024	December 31, 2023
	\$	\$
Mortgages accumulated for securitization	2,007,610	2,556,521
Mortgages accumulated for sale	102,368	27,113
	2,109,978	2,583,634

The Company's exposure to credit loss is limited to \$516,798 [December 31, 2023 – \$396,402] of principal balances of uninsured mortgages within mortgages accumulated for securitization, before consideration of the value of underlying collateral. As at September 30, 2024, 26 of these mortgages are in arrears past 31 days, with a total principal balance of \$14,635 [December 31, 2023 – 14 mortgages with a balance of \$6,524]. These are primarily uninsured mortgages. The Company has estimated expected credit loss provisions on these mortgages as described in note 3.

6. Mortgage and loan investments

Mortgage and loan investments consist of two portfolios: commercial first and second mortgages held for various terms, the majority of which mature within one year; and residential first mortgages which are held to maturity.

Except for a portion of the residential loan portfolio that is classified as amortized cost, mortgage and loans are measured at FVTPL with any change in fair value being immediately recognized in income. The portion of the residential loan portfolio that is classified at amortized cost has a total balance of \$83,093 as at September 30, 2024 [December 31, 2023 – \$45,327] which is subject to expected credit loss. The Company did not record any losses of fair value related to the commercial segment investments during the quarters ended September 30, 2024 and 2023.

The portfolio as at September 30, 2024 contains \$13,034 [December 31, 2023 – \$21,837] of insured mortgages and \$132,203 [December 31, 2023 – \$249,084] of uninsured mortgage and loan investments. Of the uninsured mortgages as at September 30, 2024, approximately \$1,109 [December 31, 2023 – \$2,439] have principal balance in arrears of more than 30 days.

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

7. Other assets

The components of other assets are as follows as at:

	September 30, 2024	December 31, 2023
	\$	\$
Property, plant and equipment, net	33,215	36,285
Right-of-use assets	43,434	46,648
Goodwill	29,776	29,776
	106,425	112,709

The right-of-use assets pertain to five premises leases for the Company's office space. The leases have remaining terms of one to fourteen years. The related lease liability of \$47,428 as at September 30, 2024 [December 31, 2023 – \$49,686] is grouped with accounts payable and accrued liabilities on the interim condensed consolidated statements of financial position.

The recoverable amount of the Company's goodwill is calculated by reference to the Company's market capitalization, mortgages under administration, origination volume, and profitability. These factors indicate that the Corporation's recoverable amount exceeds the carrying value of its net assets and accordingly, goodwill is not impaired.

8. Mortgages under administration

As at September 30, 2024, the Company managed mortgages under administration of \$150,568,194 [December 31, 2023 – \$143,546,966], including mortgages held on the Company's interim condensed consolidated statements of financial position. Mortgages under administration are serviced for financial institutions such as banks, insurance companies, pension funds, mutual funds, trust companies, credit unions and securitization vehicles. As at September 30, 2024, the Company administered 331,387 mortgages [December 31, 2023 – 333,488] for 76 institutions and securitization conduits [December 31, 2023 – 83] with an average remaining term to maturity of 40 months [December 31, 2023 – 40 months].

First National Financial Corporation

Notes to interim condensed consolidated financial statements

[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

Mortgages under administration are serviced as follows:

	September 30, 2024 \$	December 31, 2023 \$
Institutional investors	103,214,226	100,340,846
Mortgages accumulated for sale or securitization and mortgage and loan investments	2,304,381	2,819,648
Mortgages pledged under securitization	44,043,284	39,264,199
CMBS conduits	1,006,303	1,122,273
	150,568,194	143,546,966

The Company's exposure to credit loss is limited to mortgage and loan investments as described in note 6, securitized mortgages as described in note 3 and uninsured mortgages held in mortgages accumulated for securitization as described in note 5.

The Company maintains trust accounts on behalf of the investors it represents. The Company also holds municipal tax funds in escrow for mortgagors. Since the Company does not hold a beneficial interest in these funds, they are not presented on the interim condensed consolidated statements of financial position. The aggregate of these accounts as at September 30, 2024 was \$651,713 [December 31, 2023 – \$742,373].

9. Bank indebtedness

Bank indebtedness includes a revolving credit facility of \$1,500,000 as at September 30, 2024 [December 31, 2023 – \$1,500,000] maturing in March 2029. At September 30, 2024, \$999,529 [December 31, 2023 – \$1,083,000] was drawn, of which the following have been pledged as collateral:

- [a] A general security agreement over all assets, other than real property, of the Company; and
- [b] A general assignment of all mortgages owned by the Company.

