

MANAGEMENT DISCUSSION & ANALYSIS

2021



COASTAL COMMUNITY
CREDIT UNION

Coastal Community Credit Union

2021 Management Discussion and Analysis

About Coastal Community Credit Union

Providing services for over 75 years, parent company Coastal Community Credit Union (CCCU) is the largest Vancouver Island-based financial services organization and among the 23 largest credit unions in Canada when measured by asset size. CCCU provides personal, business and commercial banking services, complemented by its wholly-owned subsidiary Coastal Community Financial Management Inc., which provides wealth management services through its Coastal Community Private Wealth Group division, and its 50% equity interest in 1200089 BC Ltd. that owns two subsidiaries which offer personal and commercial insurance solutions.

The Coastal Community* family of companies serves Vancouver Island and the Gulf Islands, from Victoria to Port Hardy. With more than \$4.2 billion in total assets under management, CCCU operates a network of 24 full-service locations and one centralized contact centre with extended service hours. Coastal Community's experts offer caring and helpful service to meet all your financial and protection needs in retail banking, regional business services, insurance**, wealth management†, trust and estates***.

CCCU continues to help build healthier communities in part through donations, sponsorships, scholarships and fundraising efforts totaling over half-a-million dollars each year.

This Management Discussion and Analysis is prepared in conjunction with the audited consolidated financial statements. It is presented to provide management's overview of Coastal Community Credit Union's financial and operating performance which includes information on its wholly owned subsidiary, Coastal Community Financial Management Inc. and its 50% equity interest in 1200089 BC Ltd., a joint venture that owns Coastal Community Insurance Services (2007) Ltd. and Interior Savings Insurance Services Inc.

*References to "Coastal Community" mean "Coastal Community Credit Union"

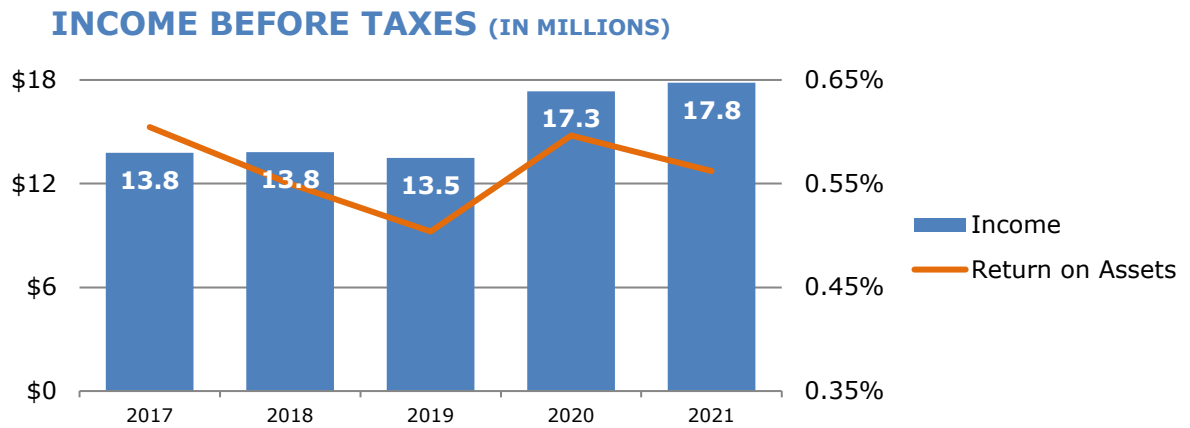
**References to "insurance" refer to insurance services provided through Coastal Community Insurance Services (2007) Ltd., which is a wholly owned subsidiary of 1200089 BC Ltd, a joint venture that also owns Interior Savings Insurance Services Inc.

†References to "wealth management," "financial planning" and "investments" refer to the financial planning and investment services provided through Coastal Community Private Wealth Group, a division of Coastal Community Financial Management Inc., which is a wholly owned subsidiary of Coastal Community Credit Union

***Trust and Estate services provided through Concentra Trust, a wholly-owned subsidiary of Concentra Bank.



2021 Financial Performance



(2019 and 2018 exclude earnings from discontinued operations)

Summary

2021 was another strong year for Coastal Community despite the challenges of the global pandemic.

