

Management's Responsibility for Financial Information

The consolidated financial statements of Home Capital Group Inc. were prepared by management, which is responsible for the integrity and fairness of the financial information presented. The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles, including the accounting requirements specified by the Office of the Superintendent of Financial Institutions Canada that apply to its subsidiary Home Trust Company. The financial statements reflect amounts which must, of necessity, be based on the best estimates and judgement of management with appropriate consideration as to materiality. The financial information presented elsewhere in this Annual Report is consistent with that in the financial statements.

Management is responsible for ensuring the fairness and integrity of the financial information. It is also responsible for the implementation of the supporting accounting systems. In discharging its responsibilities, management maintains the necessary internal control system designed to provide assurance that the transactions are properly authorized, assets are safeguarded and proper accounting records are held. The controls include quality standards in hiring and training of employees, written policies, authorized limits for managers, procedure manuals, a corporate code of conduct and appropriate management information systems.

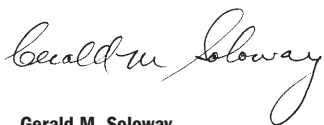
The internal control systems are further supported by a compliance function, which ensures that the Company and its employees comply with all regulatory requirements, as well as by a risk integration function and an operating risk management function that ensure proper risk control, related documentation and the measurement of the financial impact of risks. In addition, the internal auditor periodically evaluates various aspects of the Company's operations and makes recommendations to management for, among other things, improvements to the control systems.

Every year, the Office of the Superintendent of Financial Institutions Canada makes such examinations and inquiries as deemed necessary to satisfy itself that Home Trust Company is in a sound financial position and that it complies with the provisions of the Trust and Loan Companies Act (Canada).

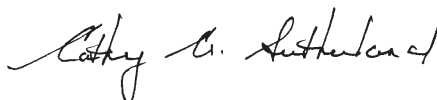
Ernst & Young LLP, independent auditors, appointed by the shareholders, perform an audit of the Company's consolidated financial statements and their report follows.

The internal auditor, the external auditors and the Office of the Superintendent of Financial Institutions Canada meet periodically with the Audit Committee, with management either present or absent, to discuss all aspects of their duties and matters arising therefrom.

The Board of Directors is responsible for reviewing and approving the financial statements and Management's Discussion and Analysis of results of operations and financial condition appearing in the Annual Report. It oversees the manner in which management discharges its responsibilities for the presentation and preparation of financial statements, maintenance of appropriate internal controls, risk management as well as assessment of significant transactions and related party transactions through its Audit Committee. The Audit Committee is composed solely of Directors who are not Officers or employees of the Company.



Gerald M. Soloway
Chief Executive Officer
Toronto, Canada
March 9, 2009



Cathy A. Sutherland, C.A.
Vice President, Finance

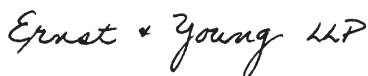
Auditors' Report

To the Shareholders of **Home Capital Group Inc.**

We have audited the consolidated balance sheets of **Home Capital Group Inc.** as at December 31, 2008 and 2007 and the consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.



Toronto, Canada
March 9, 2009

Chartered Accountants
Licensed Public Accountants

Consolidated Balance Sheets

| As at December 31 (000s) | 2008 | 2007 |
|--|--------------------------|--------------|
| ASSETS | | |
| Cash resources | | |
| Deposits with regulated financial institutions | \$ 554,422 | \$ 344,464 |
| Treasury bills guaranteed by Canada | - | 9,872 |
| | 554,422 | 354,336 |
| Securities (Note 4) | | |
| Held for trading | - | 114,423 |
| Available for sale | 519,477 | 356,458 |
| | 519,477 | 470,881 |
| Loans (Note 5) | | |
| Residential mortgages | 3,263,206 | 3,169,953 |
| Other mortgages | 826,882 | 467,921 |
| Personal and credit card loans | 368,962 | 325,393 |
| Secured loans | 72,518 | 82,304 |
| General allowance for credit losses | (25,177) | (23,400) |
| | 4,506,391 | 4,022,171 |
| Other | | |
| Securitization receivables | (Note 6) 139,870 | 65,768 |
| Capital assets | (Note 7) 5,325 | 4,837 |
| Other assets | (Note 8) 84,228 | 57,100 |
| | 229,423 | 127,705 |
| | \$ 5,809,713 | \$ 4,975,093 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Deposits (Note 9) | | |
| Payable on demand | \$ 34,808 | \$ 30,793 |
| Payable on a fixed date | 5,067,973 | 4,383,191 |
| | 5,102,781 | 4,413,984 |
| Other | | |
| Cheques and other items in transit | 4,811 | 4,393 |
| Other liabilities | (Note 10) 269,368 | 208,676 |
| | 274,179 | 213,069 |
| Commitments and contingencies | (Note 15) - | - |
| SHAREHOLDERS' EQUITY | | |
| Capital stock | (Note 11) 39,094 | 38,899 |
| Contributed surplus | 3,283 | 1,818 |
| Retained earnings | 401,429 | 313,620 |
| Accumulated other comprehensive loss | (11,053) | (6,297) |
| | 432,753 | 348,040 |
| | \$ 5,809,713 | \$ 4,975,093 |

See accompanying notes

On behalf of the Board:



Gerald M. Soloway
Chief Executive Officer



Norman F. Angus
Chairman of the Board

Consolidated Statements of Income

| Year ended December 31 (000s, except per share amounts) | 2008 | 2007 |
|--|-------------------|------------|
| Income | | |
| Interest from loans | \$ 339,242 | \$ 288,924 |
| Dividends from securities | 9,237 | 10,877 |
| Other interest | 25,524 | 21,013 |
| | 374,003 | 320,814 |
| Interest expense | | |
| Interest on deposits | 223,428 | 174,556 |
| Net interest income | 150,575 | 146,258 |
| Provision for credit losses (Note 5) | 6,638 | 6,042 |
| | 143,937 | 140,216 |
| Non-interest income (loss) | | |
| Fees and other income | 28,452 | 21,533 |
| Securitization income (Note 6) | 71,103 | 27,367 |
| Net realized and unrealized losses on investment securities | (5,365) | (1,614) |
| Net gain on disposition of subsidiary (Note 3) | 69 | - |
| Net realized and unrealized gain (loss) on derivatives | (13,567) | 781 |
| | 80,692 | 48,067 |
| | 224,629 | 188,283 |
| Non-interest expenses | | |
| Salaries and benefits | 36,182 | 30,195 |
| Premises | 4,439 | 3,837 |
| General and administration | 25,390 | 20,166 |
| | 66,011 | 54,198 |
| Income before income taxes | 158,618 | 134,085 |
| Income taxes (Note 13) | | |
| Current | 35,533 | 40,532 |
| Future | 14,398 | 3,312 |
| | 49,931 | 43,844 |
| Net income for the year | \$ 108,687 | \$ 90,241 |
| Average number of common shares outstanding (Note 11) | | |
| Basic | 34,512 | 34,447 |
| Diluted | 34,669 | 34,857 |
| Net income per common share (Note 11) | | |
| Basic | \$ 3.15 | \$ 2.62 |
| Diluted | \$ 3.13 | \$ 2.59 |

See accompanying notes

Consolidated Statements of Comprehensive Income

| Year ended December 31 (000s) | 2008 | 2007 |
|---|------------|-----------|
| Net income | \$ 108,687 | \$ 90,241 |
| Other comprehensive loss, net of tax | | |
| Net unrealized losses on securities available for sale (net of (\$4,049) tax; (\$2,458) in 2007) | (10,463) | (4,899) |
| Transfers to net income (net of \$1,796 tax; (\$434) in 2007) | 5,707 | (768) |
| | (4,756) | (5,667) |
| Comprehensive income | \$ 103,931 | \$ 84,574 |

See accompanying notes

Consolidated Statements of Changes in Shareholders' Equity

| Year ended December 31 (000s) | 2008 | 2007 |
|--|-------------|------------|
| Capital stock (Note 11) | | |
| Common shares | | |
| Balance, beginning of year | \$ 38,899 | \$ 35,436 |
| Proceeds of options exercised | 318 | 3,585 |
| Repurchase of shares | (123) | (122) |
| Balance, end of year | \$ 39,094 | \$ 38,899 |
| Contributed surplus | | |
| Balance, beginning of year | \$ 1,818 | \$ 783 |
| Amortization of fair value of employee stock options (Note 11) | 1,516 | 1,129 |
| Employee stock options exercised | (51) | (94) |
| Balance, end of year | \$ 3,283 | \$ 1,818 |
| Retained earnings | | |
| Balance, beginning of year | \$ 313,620 | \$ 240,647 |
| Transitional adjustment on adoption of new accounting policies (Note 2) | - | 1,391 |
| Net income for the year | 108,687 | 90,241 |
| Dividends paid | (13,461) | (11,043) |
| Dividends declared | (4,477) | (3,799) |
| Repurchase of shares (Note 11) | (2,940) | (3,817) |
| Balance, end of year | \$ 401,429 | \$ 313,620 |
| Accumulated other comprehensive loss | | |
| Balance, beginning of year | \$ (6,297) | \$ - |
| Transitional adjustment on adoption of financial instruments (Note 2) | - | (630) |
| Other comprehensive loss (net of (\$2,253) tax; (\$2,892) in 2007) | (4,756) | (5,667) |
| Balance, end of year | \$ (11,053) | \$ (6,297) |

