



**Interim Consolidated Financial Statements
July 31, 2020
(Unaudited)**

VERSABANK

Consolidated Balance Sheets (Unaudited)

(thousands of Canadian dollars)

As at	July 31 2020	October 31 2019	July 31 2019
Assets			
Cash	\$ 353,794	\$ 139,145	\$ 108,299
Securities	-	10,061	10,011
Loans, net of allowance for credit losses (note 4)	1,547,761	1,594,288	1,613,811
Other assets (note 5)	28,701	41,887	44,538
	<u>\$ 1,930,256</u>	<u>\$ 1,785,381</u>	<u>\$ 1,776,659</u>
Liabilities and Shareholders' Equity			
Deposits	\$ 1,565,334	\$ 1,399,889	\$ 1,398,286
Subordinated notes payable (note 6)	4,887	4,881	4,879
Securitization liabilities (note 7)	9,053	33,366	33,518
Other liabilities (note 8)	99,370	107,082	104,246
	<u>1,678,644</u>	<u>1,545,218</u>	<u>1,540,929</u>
Shareholders' equity:			
Share capital (note 9)	182,094	182,094	182,094
Retained earnings	69,518	58,069	53,636
	<u>251,612</u>	<u>240,163</u>	<u>235,730</u>
	<u>\$ 1,930,256</u>	<u>\$ 1,785,381</u>	<u>\$ 1,776,659</u>

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

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Consolidated Statements of Comprehensive Income (Unaudited)

(thousands of Canadian dollars, except per share amounts)

	for the three months ended		for the nine months ended	
	July 31	July 31	July 31	July 31
	2020	2019	2020	2019
Interest income:				
Loans	\$ 19,484	\$ 22,019	\$ 62,696	\$ 63,547
Cash and securities	688	939	2,330	2,495
	20,172	22,958	65,026	66,042
Interest expense:				
Deposits and other	7,661	8,771	24,228	25,172
Subordinated notes	127	128	381	628
	7,788	8,899	24,609	25,800
Net interest income	12,384	14,059	40,417	40,242
Non-interest income	8	19	42	42
Total revenue	12,392	14,078	40,459	40,284
Provision for (recovery of) credit losses (note 4)	(44)	381	238	(319)
	12,436	13,697	40,221	40,603
Non-interest expenses:				
Salaries and benefits	3,959	3,938	11,796	11,702
General and administrative	1,853	2,314	6,392	6,654
Premises and equipment	598	608	1,826	1,869
	6,410	6,860	20,014	20,225
Income before income taxes	6,026	6,837	20,207	20,378
Tax provision (note 10)	1,657	1,874	5,548	5,587
Net income and comprehensive income	\$ 4,369	\$ 4,963	\$ 14,659	\$ 14,791
Basic and diluted income per common share (note 11)	\$ 0.18	\$ 0.21	\$ 0.62	\$ 0.62
Weighted average number of common shares outstanding	21,123,559	21,123,559	21,123,559	21,123,559

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Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

(thousands of Canadian dollars)

	for the three months ended		for the nine months ended	
	July 31	July 31	July 31	July 31
	2020	2019	2020	2019
Common shares (note 9):				
Balance, beginning and end of the period	\$ 152,612	\$ 152,612	\$ 152,612	\$ 152,612
Preferred shares (note 9):				
<i>Series 1 preferred shares</i>				
Balance, beginning and end of the period	\$ 13,647	\$ 13,647	\$ 13,647	\$ 13,647
<i>Series 3 preferred shares</i>				
Balance, beginning and end of the period	\$ 15,690	\$ 15,690	\$ 15,690	\$ 15,690
Contributed surplus:				
Balance, beginning and end of the period	\$ 145	\$ 145	\$ 145	\$ 145
Total share capital	\$ 182,094	\$ 182,094	\$ 182,094	\$ 182,094
Retained earnings:				
Balance, beginning of the period	\$ 66,219	\$ 49,645	\$ 58,069	\$ 41,473
Impact of adopting IFRS 9	-	-	-	78
Net income	4,369	4,963	14,659	14,791
Dividends paid on common and preferred shares	(1,070)	(972)	(3,210)	(2,706)
Balance, end of the period	\$ 69,518	\$ 53,636	\$ 69,518	\$ 53,636
Total shareholders' equity	\$ 251,612	\$ 235,730	\$ 251,612	\$ 235,730

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

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Consolidated Statements of Cash Flows (Unaudited)