The credit facility bears a variable rate of interest based on prime and bankers' acceptance rates.

10. Debt related to securitized mortgages

Debt related to securitized mortgages represents the funding for mortgages pledged under the NHA-MBS, CMB and ABCP programs. As at September 30, 2024, debt related to securitized mortgages was \$43,985,222 [December 31, 2023 – \$38,880,798], net of unamortized discount of \$378,412 [December 31, 2023 – \$438,538]. A comparison of the carrying amounts of the pledged mortgages and the related debt is summarized in note 3.

Debt related to securitized mortgages is reduced on a monthly basis when the principal payments received from the mortgages are applied. Debt discounts and premiums are amortized over the term of each debt on an effective yield basis. Debt related to securitization mortgages had a similar contractual maturity profile as the associated mortgages in mortgages pledged under securitization.

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[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

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11. Shareholders' equity

[a] Authorized

Unlimited number of common shares

Unlimited number of cumulative 5-year rate reset preferred shares, Class A Series 1

Unlimited number of cumulative 5-year rate reset preferred shares, Class A Series 2

[b] Capital stock activities

	Common shares		Preferred shares	
	#	\$	#	\$
Balance, September 30, 2024 and December 31, 2023	59,967,429	122,671	4,000,000	97,394

[c] Earnings per share

	Three months ended		Nine months ended	
	September 30, 2024	September 30, 2023	September 30, 2024	September 30, 2023
	\$	\$	\$	\$
Net income attributable to shareholders	36,409	83,630	140,371	208,562
Less dividends declared on preferred shares	(983)	(964)	(2,957)	(2,852)
Net earnings attributable to common shareholders	35,426	82,666	137,414	205,710
Number of common shares outstanding	59,967,429	59,967,429	59,967,429	59,967,429
Basic earnings per common share	0.59	1.38	2.29	3.43

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12. Financial instruments and risk management

Fair value measurement

The Company uses the following hierarchy for determining and disclosing the fair value of financial instruments recorded at fair value in the interim condensed consolidated statements of financial position:

Level 1 – quoted market price observed in active markets for identical instruments;

Level 2 – quoted market price observed in active markets for similar instruments or other valuation techniques for which all significant inputs are based on observable market data; and

Level 3 – valuation techniques in which one or more significant inputs are unobservable.

Valuation methods and assumptions

The Company uses valuation techniques to estimate fair values, including reference to third-party valuation service providers using proprietary pricing models and internal valuation models such as discounted cash flow analysis. The valuation methods and key assumptions used in determining fair values for the financial assets and financial liabilities are as follows:

[a] Mortgage and loan investments

Commercial segment mortgages and certain residential loans are measured at FVTPL. The fair value of these mortgages is based on non-observable inputs and is measured at management's best estimate of the fair value.

[b] Deferred placement fees receivable

The fair value of deferred placement fees receivable at inception is determined by internal valuation models using market data inputs, where possible. The fair value is determined by discounting the expected future cash flows related to the placed mortgages at market interest rates. The expected future cash flows are estimated based on certain assumptions which are not supported by observable market data.

[c] Securities owned and sold short

The fair values of securities owned and sold short used by the Company to hedge its interest rate exposure are determined by quoted prices on a secondary market.

[d] Servicing liability

The fair value of the servicing liability at inception is determined by internal valuation models using market data inputs, where possible. The fair value is determined by discounting the expected future cost related to the servicing of explicit mortgages at market interest rates. The expected future cash flows are estimated based on certain assumptions which are not supported by observable market data.

[e] Other financial assets and financial liabilities

The fair value of mortgages accumulated for sale, cash held as collateral for securitization, restricted cash and bank indebtedness correspond to the respective outstanding amounts due to their short-term maturity profiles.

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[Unaudited – in thousands of Canadian dollars, except per share amounts or unless otherwise noted]

September 30, 2024

[f] Fair value of financial instruments not carried at fair value

The fair values of these financial instruments are determined by discounting projected cash flows using market industry pricing practices, including the rate of unscheduled prepayment. Discount rates used are determined by comparison to similar term loans made to borrowers with similar credit. This methodology will reflect changes in interest rates which have occurred since the mortgages were originated. These fair values are estimated using valuation techniques in which one or more significant inputs are unobservable [Level 3], and are calculated for disclosure purposes only.