See accompanying notes

Consolidated Statements of Cash Flows

| Year ended December 31 (000s) | 2008 | 2007 |
|--|------------------|------------------|
| OPERATING ACTIVITIES | | |
| Net income for the year | \$ 108,687 | \$ 90,241 |
| Adjustments to determine net cash flows relating to operating activities | | |
| Future income taxes | 14,398 | 3,312 |
| Amortization of capital assets | 2,823 | 1,997 |
| Amortization of intangible assets and other deferred assets | 675 | 93 |
| Amortization of securities | 25,894 | 9,601 |
| Amortization of fair value of employee stock options | 1,516 | 1,129 |
| Provision for credit losses | 6,638 | 6,042 |
| Change in accrued interest receivable | (2,553) | (6,262) |
| Change in accrued interest payable | 23,965 | 23,730 |
| Net realized and unrealized losses on investment securities | 5,365 | 1,614 |
| (Gain) loss realized and unrealized on derivatives | 13,567 | (781) |
| Securitization gains on mortgage-backed securities | (71,103) | (27,367) |
| Change in other assets | (25,250) | 14,814 |
| Change in cheques and other items in transit | 418 | 1,738 |
| Change in other liabilities | 9,871 | (368) |
| Cash provided by operating activities | 114,911 | 119,533 |
| FINANCING ACTIVITIES | | |
| Net increase in deposits | 688,797 | 972,192 |
| Issuance of capital stock | 318 | 3,585 |
| Normal course issuer bid | (3,063) | (3,939) |
| Exercise of stock options | (51) | (94) |
| Dividends paid | (17,260) | (14,119) |
| Cash provided by financing activities | 668,741 | 957,625 |
| INVESTING ACTIVITIES | | |
| Activity in available for sale and held for trading securities | | |
| Purchases | (555,804) | (271,256) |
| Proceeds on sales | 385,792 | 48,854 |
| Proceeds on maturities | 73,313 | 79,457 |
| Activity in mortgages | | |
| Net increase | (1,954,052) | (1,309,808) |
| Proceeds from securitization | 1,478,138 | 673,920 |
| Change in securitization receivables | 28,031 | 32,372 |
| Net increase in personal and credit card loans | (44,506) | (89,084) |
| Net increase in secured loans | 8,833 | (12,372) |
| Business acquisition (Note 3) | - | (16,563) |
| Purchase of capital assets | (3,311) | (1,873) |
| Cash used in investing activities | (583,566) | (866,353) |
| Net increase in cash and cash equivalents | 200,086 | 210,805 |
| Cash and cash equivalents, beginning of year | 354,336 | 143,531 |
| Cash and cash equivalents, end of year | \$ 554,422 | \$ 354,336 |
| Supplemental disclosure of cash flow information | | |
| Amount of interest paid in year | \$ 199,440 | \$ 150,824 |
| Amount of income taxes paid in year | 43,055 | 46,723 |

See accompanying notes

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Home Capital Group Inc. (the Company) have been prepared in accordance with Canadian generally accepted accounting principles (GAAP). The significant accounting policies used in the preparation of these consolidated financial statements are summarized below.

Use of Estimates

The preparation of consolidated financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the consolidated balance sheet date and the reported amounts of revenue and expenses during the reporting period. Key areas where management has made estimates include allowance for credit losses, securitization, fair values and impairment of financial instruments, goodwill and income tax. Actual results could differ from those estimates.

Principles of Consolidation

The consolidated financial statements include the assets, liabilities and results of operations of the Company and all of its subsidiaries, after the elimination of intercompany transactions and balances.

The Company also consolidates variable interest entities (VIEs) when it is the primary beneficiary. Under AcG-15, "Consolidation of Variable Interest Entities," guidance is provided for applying consolidation principles to certain entities that are subject to control on a basis other than ownership of voting interests. Under this standard, the Company must consolidate these entities if it is the primary beneficiary that is, as a result of this investment, exposed to a majority of expected losses or is in a position to benefit from a majority of the returns. Under this guideline, the QSPE-HCC Trust (operating as Regency Finance Corp.) is consolidated and its assets are reported as secured loans on the balance sheet. Regency Finance Corp. consists only of these secured loans and the Company is the sole beneficiary.

Subsidiaries are defined as the corporations whose operations are controlled by the Company and are corporations in which the Company owns more than 50% of the voting shares. The subsidiaries included in the consolidated financial statements are Home Trust Company (Home Trust), Payment Services Interactive Gateway Corp. (PSiGate) and Home Trust Asset Management Inc. (HTAM), all of which are wholly owned.

Cash Resources

For the purposes of the consolidated statement of cash flows, cash and cash equivalents comprise balances with less than 90 days to maturity from the date of acquisition, including cash and deposits with regulated financial institutions, treasury bills and other eligible deposits. Cash and deposits are carried at fair value. Interest income is recognized in income on an accrual basis and, to the extent not received at year-end, recorded as a receivable in other assets on the consolidated balance sheet.

Cheques and Other Items in Transit

Cheques and other items in transit represent uncleared settlements with other regulated financial institutions and are recorded at cost.

Securities

Securities are classified as either held for trading or available for sale based on management's intentions. On the settlement date, all securities are recognized at their fair value, which is normally the transaction price.

Held for trading securities are financial assets purchased for resale, generally within a short period of time and primarily held for liquidity purposes. Interest earned is included in other interest income. Held for trading securities are measured at fair value, using published bid prices, as at the consolidated balance sheet date. All realized and unrealized gains and losses are reported in income under non-interest income. Transaction costs are expensed as incurred. The Company has not elected under the fair value option to designate any financial asset or liability as held for trading.

Available for sale securities are financial assets purchased for longer-term investment that may be sold in response to or in anticipation of changes in market conditions. Dividends and interest earned are included in dividends from securities or other interest. Available for sale securities are measured at their fair value, using published bid prices, as at the consolidated balance sheet date. Unrealized gains and losses, net of related taxes, are included in accumulated other comprehensive income until the security is sold or an other than temporary impairment is recognized at which time the cumulative loss is transferred to net income. The Company conducts a quarterly review to identify securities which have indicators of possible impairment. Factors considered in determining whether a loss is other than temporary include the length of time and extent to which fair value has been below cost, financial condition and near-term prospects of the issuer, and the likelihood for recovery. Transaction costs are generally capitalized.

Effective January 1, 2008, all new bond acquisitions were designated as available for sale securities consistent with the Company's intention to hold them longer term.

Loans

Loans are recorded at amortized cost using the effective interest rate method. Interest income is allocated over the expected term of the loan by applying the effective interest rate to the carrying amount of the loan. The effective interest rate is the rate that exactly discounts estimated future cash receipts over the expected life of the loan. Origination revenues and costs are applied to the carrying amount of the loan.

Loans are carried net of the specific allowance for credit losses and any unearned income.

Interest income is accrued as earned until such time as the loan is recognized as impaired. At that time interest ceases to accrue and all previously accrued interest is reversed.

A loan is recognized as being impaired when the Company is no longer reasonably assured of the timely collection of the full amount of principal and interest. As a matter of practice, a loan is deemed to be impaired at the earlier of the date it has been specifically provided for or when it has been in arrears for 90 days. Secured and unsecured credit card balances that have a payment that is contractually 180 days in arrears are written off. Equityline Visa credit card balances are measured on a basis consistent with mortgage loans.

When loans are classified as impaired, the book value of these loans is brought back to their estimated realizable value based on the fair value of any security underlying the loan, net of any costs of realization, by totally or partially writing off the loan and/or establishing an allowance for loan losses.

An impaired loan cannot return to an accrual status unless all principal and interest payments are up to date and management is reasonably assured as to the recoverability of the loan.

Allowance for Credit Losses

An allowance for credit losses is maintained at an amount which in management's opinion is considered adequate to absorb all credit-related losses in its portfolio. Allowances are mainly related to loans but may also apply to other assets. The allowance consists of accumulated specific and general provisions, each of which is reviewed on a regular basis. The general allowance is increased by these provisions, which are charged to income, and reduced by write-offs, net of recoveries. The allowance is deducted from the loans on the consolidated balance sheet.

Specific Allowances

Specific allowances are determined on an item-by-item basis and reflect the associated estimated credit loss. In the case of loans and Equityline Visa credit cards, the specific provision is the amount required to reduce the carrying value of an impaired loan to its estimated realizable amount. The fair value of the underlying security is used to estimate the realizable amount of the loan. The allowance is the difference between the loan's carrying value and its estimated realizable amount. For secured and unsecured credit cards, specific provisions are provided for arrears over 120 days.

General Allowances

General allowances are established to absorb credit losses on the aggregate exposures in each of the Company's business lines for which losses are not yet specifically identified on an item-by-item basis. The general allowance is based upon statistical analysis of past performance, level of allowance already in place and management's judgement. The general allowance, based on the historical loss experience, adjusted to reflect changes in the portfolios and credit policies, is applied to each pool of loans with common risk characteristics. This estimate includes consideration of economic and business conditions, management's judgement and the risks related to the model.

The amount of the provision for credit losses that is charged to the consolidated statement of income is the amount that is required to establish a balance in the allowance for credit losses account that the Company's management considers adequate to absorb all credit-related losses in its portfolio of balance sheet items, after charging amounts written off during the year, net of any recoveries, to the allowance for credit losses account.

Loan Securitization (Securitization Receivables)

The Company periodically transfers pools of mortgages to special purpose entities or trusts which in turn issue securities to investors. Mortgage loan securitization is part of the Company's liquidity and capital management strategies. These transfers are accounted for as sales when the Company surrenders control of the transferred assets and receives consideration other than the beneficial interest in the transferred assets. The securitization trust has no recourse to the Company's other assets.

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

When such sales occur, the Company retains interest-only strips and servicing responsibilities for the assets sold. Gains or losses on these transactions are recognized as income and are dependent in part on the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the retained interests based on their relative fair value at the date of transfer, net of transaction costs. Retained interests are classified as available for sale assets and are stated at their fair value with unrealized gains and losses reported in accumulated other comprehensive income. The fair value of the retained interests is estimated using discounted cash flow methodology and management's best estimates of key assumptions, such as prepayment rates, average term of assets sold and other factors, that influence the value of the retained interests.

Retained interests are revalued quarterly to assess for other than temporary impairment.

Capital Assets

Capital assets, which are comprised of office furniture and equipment, computer equipment, software and leasehold improvements, are recorded at cost and amortized over their estimated useful lives on a declining balance basis at the following annual rates:

| | |
|--------------------------------|---------|
| Office furniture and equipment | 20% |
| Computer equipment | 30%–45% |

Software is amortized on a straight-line basis over two years. Leasehold improvements are amortized on a straight-line basis over the remaining term of the leases.

