

2023

Management Discussion & Analysis



COASTAL COMMUNITY
CREDIT UNION

Coastal Community Credit Union

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About Coastal Community Credit Union

As the largest Island-based financial organization, we serve over 120,000 members and clients on Vancouver Island and the Gulf Islands.

To help you improve your financial health, we offer a range of personal, business and commercial banking and insurance* services, as well as wealth management through Aviso Wealth.** With more than \$4.3 billion in total assets under management, CCCU operates a network of 24 branches, 15 insurance locations and one centralized contact centre with extended service hours so our caring and helpful experts can meet all your financial and protection needs.

Each year, Coastal Community*** invests over half a million dollars into communities across the Islands through community funding grants, education awards, sponsorships and fundraising initiatives.

*References to insurance refer to the property and casualty insurance services provided through Coastal Community Insurance Services (2007) Ltd. (CCIS). CCIS is a subsidiary of 1200089 B.C. Ltd., a company jointly owned by Coastal Community Credit Union and Beem Credit Union, which in turn fully owns Coastal Community Insurance Services (2007) Ltd. and Interior Savings Insurance Services Inc.

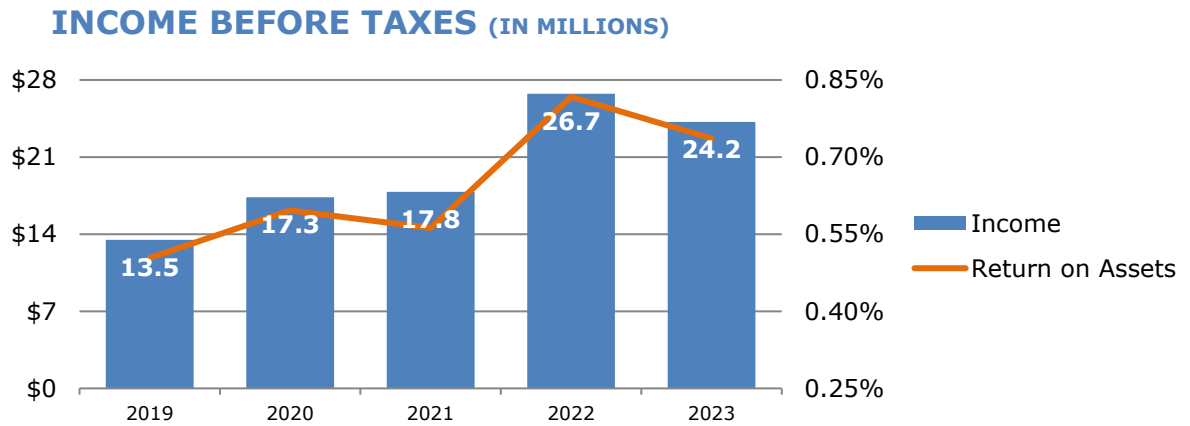
**References to “wealth management,” “financial planning” and “investments” in this document refer to mutual funds and other securities offered through Aviso Wealth, a division of Aviso Financial Inc.

***References to “Coastal Community” mean “Coastal Community Credit Union”

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.



2023 Financial Performance



(2019 excludes earnings from discontinued operations)

Summary

2023 was a strong year for Coastal Community in spite of higher interest rates, persistently high inflation and geopolitical tensions.

Loan growth slowed resulting in a marginal increase in consolidated total assets. Deposit balances contracted as our members drew down pandemic savings.