(thousands of Canadian dollars)

	for the nine months ended	
	July 31	July 31
	2020	2019
Cash provided by (used in):		
Operations:		
Net income	\$ 14,659	\$ 14,791
Adjustments to determine net cash flows:		
Items not involving cash:		
Provision for (recovery of) credit losses	238	(319)
Income tax provision	5,548	5,587
Interest income	(65,026)	(66,042)
Interest expense	24,609	25,800
Amortization	858	548
Interest received	63,964	62,884
Interest paid	(24,396)	(25,709)
Change in operating assets and liabilities:		
Loans	47,834	20,830
Deposits	165,456	(38,937)
Change in other assets and liabilities	469	(11,869)
	234,213	(12,436)
Investing:		
Proceeds from sale and maturity of securities	10,000	-
Purchase of property and equipment	(242)	(187)
	9,758	(187)
Financing:		
Repayment of subordinated notes	-	(10,000)
Issuance of subordinated notes	-	4,875
Redemption of securitization liability (note 7)	(24,531)	-
Dividends paid	(3,210)	(2,706)
Repayment of lease obligations	(270)	-
Income taxes paid	(1,311)	(1,028)
	(29,322)	(8,859)
Change in cash	214,649	(21,482)
Cash, beginning of the period	139,145	129,781
Cash, end of the period	\$ 353,794	\$ 108,299

The accompanying notes are an integral part of these interim Consolidated Financial Statements.

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Notes to Interim Consolidated Financial Statements (Unaudited)

Three month & nine month periods ended July 31, 2020 and 2019

1. Reporting entity:

VersaBank (the “Bank”) operates as a Schedule I bank under the *Bank Act (Canada)* and is regulated by the Office of the Superintendent of Financial Institutions (“OSFI”). The Bank, whose shares trade on the Toronto Stock Exchange, provides commercial lending services to select niche markets in Canada.

The Bank is incorporated and domiciled in Canada, and maintains its registered office at Suite 2002, 140 Fullarton Street, London, Ontario, Canada, N6A 5P2.

2. Basis of preparation:

a) Statement of compliance:

These interim Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and have been prepared in accordance with International Accounting Standard (“IAS”) 34 – *Interim Financial Reporting* and do not include all of the information required for full annual financial statements. These interim Consolidated Financial Statements should be read in conjunction with the Bank’s audited Consolidated Financial Statements for the year ended October 31, 2019.

The interim Consolidated Financial Statements for the three and nine months ended July 31, 2020 and 2019 were approved by the Audit Committee of the Board of Directors on August 24, 2020.

b) Basis of measurement:

These interim Consolidated Financial Statements have been prepared on the historical cost basis except for securities that are designated as fair value through other comprehensive income which are measured at fair value in the Consolidated Balance Sheets.

c) Functional and presentation currency:

These interim Consolidated Financial Statements are presented in Canadian dollars which is the Bank’s functional currency.

d) Use of estimates and judgments:

In preparing these interim Consolidated Financial Statements, management has exercised judgment and developed estimates in applying accounting policies and generating reported amounts of assets and liabilities at the date of the financial statements and income and expenses during the reporting periods. Areas where significant judgement was applied include the business model applied for the classification and measurement of financial instruments, assessing significant changes in credit risk on financial assets and in the selection of relevant forward looking information in assessing the Bank’s allowance for expected credit losses on its financial assets as described in note 4 - Loans. Estimates are applied in the determination of the allowance for expected credit losses on financial assets and the measurement of

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deferred income taxes. It is reasonably possible, on the basis of existing knowledge, that actual results may vary from that expected in the generation of these estimates. This could result in material adjustments to the carrying amounts of assets and/or liabilities affected in the future.

The impact of the COVID-19 pandemic has introduced measurable uncertainty and volatility into available forward looking information, including forecast macroeconomic and industry performance trend data, which in turn has introduced uncertainty into the assumptions and judgements made by management in the preparation of these interim Consolidated Financial Statements, including, but not limited to the impact of the pandemic on the Canadian economy, the effectiveness of the mitigating policy measures introduced by the Government and the Bank of Canada, and the impact that each of these may have on the Bank's business, operations and financial performance. As a result, the estimates developed by management, that are included in the Bank's interim Consolidated Financial Statements are subject to a higher level of uncertainty.

Estimates and their underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are applied prospectively once they are recognized.

3. Significant accounting policies and future accounting changes:

The accounting policies applied by the Bank in these interim Consolidated Financial Statements are the same as those applied by the Bank as at and for the year ended October 31, 2019 and are detailed in Note 3 of the Bank's 2019 audited Consolidated Financial Statements, except for changes to accounting policies resulting from the adoption of IFRS 16 (*Leases*) noted below.

There have been a number of standards and amendments that have been issued by the IASB that are not effective for the Bank's fiscal year end of October 31, 2020 and therefore have not been applied in preparing these interim consolidated financial statements.

Leases (IFRS 16)

Effective November 1, 2019, the Bank adopted IFRS 16 which sets out prescribed methodology related to the recognition, measurement, presentation and disclosure of operating leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all major leases. IFRS 16 supersedes previous accounting standards for leases, including IAS 17, *Leases* and IFRIC 4 – *Determining whether an arrangement contains a lease*. As a result of adopting IFRS 16, the Bank recognized an increase to both assets and liabilities on the Consolidated Balance Sheet, as well as a decrease in rent expense, with a corresponding increase in amortization expense (due to depreciation of the right-of-use assets) and an increase in finance costs (due to accretion of the lease obligation).