Loan growth was solid while cash and investments increased further bumping consolidated total assets to almost \$3.27 billion. Deposit balances increased 8.4% as our members continued to build up their savings.

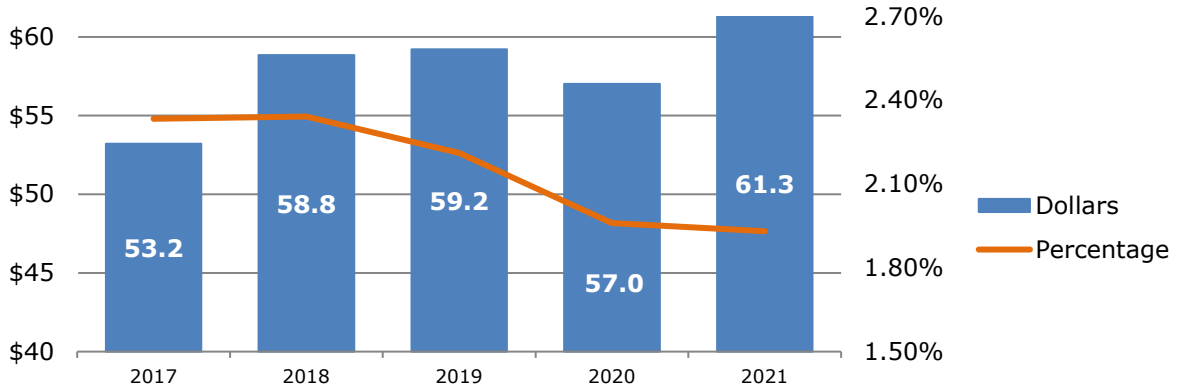
Consolidated income before taxes was \$17.8 million compared to \$17.3 million in 2020. 2021 income was higher even though 2020 included a \$4.3 million gain due to the transition of our mandatory liquidity pool. Higher financial margin was offset by higher operating expenses. Provisions for credit losses were reduced reflecting improved economic forecasts. Consolidated net income, which is our consolidated income after taxes, was \$15.0 million.

Return on average assets declined from 60 to 56 basis points.

2021's consolidated financial performance finished well ahead of plan.



NET INTEREST INCOME (IN MILLIONS)



Net Interest Income

Net interest income, the largest source of revenue for Coastal Community, represents the interest we earn on investments and member loans less the interest expense we pay on member deposits and borrowings. Net interest income improved to \$61.3 million. Fixed consumer and commercial lending rates were lower but balances were higher. Term deposit rates were also lower combined with significantly lower balances. Demand deposit rates also declined while balances grew. Overall, excess liquidity increased as deposit growth exceeded loan growth. As a percentage of average assets, interest income shrank 34 basis points over the prior year with interest expense decreasing only 31 basis points. As a result, net interest income as a percentage of average assets decreased from 1.96% in 2020 to 1.93% for 2021.

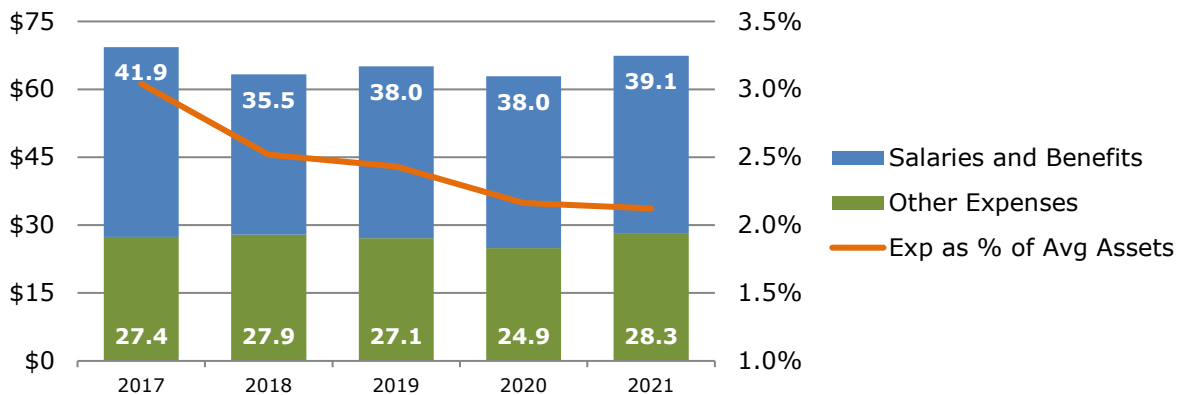
As rates start to rise in 2022 in response to record-level inflation, we expect net interest income as a percentage of average assets to improve.

