FIRST NATIONAL

FINANCIAL CORPORATION

Report to Shareholders

Period Ended March 31, 2017

100 University Avenue, Suite 700, North Tower, Toronto, ON M5J 1V6
www.firstnational.ca

Fellow Shareholders:

We are pleased to provide this report for the three months ended March 31, 2017. During this period, First National came very close to equaling last year's first quarter performance despite lower residential housing market activity in Western Canada, and intensified competition fueled by government changes to mortgage rules.

Mortgages under administration increased 5% to $99.1 billion from $94.3 billion at March 31, 2016. Revenue increased 1% to $232.2 million from $231.4 million in the first quarter of 2016. Net income was $36.1 million or $0.58 per common share compared to $37.3 million ($0.59 per common share) a year ago and Pre-Fair Market Value EBITDA, a non-IFRS measure that removes the impact of gains and losses on financial instruments, was $53.1 million, down 7% from $56.8 million a year ago.

Common share dividends in the first two months of 2017 were paid at an annualized rate of $1.70 per share, increasing to $1.85 per share annualized for the period March 1 to March 31, 2017 reflecting our Board's decision to increase the payout by 9%.

For the remainder of 2017, we anticipate lower seasonal origination in our residential segment as the full impact of new mortgage insurance rules announced in October 2016 and the higher cost of portfolio insurance affect the Company. Recent Ontario Government announcements of a foreign buyer's tax and rent controls may also affect our business but at this early stage we are unable to assess the impact on First National.

In the face of these challenges, the Company will seek to grow its commercial segment business, focus on the significant value of single family renewal opportunities and continue to generate income and cash flow from its $26 billion portfolio of mortgages pledged under securitization and $73 billion servicing portfolio.

We look forward to reporting our second quarter results in July, 2017 and to hosting our shareholders at the First National annual meeting on May 3, 2017 at the TMX Broadcast Centre in Toronto beginning at 9 am eastern time.

Yours sincerely,

Stephen Smith
Chairman and Chief Executive Officer

Moray Tawse
Executive Vice President

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 April 25, 2017. This discussion should be read in conjunction with the unaudited 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 (the "period") ended March 31, 2017. The unaudited 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 EBITDA" and "After tax Pre-FMV Dividend Payout Ratio" should not be construed as alternatives to net income or loss or other comparable measures determined in accordance with IFRS as an indicator of performance or as a measure of liquidity and cash flow. These measures do not have standard meanings prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers.

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

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

General Description of the Company

First National Financial Corporation is the parent company of First National Financial LP ("FNFLP"), a Canadian-based originator, underwriter and servicer of predominantly prime residential (single-family and multi-unit) and commercial mortgages. With almost $100 billion in mortgages under administration ("MUA"), First National is Canada's largest non-bank originator and underwriter of mortgages and is among the top three in market share in the mortgage broker distribution channel.

First National consolidates its interest in First National Mortgage Investment Fund (the "Fund"). Although the Company only owns about 21% of the units issued by the Fund, because of its status as sole seller to the Fund and its rights as promoter, the application of IFRS suggests that First National exercises control over the Fund. The Fund was created to obtain economic exposure to a diversified portfolio of primarily commercial mezzanine mortgages. Through the Fund's consolidation, the Company has effectively taken on a portfolio of about $42 million (December 31, 2016 - $42 million) of mortgages. Because of the Company's small proportionate interest in the Fund's units, it has also recorded a $28 million (December 31, 2016 - $28 million) non-controlling interest in equity which offsets these assets.

First Quarter 2017 Results Summary

Management is pleased with the results for the first quarter of 2017. Despite lower origination particularly in Western Canada, overall origination was slightly above that recorded in the 2016 first quarter. The Company also continued to invest in its portfolio of securitized mortgages.

- MUA grew to $99.1 billion at March 31, 2017 from $94.3 billion at March 31, 2016, an increase of 5%. MUA has decreased from December 31, 2016, when MUA was $99.4 billion, representing an annualized decrease of 1%. The decrease is the result of the typically slow first quarter for single-family mortgages made slower by tighter mortgage rules and, the maturity of several CMBS transactions originally put into MUA in 2007. Because of scheduled maturities in this portfolio, commercial segment is down by over $500 million since the 2016 year end;
- The Canadian single-family mortgage market slowed somewhat to start 2017, the result of the continued oil-related slowdown evident in western Canada, a new tax regime in British Columbia and tighter mortgage insurance rules announced in early October 2016. Total new single-family mortgage origination was $1.9 billion in first quarter 2017 compared to $2.0 billion in the 2016 comparative quarter. The primary reason for the change was a 12% combined decline in origination from First National's Calgary and Vancouver office. The commercial segment had a good start to 2017, increasing origination volumes to $945 million in the 2017 quarter from $886 million in 2016. The Company attributes this positive performance to its expanded presence in the conventional mortgage market. Overall origination increased by less than 1% year over year;
- The Company took advantage of opportunities in the quarter to renew $1.0 billion of single-family mortgages. In the first quarter of 2016, the Company renewed $929 million of single-family mortgages. The growth is attributable to more mortgages up for renewal than in the prior year. For the commercial segment, renewals increased to $332 million from $162 million, as the Company was able to renew some large construction mortgages into ten year terms during the 2017 quarter;
- Revenue for the first quarter of 2017 increased to $232.2 million from $231.4 million in the 2016 comparative quarter. The small increase of less than 1% is largely attributable to the increase in interest on securitized mortgages offset by lower placement fees the result of the Company's decision to allocate more of its origination to its securitization business;
- Income before income taxes decreased from $50.7 million in 2016 to $49.2 million in 2017. This measure decreased largely because of lower placement fees earned because of lower volumes allocated to institutional investors. This decrease in net placement fees offsets increases in net margin from securitized mortgages, deferred placement fees and mortgage interest income. In 2016, income before income taxes was reduced by $1.25 million of amortization on intangible assets. These asset were fully amortized in 2016 and accordingly had no effect on 2017; and
- The Company's earnings before income taxes, depreciation and amortization ("Pre-FMV EBITDA") for the quarter decreased by **7%,** from $56.8 million in 2016 to $53.1 million in 2017. The decrease was due to lower placement fees as described above.

Outstanding Securities of the Corporation

At March 31, 2017 and April 25, 2017, the Corporation had 59,967,429 common shares, 2,887,147 Class A preference shares, Series 1, 1,112,853 Class A preference shares, Series 2, and 175,000 April 2020 notes outstanding.

Selected Quarterly Information

Quarterly Results of First National Financial Corporation

($000s, except per share amounts)

	Revenue	Net Income for the period	Pre-FMV EBITDA for the period (1)	Net Income per Common Share	Total Assets
2017					
First Quarter	$232,238	$36,127	$53,084	$0.58	$29,901,289
2016					
Fourth Quarter	$290,754	$71,797	$61,064	$1.18	$30,394,465
Third Quarter	$273,754	$51,440	$67,469	$0.84	$30,527,361
Second Quarter	$253,915	$41,251	$68,187	$0.67	$31,011,683
First Quarter	$231,395	$37,341	$56,819	$0.59	$28,194,301
2015					
Fourth Quarter	$250,008	$41,084	$58,527	$0.66	$27,926,732
Third Quarter	$246,641	$29,308	$60,955	$0.46	$27,624,359
Second Quarter	$251,206	$42,538	$52,012	$0.68	$27,585,945

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

With First National's large portfolio of mortgages pledged under securitization, quarterly revenue is driven primarily by the gross interest earned on the mortgages pledged under securitization. The gross interest on the mortgage portfolio is dependent both on the size of the portfolio of mortgages pledged under securitization as well as weighted average mortgage rates. Although mortgage rates have not changed significantly in the last two years, the Company has generally increased MUA and its portfolio of securitized mortgages over the last 24 months. Net income is partially dependent on conditions in the debt markets, which affect the value of gains and losses on financial instruments arising from the Company's interest rate hedging program. Accordingly, the movement of this measurement between quarters is related to factors external to the Company's core business (primarily conditions in the bond markets). By removing this volatility and analyzing Pre-FMV EBITDA, management believes a more appropriate measurement of the Company's performance can be assessed.

Generally, in the last eight quarters, the Company has grown its origination volumes in order to build its servicing portfolio and to enable it to securitize larger amounts of mortgages in the NHA-MBS market. This longer-term strategy has been successful and Pre-FMV EBITDA has trended upwards. The table above shows a trend of growing income reflecting typical Canadian seasonality: slower first and fourth quarters and stronger mid-year quarters. The third quarter of 2015 suffered because of large losses on account of the fair value of financial instruments. Both the fourth quarter of 2015 and the first quarters of 2017 and 2016 did not have significant fair value losses and are more consistent with normalized operations of the Company. The fourth quarter of 2016 featured large fair values gains as bond prices decreased as a result of expectations from the results of the US election. This had a large impact on net income. By excluding fair value losses, Pre-FMV EBITDA for Q1 2017 declined by 7% compared to the first quarter of 2016 as lower placement fees in a slow housing market reduced earnings. With a growing base of income from the securitization portfolio and third-party servicing MUA, the Company is able to provide consistent earnings performance.