The Bank's accounting policy under IFRS 16 is set out below:

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease arrangement based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

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The Bank recognizes a right-of-use asset and a lease obligation at the lease commencement date. The right-of-use asset is initially measured based on the initial amount of the lease obligation adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset and/or the site on which it is located, less any lease incentives received. The assets are depreciated to the earlier of the end of useful life of the right-of-use asset or the lease term using the straight-line method as this methodology most closely reflects the expected pattern of consumption of the associated future economic benefits. The lease term includes periods covered by an option to extend if there is reasonable certainty that the Bank will exercise that option. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease obligation.

The lease obligation is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the incremental borrowing rate that is a function of the asset type or class and the credit quality of the borrower. Generally, the Bank will use its incremental borrowing rate as the discount rate. Variable lease payments that do not depend on an index or rate are not included in the measurement of the lease obligation.

The lease obligation is measured at amortized cost using the effective interest rate method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, or if the Bank changes its assessment of whether it will exercise a purchase, extension or termination option.

When the lease obligation is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or the remeasured amount is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

Impact of adoption of IFRS 16

Effective November 1, 2019, the Bank adopted IFRS 16 using the modified retrospective approach and accordingly the information presented for Fiscal 2019 has not been restated. It remains as previously reported under IAS 17 and related interpretations.

Prior to the adoption of IFRS 16 the Bank's total minimum operating lease commitments as at October 31, 2019 were \$6.8 million. On initial application, the Bank has elected to record right-of-use assets based on the corresponding lease obligations. Right-of-use assets and lease obligations of \$3.3 million were recorded as of November 1, 2019, with no net impact on retained earnings. When measuring its lease liabilities, the Bank discounted lease payments at its incremental borrowing rate, applicable to the asset class(es) at November 1, 2019. The weighted-average rate applied was 4.4%.

The Bank elected to apply the practical expedient to account for leases for which the lease term ends within 12 months of the date of initial application as short-term leases.

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The following table reconciles the Bank's operating lease commitments at October 31, 2019, as previously disclosed in the Bank's 2019 audited Consolidated Financial Statements, to the lease obligations recognized on initial application of IFRS 16 at November 1, 2019:

(thousands of Canadian dollars)

Operating lease commitments as at October 31, 2019	\$ 6,808
Discounted using the incremental borrowing rate as at November 1, 2019	5,557
Non-lease components included within operating lease commitments	(2,268)
Recognition exemption for short term leases	(35)
Lease obligations recognized as at November 1, 2019	\$ 3,254

4. Loans:

a) Summary of loans and allowance for credit losses:

(thousands of Canadian dollars)

	July 31 2020	October 31 2019	July 31 2019
Commercial real estate	\$ 563,032	\$ 509,564	\$ 554,956
Non-commercial real estate	36,913	44,608	43,789
Corporate and public sector	34,335	40,670	43,378
Structured finance	909,804	994,842	966,470
	1,544,084	1,589,684	1,608,593
Allowance for credit losses	(2,357)	(2,119)	(2,334)
Accrued interest	6,034	6,723	7,552
Total loans, net of allowance for credit losses	\$ 1,547,761	\$ 1,594,288	\$ 1,613,811

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The following table provides a summary of loan amounts, expected credit losses (“ECL”) allowance amounts, and expected loss (“EL”) rates by lending asset category:

(thousands of Canadian dollars)	As at July 31, 2020				As at October 31, 2019			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
Commercial real estate	\$ 473,638	\$ 82,878	\$ 6,516	\$ 563,032	\$ 448,322	\$ 54,989	\$ 6,253	\$ 509,564
ECL allowance	1,560	297	-	1,857	1,557	209	-	1,766
EL %	0.33%	0.36%	0.00%	0.33%	0.35%	0.38%	0.00%	0.35%
Non-commercial real estate	\$ 36,913	\$ -	\$ -	\$ 36,913	\$ 44,608	\$ -	\$ -	\$ 44,608
ECL allowance	227	-	-	227	86	-	-	86
EL %	0.61%	0.00%	0.00%	0.61%	0.19%	0.00%	0.00%	0.19%
Corporate and public sector	\$ 34,335	\$ -	\$ -	\$ 34,335	\$ 40,670	\$ -	\$ -	\$ 40,670
ECL allowance	52	-	-	52	38	-	-	38
EL %	0.15%	0.00%	0.00%	0.15%	0.09%	0.00%	0.00%	0.09%
Structured finance	\$ 907,025	\$ 2,616	\$ 163	\$ 909,804	\$ 991,735	\$ 3,092	\$ 15	\$ 994,842
ECL allowance	221	-	-	221	229	-	-	229
EL %	0.02%	0.00%	0.00%	0.02%	0.02%	0.00%	0.00%	0.02%
Loans	\$ 1,451,911	\$ 85,494	\$ 6,679	\$ 1,544,084	\$ 1,525,335	\$ 58,081	\$ 6,268	\$ 1,589,684
Total ECL allowance	2,060	297	-	2,357	1,910	209	-	2,119
Total EL %	0.14%	0.35%	0.00%	0.15%	0.13%	0.36%	0.00%	0.13%