Other Income

Our strategy includes supplementing net interest income with diversified income sources including contributions from our wealth management subsidiary and equity interest in a joint venture that owns two insurance subsidiaries. Other income comprises loan fees, service charges, insurance and financial commissions, foreign exchange, dividends on investments, and other miscellaneous revenues that are not interest related. Other income was lower largely due to an investment gain of \$4.3 million recognized in 2020 on deposits with Central 1 Credit Union due to transition to a new statutory liquidity structure.



OPERATING EXPENSES (IN MILLIONS)



Operating Expenses

In an environment with downward pressure on net interest income as a percentage of average assets, Coastal Community focuses on increasing efficiencies and innovating in order to help mitigate operating cost pressures. Growing our operations and investing in technology contributed to higher data processing costs in 2021. Salaries and benefits increased year over year as did other operating expenses and administration, as staffing and expenditures returned to pre-pandemic levels.

Overall, total operating expenses as a percentage of average assets declined slightly to 2.1%.

Comprehensive Income

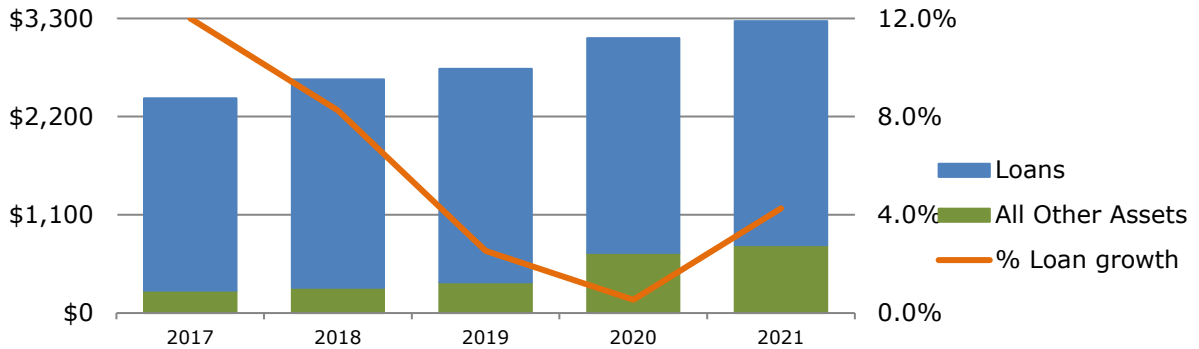
Comprehensive income includes the net income of the credit union and other comprehensive income or loss.

Coastal Community utilizes derivatives for risk management. The unrealized gains or losses from the change in the fair value of these derivatives, if the hedging relationship is effective, are recorded in other comprehensive income or loss. The gain recorded for 2021 reflects an improvement in the underlying markets. The cumulative unrealized gain or loss will net to zero when the derivative matures.

The new mandatory liquidity pool securities are held at fair value through other comprehensive income. Therefore unrealized gains or losses from the change in the fair value of these securities are recorded in other comprehensive income or loss. The loss recorded for 2021 reflects an improvement in market rates compared to when the securities were purchased.



ASSETS (IN MILLIONS)