Translation of Foreign Currencies

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates prevailing at the consolidated balance sheet date. Revenues and expenses denominated in foreign currencies are translated at the average exchange rates prevailing during the year. Realized and unrealized gains and losses on foreign currency transactions are included in fees and other income in the consolidated statement of income.

Goodwill and Intangible Assets

Goodwill and intangible assets are tested annually for impairment to ensure that their fair value is greater than or equal to book value. Any excess of book value over fair value is charged to income in the period in which the impairment is determined. It is management's belief that there is no impairment of goodwill or intangible assets as at December 31, 2008.

Intangible assets (customer contracts and lists acquired on acquisition) are amortized on a straight-line basis over their useful lives as determined at the time of valuation.

Derivative Financial Instruments

Home Trust enters into non-trading derivative financial instruments as part of the mortgage securitization program. Non-trading derivatives entered into are carried at fair value in other assets or liabilities, on a net basis, with changes in fair value recorded in non-interest income on the consolidated statements of income.

During 2008 and 2007, the Company did not designate any non-trading derivatives for hedge accounting.

Deposits

Deposits are financial liabilities that are measured at cost using the effective interest rate method. Deposit origination costs are added to deposits on the consolidated balance sheet as incurred and amortized to interest expense over the term of the deposit.

Income Taxes

The Company follows the asset and liability method of accounting for income taxes, whereby future tax assets and liabilities are recognized for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the period in which those temporary differences are expected to be recovered or settled.

Future tax liabilities are included in other liabilities on the consolidated balance sheet.

Employee Future Benefits

The Company accrues its obligations under employee benefit plans, which include post-retirement plans (health costs). The cost of the post-retirement benefits earned by the affected employees is actuarially determined using the projected benefit method pro rated on service and management's best estimate of expected health care costs.

Stock-based Compensation Plans

The Company has two stock-based compensation plans, which are described in Notes 11 and 14.

Under the Company's Stock Option Plan, the fair value of options granted after January 1, 2003 is charged to salary expense over the option vesting period. The fair value of the options granted is determined using the Black-Scholes option pricing model using management's best estimates. Refer to Note 11 for the estimates applied.

With respect to options granted prior to January 1, 2003, the Company continues to apply the previous standards under which no compensation expense is recognized at the grant date and the consideration paid by the employees or directors who exercise their stock options is credited to capital stock.

Under the Employee Share Purchase Plan, as described in Note 14, the Company's contribution is expensed when paid.

NOTE 2 CHANGES IN ACCOUNTING POLICIES

2008

Effective January 1, 2008, the Company adopted new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1535, *Capital Disclosures*; Section 3862, *Financial Instruments – Disclosures*; and Section 3863, *Financial Instruments – Presentation*. Adoption of these standards did not affect the financial position of the Company.

Capital Disclosures

As a result of adopting the new standard, additional information is provided in Note 11. The new standard requires disclosure of information about (i) the Company's objectives, policies and processes for managing capital; (ii) quantitative data about what the Company regards as capital; and (iii) whether the Company has complied with any capital requirements and consequences of non-compliance.

Financial Instruments – Disclosure and Presentation

As a result of adopting the new standards, enhanced disclosure is provided in Notes 4, 5, 12 and 20. These new standards place increased emphasis on disclosure about the nature and extent of risks arising from financial instruments and how the Company manages those risks.

2007

Effective January 1, 2007, the Company adopted new accounting standards issued by the CICA Handbook Section 3855, *Financial Instruments – Recognition and Measurement*; Section 3861, *Financial Instruments – Disclosure and Presentation*; Section 3865, *Hedges*; and Section 1530, *Comprehensive Income*.

These standards have been applied as an adjustment to opening retained earnings and accumulated other comprehensive income as of January 1, 2007.

Financial Instruments – Recognition and Measurement

As a result of adopting the new standards, all financial assets were classified as held for trading, available for sale or loans and receivables. Financial liabilities were classified as held for trading or other liabilities. The new standards require that all financial assets and liabilities be measured at fair value with the exception of loans and receivables and other liabilities which are measured at amortized cost using the effective interest method.

Effective January 1, 2007, cash resources and securities issued or guaranteed by Canada and the provinces are considered held for trading. Other securities and securitization receivable have been designated as available for sale.

Deferred loan origination costs were adjusted to what the balance would have been had the Company always used the effective interest rate method to recognize loan origination costs. These costs were reclassified against the respective loans on the consolidated balance sheet. The amortization of these costs in the current and in the prior year was reclassified from fees and other income (non-interest income) and general and administrative non-interest expenses to interest from loans on the consolidated statement of income.

Deposit origination costs were reclassified from other assets to net against deposits on the consolidated balance sheets. The amortization of these costs in the current and in the prior year was reclassified from general and administrative non-interest expenses to interest on deposits on the consolidated statement of income.

The Company reviewed its other contractual arrangements for embedded derivatives which require bifurcation from the underlying investment and separate valuation. These embedded derivatives do not currently have a significant value and therefore are not reported separately.

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

Hedges

The Company does not hold any derivatives or other financial instruments which have been designated for hedge accounting treatment.

Comprehensive Income

The new standards require the presentation of a new consolidated statement of comprehensive income, which consists of net income and other comprehensive income. Other comprehensive income represents the unrealized gains and losses on available for sale financial instruments, net of any transfers to net income of any previously unrealized gains and losses on available for sale assets, when the asset is disposed of or an other than temporary impairment is recognized, at which time the cumulative loss is transferred to net income. Accumulated other comprehensive income (AOCI) is presented as a new category of shareholders' equity in the consolidated balance sheet.

The impact of adopting these standards as at January 1, 2007 on a net of tax basis was as follows:

| (000s) | January 1, 2007 | Retained Earnings | AOCI |
|--------------------------------------|---------------------|----------------------|-----------------|
| Assets | | | |
| Cash resources | \$ 143,531 | \$ (1) | \$ - |
| Securities | 344,134 | 164 | 70 |
| Loans | 3,309,214 | 47 | - |
| Other | 105,437 | - | (700) |
| | \$ 3,902,316 | \$ 210 | \$ (630) |
| Liabilities | | | |
| Deposits | \$ 3,443,640 | \$ (1,181) | \$ - |
| Other liabilities | 181,810 | - | - |
| | 3,625,450 | (1,181) | - |
| Shareholders' equity | | | |
| Capital stock | 34,551 | - | - |
| Contributed surplus | 783 | - | - |
| Retained earnings | 241,532 | 1,391 | - |
| Accumulated other comprehensive loss | - | - | (630) |
| | 276,866 | 1,391 | (630) |
| | \$ 3,902,316 | \$ 210 | \$ (630) |

NOTE 3 DISPOSITION AND ACQUISITION

On January 1, 2008, Home Trust sold all outstanding shares of its wholly owned subsidiary, HTAM, for proceeds of \$0.2 million cash, resulting in a gain on disposition of \$0.1 million.

On October 16, 2007, the Company acquired 100% of the outstanding common shares of PSiGate for cash consideration of \$18.4 million. The estimated fair values of total assets acquired and total liabilities assumed at the date of acquisition were \$20.4 million and \$2.0 million, respectively. Included within the assets acquired is \$13.4 million of goodwill (not deductible for tax), \$1.2 million of intangible assets and \$2.1 million of cash. Income and expenses from PSiGate are included in the consumer lending segment in Note 19 and have been consolidated in the accounts of the Company from October 16, 2007. Goodwill was increased by \$0.7 million in 2008 for revisions to the purchase price allocation based on final adjustments to the opening PSiGate balance sheet.

NOTE 4 SECURITIES
(a) Securities at Fair Value by Type and Remaining Term to Maturity

| (000s) | | | | | 2008 | 2007 |
|------------------------------------|---------------|--------------|--------------|--------------|------------------|------------------|
| | Within 1 Year | 1 to 3 Years | 3 to 5 Years | Over 5 Years | Total Fair Value | Total Fair Value |
| Held for trading | | | | | | |
| Securities issued or guaranteed by | | | | | | |
| Canada | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 45,023 |
| Provinces | - | - | - | - | - | 300 |
| Corporations | - | - | - | - | - | 69,100 |
| Available for sale | | | | | | |
| Securities issued or guaranteed by | | | | | | |
| Canada | 20,201 | 60,860 | 82,427 | - | 163,488 | 179,969 |
| Corporations | - | 153,611 | 35,700 | - | 189,311 | - |
| Equity securities | | | | | | |
| Common | 5,346 | - | - | - | 5,346 | 10,693 |
| Fixed rate preferred | 44,247 | 31,425 | 32,231 | 44,749 | 152,652 | 137,307 |
| Floating rate preferred | - | 76 | 2,309 | - | 2,385 | 8,384 |
| Income trusts | 5,662 | - | - | - | 5,662 | 16,021 |
| Mutual funds | 633 | - | - | - | 633 | 4,084 |
| | \$ 76,089 | \$ 245,972 | \$ 152,667 | \$ 44,749 | \$ 519,477 | \$ 470,881 |

Effective January 1, 2008, all new bond acquisitions were designated as available for sale securities consistent with the Company's intention to hold them longer term.

During 2008, on held for trading securities, the Company recognized in net income \$0.7 million (2007 - \$0.6 million) for interest, \$1.5 million (2007 - \$0.1 million) for realized gains and nil (2007 - \$0.1 million) for unrealized gains.