Selected Annual Financial Information and Reconciliation to Pre-FMV EBITDA

($000s, except per share amounts)

	2016	2015	2014
For the Year ended December 31, Income Statement Highlights			
Revenue	1,049,818	915,315	803,107
Interest expense – securitized mortgages	(495,681)	(488,659)	(434,726)
Brokerage fees	(103,719)	(107,045)	(77,105)
Salaries, interest and other operating expenses	(169,129)	(161,821)	(143,062)
Add (deduct): realized and unrealized (gains) losses on financial instruments	(27,750)	52,143	34,916
Pre-FMV EBITDA(1)	253,539	209,933	183,130
Amortization of capital assets	(4,660)	(4,114)	(2,909)
Amortization of intangible assets	(2,500)	(5,000)	(5,000)
Add (deduct): realized and unrealized gains (losses) on financial instruments	27,750	(52,143)	(34,916)
Provision for income taxes	(72,300)	(39,245)	(35,840)
Net income	201,829	109,431	104,465
Common share dividends declared	98,946	90,451	88,952
Per Share Highlights			
Net income per common share	3.28	1.71	1.62
Dividends per common share	1.65	1.51	1.48
At Year End Balance Sheet Highlights Total assets	30,394,465	27,926,732	25,953,914
Total long-term financial liabilities	174,556	174,420	176,418

Notes:

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

Vision and Strategy

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

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

Key Performance Drivers

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

- Growth in the portfolio of mortgages under administration;
- Growth in the origination of mortgages;
- 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, longer-term value from servicing fees, mortgage administration fees, renewals and the growth of the customer base for marketing initiatives. As at March 31, 2017, MUA totalled $99.1 billion, up from $94.3 billion at March 31, 2016, an increase of 5%. This compares to $99.4 billion at December 31, 2016, representing an annualized decrease of 1% and reflects the maturity of $500 million of CMBS mortgages which had been in MUA since 2007 and slower single family originations typical of the first quarter.

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. By growing origination, not only can the Company satisfy demand from its institutional customers, but it can also produce volume for its own securitization programs. With the combination of decreased origination of 12% out of its Calgary and Vancouver offices, the Company's single-family origination decreased in the first quarter of 2017 by 3%. The commercial segment had a good start to the year as volume increased 7% over the first quarter of 2016. Together, overall origination for the first quarter of 2017 increased only marginally or by less than 1% year over year.

Third Party Mortgage Underwriting and Fulfillment Processing Services

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

Raising Capital for Operations

Bank Credit Facility

The Company uses a $1 billion revolving line of credit with a syndicate of banks. This facility enables the Company to fund the large amounts of mortgages accumulated for securitization. In the first quarter of 2017, the Company extended the term of the facility by almost two years such that the new maturity is in March 2022. 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 available to fund mortgages originated for securitization purposes; (2) the debt is revolving and can be used and repaid as the Company requires, providing more flexibility than the senior unsecured notes, which are fully drawn during their term; (3) the five-year 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.

Preferred Share Issuance

On February 24, 2016, the Company announced that it would not exercise its right to redeem the 4,000,000 Class A Series 1 preference shares issued in 2011. It also advised shareholders of their rights under the shares which allow for a one-for-one conversion from Series 1 shares which have a fixed rate dividend into Series 2 shares which have a floating rate dividend. Pursuant to these rights, a portion of Series 1 shareholders elected to convert 1,112,853 of the Series 1 shares into Series 2 shares. Accordingly, effective April 1, 2016, 1,112,853 Series 1 shares converted to Series 2 shares leaving 2,887,147 Series 1 shares outstanding. The Series 1 shares will continue to trade as FN.PR.A on the TSX, while the Series 2 shares began trading as FN.PR.B on April 1, 2016. The Series 1 shares provide an annual dividend rate of 2.79% effective April 1, 2016. Both the Series 1 and Series 2 shares pay quarterly dividends, subject to Board of Director approval and are redeemable at the discretion of the Company such that after the five-year term ending on March 31, 2021, the Company can choose to extend the shares for another five-year term at a fixed spread (2.07%) over the relevant index (5 year Government of Canada bond yield for any Series 1 shares or the 90 day T-Bill rate for any Series 2 shares). While the investors in these shares have an option on each five-year anniversary to convert their Series 1 preference shares into Series 2 preference shares (or 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 and classifies the shares as equity on its balance sheet. Management believes this capital has provided the Company with the opportunity to pursue its strategy of increased securitization, which requires upfront investment.

Employing Securitization Transactions to Minimize Funding Costs

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

The Company has been involved in the issuance of NHA-MBS as an administrator since 1995. In December 2007, the Company was approved by Canada Mortgage and Housing Corporation ("CMHC") as an issuer of NHA-MBS and as a seller into the CMB program. Issuer status has provided the Company with direct and independent access to reliable and low cost funding.

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

Period	Average five year Mortgage Spread for the Period
2006	1.12%
2007	1.50%
2008	2.68%
2009 - 2013	1.79%
2014	1.57%
2015	1.87%
2016	1.76%
Q1 2017	1.76%

The table shows an average spread of 1.12% in 2006. With the credit crisis, this spread ballooned to as high as 3.46% in 2008. Between 2009 and 2013, liquidity issues at financial institutions diminished and the competition for mortgages increased such that spreads remained consistently higher than pre-crisis levels. In 2014, more competitive pressures took mortgage rates lower and compressed mortgage spreads to 2007 levels. In 2015, mortgage spreads quickly widened as a slowdown in economic growth and the Bank of Canada rate cut reduced bond yields dramatically. While funding spreads have also moved out, spreads are wide enough to support the Company's securitization program. This trend continued into 2016, as optimism about the economy was mixed such that spreads remained at levels in excess of 1.8% until the third quarter when increased competition tightened spreads even further. In the first quarter of 2017, the Company originated and renewed for securitization purposes approximately $1.6 billion of single-family mortgages and $0.1 million of multi-unit residential mortgages. In the quarter, the Company securitized through NHA-MBS approximately $1.3 billion of single-family mortgages and $0.1 billion of multi-unit residential mortgages.

In August 2013, CMHC announced that it would be limiting the amount of guarantees it would provide on NHA-MBS pools created for sale to the "market". CMHC indicated that the amount of guarantees it was providing for such market pools (generally any pool not sold to the Canada Housing Trust ("CHT") for the CMB) was growing significantly. In order to better control the absolute amount of risk that it takes on in this respect, CMHC has implemented policies to allocate the amount of guarantees to issuers. The maximum amount allocated under the process has exceeded First National's requirements in every quarter since inception. The process was amended in July 2016 to combine both NHA MBS for sale to the market and to CHT under one allocation. The available guarantees to be allocated were increased to accommodate issuance to CHT and continue to exceed the Company's current needs.

Canada Mortgage Bonds Program

The CMB program is an initiative sponsored by CMHC whereby the CHT issues securities to investors in the form of semi-annual interest-yielding five- and 10-year bonds. Pursuant to the Company's approval as a seller into the CMB, the Company is able to make direct sales into the program. 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. Beginning in July 2016, CHT effectively increased the price of the timely payment guarantees which CMB participants are required to purchase with the issuance of each CMB transaction. Although nominally CMB fees were decreased, the new rules require guarantee fees to be levied on the creation of NHA MBS pools being sold to the CMB. Prior to this rule change, the NHA MBS pools to be sold into the CMB were exempt from such fees. In aggregate, guarantee fees have increased between 25 and 50% for CMB participants. This increase translates to approximately 5 basis points of cost over the term of the securitization. At the same time, CMHC has also modified the tiered NHA MBS guarantee fee pricing structure, increasing the issuance threshold for increased fees from $6.0 billion to $7.5 billion.

Key Performance Indicators

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

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

- Dividend payout ratio.

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

	Quarter ended	
	March 31, 2017	**March 31, 2016**
For the Period	**($ 000's)**	
Revenue	232,238	231,395
Income before income taxes	49,157	50,691
Pre-FMV EBITDA (1)	53,084	56,819
At Period end		
Total assets	29,901,289	28,194,301
Mortgages under administration	99,061,532	94,275,930

Note:

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

Since going public in 2006, First National has been considered a high-yielding dividend paying company. Over this period, the Company has paid more than $920 million of dividends/distributions to common shareholders/ unitholders. With a large MUA which generates continuing income and cash flow and a business model which is designed to make efficient use of capital, the Company has been able to pay distributions to its shareholders which represent a relatively large ratio of its earnings. The Company calculates the dividend payout ratio as dividends declared on common shares over net income attributable to common shareholders. This measure is useful to shareholders as it indicates the percentage of earnings which have been paid out in dividends. Similar to the performance measure for earnings, the Company also calculates the dividend payout ratio on a basis using after tax Pre-FMV EBITDA.

Determination of Common Share Dividend Payout Ratio

	Quarter ended March 31, 2017	March 31, 2016
For the Period	**($ 000's)**	
Net income attributable to common shareholders	34,930	35,594
Dividends paid or declared on common shares	26,236	23,237
Common Share Dividend Payout Ratio	75%	65%
After tax Pre-FMV Dividend Payout Ratio (1)	71%	61%

Note:

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

For the quarter ended March 31, 2017, the common share payout ratio was 75% compared to 65% in the comparative 2016 quarter. In the first quarter of 2017 and 2016, the Company recorded losses on account of the changes in fair value of financial instruments. The losses are recorded in the period in which yields on Government of Canada bond yields change; however, the offsetting economic impact is largely reflected in wider spreads on the mortgages pledged for securitization and will be generally realized in net interest margin over the terms of the mortgages. If the losses on financial instruments in both years are excluded from the above calculations, the dividend payout ratio for 2017 would have been 71% compared to 61% in 2016.