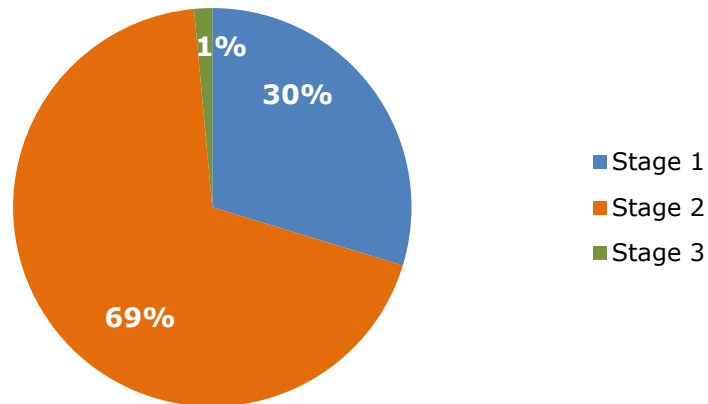


Loans

Total assets increased from \$3.08 billion to almost \$3.27 billion or by 6.1%. Member loans make up the largest proportion of total assets even with the further increase in cash and investments in 2021. We ended the year with a loan portfolio of \$2,509 million, up \$103 million or 4.3% over 2020. Loan activity improved compared to 2020 with the majority of the growth in commercial loans. At December 31, 2021, commercial loans totaled \$664 million growing by \$72 million for the year. Personal loans ended the year at \$60 million declining \$8 million compared to 2020. Residential mortgage loans grew \$39 million to \$1,787 million.



ALLOWANCE FOR CREDIT LOSSES



Allowance for Credit Losses

The expected credit loss (“ECL”) model results in an allowance for credit losses being recorded on financial assets regardless of whether there has been an actual impairment. The model requires the recognition of credit losses based on up to 12 months of expected losses for performing loans (Stage 1) and the recognition of lifetime expected losses on performing loans that have experienced a significant increase in credit risk since origination (Stage 2) and credit impaired assets (Stage 3).

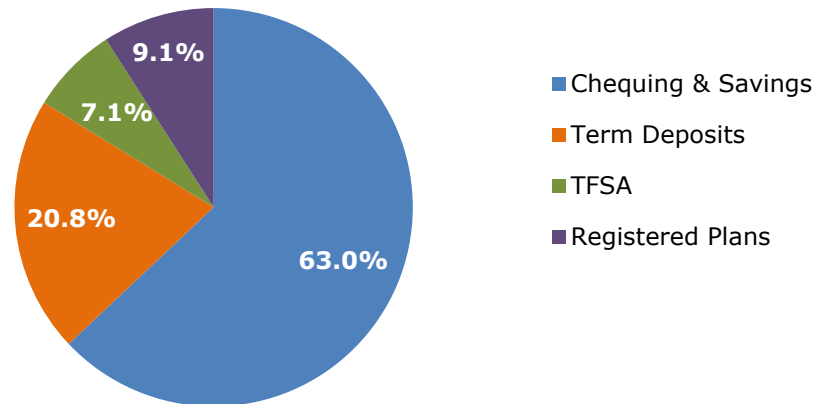
The allowance declined to \$6.5 million compared to \$7.0 million at the end of 2020 with the proportion in Stage 2 decreasing the most.

The total allowance at December 31, 2021 represents 0.26% of total loans which is lower than the 0.29% for 2020 but higher than pre-pandemic years. While the economic and credit outlook has improved, uncertainty remains.

The Credit Union regularly reviews its loan portfolios for impairment and recommends specific loans to be written off where recovery of the debt is deemed unlikely. A complete analysis of our allowance for impaired loans is provided in Note 8 of the audited consolidated financial statements.



DEPOSIT MIX



Deposits

Member deposits are the largest component of liabilities. Deposits grew by 8.4% or \$228 million to over \$2,943 million at the end of the year. Growth was lower than the record 14.7% set for 2020 but still high. Expectations for deposits to decline did not materialize as members continued to increase their savings. Chequing and Savings accounts increased the most as our members chose to keep their funds accessible. For the same reason, we saw a decrease in the proportion of deposits held in Term Deposits.

Tax-Free Savings deposit products include a high interest savings account and a full suite of term deposits. Registered plans include RRSPs, RRIFs, RDSPs and RESPs.