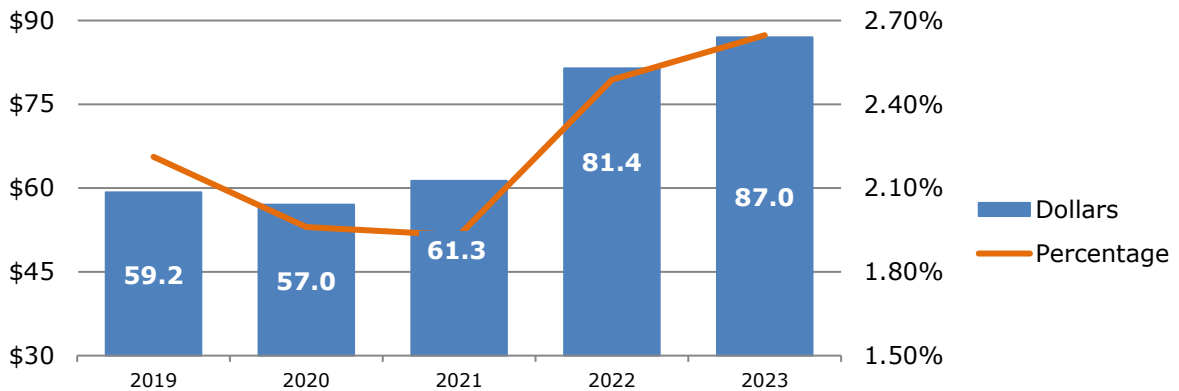
Consolidated income before taxes was \$24.2 million compared to \$26.7 million in 2022. Financial margin benefitted from three Bank of Canada rate hikes over the year. Operating expenses increased as did the provisions for credit losses. Consolidated net income, which is our consolidated income after taxes, was \$19.1 million.

Return on average assets slipped from 82 to 74 basis points.

Coastal Community's 2023 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 \$87.0 million. Fixed and variable consumer and commercial lending rates were higher plus balances were higher. Term deposit rates also increased combined with significantly higher balances. Demand deposit balances fell considerably. Overall, excess liquidity declined as loan growth exceeded deposit growth. As a percentage of average assets, interest income improved 97 basis points over the prior year with interest expense increasing 81 basis points. As a result, net interest income as a percentage of average assets increased from 2.49% in 2022 to 2.65% for 2023.

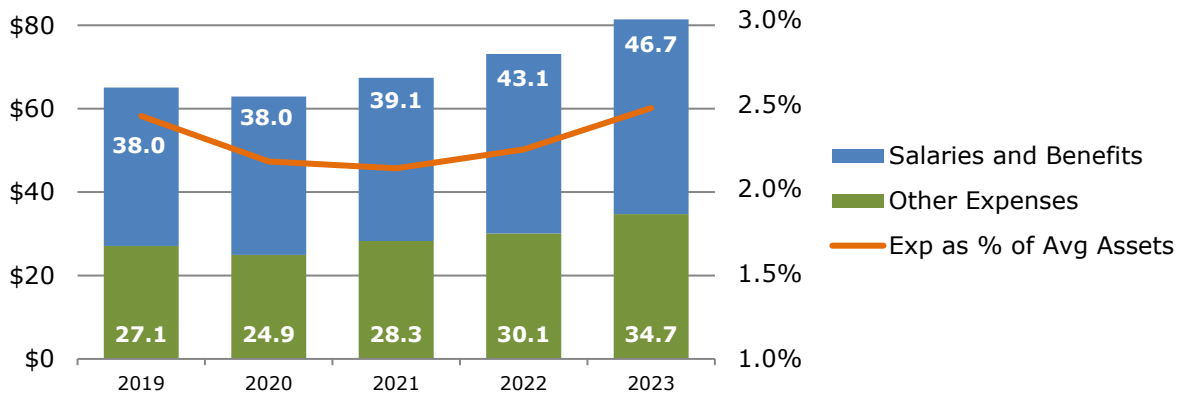
When rates start to decline, we expect net interest income as a percentage of average assets to decline.

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, and other miscellaneous revenues that are not interest related. Other income was slightly lower due to a decline in mortgage payout fees.



OPERATING EXPENSES (IN MILLIONS)



Operating Expenses

As the Bank of Canada hiked rates three more times, Coastal Community focused on increasing efficiencies and innovating to help mitigate operating cost pressures. In addition to high inflationary pressure on operating costs, growing our operations and investing in technology contributed to higher data processing costs in 2023. Salaries and benefits increased year over year as did other operating and administration expenses.