(b) Unrealized Gains and Losses on Available for Sale Securities

| (000s, except %) | | | | | 2008 | |
|------------------------------------|----------------|------------------------|-------------------------|------------------|------------------------|--|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Total Fair Value | Weighted-average Yield | |
| Securities issued or guaranteed by | | | | | | |
| Canada | \$ 161,943 | \$ 1,545 | \$ - | \$ 163,488 | 4.2% | |
| Corporations | 186,966 | 2,345 | - | 189,311 | 4.3% | |
| Equity securities | | | | | | |
| Common | 7,447 | 569 | (2,670) | 5,346 | 2.6% | |
| Fixed rate preferred | 182,572 | 253 | (30,173) | 152,652 | 5.1% | |
| Floating rate preferred | 4,756 | - | (2,371) | 2,385 | 3.2% | |
| Income trusts | 8,408 | - | (2,746) | 5,662 | 6.9% | |
| Mutual funds | 1,000 | - | (367) | 633 | - | |
| | \$ 553,092 | \$ 4,712 | \$ (38,327) | \$ 519,477 | | |

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

| | 2007 | | | | |
|------------------------------------|-------------------|------------------------------|-------------------------------|---------------------|-------------------------------|
| (000s, except %) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Total Fair Value | Weighted- average Yield |
| Securities issued or guaranteed by | | | | | |
| Canada | \$ 180,080 | \$ 400 | \$ (511) | \$ 179,969 | 3.9% |
| Equity securities | | | | | |
| Common | 11,187 | 538 | (1,032) | 10,693 | 2.1% |
| Fixed rate preferred | 142,060 | 544 | (5,297) | 137,307 | 5.2% |
| Floating rate preferred | 8,654 | 32 | (302) | 8,384 | 5.3% |
| Income trusts | 18,912 | 67 | (2,958) | 16,021 | 7.7% |
| Mutual funds | 4,089 | - | (5) | 4,084 | 4.2% |
| | \$ 364,982 | \$ 1,581 | \$ (10,105) | \$ 356,458 | |

The above unrealized losses represent differences between the carrying value of a security and its current fair value. The Company does not consider these losses to be other than temporary based on market conditions at the reporting date and continues to regularly monitor these investments and market conditions.

As at December 31, 2008, the Company had \$1.8 million of unrealized losses on available for sale securities which are other than temporary in nature and have been transferred into net income. These unrealized losses are not included in the table above.

NOTE 5 LOANS

(a) Loans by Geographic Region and Type

| | 2008 | | | | |
|---------------------------|--------------------------|--------------------------------------|--------------------|------------------|---------------------|
| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
| British Columbia | \$ 333,668 | \$ 31,118 | \$ 8,998 | \$ 9 | \$ 373,793 |
| Alberta | 398,939 | 78,157 | 115,336 | 8,319 | 600,751 |
| Ontario | 2,267,199 | 250,611 | 630,953 | 61,929 | 3,210,692 |
| Quebec | 105,236 | 1,477 | 48,701 | - | 155,414 |
| Maritimes | 90,167 | 6,002 | 12,408 | 2,261 | 110,838 |
| Manitoba and Saskatchewan | 67,997 | 1,597 | 10,486 | - | 80,080 |
| | \$ 3,263,206 | \$ 368,962 | \$ 826,882 | \$ 72,518 | \$ 4,531,568 |

| | 2007 | | | | |
|---------------------------|--------------------------|--------------------------------------|--------------------|------------------|---------------------|
| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
| British Columbia | \$ 303,150 | \$ 22,828 | \$ 6,555 | \$ 213 | \$ 332,746 |
| Alberta | 387,168 | 70,781 | 50,210 | 7,957 | 516,116 |
| Ontario | 2,265,487 | 222,230 | 390,661 | 70,692 | 2,949,070 |
| Quebec | 59,952 | 24 | 12,066 | - | 72,042 |
| Maritimes | 118,297 | 7,661 | 8,429 | 3,442 | 137,829 |
| Manitoba and Saskatchewan | 35,899 | 1,869 | - | - | 37,768 |
| | \$ 3,169,953 | \$ 325,393 | \$ 467,921 | \$ 82,304 | \$ 4,045,571 |

(b) Past Due Loans That Are Not Impaired**2008**

| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
|-------------|--------------------------|--------------------------------------|--------------------|------------------|------------|
| 1-30 days | \$ 142,287 | \$ 3,365 | \$ 4,406 | \$ 973 | \$ 151,031 |
| 31-60 days | 9,249 | 1,896 | 2,407 | 98 | 13,650 |
| 61-90 days | 31,828 | 2,527 | 647 | - | 35,002 |
| 91-120 days | - | 1,887 | - | - | 1,887 |
| | \$ 183,364 | \$ 9,675 | \$ 7,460 | \$ 1,071 | \$ 201,570 |

2007

| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
|-------------|--------------------------|--------------------------------------|--------------------|------------------|------------|
| 1-30 days | \$ 114,316 | \$ 3,181 | \$ 2,918 | \$ 1,314 | \$ 121,729 |
| 31-60 days | 7,691 | 1,497 | 343 | 63 | 9,594 |
| 61-90 days | 28,143 | 1,508 | 657 | 241 | 30,549 |
| 91-120 days | - | 785 | - | - | 785 |
| | \$ 150,150 | \$ 6,971 | \$ 3,918 | \$ 1,618 | \$ 162,657 |

(c) Impaired Loans and Specific Allowances for Credit Losses**2008**

| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
|--------------------------------|--------------------------|--------------------------------------|--------------------|------------------|-----------|
| Gross amount of impaired loans | \$ 34,643 | \$ 6,309 | \$ 164 | \$ 1,007 | \$ 42,123 |
| Specific allowances | (1,680) | (547) | - | (699) | (2,926) |
| | \$ 32,963 | \$ 5,762 | \$ 164 | \$ 308 | \$ 39,197 |

2007

| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total |
|--------------------------------|--------------------------|--------------------------------------|--------------------|------------------|-----------|
| Gross amount of impaired loans | \$ 27,849 | \$ 1,521 | \$ 242 | \$ 400 | \$ 30,012 |
| Specific allowances | (634) | (128) | - | (231) | (993) |
| | \$ 27,215 | \$ 1,393 | \$ 242 | \$ 169 | \$ 29,019 |

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(d) Allowance for Credit Losses

| | 2008 | | | | | |
|--------------------------------------|--------------------------|--------------------------------------|--------------------|------------------|------------------|--|
| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total | |
| Specific allowances | | | | | | |
| Balance at the beginning of the year | \$ 634 | \$ 128 | \$ - | \$ 231 | \$ 993 | |
| Provision for credit losses | 2,971 | 937 | - | 953 | 4,861 | |
| Write-offs | (2,176) | (644) | - | (541) | (3,361) | |
| Recoveries | 251 | 126 | - | 56 | 433 | |
| | 1,680 | 547 | - | 699 | 2,926 | |
| General allowance | | | | | | |
| Balance at the beginning of the year | 17,127 | 3,201 | 2,216 | 856 | 23,400 | |
| Provision for credit losses | (991) | 499 | 2,364 | (95) | 1,777 | |
| | 16,136 | 3,700 | 4,580 | 761 | 25,177 | |
| Total allowance | \$ 17,816 | \$ 4,247 | \$ 4,580 | \$ 1,460 | \$ 28,103 | |
| | 2007 | | | | | |
| (000s) | Residential Mortgages | Personal and Credit Card Loans | Other Mortgages | Secured Loans | Total | |
| Specific allowances | | | | | | |
| Balance at the beginning of the year | \$ 386 | \$ 148 | \$ - | \$ 108 | \$ 642 | |
| Provision for credit losses | 1,183 | 728 | - | 375 | 2,286 | |
| Write-offs | (1,001) | (918) | - | (262) | (2,181) | |
| Recoveries | 66 | 170 | - | 10 | 246 | |
| | 634 | 128 | - | 231 | 993 | |
| General allowance | | | | | | |
| Balance at the beginning of the year | 15,886 | 2,378 | 659 | 721 | 19,644 | |
| Provision for credit losses | 1,241 | 823 | 1,557 | 135 | 3,756 | |
| | 17,127 | 3,201 | 2,216 | 856 | 23,400 | |
| Total allowance | \$ 17,760 | \$ 3,329 | \$ 2,216 | \$ 1,088 | \$ 24,393 | |

(e) Loan Maturities

| | 2008 | | | | | 2007 |
|--|---------------------|---------------------|-------------------|------------------|---------------------|---------------------|
| (000s) | Within 1 Year | 1 to 3 Years | 3 to 5 Years | Over 5 Years | Total Book Value | Total Book Value |
| Residential mortgages | \$ 1,574,657 | \$ 1,126,767 | \$ 512,973 | \$ 48,809 | \$ 3,263,206 | \$ 3,169,953 |
| Other mortgages | 433,167 | 206,002 | 183,668 | 4,045 | 826,882 | 467,921 |
| Personal and credit card loans | 358,192 | 526 | 1,791 | 8,453 | 368,962 | 325,393 |
| Secured loans ¹ | 31,860 | 29,335 | 11,323 | - | 72,518 | 82,304 |
| | 2,397,876 | 1,362,630 | 709,755 | 61,307 | 4,531,568 | 4,045,571 |
| General allowance for credit losses | - | - | - | - | (25,177) | (23,400) |
| | \$ 2,397,876 | \$ 1,362,630 | \$ 709,755 | \$ 61,307 | \$ 4,506,391 | \$ 4,022,171 |

¹ Secured loans are held by Regency Finance Corp., which is consolidated as a variable interest entity.

(f) Collateral

The fair value of collateral held against mortgages is based on appraisals at the time a loan is originated. Appraisals are only updated should circumstances warrant it or if a mortgage becomes impaired. As at December 31, 2008, the total appraised value of the collateral for mortgages past due that are not impaired, as determined when the mortgages were originated, is \$302.8 million. For impaired mortgages, the total appraised value of collateral at December 31, 2008 is \$48.4 million.