The Company also paid $0.68 million of dividends on its preferred shares in the first quarter of 2017 compared to $1.16 million in the 2016 first 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. Depending upon market conditions, either an institutional placement or a securitization conduit may be the most cost-effective means for the Company to fund individual mortgages. In general, originations are allocated from one funding source to another depending on market conditions and strategic considerations related to maintaining diversified funding sources. The Company retains servicing rights on virtually all of the mortgages it originates, which provide the Company with servicing fees to complement revenue earned through originations. For both quarters ended March 31, 2017 and 2016, new origination volume was $2.9 billion.

Securitization

The Company securitizes a portion of its origination through various vehicles, including NHA-MBS, CMB and Asset-backed Commercial Paper ("ABCP"). Although legally these transactions represent sales of mortgages, for accounting purposes they do not meet the requirements for sale recognition and instead are accounted for as secured financings. These mortgages remain as mortgage assets of the Company for the full term and are funded with securitization-related debt. Of the Company's $4.3 billion of new originations and renewals for the quarter ended March 31, 2017, $1.6 billion was originated for its own securitization programs.

Placement Fees and Gain on Deferred Placement Fees

The Company recognizes revenue at the time that a mortgage is placed with an institutional investor. Cash amounts received in excess of the mortgage principal at the time of placement are recognized in revenue as "placement fees". The present value of additional amounts expected to be received over the remaining life of the mortgage sold (excluding normal market-based servicing fees) is recorded as a "deferred placement fee". A deferred placement fee arises when mortgages with spreads in excess of a base spread are sold. Normally the Company would earn an upfront cash placement fee, but investors prefer paying the Company over time as they earn net interest margin on such transactions. Upon the recognition of a deferred placement fee, the Company establishes a "deferred placement fee receivable" that is amortized as the fees are received by the Company. Of the Company's $4.3 billion of new originations and renewals in the first quarter of 2017, $2.5 billion was placed with institutional investors.

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

Mortgage Servicing and Administration

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

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

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

Results of Operations

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

	Quarter ended March 31, 2017	March 31, 2016
	($ millions)	
Mortgage Originations by Segment		
New Single-family residential	1,936	1,986
New Multi-unit and commercial	945	886
Sub-total	2,881	2,872
Single-family residential renewals	1,048	929
Multi-unit and commercial renewals	332	162
Total origination and renewals	4,261	3,963
Mortgage Originations by Funding Source		
Institutional investors – new residential	1,085	1,317
Institutional investors – renew residential	299	409
Institutional investors – multi/commercial	1,086	773
NHA-MBS/ CMB/ ABCP securitization	1,667	1,363
Internal Company resources /CMBS	124	101
Total	4,261	3,963
Mortgages under Administration		
Single-family residential	76,945	73,668
Multi-unit residential and commercial	22,117	20,608
Total	99,062	94,276

Total new mortgage origination volumes increased in the first quarter of 2017 compared to 2016 by less than 1%. Single-family volumes decreased by 3% and commercial segment volumes increased by 7% year over year as demand for housing and commercial real estate continued but was mitigated by regional disparities. Most of the decrease in the single-family segment is due to 12% lower volumes from the Company’s Vancouver and Calgary offices as real estate markets slowed in both regions. In the other parts of Canada, the Company’s volumes were up 9% in Ontario and down 6% in Quebec. When combined with renewals, total production increased from $4.0 billion in the 2016 first quarter to $4.3 billion in 2017, or almost 8%. The low interest rate environment which existed for most of 2016 continued in 2017. Low mortgage rates, which stimulate increased real estate transactions, together with the Company’s expertise in mortgage underwriting, drove origination volumes. Origination for direct securitization into NHA-MBS, CMB and ABCP programs remained a large part of the Company’s strategy with volumes of $1.7 billion in the first quarter of 2017. The Company used more securitization to begin 2017 as opposed to institutional placements to fund its origination than in 2016. Generally securitization spreads narrowed in 2017 to improve the profitability of this funding source. This may be the result of increased demand for NHA MBS pursuant to the changes in the mortgage insurance announced by the Minister of Finance in October 2016. With lower availability of insured mortgages, investors may be anticipating a scarcity of NHA MBS in the near future such that recent demand has increased and credit spreads have narrowed accordingly.

Net Interest - Securitized Mortgages

Comparing the quarter ended March 31, 2017 to the quarter ended March 31, 2016, "net interest – securitized mortgages" increased by 2% to $37.2 million from $36.6 million. The increase was due to a larger portfolio of securitized mortgages offset by a slightly tighter weighted-average spreads on the portfolio year over year. The portfolio of mortgages funded through securitization increased by 4% from $25.0 billion as at March 31, 2016 to $26.1 billion as at March 31, 2017. Net interest is also affected by the amortization of deferred origination and other costs that are capitalized on securitized mortgages. The charge for this amortization has increased with higher per unit broker fees.

Placement Fees

Placement fee revenue decreased by 24% to $26.6 million from $34.9 million in 2016. New residential origination volume for institutional customers, excluding renewals, decreased from $1.3 billion in the first quarter of 2016 to $1.1 billion in the 2017 quarter or by 18%. Placement fees were also reduced between the two quarters from renewal transactions. In 2016, renewals were largely placed with institutional investors. In 2017 the Company has retained more of these mortgages for its own securitization programs. This accounts for a 5% drop five in overall placement fees between the two first quarters.

Gains on Deferred Placement Fees

Gains on deferred placement fees revenue increased 3% to $3.7 million from $3.6 million. The gains relate to multi-unit residential mortgages originated and sold to institutional NHA-MBS issuers. Although volumes for these transactions increased by 31% from the first quarter of 2016 to 2017, spreads on these transactions tightened such that the Company realized lower per unit gains.

Mortgage Servicing Income

Mortgage servicing income increased 6% to $30.2 million from $28.5 million. This increase was due to revenue earned on the underwriting and fulfillment processing services business which the Company launched in January 2015 which has successfully grown in the past 12 months. Without this revenue, mortgage servicing income grew in line with the MUA growth.

Mortgage Investment Income

Mortgage investment income increased 11% to $13.9 million from $12.5 million. The increase is due largely to the Company's securitization program. As the Company elects to securitize, it warehouses mortgages until securitization and earns interest at the face rate of the mortgage in the warehousing period. The amount of mortgages accumulated for sale has increased by 31% from $1.3 billion average for the first quarter of March 2016 to $1.7 billion for the first quarter of 2017. This growth has been offset by investment income on other assets which have not grown as quickly including mortgage and loan investments. A loan loss provision of $1.0 million (2016 - $0.5 million) was taken in the quarter on four non-performing related commercial mortgages, reducing mortgage investment income in both quarters.

Realized and Unrealized Gains (Losses) on Financial Instruments

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

Summary of realized and unrealized gains (losses) on financial instruments	Quarter ended March 31, 2017	March 31, 2016
	($ 000's)	
Losses on short bonds used for the economic hedging program	(3,467)	(5,053)
Gains on mortgages held at fair value	4,785	4,651
Losses on interest rate swaps	(4,053)	(3,426)
Other gains	-	95
Total losses on financial instruments	(2,735)	(3,733)

As 2016 began, economic sentiment was uncertain and 5-year bond prices increased which meant generally the Company recorded losses on its hedging program. In the fourth quarter of 2016, with the promise of increased economic stimulus from the election of the Republican candidate in the United States, the bond market moved dramatically and bond prices decreased significantly. This momentum subsided in the first quarter of 2017 and bond prices increased such that the result was First National's short bond position, which is used to economically hedge mortgages, had a small decrease in value in the quarter. This is comparable to 2016 which also featured losses on the Company's short bond position.

The Company uses short Government of Canada bonds (including CHT-issued bonds) together with repurchase agreements to create synthetic forward interest rate contracts to hedge the interest rate risk associated with fixed rate mortgages originated for its own securitization programs. For accounting purposes, these do not qualify as interest rate hedges as the bonds used are not derivatives but cash-based financial instruments. These gains or losses are recorded in the period in which the bond prices change; however, the offsetting economic gains or losses are not recorded in the same period. Instead, the resulting economic gain (or loss) will be reflected primarily in wider or narrower spreads on the mortgages pledged for securitization and will be realized in net interest margin over the terms of the mortgages and the related debts. In first quarter of 2017, the Company recorded losses on these instruments of $3.5 million (2016 – loss of $5.1 million). While the 2017 losses reduced net income earned in the quarter, the gross spread on the related portfolio of securitized mortgages going forward will be proportionally wider as the Company issues securitization-related debt at lower relative interest rates than it would have prior to the movement in bond yields. In order to adequately hedge its interest rate exposure, the Company had almost $950 million of bonds sold short as at March 31, 2017.