Overall, total operating expenses as a percentage of average assets increased to 2.5% from 2.2% in 2022.

Comprehensive Income

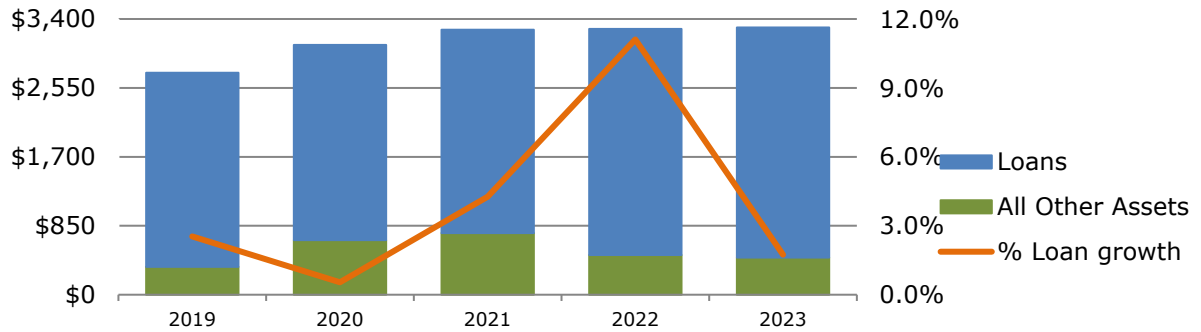
Comprehensive income includes the net income of the credit union and other comprehensive income or loss.

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 2023 reflects an improvement in the underlying markets. The cumulative unrealized gain or loss will net to zero when the derivative matures.

Mandatory liquidity pool securities are held at fair value through other comprehensive income. As a result, unrealized gains or losses from the change in the fair value of these securities are recorded in other comprehensive income or loss. The gain recorded for 2023 reflects an improvement in market rates compared to when the securities were purchased.



ASSETS (IN MILLIONS)

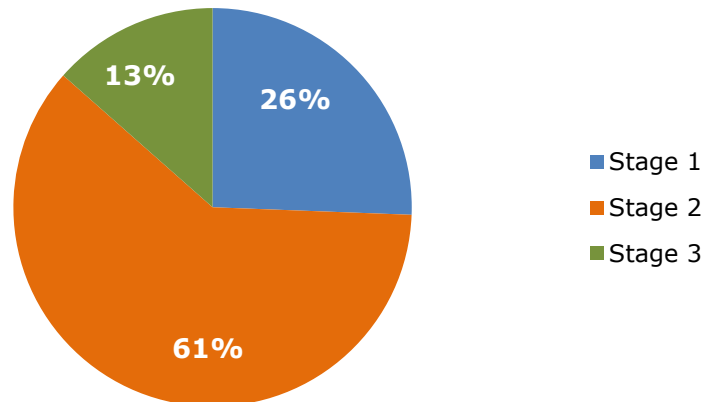


Loans

Total assets increased marginally from almost \$3.28 billion to over \$3.29 billion as excess cash and investments were used to fund loan growth. Member loans make up the largest proportion of total assets. We ended the year with a loan portfolio of \$2,837 million, up \$49 million or 1.7% over 2022. Loan activity slowed compared to 2022 with the majority of the increase in residential mortgages. At December 31, 2023, residential mortgage loans totaled \$2,031 million, growing by \$76 million for the year. Personal loans ended the year at \$54 million, declining \$4 million compared to 2022. Commercial loans decreased by \$24 million to \$752 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).