NOTE 6 LOAN SECURITIZATION (SECURITIZATION RECEIVABLE)

The Company's subsidiary, Home Trust, securitizes residential mortgage loans, and in these securitizations Home Trust retains interest-only strips and servicing responsibilities. The retained interests consist of Home Trust's rights to future cash flows arising after the investors in the special purpose entity have received the return for which they contracted. The investors and the special purpose entity have no recourse to other assets of either the Company or Home Trust for failure of debtors to pay when due. During the year, Home Trust sold \$1.50 billion (2007 - \$692.3 million) of mortgages receivable in securitization transactions. This value is subject to prepayment and interest rate risks on the transferred receivables. The retained interest in the securitization receivable recorded on the consolidated balance sheet for securitization transactions totaled \$139.9 million (2007 - \$65.8 million). Since these loans are transferred on a serviced basis, Home Trust has a servicing liability of \$10.3 million (2007 - \$1.8 million) included on the consolidated balance sheet. Mortgage payments, which have been collected and are payable to the National Housing Authority (NHA) trusts, as at December 31, 2008 totaled \$41.4 million (2007 - \$35.8 million) and are reported under other liabilities. There are no expected credit losses as the mortgages are guaranteed by Canada Mortgage and Housing Corporation, an agency of the federal government.

During the year, the Company expanded its loan securitization program by participating in the Canada Mortgage Bond (CMB) program. Total mortgage receivables of \$1.09 billion (2007 - \$119.6 million) were transferred. The securitization receivable includes \$89.6 million (2007 - \$7.8 million) for the CMB retained interest. A servicing liability of \$9.1 million (2007 - \$0.2 million) is included on the consolidated balance sheet.

The impact of securitizations on the consolidated statement of income for the years ended December 31 is as follows:

| (000s) | 2008 | 2007 |
|--|-----------|-----------|
| Gain on sales of mortgages | \$ 61,314 | \$ 22,763 |
| Reduction in value to reflect increase in prepayment rate assumption | - | (770) |
| Change in retained interest | 8,990 | 4,589 |
| Change in servicing liability | 1,004 | 772 |
| Other securitization revenues (expenses) | (205) | 13 |
| | \$ 71,103 | \$ 27,367 |

The following table provides quantitative information about key assumptions in measuring retained interests at the date of securitization of residential mortgages securitized during the years ended December 31:

| | 2008 | 2007 |
|--------------------------------|------|-------|
| Prepayment rate | 7.6% | 13.2% |
| Discount rate | 3.4% | 4.3% |
| Excess spread | 2.6% | 2.7% |
| Weighted-average life in years | 4.0 | 4.0 |

There are no assumptions for expected credit losses as these mortgages are all government-guaranteed.

At December 31, key economic assumptions and the sensitivity of the current fair value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions are as follows:

| (000s, except % and number of years) | 2008 | 2007 |
|--|------------|-----------|
| Carrying amount of retained interest | \$ 139,870 | \$ 65,768 |
| Weighted-average life in years | 3.7 | 2.4 |
| Prepayment rate | 11.6% | 19.4% |
| Impact on fair value of 10% adverse change | (2,280) | (1,481) |
| Impact on fair value of 20% adverse change | (4,491) | (2,916) |
| Residual cash flows discount rate | 2.7% | 4.2% |
| Impact on fair value of 10% adverse change | (647) | (330) |
| Impact on fair value of 20% adverse change | (1,287) | (656) |

There are no assumptions for expected credit losses as these mortgages are all government-guaranteed.

The table below summarizes certain cash flows received from the securitization trusts:

| (000s) | 2008 | 2007 |
|---|--------------|------------|
| Net proceeds from new securitizations | \$ 1,478,138 | \$ 673,920 |
| Cash flows received on retained interests | 46,780 | 32,772 |

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

The table below summarizes quantitative information about the Company's loans:

| | | | 2008 |
|---|------------------------|---|---------------|
| (000s) | Total Principal Amount | Principal Amount of Loans 61 or More Days Past Due | |
| Total loans managed or securitized | \$ 7,145,826 | \$ | 105,759 |
| Less mortgages securitized | 2,614,258 | | 26,811 |
| Total gross loans reported on the consolidated balance sheet | \$ 4,531,568 | \$ | 78,948 |
| | | | 2007 |
| (000s) | Total Principal Amount | Principal Amount of Loans 61 or More Days Past Due | |
| Total loans managed or securitized | \$ 5,505,026 | \$ | 46,401 |
| Less mortgages securitized | 1,459,455 | | 10,605 |
| Total gross loans reported on the consolidated balance sheet | \$ 4,045,571 | \$ | 35,796 |

NOTE 7 CAPITAL ASSETS

| | | | 2008 | 2007 |
|--------------------------------|------------------|-----------------------------|-------------------|-------------------|
| (000s) | Cost | Accumulated Amortization | Net Book Value | Net Book Value |
| Computer equipment | \$ 8,907 | \$ 7,058 | \$ 1,849 | \$ 1,793 |
| Software | 112 | 60 | 52 | 78 |
| Office furniture and equipment | 6,472 | 3,815 | 2,657 | 2,547 |
| Leasehold improvements | 2,920 | 2,153 | 767 | 419 |
| | \$ 18,411 | \$ 13,086 | \$ 5,325 | \$ 4,837 |

Amortization in respect of the above-noted capital assets for the year amounted to \$2.8 million (2007 - \$2.0 million).

NOTE 8 OTHER ASSETS

| (000s) | 2008 | 2007 |
|---|------------------|------------------|
| Accrued interest receivable | \$ 27,861 | \$ 25,308 |
| Income taxes receivable | 10,472 | - |
| Goodwill | 15,752 | 15,028 |
| Intangible assets | 558 | 1,158 |
| Other prepaid assets and deferred items | 29,585 | 15,606 |
| | \$ 84,228 | \$ 57,100 |

The increase in goodwill reflects adjustments to the purchase price allocation related to the finalization of the PSiGate balance sheet as at October 16, 2007, the date of acquisition as described in Note 3.

| NOTE 9 DEPOSITS | | | | | | | 2008 | 2007 |
|------------------------|-------------------|---------------|--------------|--------------|--------------|--------------|-------|------|
| (000s, except %) | Payable on Demand | Within 1 Year | 1 to 3 Years | 3 to 5 Years | Total | Total | Total | |
| Individuals | \$ 34,808 | \$ 3,269,000 | \$ 1,310,772 | \$ 447,023 | \$ 5,061,603 | \$ 4,380,835 | | |
| Businesses | - | 28,947 | 8,151 | 4,080 | 41,178 | 33,149 | | |
| | \$ 34,808 | \$ 3,297,947 | \$ 1,318,923 | \$ 451,103 | \$ 5,102,781 | \$ 4,413,984 | | |
| Effective yield | - | 3.9% | 4.4% | 4.7% | 4.1% | 4.4% | | |

| NOTE 10 OTHER LIABILITIES | | | | 2008 | 2007 |
|--|--|--|--|------------|------------|
| (000s) | | | | | |
| Accrued interest payable | | | | \$ 159,615 | \$ 135,650 |
| Income taxes payable | | | | - | 5,795 |
| Dividends payable | | | | 4,476 | 3,799 |
| Future income taxes (Note 13) | | | | 36,974 | 16,586 |
| Securitization servicing liability | | | | 10,288 | 1,786 |
| Other, including accounts payable and accrued liabilities ¹ | | | | 58,015 | 45,060 |
| | | | | \$ 269,368 | \$ 208,676 |

¹ The Company has recognized a liability for employee future benefits in the amount of \$140,000 (2007 - \$128,000).

| NOTE 11 CAPITAL | | | | | |
|---|--|------------------|------------------|------------------|------------------|
| (a) Authorized | | | | | |
| An unlimited number of common shares. | | | | | |
| An unlimited number of preferred shares, issuable in series, to be designated as Senior preferred shares. | | | | | |
| An unlimited number of preferred shares, issuable in series, to be designated as Junior preferred shares. | | | | | |
| (b) Issued and Outstanding | | | | | |
| (000s) | | Number of Shares | 2008 Book Value | Number of Shares | 2007 Book Value |
| Common shares | | | | | |
| Balance, beginning of year | | 34,532 | \$ 38,899 | 34,166 | \$ 35,436 |
| Options exercised | | 10 | 318 | 477 | 3,585 |
| Repurchase of shares | | (108) | (123) | (111) | (122) |
| Balance, end of year | | 34,434 | \$ 39,094 | 34,532 | \$ 38,899 |

The purchase price of shares acquired through the Normal Course Issuer Bid is allocated between capital stock and retained earnings. Comparative figures have been reclassified to conform to this presentation.

(c) Normal Course Issuer Bid

On July 28, 2008, the Company filed a Normal Course Issuer Bid which allows it to purchase over a twelve-month period, beginning August 1, 2008, up to 10% of the public float outstanding on July 28, 2008.

On July 30, 2007, the Company filed a Normal Course Issuer Bid which allowed it to purchase over a twelve-month period, beginning August 1, 2007, up to 10% of the public float outstanding on July 27, 2007.

During the year, 108,400 (2007 - 110,400) common shares were purchased for \$3.0 million (2007 - \$3.9 million). The purchase price of shares acquired through the Normal Course Issuer Bid is allocated between capital stock and retained earnings. Comparative figures have been reclassified to conform to this presentation. The cost of the common shares was reduced by \$123,000 in 2008 (2007 - \$122,000).