The accounting policies applied by the Bank in these interim Consolidated Financial Statements related to Financial Instruments are the same as those applied by the Bank as at and for the year ended October 31, 2019 and are detailed in Note 3 of the Bank’s 2019 audited Consolidated Financial Statements. However, last quarter, and continuing this quarter the Bank expanded the depth and scope of its analysis supporting its assessment of impairment, or more specifically in the estimation of its allowance for expected credit losses as a result of the material deterioration in macroeconomic conditions precipitated by the COVID-19 epidemic.

Impairment – Allowance for Credit Losses

The Bank must maintain an allowance for expected credit losses that is adequate, in management’s opinion, to absorb all credit related losses in the Bank’s lending and treasury portfolios. Under IFRS 9 the Bank’s allowance for expected credit losses is estimated using the expected credit loss methodology and is comprised of expected credit losses recognized on both performing loans, and non-performing, or impaired loans even if no actual loss event has occurred.

For performing loans, the allowance for expected credit losses is an estimate of the expected cash shortfalls discounted at the effective interest rate, where a cash shortfall is the difference between the contractual cash flows that are due to the Bank and the cash flows that the Bank actually expects to receive. The ECL calculation is a function of the credit risk parameters; probability of default (“PD”), exposure at default (“EAD”), and loss given default (“LGD”) associated with each loan, sensitized to future market and macroeconomic conditions through the incorporation of forward-looking information derived from multiple economic forecast scenarios. (see Forward-Looking Information below).

Individual allowances are estimated for non-performing loans that are determined to be credit impaired. A loan or financial instrument is classified as credit impaired when the Bank becomes aware that all, or a portion of the contractual cashflows associated with the loan may be in jeopardy and as a result may not

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be realized by the Bank under the repayment schedule set out in the contractual terms associated with the loan.

Assessment of significant increase in credit risk ("SICR")

At each reporting date, the Bank assesses whether or not there has been a SICR for loans since initial recognition by comparing, at the reporting date, the risk of default occurring over the remaining expected life against the risk of default at initial recognition.

Again this quarter management considered the Bank's SICR methodology in the context of the material deterioration in macroeconomic conditions precipitated by COVID-19 with specific focus on the potential impact of deferrals, concessions or restructuring of principal and interest payments and has determined that such arrangements on their own do not qualify as a SICR. Further, management concluded that the determination of a SICR remains a function of the loan's internal risk rating assignment, internal watchlist status, and delinquency status which are updated as necessary in response to changes including, but not limited to changes in macroeconomic and/or market conditions, changes in a borrower's credit risk profile, and changes in the strength of the underlying security, including guarantor status, if a guarantor exists.

Quantitative models may not always be able to capture all reasonable and supportable information that may indicate a SICR. As a result, qualitative factors may be considered to supplement such a gap. Examples include changes in adjudication criteria for a particular group of borrowers or asset categories or changes in portfolio composition, and more specifically for the current quarter, changes attributable to the continued impact of COVID-19 on the Canadian economy.

Expected credit loss model - Estimation of expected credit losses

Expected credit losses are an estimate of a loan's expected cash shortfalls discounted at the effective interest rate, where a cash shortfall is the difference between the contractual cash flows that are due to the Bank and the cash flows that the Bank actually expects to receive. The ECL calculation is a function of the credit risk parameters: PD, LGD, and EAD associated with each loan, sensitized to future market and macroeconomic conditions through the incorporation of forward looking information ("FLI") derived from multiple economic forecast scenarios, typically including baseline, upside, and downside scenarios. Management reviewed its ECL model in the context of the material deterioration in macroeconomic conditions precipitated by the COVID-19 pandemic and the impact of same on the FLI applied to the model, and concluded that both the model, and the associated methodology were generally capable of effectively interpreting and incorporating an economic shock of this nature, as well as the residual effects of same into the estimation of expected credit losses on the Bank's lending portfolio.

Forward-Looking Information

The IFRS 9 standard requires consideration of past events, current market conditions and reasonable, supportable information about future economic conditions that is available without undue cost and effort in the estimation of expected credit losses for loans. More specifically, under IFRS 9 expected credit losses represents an unbiased, probability-weighted estimate of the present value of cash shortfalls (i.e., the

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weighted average of credit losses, with the respective risks of a default occurring in a given time period used as the weights). Additionally, IFRS 9 stipulates that future economic conditions are to be based on an unbiased, probability-weighted assessment of possible future outcomes. The estimation and application of forward-looking information, in an attempt to capture the impact of future economic conditions, requires significant judgement.