The portion of the Company's mortgages which is held at fair value (primarily those funded through ABCP), are also affected by changes in bond prices. Generally, lower bond yields (higher bond prices) increase the relative value of these mortgages. However, this mortgage portfolio is much smaller than the Company's short bond position, such that the impact to earnings is typically lower. The mortgages were also positively affected by a moderate tightening of mortgage funding credit spreads experienced in the first quarter of 2017. In the 2016 quarter these credit spreads widened to offset the positive impact of lower bond yields on such mortgages. Altogether these mortgages gained $4.8 million of fair value in the first quarter of 2017 (2016 - $4.7 million gain). The valuation of interest rate swaps, which are used primarily to manage the interest rate exposure from fixed-rate mortgages in the ABCP portfolio, was negatively affected in 2017 by changing bond yields such that unrealized losses of $4.0 million were incurred in the first quarter of 2017 (2016 - $3.4 million loss).

Brokerage Fees Expense

Brokerage fees expense decreased 25% to $14.3 million from $19.1 million. This decrease is explained almost entirely by lower origination volumes of single-family mortgages for institutional investors, which decreased by 18%. This decrease was also the result of electronic delivery costs which were accounted for as a fixed monthly fee in 2016, but were adjusted to variable in the 2017. Accordingly in the first quarter when there are generally lower volumes, the expense is now correspondingly low compared to the other quarters of the year. The Company also changed the allocation of broker costs on securitization such that more broker costs per unit were capitalized in the 2017 first quarter than in the comparative quarter.

Salaries and Benefits Expense

Salaries and benefits expense increased by 7% to $23.1 million from $21.5 million. Salaries were higher as overall headcount increased by 2% from 919 employees at the end of March 2016 to 937 as at the end of March 2017. This growth together with regular cost of living increases and higher compensation to commercial sales staff on higher volumes accounts for the additional 5% of the increase. Management salaries were paid to the two senior executives (Co-founders) who together control about 74% of the Company's common shares. The current period expense is a result of the compensation arrangement executed on the closing of the initial public offering ("IPO").

Interest Expense

Interest expense increased 16% to $9.6 million from $8.3 million. As discussed in the "Liquidity and Capital Resources" section of this analysis, the Company warehouses a portion of the mortgages it originates prior to settlement with the ultimate investor or funding with a securitization vehicle. The Company used the senior unsecured notes together with a $1 billion credit facility with a syndicate of banks and 30-day repurchase facilities to fund the mortgages during this period. The overall interest expense has increased from the prior period due to higher balances of mortgages accumulated for sale or securitization which required greater use of the Company's credit facilities.

Other Operating and Amortization of Intangibles Expenses

Other operating expenses increased by 8% to $12.6 million from $11.7 million. Other operating expenses increased by $0.9 million related to general increases in line with MUA growth of 5% including increased expenses related to the Company's NHA MBS program. The amortization of intangible assets recognized on the IPO was $1.25 million in the first quarter of 2016 but there is no expense in the 2017 comparative quarter as these assets were fully amortized in 2016.

Income before Income Taxes and Pre-FMV EBITDA

Income before income taxes decreased 4% to $49.2 million from $51.0 million. This change was primarily the result of changing capital markets, which affected the Company's economic interest rate hedges. In both the first quarters of 2016 and 2017, bond prices rose which resulted in the Company incurring losses on account of the fair value of financial instruments. The change in these amounts accounts for a $1.0 million increase in income before income taxes. Pre-FMV EBITDA, which eliminates the impact of gains and losses on financial instruments, decreased 7% to $53.1 million from $56.8 million. The decrease was due primarily to lower net placement fees as the Company elected to place less mortgages with institutional investors and use securitization funding sources instead. In the first quarter of 2017, the Company continued to earn growing returns from its $26 billion portfolio of mortgages pledged under securitization and its $73 billion MUA serviced for institutional customers.

Provision for Income Taxes

The provision for taxes decreased by 3% to $13.0 million from $13.4 million. The provision is lower due to the lower net income before income taxes earned in the 2017 first quarter. The overall effective tax rate is consistent between the quarters.

Operating Segment Review

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

	Operating Business Segments			
	Residential		Commercial	
	($000's except percent amounts)			
For the quarter ended	**March 31, 2017**	**March 31, 2016**	**March 31, 2017**	**March 31, 2016**
Originations and renewals	2,984,413	2,915,061	1,276,327	1,047,739
Percentage change	*2%*		*22%*	
Revenue	175,930	178,553	56,308	52,842
Percentage change	*(1%)*		*7%*	
Income before income taxes	33,850	38,387	15,307	12,304
Percentage change	*(12%)*		*24%*	
As at	**March 31, 2017**	**December 31, 2016**	**March 31, 2017**	**December 31, 2016**
Identifiable assets	24,344,217	24,718,010	5,527,296	5,646,679
Mortgages under administration	76,944,995	77,152,605	22,116,537	22,238,885

Residential Segment

Overall residential origination including renewals increased by 2% between the first quarters of 2017 and 2016, while residential revenues decreased by about 1%. A large part of the change in revenue is due to the change in gains and losses on financial instruments. Excluding these changes, revenue decreased by less than 1% as lower revenue from placement fees offset higher revenues from securitized mortgage interest. The net change in gains and losses on financial instruments for the residential segment of $2.2 million also affected net income before income taxes. Without the impact of this fair value change, net income before income taxes for the residential segment would have decreased by 6% year over year. This retraction is a result of the Company electing to securitize more of its newly originated mortgages as well as its renewals. Management believes this is more profitable to the Company over the long term as net margins from securitization will grow. Identifiable assets decreased from December 31, 2016, as the amount of mortgages accumulated for sale or securitization decreased by more than $150 million, government bonds purchased under resale agreements for hedging purposes decreased by about $120 million and restricted cash decreased by about $135 million.

Commercial Segment

First quarter 2017 commercial revenues increased by about 7% compared to 2016, but increased by 1% if the impacts of changes in gains and losses on the fair value of financial instruments are excluded. Most of the growth in origination volume was funded using deferred placement fee transactions. The profitability of these transactions was lower than in 2016 due to tighter mortgage spreads such that revenue did not track origination growth. In addition the Company recorded a higher provision for loss of $0.5 million which reduced mortgage investment revenue. Excluding fair value gains and losses, net income before tax was slightly lower in the 2017 quarter as the sales compensation on higher origination was higher than the marginal revenue earned. Identifiable assets decreased from those at December 31, 2016, as the Company had lower amounts of mortgages accumulated for securitization on hand by about $85 million.

Liquidity and Capital Resources

The Company's fundamental liquidity strategy has been to invest in prime Canadian mortgages. Management's belief has always been that these mortgages are considered "AAA" by investors and should always be well bid and highly liquid. This strategy proved effective during the turmoil experienced in 2007 through 2009, when capital markets retreated and only the highest-quality assets were bid. As the Company's results in those years demonstrated, First National had little trouble finding investors to purchase its mortgage origination at profitable margins. Originating prime mortgages also allows the Company to securitize in the capital markets; however, this activity requires significant cash resources to purchase and hold mortgages prior to arranging for term debt through the securitization markets. For this purpose, the Company uses the combination of the $175 million unsecured notes and the Company's revolving bank credit facility. This aggregate indebtedness is typically used to fund: (1) mortgages accumulated for sale or securitization, (2) the origination costs associated with securitization, and (3) mortgage and loan investments. The Company has a credit facility with a syndicate of ten financial institutions for a total credit of $1 billion. This facility was extended in March 2017 for a five-year term maturing in March 2022. Bank indebtedness may also include borrowings obtained through overdraft facilities. At March 31, 2017, the Company entered into repurchase transactions with financial institutions to borrow $930 million related to $951 million of mortgages held in "mortgages accumulated for sale or securitization" on the balance sheet.

At March 31, 2017, outstanding bank indebtedness (excluding indebtedness at the Fund level) was $560.9 million (December 31, 2016 - $622.9 million). Together with the unsecured notes of $175 million (December 31, 2016 – $175 million), this "combined debt" was used to fund $639.9 million (December 31, 2016 - $800.3 million) of mortgages accumulated for sale or securitization. At March 31, 2017, the Company's other interest-yielding assets included: (1) deferred placement fees receivable of $44.7 million (December 31, 2016 – $43.9 million) and (2) mortgage and loan investments of $322.5 million (December 31, 2015 - $255.2 million). The difference between "combined debt" and the mortgages accumulated for sale or securitization funded by it, which the Company considers a proxy for "true leverage", has increased between December 31, 2016 and March 31, 2017, and now stands at $95.4 million (December 31, 2016 – no true leverage). This represents a debt-to-equity ratio of approximately 0.18:1. This has increased from December 31, 2016 when there was no "debt", as generally, the Company invested $62 million in net new mortgage and loan investments and made corporate tax payments related to 2016 of $23 million. The Company also paid broker related volume bonuses and employee compensation related to 2016 which had the effect of increasing leverage. The Company believes the ratio is low given the nature of the assets which the debt is funding.

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 on the day of the advance of the mortgage. 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 term funding through securitization. The Company uses a portion of the committed credit facility with the banking syndicate to fund the mortgages during this warehouse period. The credit facility is designed to be able to fund the highest balance of warehoused mortgages in a month and is normally only partially drawn.