Notes to Consolidated Financial Statements

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(d) Stock Options

The details and changes in the issued and outstanding options are as follows:

| | 2008 | | 2007 | |
|---|-------------------|---------------------------------|-------------------|---------------------------------|
| (000s, except exercise price and number of years) | Number of Options | Weighted-average Exercise Price | Number of Options | Weighted-average Exercise Price |
| Outstanding, beginning of year | 1,294 | \$ 27.15 | 1,266 | \$ 15.43 |
| Issued | 205 | 16.27 | 505 | 37.78 |
| Exercised | (10) | 28.12 | (477) | 7.31 |
| Cancelled | (82) | 35.32 | - | - |
| Outstanding, end of year | 1,407 | \$ 25.08 | 1,294 | \$ 27.15 |
| Exercisable at year end | 661 | \$ 18.73 | 526 | \$ 15.04 |
| Weighted-average term to maturity in years | | 3.4 | | 3.9 |

The Company's Stock Option Plan was approved by the shareholders of the Company on December 31, 1986. The plan was amended, effective May 29, 2002, to conform the plan to the Toronto Stock Exchange's Revised Policy on Listed Company Share Incentive Arrangements. As at December 31, 2008, the maximum number of common shares that may be issued was 4,585,198, representing approximately 11.7% of the aggregate number of common shares. The exercise price of the options shall be fixed by the Board of Directors (the Board) at the time of issuance at the market price of such shares subject to all applicable regulatory requirements. The market price per share shall not be less than the weighted-average price at which the common shares of the Company trade on the Toronto Stock Exchange during the two trading days immediately preceding the date on which the option is approved by the Board. The exercise period of any option will not extend beyond a period of seven years from the date of grant of the option. The period within which an option or portion thereof may be exercised by a participant will be determined in each case by the Board.

As at December 31, 2008, stock options outstanding to acquire common shares were as follows:

| | Stock Options Outstanding | Stock Options Exercisable | Exercise Price per Share | Expiry Date |
|---------------------------|---------------------------|---------------------------|--------------------------|-------------|
| Options granted to | | | | |
| Directors | 265,000 | 265,000 | \$ 7.15 | 12/05/2009 |
| | 100,000 | 25,000 | 34.51 ¹ | 02/14/2012 |
| | 20,000 | - | 41.29 ¹ | 12/07/2014 |
| | 20,000 | - | 16.27 ² | 12/08/2015 |
| | 405,000 | 290,000 | | |
| Employees | 15,000 | 15,000 | 7.15 | 12/05/2009 |
| | 95,500 | 95,500 | 10.56 | 07/23/2010 |
| | 37,500 | 28,125 | 34.55 | 02/14/2010 |
| | 10,000 | 7,500 | 34.53 | 04/26/2010 |
| | 123,750 | 92,500 | 35.25 | 12/06/2010 |
| | 10,000 | 7,500 | 42.02 | 03/03/2011 |
| | 15,000 | 15,000 | 26.16 | 03/10/2011 |
| | 30,000 | 15,000 | 31.20 | 07/26/2011 |
| | 105,000 | 52,500 | 27.89 | 10/25/2011 |
| | 50,000 | 12,500 | 27.71 | 12/01/2011 |
| | 100,000 | 25,000 | 34.51 ¹ | 02/14/2012 |
| | 20,000 | 5,000 | 33.76 ¹ | 03/07/2014 |
| | 205,000 | - | 41.29 ¹ | 12/07/2014 |
| | 185,000 | - | 16.27 ² | 12/08/2015 |
| | 1,001,750 | 371,125 | | |
| Total | 1,406,750 | 661,125 | \$ 18.73 | |

¹ In 2007, the Company granted certain employees the right to receive stock options of 200,000, 20,000, and 225,000 if certain performance criteria were met. As at December 31, 2008, one level of the performance criteria for the 200,000 and the 20,000 had been met. As a result, 25% of these contingently assumable options have been included in the computation of diluted income per common share.

² In 2008, the Company granted certain employees the right to receive stock options of 205,000 if certain performance criteria were met. As at December 31, 2008, none of the performance criteria had been met. As a result, the contingently assumable options have not been included in the computation of diluted income per common share.

(e) Fair Value Compensation of Stock Options

The Company determines the fair value of options granted using the Black-Scholes option pricing model. The weighted-average fair value of the options granted during the year ended December 31, 2008 was \$5.36 for the December 2008 issue. The weighted-average fair value of the options granted during the year ended December 31, 2007 was \$14.43 for the December 2007 issue, \$12.02 for the August 2007 issue, \$12.76 for the March 2007 issue and \$8.36 for the February 2007 issue.

The following weighted-average assumptions were used to determine the fair value of the options on the date of grant:

| | December 2008 | | | | |
|---|--------------------------|------------------|----------------|---------------|------------------|
| Expected dividend yield | 2.51% | | | | |
| Expected share price volatility | 33.2% | | | | |
| Risk-free rate of return | 2.67% | | | | |
| Expected period until exercise in years | 7.0 | | | | |
| | | December 2007 | August 2007 | March 2007 | February 2007 |
| Expected dividend yield | | 1.20% | 1.27% | 1.04% | 0.89% |
| Expected share price volatility | | 28.7% | 28.3% | 27.8% | 27.0% |
| Risk-free rate of return | | 3.94% | 4.53% | 3.91% | 4.06% |
| Expected period until exercise in years | | 7.0 | 7.0 | 7.0 | 5.0 |

For options granted after January 1, 2003, the Company determines the fair value of stock options on their grant date and records this amount as compensation expense over the period that the stock options vest, with a corresponding increase to contributed surplus. When these stock options are exercised, the Company records the amount of proceeds, together with the amount recorded in contributed surplus, in capital stock. Employee compensation expense increased by \$1.5 million (2007 - \$1.1 million) and net income decreased by the same amount with respect to options granted during the year.

The Company will not record any compensation expense for stock options granted prior to January 1, 2003. When these stock options are exercised, the Company will include the amount of proceeds in capital stock. If the Company had recorded compensation expense for such options based on their fair value, the pro forma effect on net income and income per share would have been as follows:

| (000s, except per share amounts) | 2008 | 2007 |
|---|-------------------|-----------|
| Pro forma net income | \$ 108,687 | \$ 90,241 |
| Pro forma income per common share - basic | 3.15 | 2.62 |
| Pro forma income per common share - diluted | 3.13 | 2.59 |

(f) Income per Common Share

Basic income per common share is determined as net income for the year divided by the average number of common shares outstanding of 34,512,283 (2007 - 34,446,847).

Diluted income per common share is determined as net income for the year divided by the average number of common shares outstanding of 34,512,283 (2007 - 34,446,847) plus the stock options potentially exercisable as determined under the treasury stock method of 157,019 (2007 - 410,106) for a total of 34,669,302 (2007 - 34,856,953) diluted common shares.

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(g) Capital Management

The Company has a Capital Management Policy which governs the quantity and quality of capital held. The objective of the policy is to ensure that regulatory capital requirements are met, while also providing a sufficient return to investors. The Risk and Capital Committee and the Board of Directors annually review the policy and monitor compliance with the policy on a quarterly basis.

The Company's subsidiary Home Trust is subject to the regulatory capital requirements governed by the Office of the Superintendent of Financial Institutions (OSFI). These requirements are consistent with international standards set by the Bank for International Settlements (BIS). Effective January 1, 2008, Home Trust Company adopted the new capital framework (Basel II) as required by OSFI. Under Basel II, the computation of risk-weighted assets was revised and a new measure for operational risk was introduced. Home Trust follows the Standardized Approach for calculating credit risk and the Basic Indicator Approach for operational risk.

The regulatory capital position of Home Trust Company was as follows:

| (000s, except ratios and multiple) | 2008 | 2007 |
|------------------------------------|------------|------------|
| Regulatory capital | | |
| Tier 1 | \$ 384,025 | \$ 311,760 |
| Total | 424,202 | 350,160 |
| Regulatory ratios | | |
| Tier 1 | 12.9% | 11.1% |
| Total | 14.2% | 12.5% |
| Assets to capital multiple | 13.7 | 14.2 |

Figures for 2007 were calculated in accordance with the Basel I capital rules in effect at the time.

Under Basel II, OSFI considers a financial institution to be well capitalized if it maintains a Tier 1 capital ratio of 7% and a total capital ratio of 10%. Home Trust Company is in compliance with the OSFI capital guidelines.

NOTE 12 ACCUMULATED OTHER COMPREHENSIVE LOSS

The components comprising the accumulated other comprehensive loss are:

| (000s) | 2008 | 2007 |
|--------------------------------------|-------------|------------|
| Unrealized losses on | | |
| Available for sale securities | \$ (33,615) | \$ (8,524) |
| Income taxes recovery | 10,473 | 2,226 |
| | (23,142) | (6,298) |
| Unrealized gains on | | |
| Securitization receivables | 18,080 | 2 |
| Income taxes expense | (5,991) | (1) |
| | 12,089 | 1 |
| Accumulated other comprehensive loss | \$ (11,053) | \$ (6,297) |

NOTE 13 INCOME TAXES
(a) Components of the Provision for Income Taxes

| (000s) | 2008 | 2007 |
|-----------------------------|------------------|-----------|
| Current income taxes | | |
| Federal | \$ 20,914 | \$ 24,822 |
| Provincial | 14,619 | 15,710 |
| | 35,533 | 40,532 |
| Future income taxes | | |
| Federal | 7,900 | 2,053 |
| Provincial | 6,498 | 1,259 |
| | 14,398 | 3,312 |
| | \$ 49,931 | \$ 43,844 |

(b) Reconciliation of Income Taxes

| (000s) | 2008 | 2007 |
|---|------------------|------------|
| Income before income taxes | \$ 158,618 | \$ 134,085 |
| Income taxes at statutory combined federal and provincial income tax rate | \$ 52,565 | \$ 48,377 |
| Increase (decrease) in income taxes resulting from: | | |
| Tax-exempt income | (2,835) | (3,484) |
| Non-deductible expenses | 1,491 | 723 |
| Future tax rate changes | (1,378) | (1,503) |
| Other | 88 | (269) |
| | \$ 49,931 | \$ 43,844 |

The combined federal and provincial income tax rate varies each year according to changes in the statutory tax rate imposed by the federal and provincial governments. The effective rate of income tax in the consolidated statement of income is different from the combined federal and provincial income tax rate of 31.5% (2007 - 32.7%).