Carrying value and fair value of selected financial instruments

The fair value of the financial assets and financial liabilities of the Company approximates its carrying value as at September 30, 2024, except for mortgages pledged under securitization, which have a carrying value of \$44,392,673 [December 31, 2023 – \$39,427,192] and a fair value of \$44,583,156 [December 31, 2023 – \$38,647,614], debt related to securitized mortgages, which has a carrying value of \$43,985,222 [December 31, 2023 – \$38,880,798] and a fair value of \$43,085,714 [December 31, 2023 – \$37,270,328], and senior unsecured notes, which have a carrying value of \$798,425 [December 31, 2023 – \$598,745] and a fair value of \$814,720 [December 31, 2023 – \$590,820]. These fair values are estimated using valuation techniques in which one or more significant inputs are unobservable [Level 3].

The following tables represent the Company's financial instruments measured at fair value on a recurring basis:

	September 30, 2024			
	Level 1	Level 2	Level 3	Total
	\$	\$	\$	\$
Financial assets				
Mortgages accumulated for sale	—	102,368	—	102,368
Mortgage and loan investments	—	—	62,144	62,144
Total financial assets	—	102,368	62,144	164,512
Financial liabilities				
Securities sold short	—	2,496,871	—	2,496,871
Interest rate swaps	—	3,918	—	3,918
Total financial liabilities	—	2,500,789	—	2,500,789

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September 30, 2024

	December 31, 2023		
	Level 1	Level 2	Level 3
	\$	\$	\$
			Total
			\$
Financial assets			
Mortgages accumulated for sale	—	27,113	—
Mortgage and loan investments	—	—	189,523
Total financial assets	—	27,113	189,523
			216,636
Financial liabilities			
Securities sold short	—	2,649,249	—
Interest rate swaps	—	7,616	—
Total financial liabilities	—	2,656,865	—
			2,656,865

In estimating the fair value of financial assets and financial liabilities using valuation techniques or pricing models, certain assumptions are used including those that are not fully supported by observable market prices or rates [Level 3]. The amount of the change in fair value recognized by the Company in net income that was estimated using a valuation technique based on assumptions that are not fully supported by observable market prices or rates was nil for the three months ended September 30, 2024 and 2023. Although the Company's management believes that the estimated fair values are appropriate as at the date of the interim condensed consolidated statements of financial position, those fair values may differ if other reasonably possible alternative assumptions are used.

Transfers between levels in the fair value hierarchy are deemed to have occurred at the beginning of the period in which the transfer is made. Transfers between levels can occur as a result of additional or new information regarding valuation inputs and changes in their observability. During the quarter, there were no transfers between levels.

The following table presents changes in the fair values including realized losses of \$75,578 [2023 – gains of \$50,260] of the Company's financial assets and financial liabilities for the three months ended September 30, 2024 and 2023, all of which have been classified as FVTPL:

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
FVTPL mortgages	—	61	—	61
Securities sold short	(28,654)	19,105	(26,923)	43,335
Interest rate swaps	3,089	(731)	2,497	(4,381)
	(25,565)	18,435	(24,426)	39,015

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Movement in Level 3 financial instruments measured at fair value

The following tables show the movement in Level 3 financial instruments in the fair value hierarchy for the nine months ended September 30, 2024 and 2023. The Company classifies financial instruments as Level 3 when there is reliance on at least one significant unobservable input in the valuation models.

	Fair value as at January 1, 2024 \$	Investments \$	Unrealized gains recorded in income \$	Payment and amortization \$	Fair value as at September 30, 2024 \$
Financial assets					
Mortgage and loan investments	189,523	526,874	—	(654,253)	62,144

	Fair value as at January 1, 2023 \$	Investments \$	Unrealized gains recorded in income \$	Payment and amortization \$	Fair value as at September 30, 2023 \$
Financial assets					
Mortgage and loan investments	164,919	714,484	61	(779,563)	99,901

13. Capital management

The Company's objective is to maintain a capital base so as to maintain investor, creditor and market confidence and sustain future development of the business. Management defines capital as the Company's common share capital and retained earnings. FNFLP has a minimum capital requirement as stipulated by its bank credit facility. The agreement limits the debt under bank indebtedness together with the unsecured notes to four times FNFLP's equity. As at September 30, 2024, the ratio was 2.09:1 [December 31, 2023 – 1.89:1]. The Company was in compliance with the bank covenant throughout the period.

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14. Earnings by business segment

The Company operates principally in two business segments, Residential and Commercial. These segments are organized by mortgage type and contain revenue and expenses related to origination, underwriting, securitization and servicing activities. Identifiable assets are those used in the operations of the segments.