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

The Company has used ABCP as an efficient source of funding primarily for short term insured mortgages. In the May 2013 federal budget, the government announced it was going to take steps to limit the securitization of government insured mortgages to CMHC sponsored programs. As ABCP is not sponsored by CMHC, such a limitation would impact the Company. Almost two years after the announcement, legislation was passed and detailed transition information was published. With the change in the federal government, the legislation was reconfirmed in February 2016 with some delayed application dates. Generally, the regulations make mortgage default insurance invalid for any single-family mortgages with maturity dates beyond December 31, 2021 in a non-CMHC sponsored securitization vehicle. Accordingly, existing single-family mortgages in ABCP conduits as at December 31, 2016 can be funded by ABCP until their maturity, not to exceed 5 years and new insured single family mortgages can be sold in as long as the maturity date of the mortgage is prior to January 1, 2022. As this date is approached, the Company must find other funding sources for the insured mortgages it has historically funded with ABCP. The Company is considering various alternatives including whole loan sales and selling short term NHA-MBS pools to ABCP conduits. The Company may also adjust its renewal offering to provide incentives to borrowers to select five year terms as opposed to shorter terms. These alternatives may not be as economical to the Company as ABCP. A portion of the Company's capital has been employed to support its ABCP and NHA-MBS programs, primarily to provide credit enhancements as required by rating agencies. The most significant portion of cash collateral is the investment made on behalf of the Company's ABCP programs. As at March 31, 2017, the investment in cash collateral was $21.8 million (December 31, 2016 - $22.9 million).

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

Financial Instruments and Risk Management

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

The Company believes its hedging policies are suitably designed such that the interest rate risk of holding mortgages prior to securitization is mitigated. From an accounting perspective, any gains or losses on these instruments are recorded in the current period, as the Company's economic hedging strategy does not qualify as hedging for accounting purposes. The Company uses synthetic bond forwards (consisting of bonds sold short and bonds purchased under resale agreements) to manage interest rate exposure between the time a mortgage rate is committed to the borrower and the time the mortgage is transferred to the securitization vehicle and the matched term debt is arranged. As interest rates change, the value of these short bonds will vary inversely with the value of the related mortgages. As interest rates increase, a gain will be recorded on the bonds, which should be offset by a tighter interest rate spread between the interest rates on mortgages and the securitization debt. This spread will be earned over the term of the related mortgages. For single-family mortgages, primarily mortgages for the Company's own securitization programs, only some of the mortgage commitments issued by the Company eventually fund. The Company must assign a probability of funding to each mortgage in the pipeline and estimate how that probability changes as mortgages move through the various stages of the pipeline. The amount that is actually hedged is the expected value of mortgages funding within the next 120 days (120 days being the standard maximum rate hold period available for the mortgages). As at March 31, 2017, the Company had more than $0.9 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 for transfer to the Company's other securitization vehicles. As at March 31, 2017, the Company had entered into $22 million of notional value forward bond sales for this segment. The total net value of realized and unrealized gains and losses on account of all notional hedges pertaining to the period January 1, 2017 to March 31, 2017 was a $3.4 million loss. This amount has been included in revenue in the statement of comprehensive income.

The Company is party to three interest rate swaps that economically hedge the interest rate exposure related to certain CMB transactions in which the Company has replacement obligations. As at March 31, 2017, the aggregate notional value of these swaps was $10.7 million. During the first quarter of 2017, the value of these swaps increased by $0.5 million. The swaps mature between 2021 and December 2026.

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

The same exposure to risk is inherent in the Company's securitization through ABCP. The Company is exposed to the risk that 30-day ABCP rates are greater than 30-day BA rates. Prior to the financial crisis, the Company considered this a low risk given the quality of the assets securitized, the amount of credit enhancements provided by the Company and the strong covenant of the bank-sponsored conduits with which the Company transacted. In 2008, 30-day ABCP traded at approximately 1.10 percentage points over BAs; but by the end of March 2011 and continuing through the current period, it was priced at a discount to BAs. At the same time the Company has leveraged on changing credit spreads. The success of this approach has been demonstrated through the increase in volume and profitability of the NHA-MBS program and significant increases in gains on deferred placement fees from the sale of prime insured mortgages. As at March 31, 2017, the Company had various exposures to changing credit spreads. In particular, in mortgages accumulated for sale or securitization, there were almost $1.6 billion of mortgages that are susceptible to some degree of changing credit spreads.

Capital Expenditures

A significant portion of First National's business model consists of the origination and placement or securitization of financial assets. Generally, placement activities do not require much capital investment as the Company acts primarily in the capacity of a broker. On the other hand, the undertaking of securitization transactions may require significant amounts of the Company's own capital. This capital is provided in the form of cash collateral, credit enhancements, and the upfront funding of broker fees and other origination costs. These are described more fully in the "Liquidity and Capital Resources" section above. For fixed assets, the business requires capital expenditures on technology (both software and hardware), leasehold improvements and office furniture. During the quarter ended March 31, 2017, the Company purchased new computer equipment and leasehold improvements. In the long term, the Company expects capital expenditures on fixed assets will be approximately $5.0 million annually.

Summary of Contractual Obligations

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

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, 2016. The policies which First National believes are the most critical to aid in fully understanding and evaluating its reported financial results include the determination of the gains on deferred placement fees and the impact of fair value accounting on financial instruments.

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

On a quarterly basis, the Company reviews the estimates used to ensure their appropriateness and monitors the performance statistics of the relevant mortgage portfolios to adjust and improve these estimates. The estimates used reflect the expected performance of the mortgage portfolio over the lives of the mortgages. The assumptions underlying the estimates used for the quarter ended March 31, 2017 continue to be consistent with those used for the year ended December 31, 2016 and the quarter ended March 31, 2016.

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

Future Accounting Changes

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

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

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

IFRS 15 is effective for fiscal years ending on or after December 31, 2018. The Company intends to adopt IFRS 15 in its financial statements for the annual period beginning on January 1, 2018 and has begun its analysis. It has determined that most of its servicing contracts are inherently linked to mortgage purchase agreements such that placement fee and servicing revenue are interdependent. Therefore, the Company must determine the appropriate allocation of compensation between current period earnings and future period earnings from these contracts when the underlying mortgages are placed initially. The Company is assessing if the current allocation of revenue from these contracts for these two components may change under IFRS 15.

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

Disclosure Controls and Internal Controls over Financial Reporting

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

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 March 31, 2017 that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

Risks and Uncertainties Affecting the Business

The business, financial condition and results of operations of the Company are subject to a number of risks and uncertainties, and are affected by a number of factors outside the control of management of the Company. In addition to the risks addressed elsewhere in this discussion and the financial statements, these risks include: ability to sustain performance and growth, reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers, changes in interest rates, repurchase obligations and breach of representations and warranties on mortgage sales, risk of servicer termination events and trigger events on cash collateral and retained interests, reliance on multi-unit residential and commercial mortgages, general economic conditions, legislation and government regulation (including regulations imposed by the Department of Finance, CMHC and the policies set by and for mortgage default insurance companies), competition, reliance on mortgage insurers, reliance on key personnel and the ability to attract and retain employees and executives, conduct and compensation of independent mortgage brokers, failure or unavailability of computer and data processing systems and software, insufficient insurance coverage, change in or loss of ratings, impact of natural disasters and other events, and environmental liability. In addition, there are risks associated with the structure of the Company including: those related to the dependence on FNFLP, leverage and restrictive covenants, dividends which 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 to the detriment of 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. For a more complete discussion of the risks affecting the Company, reference should be made to the Company's Annual Information Form.

Forward-Looking Information

Forward-looking information is included in this MD&A. In some cases, forward-looking information can be identified by the use of terms such as ''may'', ''will'', ''should'', ''expect'', ''plan'', ''anticipate'', ''believe'', ''intend'', ''estimate'', ''predict'', ''potential'', ''continue'' or other similar expressions concerning matters that are not historical facts. Forward-looking information may relate to management's future outlook and anticipated events or results, and may include statements or information regarding the future financial position, business strategy and strategic goals, product development activities, projected costs and capital expenditures, financial results, risk management strategies, hedging activities, geographic expansion, licensing plans, taxes and other plans and objectives of or involving the Company. Particularly, information regarding growth objectives, any increase in mortgages under administration, future use of securitization vehicles, industry trends and future revenues is forward-looking information. Forward-looking information is based on certain factors and assumptions regarding, among other things, interest rate changes and responses to such changes, the demand for institutionally placed and securitized mortgages, the status of the applicable regulatory regime, and the use of mortgage brokers for single-family residential mortgages. This forward-looking information should not be read as providing guarantees of future performance or results, and will not necessarily be an accurate indication of whether or not, or the times by which, those results will be achieved. While management considers these assumptions to be reasonable based on information currently available to it, they may prove to be incorrect. Forward-looking information is subject to certain factors, including risks and uncertainties, which could cause actual results to differ materially from what management currently expects. These factors include reliance on sources of funding, concentration of institutional investors, reliance on independent mortgage brokers, and changes in interest rates as outlined under ''Risk and Uncertainties Affecting the Business''. In evaluating this information, the reader should specifically consider various factors, including the risks outlined under ''Risk and Uncertainties Affecting the Business'', which may cause actual events or results to differ materially from any forward-looking information. The forward-looking information contained in this discussion represents management's expectations as of April 25, 2017, and is subject to change after such date. However, management and the Company disclaim any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as required under applicable securities regulations.