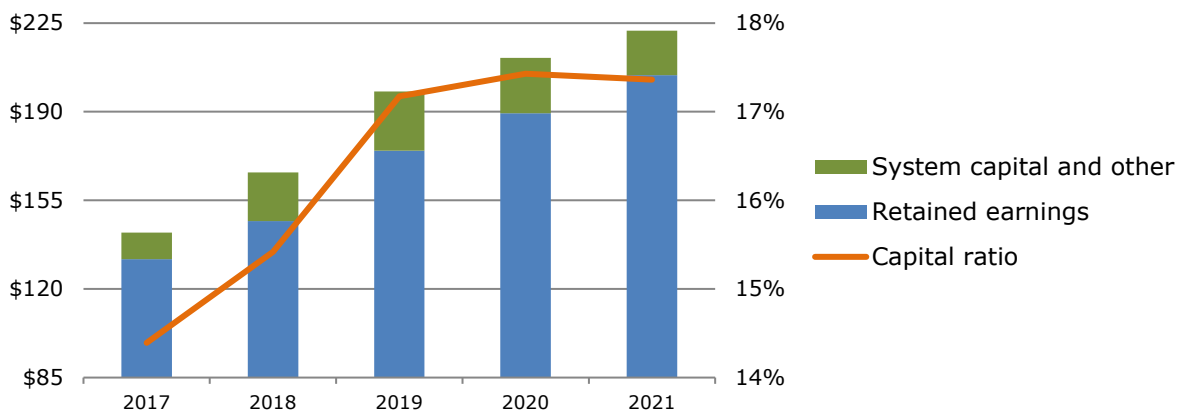
Borrowings

The Credit Union maintains operating lines of credit with Central 1 Credit Union and another financial institution. Access to borrowing facilities is an important part of effective liquidity management. Outstanding short-term borrowings remained at zero as of December 31, 2021.

During the year, Coastal Community did not participate in the Canada Mortgage Bond program as we had significant excess liquidity. At the end of 2021, the carrying amount of secured borrowings declined to \$82 million.



CAPITAL (IN MILLIONS)



Retained Earnings and Capital

Retained earnings, which represent the main source of capital for Coastal Community Credit Union, grew by \$15.0 million to \$204.4 million in 2021. A strong and stable capital base provides security against unexpected events and supports our ongoing growth. Increased capital allows us to pursue new initiatives including enhanced service to members and clients as well as expansion into the Capital region. Capital management objectives are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations. To ensure processes are in place to meet these objectives, Coastal Community follows policies approved by the Board of Directors. Management monitors capital levels on a regular basis.

Capital requirements are regulated by the BC Financial Services Authority (BCFSA). A minimum ratio of capital to risk-weighted assets of 8.0% must be maintained. Coastal Community Credit Union's capital adequacy ratio at December 31, 2021 slipped from 17.43% to 17.36%.

Risk Management

The Board of Directors has overall responsibility for the establishment and oversight of the Credit Union's Enterprise Risk Management (ERM) framework. This responsibility includes approving the ERM framework and the policies that comprise that framework and setting the organization's risk appetite. In addition to the risks identified in Note 21 of the audited consolidated financial statements, the Credit Union is also exposed to operational, strategic, legal, regulatory, and reputational risk. Coastal Community Credit Union has a solid framework in place that identifies and addresses these risks and maintains systems of internal accounting and administrative controls of high quality, consistent with reasonable cost. These systems are designed to provide reasonable assurance that the financial information is relevant, reliable and accurate, and that the Credit Union's assets are appropriately accounted for and adequately safeguarded.

Coastal Community follows the three lines of defense model. The first line (risk owners): Operational employees and managers who understand and correctly carry



out their roles and responsibilities following management and internal control measures; second line (Risk control and compliance as an oversight function): Independent oversight employees that monitor risk and compliance among operational employees; and third line (risk assurance): Internal audit, independent review, and legal review. The Corporate Governance of the Executive Team and the Board of Directors together oversee the 3 lines of defense functions to confirm they are performing at appropriate levels for risk tolerance and regulatory compliance.

2022 Outlook

Looking ahead to 2022, the Credit Union expects net interest income to improve as longer-term rates increase and members' accumulated savings are drawn down. While market competition for loans will continue, loan growth is expected to increase slightly compared to 2021 as our branches in the Capital Regional District expand their member base and all market areas experience continued population migration.

Canada's macroeconomic forecast is more favourable than the economic forecast one year ago. Current inflation concerns have markets pricing in multiple rate hikes. The impact of this is unknown. The Credit Union will continue its focus on the financial health and safety of its members and clients throughout this time.

Coastal Community Credit Union has been an established Vancouver Island company for over 75 years. Along with being the largest Island-based credit union and 100% Island operated, Coastal Community remains one of the top ten largest credit unions in British Columbia when measured by asset size. The key aspects that set Coastal Community apart from the rest are our integrated approach to providing expert financial advice and personalized solutions across all of our business lines and our 100% Island focus. Our vision to improve financial health, enrich people's lives and build healthier communities will allow us to continue to do *Great Things* well into the future.