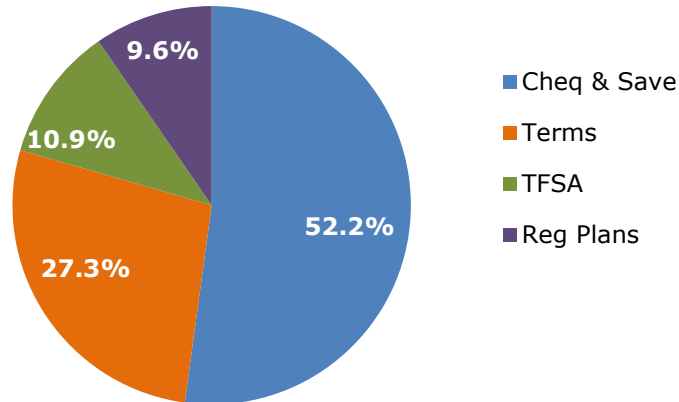
The allowance increased to \$9.4 million compared to \$8.8 million at the end of 2022, with the proportion in Stage 3 increasing the most.

The total allowance at December 31, 2023 represents 0.33% of total loans which is higher than the 0.32% for 2022. While the economic outlook has improved, the impact of higher rates and inflation is unknown.

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 declined by 0.9% or \$25 million to over \$2,965 million at the end of the year. Members continued to spend the significant savings they built up over the pandemic as expected. Chequing and Savings accounts declined the most as our members moved funds into Term Deposits. Growth in Term Deposits was the second highest on record.

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.

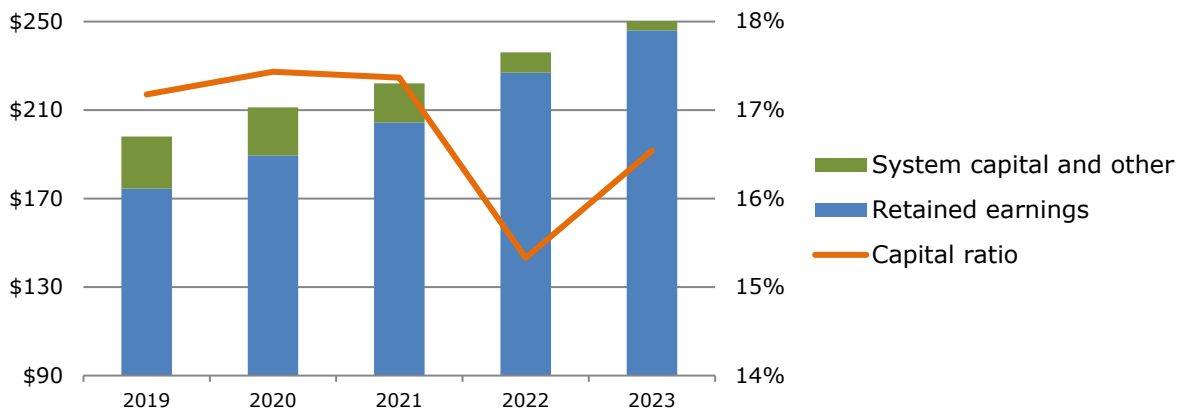
Borrowings

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, 2023.

During the year, Coastal Community participated in the Canada Mortgage Bond program. At the end of 2023, the carrying amount of secured borrowings increased from \$27 million to \$43 million.



CAPITAL (IN MILLIONS)



Retained Earnings and Capital

Retained earnings, which represent the main source of capital for Coastal Community Credit Union, grew by \$19.1 million to \$246.0 million in 2023. 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, 2023 improved from 15.33% to 16.54%.

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.

2024 Outlook

Looking ahead to 2024, the Credit Union expects net interest income to decline as Prime and longer-term rates decrease and members continue to shift funds from demand to Term Deposits. Market competition for deposits will intensify as liquidity declines. Loan growth will remain slow until rates drop sufficiently and the housing supply increases.

Current economic forecasts are pricing in three to four rate cuts by the Bank of Canada in 2024. There is considerable uncertainty as underlying inflationary pressures persist even as the economy is in modest excess supply. The Credit Union will continue its focus on the financial health and safety of its members and clients throughout this time.

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.