Outlook

Management is pleased with the results of the first quarter of 2017. As expected a slowing high ratio mortgage market resulted in lower mortgage origination particularly in western Canada. This had little impact on the quarter's earnings which featured growing revenue from both securitization and servicing departments as the Company continued to profit from its large MUA.

For the remainder of 2017, the Company anticipates lower seasonal origination in the residential segment as the full impact of new mortgage insurance rules announced in October 2016 and the higher cost of portfolio insurance are realized. The rules, which increase the qualifying rate for 5 year term fixed rate borrowers and reduce the scope of portfolio insurance, combined with regional slowing housing markets will likely reduce First National's origination volumes. Although the Company sees growth in the commercial segment and in single-family renewals, it expects that new single-family origination could be significantly reduced from the volumes recorded in 2016. Competitive pressures from other mortgage lenders originating insured mortgages may also negatively impact origination volumes and the cost of broker fees as lenders compete for market share in a shrinking market. Recent Ontario Government announcements of a foreign buyer's tax and rent controls may also affect origination but at this early stage, management is unable to assess the impact on First National

In the face of these challenges in the residential market for new mortgage originations, the Company will endeavor to grow its commercial segment business, focus on the significant value of single family renewal opportunities and continue to generate income and cash flow from its $26 billion portfolio of mortgages pledged under securitization and $73 billion servicing portfolio.

Interim condensed consolidated financial statements

First National Financial Corporation

[Unaudited]

First quarter 2017

First National Financial Corporation

Interim condensed consolidated statements of financial position

[Unaudited – in thousands of Canadian dollars]

As at

	March 31, 2017	December 31, 2016
	$	$
Assets		
Restricted cash *[note 3]*	**546,086**	685,347
Cash held as collateral for securitization *[note 3]*	**21,804**	22,877
Accounts receivable and sundry	**96,182**	91,701
Securities purchased under resale agreements and owned	**1,085,387**	1,307,801
Mortgages accumulated for sale or securitization *[note 5]*	**1,591,170**	1,837,916
Mortgages pledged under securitization *[note 3]*	**26,147,603**	26,106,664
Deferred placement fees receivable *[note 4]*	**44,679**	43,933
Mortgage and loan investments *[note 6]*	**322,507**	255,230
Income taxes recoverable	**1,890**	—
Other assets	**43,981**	42,996
Total assets	**29,901,289**	30,394,465
Liabilities and equity		
Liabilities		
Bank indebtedness *[note 8]*	**566,927**	628,522
Obligations related to securities and mortgages sold under repurchase agreements	**930,031**	1,009,572
Accounts payable and accrued liabilities	**110,131**	122,499
Securities sold under repurchase agreements and sold short	**1,084,987**	1,308,483
Debt related to securitized and participation mortgages *[note 9]*	**26,412,213**	26,514,181
Senior unsecured notes	**174,591**	174,556
Income taxes payable	**—**	23,255
Deferred tax liabilities	**63,400**	63,100
Total liabilities	**29,342,280**	29,844,168
Equity attributable to shareholders		
Common shares *[note 10]*	**122,671**	122,671
Preferred shares *[note 10]*	**97,394**	97,394
Retained earnings	**310,965**	302,271
	531,030	522,336
Non-controlling interests	**27,979**	27,961
Total equity	**559,009**	550,297
Total liabilities and equity	**29,901,289**	30,394,465

See accompanying notes

On behalf of the Board:

John Brough

Robert Mitchell

First National Financial Corporation

Interim condensed consolidated statements of comprehensive income

[Unaudited – in thousands of Canadian dollars]

	Three months ended	
	March 31, 2017	**March 31, 2016**
	$	$
Revenue		
Interest revenue – securitized mortgages	**160,644**	155,591
Interest expense – securitized mortgages	**(123,467)**	(118,946)
Net interest – securitized mortgages *[note 3]*	**37,177**	36,645
Placement fees	**26,625**	34,898
Gains on deferred placement fees *[note 4]*	**3,684**	3,603
Mortgage investment income	**13,869**	12,539
Mortgage servicing income	**30,151**	28,497
Realized and unrealized losses on financial instruments	**(2,735)**	(3,733)
	108,771	112,449
Expenses		
Brokerage fees	**14,269**	19,108
Salaries and benefits	**23,138**	21,454
Interest	**9,574**	8,258
Other operating	**12,633**	11,688
Amortization of intangible assets	**—**	1,250
	59,614	61,758
Income before income taxes	**49,157**	50,691
Income tax expense	**13,030**	13,350
Net income and comprehensive income for the period	**36,127**	37,341
Net income and comprehensive income attributable to		
Shareholders	**35,610**	36,756
Non-controlling interests	**517**	585
	36,127	37,341
Earnings per share		
Basic *[note 10]*	**0.58**	0.59

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** $	**Non-controlling interests** $	**Total equity** $
Balance as at January 1, 2017	**122,671**	**97,394**	**302,271**	**27,961**	**550,297**
Comprehensive income	**—**	**—**	**35,610**	**517**	**36,127**
Dividends paid or declared	**—**	**—**	**(26,916)**	**(449)**	**(27,365)**
Redemption by non-controlling interests	**—**	**—**	**—**	**(50)**	**(50)**
Balance as at March 31, 2017	**122,671**	**97,394**	**310,965**	**27,979**	**559,009**

	Common shares $	**Preferred shares** $	**Retained earnings** $	**Non-controlling interests** $	**Total equity** $
Balance as at January 1, 2016	122,671	97,394	204,686	32,779	457,530
Comprehensive income	—	—	36,756	585	37,341
Dividends paid or declared	—	—	(24,400)	(530)	(24,930)
Balance as at March 31, 2016	122,671	97,394	217,042	32,834	469,941

See accompanying notes

First National Financial Corporation

Interim condensed consolidated statements of cash flows

[Unaudited – in thousands of Canadian dollars]

	Three months ended	
	March 31, 2017	March 31, 2016
	$	$
Operating activities		
Net income for the period	**36,127**	37,341
Add (deduct) items		
Deferred income taxes	**300**	(3,800)
Non-cash portion of gains on deferred placement fees	**(3,575)**	(3,456)
Decrease in restricted cash	**139,261**	70,846
Net investment in mortgages pledged under securitization	**(36,155)**	(490,959)
Net increase (decrease) in debt related to securitized mortgages	**(106,820)**	433,453
Provision for loan loss	**1,000**	500
Amortization of deferred placement fees receivable	**2,829**	2,352
Amortization of property, plant and equipment	**1,192**	1,145
Amortization of other intangible assets	**246**	1,444
Unrealized losses on financial instruments	**9,886**	882
	44,291	49,748
Net change in non-cash working capital balances related to operations	**199,990**	376,562
Cash provided by operating activities	**244,281**	426,310
Investing activities		
Additions to property, plant and equipment	**(2,423)**	(798)
Repayment of cash held as collateral for securitization	**1,073**	10,552
Investment in mortgage and loan investments	**(99,877)**	(63,689)
Repayment of mortgage and loan investments	**31,600**	30,263
Cash used in investing activities	**(69,627)**	(23,672)
Financing activities		
Dividends paid	**(26,621)**	(24,930)
Obligations related to securities and mortgages sold under repurchase agreements	**(79,541)**	(406,037)
Increase (decrease) in debt related to participation mortgages	**4,852**	(6,190)
Securities purchased under resale agreements and owned, net	**222,414**	(201,980)
Securities sold under repurchase agreements and sold short, net	**(234,113)**	201,314
Redemption by non-controlling interests	**(50)**	—
Cash used in financing activities	**(113,059)**	(437,823)
Net decrease (increase) in bank indebtedness during the period	**61,595**	(35,185)
Bank indebtedness, beginning of period	**(628,522)**	(582,973)
Bank indebtedness, end of period	**(566,927)**	(618,158)
Supplemental cash flow information		
Interest received	**192,574**	184,313
Interest paid	**127,285**	121,116
Income taxes paid	**37,875**	20,450

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]

March 31, 2017

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 $99 billion in mortgages under administration as at March 31, 2017, FNFLP is an originator and underwriter of mortgages and 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 100 University Avenue, 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. Significant accounting policies

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, 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, 2016.

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 April 25, 2017.

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 Asset-backed Commercial Paper ["ABCP"], NHA-MBS, and the Canada Mortgage Bonds ["CMB"] program. 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 March 31, 2017, the cash held as collateral for securitization was $21,804 [December 31, 2016 – $22,877].

Notes to interim condensed consolidated financial statements

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

March 31, 2017

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

	March 31, 2017		December 31, 2016	
	Carrying amount of securitized mortgages $	Carrying amount of associated liabilities $	Carrying amount of securitized mortgages $	Carrying amount of associated liabilities $
Securitized mortgages at face value	**25,983,606**	**26,465,126**	25,946,355	26,565,848
Mark-to-market adjustment	**24,171**	**––**	21,369	—
Capitalized origination costs	**139,826**	**––**	138,940	—
Debt discounts	**––**	**(63,863)**	—	(57,765)
	26,147,603	**26,401,263**	26,106,664	26,508,083
Add				
Principal portion of payments held in restricted cash	**498,000**	**––**	636,763	—
Participation debt	**––**	**10,950**	—	6,098
	26,645,603	**26,412,213**	26,743,427	26,514,181

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 period end. 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.