(c) Sources of Future Income Tax Assets and Liabilities

| (000s) | 2008 | 2007 |
|--|------------------|-----------|
| Future income tax liabilities | | |
| Deferred agent commissions and other charges | \$ 7,761 | \$ 7,907 |
| Mortgage-backed securities receivable | 40,828 | 21,282 |
| | 48,589 | 29,189 |
| Future income tax assets | | |
| Allowance for credit losses | 7,776 | 6,767 |
| Deferred commitment fees and unearned income | 3,839 | 4,466 |
| Future taxes recoverable in subsidiary | - | 1,370 |
| | 11,615 | 12,603 |
| Net future income tax liability | \$ 36,974 | \$ 16,586 |

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NOTE 14 EMPLOYEE BENEFITS

(a) Employee Share Purchase Plan

Effective January 1, 2001, qualifying employees of Home Trust have the ability to purchase shares in the Company. Under the Employee Share Purchase Plan, qualifying employees can choose each year to have up to 10% of their annual base earnings withheld to purchase common shares. The Company matches 50% of the employee's contribution amount. All contributions are used by the plan's trustee to purchase the common shares during each pay period in the open market. The Company's contributions are fully vested immediately. The Company's contributions are expensed as paid and totaled \$0.5 million for 2008 (2007 - \$0.4 million).

(b) Employee Retirement Savings Plan

During the year ended December 31, 2008, Home Trust contributed \$0.4 million (2007 - \$0.3 million) to the employee group registered retirement savings plan.

NOTE 15 COMMITMENTS AND CONTINGENCIES

(a) Lease Commitments

Contractual obligations in respect of premises and equipment leases as at December 31, 2008 are as follows:

| (000s) | | |
|---------------------|----|--------|
| 2009 | \$ | 2,224 |
| 2010 | | 2,028 |
| 2011 | | 1,991 |
| 2012 | | 1,890 |
| 2013 | | 1,881 |
| 2014 and thereafter | | 3,564 |
| | \$ | 13,578 |

| (000s) | 2008 | 2007 |
|-----------|----------|----------|
| Rent paid | \$ 3,426 | \$ 3,058 |

(b) Credit Commitments

Outstanding commitments for funding on mortgages amounted to \$242.4 million as at December 31, 2008 (2007 - \$447.3 million). The commitments remain open for various dates until December 2009 for 2008 and July 2009 for 2007. The average rate on mortgage commitments is 5.94% (2007 - 6.97%).

The Company also has contractual commitments to extend credit to its clients for its credit card products. The contractual commitment for this product represents the maximum potential credit risk, assuming the contractual amount is fully utilized and the client defaults and collection efforts are unsuccessful. At December 31, 2008, these contractual commitments in aggregate were \$415.0 million (2007 - \$392.2 million) of which \$62.9 million (2007 - \$78.0 million) has not been drawn by customers. In addition, outstanding commitments for new Equityline Visa accounts were \$2.5 million at December 31, 2008 (2007 - \$5.9 million).

These amounts in aggregate are not indicative of future cash requirements. Management does not expect any material adverse consequence to the Company's financial position to result from these commitments. Secured credit cards have spending limits restricted by collateral held by the Company.

(c) Directors' and Officers' Indemnification

The Company indemnifies directors and officers, to the extent permitted by law, against certain claims that may be made against them as a result of their being, or having been, directors and officers at the request of the Company. The nature of this indemnification prevents the Company from making a reasonable estimate of the maximum potential amount the Company could be required to pay to third parties. Management believes that the likelihood that the Company would incur a significant liability under these indemnifications is remote. The Company has purchased directors' and officers' liability insurance.

NOTE 16 DERIVATIVE FINANCIAL INSTRUMENTS

In the normal course of business, the Company enters into contracts and commitments in order to protect itself against the risk of fluctuations in interest rates.

During the year the Company entered into interest rate swaps to hedge the economic fair value exposure of movements in interest rates from the Company's participation in the CMB program. The intent of the swaps is to have fair value movements in the swap be effective in offsetting the fair value movements of the Company's funding commitments under the CMB program. These transactions did not qualify for hedge accounting and therefore were accounted for on a mark-to-market basis, with changes in the fair value of the swap being recognized in income.

The following table summarizes the Company's derivative holdings as at December 31, 2008:

| | | | | | | 2008 |
|---------------------|---------------------|--------------------------|--------------------------|-----------------------|-------------------|------|
| (000s) | Notional Amount | Current Replacement Cost | Credit Equivalent Amount | Risk-weighted Balance | Fair Market Value | |
| Interest rate swaps | | | | | | |
| Maturing in 2011 | \$ 110,187 | \$ 1,668 | \$ 1,687 | \$ 337 | \$ 787 | |
| Maturing in 2012 | 136,155 | 5,635 | 5,723 | 1,145 | 4,037 | |
| Maturing in 2013 | 947,702 | 13,580 | 13,721 | 2,744 | (3,443) | |
| Maturing in 2018 | 68,814 | 196 | 196 | 39 | (947) | |
| | \$ 1,262,858 | \$ 21,079 | \$ 21,327 | \$ 4,265 | \$ 434 | |

The Company held the following financial derivatives as at December 31, 2007:

| | | | | | | 2007 |
|---------------------|-----------------|--------------------------|--------------------------|-----------------------|-------------------|------|
| (000s) | Notional Amount | Current Replacement Cost | Credit Equivalent Amount | Risk-weighted Balance | Fair Market Value | |
| Interest rate swaps | | | | | | |
| Maturing in 2012 | \$ 120,715 | \$ 983 | \$ 2,794 | \$ 559 | \$ 983 | |

The following terms are used in the above table: "notional amount" represents the amount to which a rate or price is applied in order to calculate the amount of cash that must be exchanged under the contract; "current replacement cost" represents the cost of replacing the contract which has a positive fair value using current market rates; "credit equivalent amount" represents the total replacement cost and the potential future credit exposure, if the counterparty defaults; "risk-weighted balance" represents the credit risk equivalent, weighted based on the creditworthiness of the counterparty, as prescribed by OFSI; and "fair market value" represents the value of the contract using current interest rates.

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NOTE 17 INTEREST RATE SENSITIVITY

The Company is exposed to interest rate risk as a result of a difference, or gap, between the maturity or repricing date of interest sensitive assets and liabilities. The following table shows the gap position at December 31 for selected period intervals. Figures in parentheses represent an excess of liabilities over assets or a negative gap position.

This schedule reflects the contractual maturities of both assets and liabilities, adjusted for assumptions regarding the effective change in the maturity date as a result of a mortgage becoming impaired and for credit commitments and derivatives.

Based on the current interest rate gap position as at December 31, 2008, the Company estimates that a 100 basis point decrease in interest rates would decrease net interest income after tax over the next twelve months by \$3.9 million. A 100 basis point increase in interest rates would increase net income after tax over the next twelve months by a similar amount.

| | 2008 | | | | | | | |
|---|------------------|---------------------|--------------------|---------------------|---------------------|-------------------|------------------------|---------------------|
| (000s, except %) | Floating | 0 to 3 Months | 3 to 6 Months | 6 to 12 Months | 1 to 3 Years | Over 3 Years | Non-interest Sensitive | Total |
| Assets | | | | | | | | |
| Cash resources | \$ 29,006 | \$ 525,416 | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 554,422 |
| Weighted-average interest rate | 0.5% | 1.5% | - | - | - | - | - | 1.5% |
| Securities | - | 17,336 | 32,670 | 26,083 | 245,972 | 197,416 | - | 519,477 |
| Weighted-average interest rate | - | 5.0% | 5.5% | 4.2% | 4.3% | 4.7% | - | 4.5% |
| Loans | - | 900,115 | 494,177 | 953,676 | 1,355,465 | 768,084 | 34,874 | 4,506,391 |
| Weighted-average interest rate | - | 8.2% | 7.0% | 7.3% | 7.3% | 6.6% | - | 7.3% |
| Other assets | - | - | - | - | - | - | 229,423 | 229,423 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Total | \$ 29,006 | \$ 1,442,867 | \$ 526,847 | \$ 979,759 | \$ 1,601,437 | \$ 965,500 | \$ 264,297 | \$ 5,809,713 |
| Weighted-average interest rate | 0.5% | 5.7% | 6.9% | 7.2% | 6.8% | 6.3% | - | 6.2% |
| Liabilities and shareholders' equity | | | | | | | | |
| Deposits payable on demand | \$ 6 | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 34,802 | \$ 34,808 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Deposits payable on a fixed date | - | 923,590 | 574,581 | 1,785,252 | 1,318,923 | 451,102 | 14,525 | 5,067,973 |
| Weighted-average interest rate | - | 4.0% | 4.0% | 3.9% | 4.4% | 4.7% | 0.0% | 4.1% |
| Other liabilities | - | - | - | - | - | - | 274,179 | 274,179 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Shareholders' equity | - | - | - | - | - | - | 432,753 | 432,753 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Total | \$ 6 | \$ 923,590 | \$ 574,581 | \$ 1,785,252 | \$ 1,318,923 | \$ 451,102 | \$ 756,259 | \$ 5,809,713 |
| Weighted-average interest rate | - | 4.0% | 4.0% | 3.9% | 4.4% | 4.7% | - | 3.6% |
| | \$ 29,000 | \$ 519,277 | \$ (47,734) | \$ (805,493) | \$ 282,514 | \$ 514,398 | \$ (491,962) | 2.3% |
| Credit commitments and derivatives | - | (145,838) | 30,130 | 34,825 | 80,837 | 46 | - | - |
| Weighted-average interest rate | - | 6.2% | 7.5% | 5.0% | 6.3% | 3.5% | - | - |
| Interest rate sensitivity gap | \$ 29,000 | \$ 373,439 | \$ (17,604) | \$ (770,668) | \$ 363,351 | \$ 514,444 | \$ (491,962) | \$ - |
| Cumulative gap | \$ 29,000 | \$ 402,439 | \$ 384,835 | \$ (385,833) | \$ (22,482) | \$ 491,962 | \$ - | \$ - |