	Three months ended September 30, 2024			Nine months ended September 30, 2024		
	Residential	Commercial	Total	Residential	Commercial	Total
	\$	\$	\$	\$	\$	\$
Revenue						
Interest revenue – securitized mortgages	294,070	124,828	418,898	824,946	355,094	1,180,040
Interest expense – securitized mortgages	(253,468)	(105,244)	(358,712)	(714,092)	(297,987)	(1,012,079)
Net interest – securitized mortgages	40,602	19,584	60,186	110,854	57,107	167,961
Placement and servicing	98,603	27,532	126,135	251,247	102,133	353,380
Mortgage investment income	27,065	13,853	40,918	72,089	35,798	107,887
Realized and unrealized losses on financial instruments	(25,565)	—	(25,565)	(24,426)	—	(24,426)
	140,705	60,969	201,674	409,764	195,038	604,802
Expenses						
Amortization	3,597	625	4,222	10,789	1,877	12,666
Interest	35,431	12,063	47,494	84,879	34,213	119,092
Other operating	80,633	19,636	100,269	215,014	66,959	281,973
	119,661	32,324	151,985	310,682	103,049	413,731
Income before income taxes	21,044	28,645	49,689	99,082	91,989	191,071
Identifiable assets	33,124,574	17,305,936	50,430,510	33,124,574	17,305,936	50,430,510
Goodwill	—	—	29,776	—	—	29,776
Total assets	33,124,574	17,305,936	50,460,286	33,124,574	17,305,936	50,460,286

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September 30, 2024

	Three months ended September 30, 2023			Nine months ended September 30, 2023		
	Residential	Commercial	Total	Residential	Commercial	Total
	\$	\$	\$	\$	\$	\$
Revenue						
Interest revenue – securitized mortgages	245,283	102,751	348,034	683,023	290,890	973,913
Interest expense – securitized mortgages	(203,870)	(86,463)	(290,333)	(572,707)	(242,628)	(815,335)
Net interest – securitized mortgages	41,413	16,288	57,701	110,316	48,262	158,578
Placement and servicing	115,446	38,708	154,154	300,601	105,834	406,435
Mortgage investment income	34,282	7,956	42,238	79,314	22,167	101,481
Realized and unrealized gains on financial instruments	18,362	73	18,435	38,942	73	39,015
	209,503	63,025	272,528	529,173	176,336	705,509
Expenses						
Amortization	3,305	567	3,872	9,914	1,703	11,617
Interest	38,876	7,498	46,374	88,301	19,381	107,682
Other operating	89,368	19,084	108,452	248,357	53,841	302,198
	131,549	27,149	158,698	346,572	74,925	421,497
Income before income taxes	77,954	35,876	113,830	182,601	101,411	284,012
Identifiable assets	30,917,983	14,228,784	45,146,767	30,917,983	14,228,784	45,146,767
Goodwill	—	—	29,776	—	—	29,776
Total assets	30,917,983	14,228,784	45,176,543	30,917,983	14,228,784	45,176,543

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15. Related party and other transactions

The Company has servicing contracts in connection with commercial bridge and mezzanine mortgages originated by the Company and subsequently sold to various entities controlled by a senior executive and shareholder of the Company. The Company services these mortgages during their terms at market commercial servicing rates. During the quarter, the Company originated \$8,640 of new mortgages for the related parties. The related parties also funded several progress draws totaling \$1,157 on existing mortgages originated by the Company. All such mortgages, which are administered by the Company, have a balance of \$188,235 as at September 30, 2024 [December 31, 2023 – \$204,011].

A senior executive and shareholder of the Company has a significant investment in a mortgage default insurance company. In the ordinary course of business, the insurance company provides insurance policies to the Company's borrowers at market rates. In addition, the insurance company has also provided the Company with portfolio insurance at market premiums. The total bulk insurance premium paid by the Company during the three months ended September 30, 2024 was \$2,881 [2023 – \$1,402], net of third-party investor reimbursement.

A senior executive and shareholder of the Company has a significant investment in a Canadian bank. The Company has an agreement to originate and adjudicate applications for secured credit cards for the bank. These applications are originated through the Company's mortgage broker relationships. The Company receives a market fee for successfully adjudicating such applications.

A senior executive and shareholder of the Company has a significant investment in a Canadian financial institution. The Company has existing agreements to service mortgages with the financial institution. As at September 30, 2024, the Company administered a \$4,761,842 [December 31, 2023 – \$5,132,839] mortgage portfolio for the financial institution at market servicing rates.

First National Financial Corporation

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