The changes in capitalized origination costs for the three months ended March 31 are as follows:

	2017 $	2016 $
Opening balance, January 1	**138,940**	137,965
Add: new origination costs capitalized in the period	**17,047**	7,048
Less: amortization in the period	**(16,161)**	(14,406)
Ending balance, March 31	**139,826**	130,607

Mortgages pledged under securitization have been classified as loans and receivables, except for approximately $2.6 billion [December 31, 2016 – $2.7 billion] of fair valued mortgages included in fair value through profit or loss ["FVTPL"] mortgages. The mortgages classified as loans and receivables are carried at par plus adjustment for unamortized origination costs.

Notes to interim condensed consolidated financial statements

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

March 31, 2017

Within mortgages pledged under securitization, the Company's exposure to credit loss is limited to uninsured mortgages with principal balances totaling $139,486 [December 31, 2016 – $125,092], before consideration of the value of underlying collateral. None of these mortgages have principal and interest payments in arrears as at March 31, 2017 or December 31, 2016. All such mortgages are conventional prime single-family mortgages, with an 80% or less loan to value, and verified borrower income. Accordingly, the Company considers there to be a very small risk of loss, and no provision for credit loss has been recorded related to these mortgages.

The Company uses various assumptions to value the FVTPL mortgages, which are set out in the table below, including the rate of unscheduled prepayment. Accordingly, FVTPL mortgages are subject to measurement uncertainty. The effect of variations between actual experience and assumptions will be recorded in future statements of comprehensive income. Key economic weighted average assumptions and the sensitivities of the current carrying values to immediate 10% and 20% adverse changes in those assumptions are as follows:

	March 31, 2017	
	Commercial mortgages	**Residential mortgages**
	$	$
FVTPL mortgages	**80,364**	**2,490,666**
Average life [in months] [1]	**27**	**21**
Prepayment speed assumption [annual rate]	**0.0%**	**10.6%**
Impact on fair value of 10% adverse change	**––**	**235**
Impact on fair value of 20% adverse change	**––**	**467**
Discount rate [annual rate]	**1.9%**	**1.7%**
Impact on fair value of 10% adverse change	**359**	**6,447**
Impact on fair value of 20% adverse change	**714**	**12,859**

	December 31, 2016	
	Commercial mortgages	**Residential mortgages**
	$	$
FVTPL mortgages	84,777	2,578,979
Average life [in months] [1]	28	21
Prepayment speed assumption [annual rate]	0.1%	10.7%
Impact on fair value of 10% adverse change	—	192
Impact on fair value of 20% adverse change	—	383
Discount rate [annual rate]	2.0%	1.8%
Impact on fair value of 10% adverse change	402	7,152
Impact on fair value of 20% adverse change	799	14,262

[1] The weighted average life of prepayable assets in periods [for example, months or years] can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

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

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in carrying value based on a 10% or 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another [for example, increases in market interest rates may result in lower prepayments], which might magnify or counteract the sensitivities.

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.

During the three months ended March 31, 2017, $552,631 [2016 – $421,822] of mortgages were placed with institutional investors, which created gains on deferred placement fees of $3,684 [2016 – $3,603]. Cash receipts on deferred placement fees receivable for the three months ended March 31, 2017 were $3,251 [2016 – $2,680].

The Company uses various assumptions to value the deferred placement fees receivable, which are set out in the table below. Accordingly, the deferred placement fees receivable are subject to measurement uncertainty. As at March 31, 2017, the fair value of deferred placement fees receivable is $44,679 [December 31, 2016 – $43,933]. An assumption of no credit losses was used, commensurate with the credit quality of the investors. An assumption of no prepayment for the commercial segment was used, as borrowers cannot refinance for financial advantage without paying the Company a fee commensurate with its investment in the mortgage. The effect of variations between actual experience and assumptions will be recorded in future statements of comprehensive income. Key economic weighted average assumptions and the sensitivity of the current carrying value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions are summarized as follows:

	March 31, 2017	**December 31, 2016**
Average life [in months] [1]	**62**	63
Residual cash flows discount rate [annual rate]	**3.9%**	3.9%
Impact on fair value of 10% adverse change	**$445**	$435
Impact on fair value of 20% adverse change	**$881**	$863

[1] The weighted average life of prepayable assets in periods [for example, months or years] can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in carrying value based on a 10% or 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear.

Notes to interim condensed consolidated financial statements

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

March 31, 2017

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 loans and receivables and are recorded at amortized cost. 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 due to their short-term nature. The following table summarizes the components of mortgages according to their classification:

	March 31, 2017	**December 31, 2016**
	$	$
Mortgages accumulated for securitization	**1,584,960**	1,797,321
Mortgages accumulated for sale	**6,210**	40,595
	1,591,170	1,837,916

The Company's exposure to credit loss is limited to $326,426 [December 31, 2016 – $345,179] of principal balances of uninsured mortgages within mortgages accumulated for sale or securitization, before consideration of the value of underlying collateral. These are conventional prime single-family mortgages similar to the mortgages described in note 3. For the same rationale, the Company has not recorded any provision for credit loss related to these mortgages.

6. Mortgage and loan investments

Mortgage and loan investments consist primarily of commercial first and second mortgages held for various terms, the majority of which mature within one year.

Mortgage and loan investments consist of the following:

	March 31, 2017	**December 31, 2016**
	$	$
Mortgage loans, classified as loans and receivables	**280,288**	213,372
Mortgage loans, designated as FVTPL	**42,219**	41,858
	322,507	255,230

Mortgage and loan investments classified as loans and receivables are carried at outstanding principal balances adjusted for unamortized premiums or discounts and are net of specific provisions for credit losses, if any.

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

Within mortgage and loan investments, the total of uninsured mortgages in arrears is approximately $44,691 [December 31, 2016 – $44,231]. Three of these mortgages are non-performing and have principal balances totaling $43,927 as at March 31, 2017 [December 31, 2016 – three mortgages, totaling $43,286]. The Company has stopped accruing interest on these mortgages, and has provided an allowance for potential credit loss of $11,041 as at March 31, 2017 [December 31, 2016 – $10,041]. The Company acknowledges that there is a higher risk of credit losses on this portfolio than the other mortgage portfolios on its statement of financial position. The Company believes it has adequately provided for such losses in the allowance for potential credit loss disclosed above and considers there to be a lower risk of credit loss on performing mortgages, such that credit losses have been recorded only on account of non-performing mortgages.

7. Mortgages under administration

As at March 31, 2017, the Company had mortgages under administration of $99,061,532 [December 31, 2016 – $99,391,490], 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 March 31, 2017, the Company administered 302,962 mortgages [December 31, 2016 – 303,389] for 101 institutional investors [December 31, 2016 – 102] with an average remaining term to maturity of 40 months [December 31, 2016 – 41 months].

Mortgages under administration are serviced as follows:

	March 31, 2017	**December 31, 2016**
	$	$
Institutional investors	**59,068,950**	59,062,554
Mortgages accumulated for sale or securitization and mortgage and loan investments	**1,929,703**	2,099,598
Deferred placement investors	**10,721,484**	10,417,963
Mortgages pledged under securitization	**25,983,606**	25,946,355
CMBS conduits	**1,357,789**	1,865,020
	99,061,532	99,391,490

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. As at March 31, 2017, the Company has included in accounts receivable and sundry nil [December 31, 2016 – $18] uninsured non-performing mortgages, net of provisions for credit losses and outstanding claims from mortgage default insurers. The Company incurred actual credit losses of $27 [2016 – nil] during the three months ended March 31, 2017.

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 March 31, 2017 was $740,067 [December 31, 2016 – $798,876].

8. Bank indebtedness

Bank indebtedness includes a revolving credit facility of $1,000,000 [December 31, 2016 – $1,000,000] maturing in March 31, 2022, of which $563,254 [December 31, 2016 – $624,904] was drawn as at March 31, 2017 and against 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.

9. Debt related to securitized and participation mortgages

Debt related to securitized mortgages represents the funding for mortgages pledged under the NHA-MBS, CMB and ABCP programs. As at March 31, 2017, debt related to securitized mortgages was $26,401,263 [December 31, 2016 – $26,508,083], net of unamortized discounts of $63,863 [December 31, 2016 – $57,765]. A comparison of the carrying amounts of the pledged mortgages and the related debt is summarized in note 3.

As at March 31, 2017, debt related to participation mortgages was $10,950 [December 31, 2016 – $6,098].

Debt related to securitized and participation 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.

10. 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

Notes to interim condensed consolidated financial statements

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

March 31, 2017

[b] Capital stock activities

	Common shares		Preferred shares	
	#	$	#	$
Balance, December 31, 2016 and March 31, 2017	**59,967,429**	**122,671**	**4,000,000**	**97,394**

[c] Earnings per share

	Three months ended	
	March 31, 2017	**March 31, 2016**
Net income attributable to shareholders	**$35,610**	$36,756
Less: dividends declared on preferred shares	**(680)**	(1,163)
Net earnings attributable to common shareholders	**34,930**	35,593
Number of common shares outstanding	**59,967,429**	59,967,429
Basic earnings per common share	**$0.58**	$0.59

11. 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] FVTPL mortgages in mortgages under securitization and certain mortgage and loan investments

The fair value of these mortgages is determined by discounting projected cash flows using market industry pricing practices. 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. Impaired mortgages are recorded at net realizable value. Refer to note 3 “Mortgages pledged under securitization” for the key assumptions used and sensitivity analysis.