The Bank incorporates the impact of future economic conditions, or more specifically forward-looking information into the estimation of expected credit losses at the credit risk parameter level. This is accomplished via the credit risk parameter models and proxy datasets that the Bank utilizes to develop PD and LGD term structure forecasts for its loans. The Bank has sourced credit risk modeling systems and forecast macroeconomic scenario data from Moody's Analytics for the purpose of computing forward-looking credit risk parameters under multiple macroeconomic scenarios that consider both market-wide and idiosyncratic factors and influences. These systems are integrated with the Bank's internally developed ECL models. Given that the Bank has experienced very limited historical losses and, therefore, does not have available statistically significant loss data inventory for use in developing forward looking expected credit loss trends, the integration of unbiased, third party forward-looking risk parameter modeling systems is particularly important for the Bank in the context of the estimation of expected credit losses.

The Bank typically utilizes macroeconomic indicator data derived from multiple macroeconomic scenarios, those typically being baseline, upside, and downside scenarios in order to mitigate volatility in the estimation of expected credit losses as well as to satisfy the IFRS 9 requirement that future economic conditions are to be based on an unbiased, probability-weighted assessment of possible future outcomes. More specifically, the macroeconomic indicators set out in the three scenarios are used as inputs for the credit risk parameter models utilized by the Bank to sensitize the individual, PD and LGD term structure forecasts to the respective macroeconomic trajectory set out in each of the scenarios. As a result of the onset of the COVID-19 pandemic and the ensuing economic shock to the Canadian economy management continues to consider a broader range of alternative macroeconomic scenarios in addition to the baseline, upside and downside scenarios referenced previously in the development of individual loan PD and LGD term structure forecasts for use in estimating the Bank's expected credit losses, and further, in its assessment of the adequacy of same.

The macroeconomic indicator data utilized by the Bank for the purpose of sensitizing PD and LGD term structure data to forward economic conditions include, but are not limited to: real GDP, the national unemployment rate, long term interest rates, the consumer price index, and the price of oil. These specific macroeconomic indicators were selected in an attempt to ensure that the spectrum of fundamental macroeconomic influences on the key drivers of the credit risk profile of the Bank's balance sheet, including: corporate, consumer and real estate market dynamics; corporate, consumer and small and medium-sized enterprises ("SME") borrower performance; geography; as well as collateral value trajectories, are appropriately captured and incorporated into the Bank's forward macroeconomic sensitivity analysis.

The forecast macroeconomic scenarios utilized by the Bank in the current quarter benefit from updated data which provide additional insight into the magnitude of the initial impact of COVID-19 on Canada's economy, and as a result this quarter's forecast scenarios consistently present a level of deterioration that is measurably sharper and deeper than was anticipated by the previous quarter's forecast scenarios. At the

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same time, the duration of the recession is notably short as each of the forecast scenarios present a steep recovery over the course of the summer and into the late fall, with the magnitude of the recovery varying across each scenario. The baseline forecast scenario contemplates the Canadian economy recovering reasonably quickly and peaking late in the third quarter (calendar), at which point the recovery moderates, and eventually modestly contracts over the course of the fourth quarter (calendar) and into the first half of 2021 before returning to more sustained, normalized levels over the course of the latter half of calendar 2021. While the upside and downside scenarios present somewhat similar economic profiles to that of the baseline scenario set out above, the downside scenario presents measurably lower, initial recovery levels and more pronounced and prolonged economic contraction over the course of the fourth quarter (calendar) and into and through 2021, while the upside scenario anticipates a more robust, initial recovery with a much more modest contraction over the second half of calendar 2020 and into calendar 2021, with the economy achieving more normalized levels over the course of the third quarter (calendar) 2021.

Key assumptions driving each of the macroeconomic scenarios utilized by the Bank include, but are not limited to; the number of businesses that are able to reopen and operate as the provinces continue to advance their re-opening plans, anticipated consumer spending levels, expectations for the realization, (or not) of a second wave of COVID-19, the volume of confirmed COVID-19 cases and the rate of new infections, the impact of elevated unemployment levels on loan defaults, the expiry or potential extension of federal government stimulus programs, and the Bank of Canada's position on monetary policy, specifically related to the commitment to keep the overnight rate fixed at 0.25% into 2023.

Management remains of the view that forward looking macroeconomic and industry data will continue to change as the provinces continue to re-open their economies, as more information becomes available related to understanding the correlation, if any, between loan deferrals granted by banks and future loan defaults, as the potential duration and scope of federal government and Bank of Canada stimulus programs are clarified, and a better understanding of the epidemiological trajectory of COVID-19 is accomplished. As a result, the Bank expects that its estimated ECL amounts may continue to exhibit some volatility in the coming quarters.