| (000s, except %) | Floating | 0 to 3 Months | 3 to 6 Months | 6 to 12 Months | 1 to 3 Years | Over 3 Years | Non-interest Sensitive | Total |
|---|------------------|-------------------|---------------------|---------------------|---------------------|-------------------|---------------------------|---------------------|
| Assets | | | | | | | | |
| Cash resources | \$ 59,161 | \$ 261,438 | \$ 13,837 | \$ 19,900 | \$ - | \$ - | \$ - | \$ 354,336 |
| Weighted-average interest rate | 3.0% | 4.7% | 4.2% | 4.3% | - | - | - | 4.4% |
| Securities | - | 96,112 | 19,872 | 46,833 | 183,327 | 124,737 | - | 470,881 |
| Weighted-average interest rate | - | 4.7% | 5.8% | 4.1% | 4.4% | 4.8% | - | 4.6% |
| Loans | - | 543,641 | 390,245 | 1,163,166 | 1,423,865 | 471,387 | 29,867 | 4,022,171 |
| Weighted-average interest rate | - | 9.2% | 7.3% | 7.5% | 7.3% | 7.3% | - | 7.6% |
| Other assets | - | - | - | - | - | - | 127,705 | 127,705 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Total | \$ 59,161 | \$ 901,191 | \$ 423,954 | \$ 1,229,899 | \$ 1,607,192 | \$ 596,124 | \$ 157,572 | \$ 4,975,093 |
| Weighted-average interest rate | 3.0% | 7.4% | 7.2% | 7.3% | 7.0% | 6.8% | - | 6.9% |
| Liabilities and shareholders' equity | | | | | | | | |
| Deposits payable on demand | \$ - | \$ 229 | \$ - | \$ - | \$ - | \$ - | \$ 30,564 | \$ 30,793 |
| Weighted-average interest rate | - | 2.9% | - | - | - | - | - | - |
| Deposits payable on a fixed date | - | 445,878 | 630,401 | 1,506,590 | 1,330,558 | 452,096 | 17,668 | 4,383,191 |
| Weighted-average interest rate | - | 4.1% | 4.3% | 4.5% | 4.4% | 4.7% | - | 4.4% |
| Other liabilities | - | - | - | - | - | - | 213,069 | 213,069 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Shareholders' equity | - | - | - | - | - | - | 348,040 | 348,040 |
| Weighted-average interest rate | - | - | - | - | - | - | - | - |
| Total | \$ - | \$ 446,107 | \$ 630,401 | \$ 1,506,590 | \$ 1,330,558 | \$ 452,096 | \$ 609,341 | \$ 4,975,093 |
| Weighted-average interest rate | - | 4.1% | 4.3% | 4.5% | 4.4% | 4.7% | - | 3.9% |
| Credit commitments and derivatives | \$ 59,161 | \$ 455,084 | \$ (206,447) | \$ (276,691) | \$ 276,634 | \$ 144,028 | \$ (451,769) | 3.0% |
| Weighted-average interest rate | - | (437,032) | 2,414 | 191,279 | 110,534 | 132,805 | - | - |
| Weighted-average interest rate | - | 6.9% | 3.2% | 3.2% | 7.4% | 7.0% | - | - |
| Interest rate sensitivity gap | \$ 59,161 | \$ 18,052 | \$ (204,033) | \$ (85,412) | \$ 387,168 | \$ 276,833 | \$ (451,769) | \$ - |
| Cumulative gap | \$ 59,161 | \$ 77,213 | \$ (126,820) | \$ (212,232) | \$ 174,936 | \$ 451,769 | \$ - | \$ - |

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NOTE 18 FAIR VALUE OF FINANCIAL INSTRUMENTS

The amounts set out in the following table represent the fair values of the Company's financial instruments, both on- and off-balance sheet, the valuation methods and assumptions of which are described below.

The estimated fair value amounts are designed to approximate amounts at which financial instruments could be exchanged in a current transaction between willing parties who are under no compulsion to act. For financial instruments which lack an available trading market, the Company applies present value and valuation techniques that use observable or unobservable market inputs. Because of the estimation process and the need to use judgement, the aggregate fair value amounts should not be interpreted as being necessarily realizable in an immediate settlement of the instruments.

| (000s) | Carrying Value | Fair Value | 2008 | | 2007 | |
|--|----------------|------------|--------------------------------|----------------|------------|--------------------------------|
| | | | Fair Value Over Carrying Value | Carrying Value | Fair Value | Fair Value Over Carrying Value |
| Assets | | | | | | |
| Cash resources | \$ 554,422 | \$ 554,422 | \$ - | \$ 354,336 | \$ 354,336 | \$ - |
| Securities | 519,477 | 519,477 | - | 470,881 | 470,881 | - |
| Loans | 4,506,391 | 4,532,833 | 26,442 | 4,022,171 | 4,032,040 | 9,869 |
| Other | 229,423 | 229,423 | - | 127,705 | 127,705 | - |
| Liabilities | | | | | | |
| Deposits and borrowings | 5,102,781 | 5,411,281 | 308,500 | 4,413,984 | 4,519,437 | 105,453 |
| Other | 274,179 | 274,179 | - | 213,069 | 213,069 | - |
| Off-balance sheet financial instruments | | | | | | |
| Credit commitments | \$ 307,820 | \$ 305,468 | \$ (2,352) | \$ 531,151 | \$ 541,005 | \$ 9,854 |

The following methods and assumptions were used to estimate the fair values of both on- and off-balance sheet financial instruments:

- > Cash resources are assumed to approximate their carrying values due to their short-term nature. The fair value of treasury bills is determined using rates from the Bank of Canada.
- > Securities are valued based on the quoted bid price as provided in Note 4.
- > Fair value of loans is determined by discounting the expected future cash flows of the loans at market rates for loans with similar terms and credit risks.
- > Other assets are assumed to approximate their carrying values due to their short-term nature. Other assets include securitization receivable which is valued as described in Notes 1 and 6.
- > Fair value of deposits payable on demand approximates their carrying value; fixed-rate deposits are determined by discounting the contractual cash flows using the market interest rates currently offered for deposits with similar terms and risks.
- > Other liabilities are assumed to approximate their carrying values due to their short-term nature.
- > Fair value of credit commitments is determined by discounting the expected future cash flows of the credit commitments at market rates for loans with similar terms and credit risks. Book and fair value amounts for credit commitments represent the notional amount of the commitment.
- > Derivative financial instruments are assumed to approximate their fair values as provided in Note 16.

NOTE 19 EARNINGS BY BUSINESS SEGMENT

The Company operates principally through two operations – mortgage lending and consumer lending. The mortgage lending operation consists of mortgage lending, securitization of government-insured mortgages and secured loans. The consumer lending operation consists of credit cards, PSiGate and individual loans to customers of retail businesses. The other category includes treasury and security investments and corporate activities.

The following tables detail the earnings of the Company by business segment:

| | 2008 | | | |
|--|-----------------------------|-----------------------------|-------------------|---------------------|
| (000s) | Mortgage Lending | Consumer Lending | Other | Total |
| Net interest income | \$ 89,505 | \$ 26,459 | \$ 34,611 | \$ 150,575 |
| Provision for credit losses | (5,202) | (1,436) | - | (6,638) |
| Fees and other income | 15,163 | 12,888 | 401 | 28,452 |
| Gain on securities and mortgage-backed securities and disposition of subsidiary | 57,536 | - | (5,296) | 52,240 |
| Non-interest expenses | (39,528) | (9,000) | (17,483) | (66,011) |
| Income before income taxes | 117,474 | 28,911 | 12,233 | 158,618 |
| Provision for income taxes | 37,749 | 9,849 | 2,333 | 49,931 |
| Net income | \$ 79,725 | \$ 19,062 | \$ 9,900 | \$ 108,687 |
| Goodwill | \$ 2,324 | \$ 13,428 | \$ - | \$ 15,752 |
| Total assets | \$ 4,709,331 | \$ 392,458 | \$ 707,924 | \$ 5,809,713 |

| | 2007 | | | |
|---|-----------------------------|-----------------------------|-------------------|---------------------|
| (000s) | Mortgage Lending | Consumer Lending | Other | Total |
| Net interest income | \$ 93,466 | \$ 21,005 | \$ 31,787 | \$ 146,258 |
| Provision for credit losses | (4,491) | (1,551) | - | (6,042) |
| Fees and other income | 12,050 | 9,155 | 328 | 21,533 |
| Gain on securities and mortgage-backed securities | 28,148 | - | (1,614) | 26,534 |
| Non-interest expenses | (35,050) | (5,068) | (14,080) | (54,198) |
| Income before income taxes | 94,123 | 23,541 | 16,421 | 134,085 |
| Provision for income taxes | 32,093 | 8,451 | 3,300 | 43,844 |
| Net income | \$ 62,030 | \$ 15,090 | \$ 13,121 | \$ 90,241 |
| Goodwill | \$ 2,324 | \$ 12,704 | \$ - | \$ 15,028 |
| Total assets | \$ 3,867,949 | \$ 337,783 | \$ 769,361 | \$ 4,975,093 |

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NOTE 20 RISK MANAGEMENT

The Company is exposed to various types of risks owing to the nature of the business activities it carries on. Types of risk to which the Company is subject include credit, liquidity, interest rate and other price risks. The Company has adopted enterprise risk management (ERM) as a discipline for managing risk. The Company's ERM structure is supported by a comprehensive governance framework which includes policies, management standards, guidelines and procedures appropriate to each business activity. The policies are reviewed and approved annually by the Board of Directors.

A description of the Company's risk management policies and procedures is included in the shaded text on pages 28 to 35 of the Risk Management Section of the MD&A. Significant exposures to credit, liquidity, interest rate risks are described in Notes 4, 5, 16 and 17.

NOTE 21 COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current year's presentation.

NOTE 22 FUTURE ACCOUNTING CHANGES

International Financial Reporting Standards

The CICA will transition financial reporting for Canadian public entities to International Financial Reporting Standards (IFRS) effective for fiscal years beginning on or after January 1, 2011. The Company has initiated an IFRS transition project. At this time, it is too early to comment on the anticipated financial impact to the balance sheet and income statement. The Company will provide progress updates through its quarterly reports during 2009. For additional information about the project, refer to page 43 in the MD&A.