[b] Deferred placement fees receivable

The fair value of deferred placement fees receivable 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. Refer to note 4 “Deferred placement fees receivable” for the key assumptions used and sensitivity analysis.

[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.

[d] Servicing liabilities

The fair value of the servicing liability 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 values of mortgage and loan investments classified as loans and receivables, mortgages accumulated for sale or securitization, cash held as collateral for securitization, restricted cash and bank indebtedness correspond to the respective outstanding amounts due to their short-term maturity profiles.

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, except for mortgages pledged under securitization, which has a carrying value of $26,147,603 [December 31, 2016 – $26,106,664] and a fair value of $26,514,701 [December 31, 2016 – $26,388,372], debt related to securitized and participation mortgages, which has a carrying value of $26,412,213 [December 31, 2016 – $26,514,181] and a fair value of $26,677,529 [December 31, 2016 – $26,681,028], and senior unsecured notes, which have a carrying value of $174,591 [December 31, 2016 – $174,556] and a fair value of $177,930 [December 31, 2016 – $174,349]. These fair values are estimated using valuation techniques in which one or more significant inputs are unobservable [Level 3].

Notes to interim condensed consolidated financial statements

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

March 31, 2017

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

	March 31, 2017			
	Level 1	**Level 2**	**Level 3**	**Total**
	$	$	$	$
Financial assets				
Mortgages accumulated for sale	**––**	**6,210**	**––**	**6,210**
FVTPL mortgages	**––**	**––**	**2,571,030**	**2,571,030**
Deferred placement fees receivable	**––**	**––**	**44,679**	**44,679**
Mortgage and loan investments	**––**	**––**	**42,219**	**42,219**
Interest rate swaps	**––**	**18,824**	**––**	**18,824**
Total financial assets	**––**	**25,034**	**2,657,928**	**2,682,962**
Financial liabilities				
Securities sold under repurchase agreements and sold short	**––**	**1,084,987**	**––**	**1,084,987**
Interest rate swaps	**––**	**15,090**	**––**	**15,090**
Total financial liabilities	**––**	**1,100,077**	**––**	**1,100,077**

	December 31, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
	$	$	$	$
Financial assets				
Mortgages accumulated for sale	—	40,595	—	40,595
FVTPL mortgages	—	—	2,663,755	2,663,755
Deferred placement fees receivable	—	—	43,933	43,933
Mortgage and loan investments	—	—	41,858	41,858
Interest rate swaps	—	22,227	—	22,227
Total financial assets	—	62,822	2,749,546	2,812,368
Financial liabilities				
Securities sold under repurchase agreements and sold short	—	1,308,483	—	1,308,483
Interest rate swaps	—	16,873	—	16,873
Total financial liabilities	—	1,325,356	—	1,325,356

Notes to interim condensed consolidated financial statements

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

March 31, 2017

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 for the three months ended March 31, 2017 that was estimated using a valuation technique based on assumptions that are not fully supported by observable market prices or rates, was a gain of $4,784 [2016 – $4,746]. 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 gains of $7,151 [2016 – losses of $2,851] of the Company's financial assets and financial liabilities for the three months ended March 31 2017 and 2016, all of which have been classified as FVTPL:

	Three months ended March 31	
	2017	**2016**
	$	$
FVTPL mortgages	**4,784**	4,651
Deferred placement fees receivable	**––**	95
Securities owned and sold short	**(3,466)**	(5,053)
Interest rate swaps	**(4,053)**	(3,426)
	(2,735)	(3,733)

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 three months ended March 31, 2017 and 2016. The Company classifies financial instruments as Level 3 when there is reliance on at least one significant unobservable input in the valuation models.

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

	Fair value as at January 1, 2017 $	Investments $	Unrealized gains recorded in income $	Payment and amortization $	Fair value as at March 31, 2017 $
Financial assets					
FVTPL mortgages	**2,663,755**	**308,883**	**4,784**	**(406,392)**	**2,571,030**
Deferred placement fees receivable	**43,933**	**3,575**	**––**	**(2,829)**	**44,679**
Mortgage and loan investments	**41,858**	**3,594**	**––**	**(3,233)**	**42,219**
	2,749,546	**316,052**	**4,784**	**(412,454)**	**2,657,928**

	Fair value as at January 1, 2016 $	Investments $	Unrealized gains recorded in income $	Payment and amortization $	Fair value as at March 31, 2016 $
Financial assets					
FVTPL mortgages	3,460,924	815,143	4,651	(773,382)	3,507,336
Deferred placement fees receivable	38,164	3,456	95	(2,352)	39,363
Mortgage and loan investments	47,267	4,309	—	(738)	50,838
	3,546,355	822,908	4,746	(776,472)	3,597,537

12. Capital management

The Company's objective is to maintain a strong 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 equity, long-term debt and retained earnings. The Company 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 March 31, 2017, the ratio was 1.32:1 [December 31, 2016 – 1.39:1]. The Company was in compliance with the bank covenant throughout the period.

Notes to interim condensed consolidated financial statements

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

March 31, 2017

13. 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 March 31, 2017		
	Residential	Commercial	Total
	$	$	$
Revenue			
Interest revenue – securitized mortgages	**122,896**	**37,748**	**160,644**
Interest expense – securitized mortgages	**(92,670)**	**(30,797)**	**(123,467)**
Net interest – securitized mortgages	**30,226**	**6,951**	**37,177**
Placement and servicing	**46,432**	**14,028**	**60,460**
Mortgage investment income	**9,840**	**4,029**	**13,869**
Realized and unrealized gains (losses) on financial instruments	**(3,238)**	**503**	**(2,735)**
	83,260	**25,511**	**108,771**
Expenses			
Amortization	**999**	**193**	**1,192**
Interest	**8,216**	**1,358**	**9,574**
Other operating	**40,195**	**8,653**	**48,848**
	49,410	**10,204**	**59,614**
Income before income taxes	**33,850**	**15,307**	**49,157**
Identifiable assets	**24,344,417**	**5,527,096**	**29,871,513**
Goodwill	**—**	**—**	**29,776**
Total assets	**24,344,417**	**5,527,096**	**29,901,289**
Capital expenditures	**1,696**	**727**	**2,423**

Notes to interim condensed consolidated financial statements

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

March 31, 2017

	Three months ended March 31, 2016		
	Residential	Commercial	Total
	$	$	$
Revenue			
Interest revenue – securitized mortgages	118,268	37,323	155,591
Interest expense – securitized mortgages	(88,765)	(30,181)	(118,946)
Net interest – securitized mortgages	29,503	7,142	36,645
Placement and servicing	53,970	13,028	66,998
Mortgage investment income	7,368	5,171	12,539
Realized and unrealized losses on financial instruments	(1,053)	(2,680)	(3,733)
	89,788	22,661	112,449
Expenses			
Amortization	1,718	677	2,395
Interest	6,572	1,686	8,258
Other operating	43,111	7,994	51,105
	51,401	10,357	61,758
Income before income taxes	38,387	12,304	50,691
Identifiable assets	22,554,139	5,610,386	28,164,525
Goodwill	—	—	29,776
Total assets	22,554,139	5,610,386	28,194,301
Capital expenditures	558	240	798

Notes to interim condensed consolidated financial statements

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

March 31, 2017

14. Related party and other transactions

In the past ten years, the Company has originated and sold several commercial mezzanine mortgages 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, one of the related entities funded several progress draws totaling $1,646 on existing mortgages. Subsequent to the quarter end, the Company took on the servicing of a $2,176 mortgage which one of the related parties originated. The mortgages, which are administered by the Company, have a balance of $71,100 as at March 31, 2017 [December 31, 2016 – $69,115]. As at March 31, 2017, three of the mortgages are secured by real estate in which the Company is also a subordinate mortgage lender.

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 March 31, 2017 was $270 [2016 – $240], net of third-party investor reimbursement. The insurance company has also engaged the Company to service a portfolio of mortgages at market servicing rates. As at March 31, 2017, the portfolio's balance was $3,930 [December 31, 2016 – $3,965].

First National Financial Corporation

Shareholder Information

Corporate Office
100 University Avenue
North Tower, Suite 700
Toronto, Ontario
M5J 1V6
Phone: 416-593-1100
Fax: 416-593-1900

Transfer Agent and Registrar
Computershare Investor Services Inc.
Toronto, Ontario
Phone: 1-800-564-6253

Auditors
Ernst & Young LLP
222 Bay Street, P.O. Box 251
Toronto, Ontario
M5K 1J7

TSX Symbol
FN

Investor Relations

Rob Inglis
Chief Financial Officer
First National Financial LP
Tel: 416-593-1100
Email: rob.inglis@firstnational.ca

Ernie Stapleton
President
Fundamental Creative Inc.
Tel: 905.648.9354
Email: ernie@fundamental.ca