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The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the three months ended July 31, 2020:

(thousands of Canadian dollars)	Stage 1	Stage 2	Stage 3	Total
Commercial real estate				
Balance at beginning of period	\$ 1,580	\$ 286	\$ -	\$ 1,866
Transfer in (out) to Stage 1	5	(5)	-	-
Transfer in (out) to Stage 2	(68)	68	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(72)	(52)	-	(124)
Loan originations	118	-	-	118
Derecognitions and maturities	(3)	-	-	(3)
Provision for (recovery of) credit losses	(20)	11	-	(9)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 1,560	\$ 297	\$ -	\$ 1,857
Non-commercial real estate				
Balance at beginning of period	\$ 179	\$ -	\$ -	\$ 179
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	48	-	-	48
Loan originations	-	-	-	-
Derecognitions and maturities	-	-	-	-
Provision for (recovery of) credit losses	48	-	-	48
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 227	\$ -	\$ -	\$ 227
Corporate and public sector				
Balance at beginning of period	\$ 59	\$ 1	\$ -	\$ 60
Transfer in (out) to Stage 1	1	(1)	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(3)	-	-	(3)
Loan originations	-	-	-	-
Derecognitions and maturities	(5)	-	-	(5)
Provision for (recovery of) credit losses	(7)	(1)	-	(8)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 52	\$ -	\$ -	\$ 52
Structured finance				
Balance at beginning of period	\$ 296	\$ -	\$ -	\$ 296
Transfer in (out) to Stage 1	45	(45)	-	-
Transfer in (out) to Stage 2	(60)	60	-	-
Transfer in (out) to Stage 3	(5)	-	5	-
Net remeasurement of loss allowance	(719)	6	(5)	(718)
Loan originations	1,220	-	-	1,220
Derecognitions and maturities	(556)	(21)	-	(577)
Provision for (recovery of) credit losses	(75)	-	-	(75)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 221	\$ -	\$ -	\$ 221
Total balance at end of period	\$ 2,060	\$ 297	\$ -	\$ 2,357

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Notes to Interim Consolidated Financial Statements (Unaudited)

Three month & nine month periods ended July 31, 2020 and 2019

The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the nine months ended July 31, 2020:

(thousands of Canadian dollars)	Stage 1	Stage 2	Stage 3	Total
Commercial real estate				
Balance at beginning of period	\$ 1,557	\$ 209	\$ -	\$ 1,766
Transfer in (out) to Stage 1	10	(10)	-	-
Transfer in (out) to Stage 2	(87)	87	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(140)	11	-	(129)
Loan originations	240	-	-	240
Derecognitions and maturities	(20)	-	-	(20)
Provision for (recovery of) credit losses	3	88	-	91
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 1,560	\$ 297	\$ -	\$ 1,857
Non-commercial real estate				
Balance at beginning of period	\$ 86	\$ -	\$ -	\$ 86
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	98	-	-	98
Loan originations	45	-	-	45
Derecognitions and maturities	(2)	-	-	(2)
Provision for (recovery of) credit losses	141	-	-	141
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 227	\$ -	\$ -	\$ 227
Corporate and public sector				
Balance at beginning of period	\$ 38	\$ -	\$ -	\$ 38
Transfer in (out) to Stage 1	1	(1)	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	18	1	-	19
Loan originations	-	-	-	-
Derecognitions and maturities	(5)	-	-	(5)
Provision for (recovery of) credit losses	14	-	-	14
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 52	\$ -	\$ -	\$ 52
Structured finance				
Balance at beginning of period	\$ 229	\$ -	\$ -	\$ 229
Transfer in (out) to Stage 1	87	(87)	-	-
Transfer in (out) to Stage 2	(164)	164	-	-
Transfer in (out) to Stage 3	(5)	-	5	-
Net remeasurement of loss allowance	(4,666)	(37)	(5)	(4,708)
Loan originations	6,228	-	-	6,228
Derecognitions and maturities	(1,488)	(40)	-	(1,528)
Provision for (recovery of) credit losses	(8)	-	-	(8)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 221	\$ -	\$ -	\$ 221
Total balance at end of period	\$ 2,060	\$ 297	\$ -	\$ 2,357

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Three month & nine month periods ended July 31, 2020 and 2019

The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the three months ended July 31, 2019:

(thousands of Canadian dollars)	Stage 1		Stage 2		Stage 3		Total
Commercial real estate							
Balance at beginning of period	\$	1,047	\$	202	\$	-	\$ 1,249
Transfer in (out) to Stage 1		15		(15)		-	-
Transfer in (out) to Stage 2		(43)		43		-	-
Transfer in (out) to Stage 3		-		-		-	-
Net remeasurement of loss allowance		127		(13)		-	114
Loan originations		116		-		-	116
Derecognitions and maturities		(65)		-		-	(65)
Provision for (recovery of) credit losses		150		15		-	165
Write-offs		-		-		-	-
Recoveries		-		-		-	-
Balance at end of period	\$	1,197	\$	217	\$	-	\$ 1,414
Non-commercial real estate							
Balance at beginning of period	\$	84	\$	-	\$	-	\$ 84
Transfer in (out) to Stage 1		-		-		-	-
Transfer in (out) to Stage 2		-		-		-	-
Transfer in (out) to Stage 3		-		-		-	-
Net remeasurement of loss allowance		(10)		-		-	(10)
Loan originations		-		-		-	-
Derecognitions and maturities		(1)		-		-	(1)
Provision for (recovery of) credit losses		(11)		-		-	(11)
Write-offs		-		-		-	-
Recoveries		-		-		-	-
Balance at end of period	\$	73	\$	-	\$	-	\$ 73
Corporate and public sector							
Balance at beginning of period	\$	58	\$	-	\$	400	\$ 458
Transfer in (out) to Stage 1		-		-		-	-
Transfer in (out) to Stage 2		(1)		1		-	-
Transfer in (out) to Stage 3		-		-		-	-
Net remeasurement of loss allowance		(14)		1		227	214
Loan originations		-		-		-	-
Derecognitions and maturities		-		-		-	-
Provision for (recovery of) credit losses		(15)		2		227	214
Write-offs		-		-		-	-
Recoveries		-		-		-	-
Balance at end of period	\$	43	\$	2	\$	627	\$ 672
Structured finance							
Balance at beginning of period	\$	161	\$	1	\$	-	\$ 162
Transfer in (out) to Stage 1		26		(26)		-	-
Transfer in (out) to Stage 2		(27)		27		-	-
Transfer in (out) to Stage 3		-		-		-	-
Net remeasurement of loss allowance		(1,126)		14		-	(1,112)
Loan originations		1,481		-		-	1,481
Derecognitions and maturities		(340)		(16)		-	(356)
Provision for (recovery of) credit losses		14		(1)		-	13
Write-offs		-		-		-	-
Recoveries		-		-		-	-
Balance at end of period	\$	175	\$	-	\$	-	\$ 175
Total balance at end of period	\$	1,488	\$	219	\$	627	\$ 2,334

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Notes to Interim Consolidated Financial Statements (Unaudited)

Three month & nine month periods ended July 31, 2020 and 2019

The following table provides a reconciliation of the Bank's ECL allowance by lending asset category for the nine months ended July 31, 2019:

(thousands of Canadian dollars)	Stage 1	Stage 2	Stage 3	Total
Commercial real estate				
Balance at beginning of period	\$ 1,257	\$ 348	\$ -	\$ 1,605
Transfer in (out) to Stage 1	37	(37)	-	-
Transfer in (out) to Stage 2	(52)	52	-	-
Transfer in (out) to Stage 3	-	(177)	177	-
Net remeasurement of loss allowance	(178)	32	(177)	(323)
Loan originations	273	-	-	273
Derecognitions and maturities	(140)	(1)	-	(141)
Provision for (recovery of) credit losses	(60)	(131)	-	(191)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 1,197	\$ 217	\$ -	\$ 1,414
Non-commercial real estate				
Balance at beginning of period	\$ 151	\$ -	\$ -	\$ 151
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	-	-	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(77)	-	-	(77)
Loan originations	-	-	-	-
Derecognitions and maturities	(1)	-	-	(1)
Provision for (recovery of) credit losses	(78)	-	-	(78)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 73	\$ -	\$ -	\$ 73
Corporate and public sector				
Balance at beginning of period	\$ 81	\$ -	\$ 400	\$ 481
Transfer in (out) to Stage 1	-	-	-	-
Transfer in (out) to Stage 2	(1)	1	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(39)	1	227	189
Loan originations	2	-	-	2
Derecognitions and maturities	-	-	-	-
Provision for (recovery of) credit losses	(38)	2	227	191
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 43	\$ 2	\$ 627	\$ 672
Structured finance				
Balance at beginning of period	\$ 415	\$ 1	\$ -	\$ 416
Transfer in (out) to Stage 1	61	(61)	-	-
Transfer in (out) to Stage 2	(119)	119	-	-
Transfer in (out) to Stage 3	-	-	-	-
Net remeasurement of loss allowance	(3,250)	(21)	-	(3,271)
Loan originations	4,077	-	-	4,077
Derecognitions and maturities	(1,009)	(38)	-	(1,047)
Provision for (recovery of) credit losses	(240)	(1)	-	(241)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Balance at end of period	\$ 175	\$ -	\$ -	\$ 175
Total balance at end of period	\$ 1,488	\$ 219	\$ 627	\$ 2,334

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Three month & nine month periods ended July 31, 2020 and 2019

The Bank holds security against the majority of its loans in the form of either mortgage interests over property, other registered securities over assets, guarantees and holdbacks on loan and lease receivables (see note 8).

b) Impaired loans:

At July 31, 2020, impaired loans were \$6.7 million (October 31, 2019 - \$6.3 million).

5. Other assets:

(thousands of Canadian dollars)

	July 31 2020	October 31 2019	July 31 2019
Accounts receivable	\$ 504	\$ 437	\$ 533
Funds held for securitization liabilities	3,295	17,073	16,928
Prepaid expenses and other	7,626	4,840	5,604
Property and equipment	7,608	7,911	8,029
Right-of-use assets	2,941	-	-
Deferred income tax asset	6,727	11,626	13,444
	<u>\$ 28,701</u>	<u>\$ 41,887</u>	<u>\$ 44,538</u>

6. Subordinated notes payable:

(thousands of Canadian dollars)

	July 31 2020	October 31 2019	July 31 2019
Ten year term, unsecured, non-viability contingent capital compliant, subordinated notes payable, principal amount of \$5.0 million, effective interest rate of 10.41%, maturing March 2029.	\$ 4,887	\$ 4,881	\$ 4,879
	<u>\$ 4,887</u>	<u>\$ 4,881</u>	<u>\$ 4,879</u>

7. Securitization liabilities:

Securitization liabilities include amounts payable to counterparties for cash received upon initiation of securitization transactions, accrued interest on amounts payable to counterparties, and the unamortized balance of deferred costs and discounts which arose upon initiation of the securitization transactions. During the quarter ended April 30, 2020, the Bank redeemed \$24.5 million (October 31, 2019 – nil) of maturing securitization liabilities.

The amounts payable to counterparties bear interest at 3.55% and mature in December 2020. Securitized residential insured mortgages and other assets are pledged as collateral for these liabilities.

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Three month & nine month periods ended July 31, 2020 and 2019

8. Other liabilities:

(thousands of Canadian dollars)

	July 31 2020	October 31 2019	July 31 2019
Accounts payable and other	\$ 2,640	\$ 3,983	\$ 3,565
Lease obligations	2,980	-	-
Cash collateral and amounts held in escrow	4,207	6,098	6,156
Holdbacks payable on loan and lease receivables	89,543	97,001	94,525
	<u>\$ 99,370</u>	<u>\$ 107,082</u>	<u>\$ 104,246</u>

9. Share capital:

a) Common shares:

At July 31, 2020, there were 21,123,559 (October 31, 2019 – 21,123,559) common shares outstanding.

b) Preferred shares:

At July 31, 2020, there were 1,461,460 (October 31, 2019 – 1,461,460) Series 1 preferred shares and 1,681,320 (October 31, 2019 – 1,681,320) Series 3 preferred shares outstanding. These shares are Basel III compliant, non-cumulative rate reset preferred shares which include NVCC provisions. As a result, these shares qualify as Additional Tier 1 Capital (see note 15).

c) Stock options:

At July 31, 2020, there were 42,017 common share stock options outstanding (October 31, 2019 – 42,934).

10. Tax provision:

Tax provision for the three months and nine months ended July 31, 2020 was \$1.7 million (July 31, 2019 - \$1.9 million) and \$5.5 million (July 31, 2019 - \$5.6 million) respectively. The Bank's statutory federal and provincial income tax rate is approximately 27% (2019 – 27%). The effective rate is affected by certain items not being taxable or deductible for income tax purposes.

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Three month & nine month periods ended July 31, 2020 and 2019

11. Income per common share:

(thousands of Canadian dollars)

	for the three months ended		for the nine months ended	
	July 31 2020	July 31 2019	July 31 2020	July 31 2019
Net income	\$ 4,369	\$ 4,963	\$ 14,659	\$ 14,791
Less: dividends on preferred shares	(542)	(550)	(1,626)	(1,650)
	3,827	4,413	13,033	13,141
Weighted average number of common shares outstanding	21,123,559	21,123,559	21,123,559	21,123,559
Income per common share:	\$ 0.18	\$ 0.21	\$ 0.62	\$ 0.62

The Series 1 and Series 3 NVCC preferred shares are contingently issuable shares and do not have a dilutive impact.

12. Commitments and contingencies:

The amount of credit related commitments represents the maximum amount of additional credit that the Bank could be obligated to extend.

(thousands of Canadian dollars)

	July 31 2020	October 31 2019	July 31 2019
Loan commitments	\$ 259,418	\$ 261,366	\$ 219,227
Letters of credit	48,643	48,074	35,484
	\$ 308,061	\$ 309,440	\$ 254,711

13. Related party transactions:

The Bank's Board of Directors and Senior Executive Officers represent key management personnel and are related parties. At July 31, 2020, amounts due from these related parties totalled \$3.8 million (October 31, 2019 - \$1.4 million). The interest rates charged on loans and advances to related parties are typically similar to those charged in an arms-length transaction. Interest income earned on the above loans for the three months and nine months ended July 31, 2020 was \$17,000 (July 31, 2019 - \$13,000) and \$45,000 (July 31, 2019 - \$34,000) respectively. All loans issued to key management personnel were current as at July 31, 2020 and 2019.

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Notes to Interim Consolidated Financial Statements (Unaudited)

Three month & nine month periods ended July 31, 2020 and 2019

14. Nature and extent of risks arising from financial instruments:

Risk management involves the identification, ongoing assessment, managing and monitoring of material risks that could adversely affect the Bank. The Bank is exposed to credit risk, liquidity risk, and market risks. Expanded disclosure related to how the Bank manages these risks are provided in the Bank's 2019 Annual Financial Statements.

Credit Risk

Credit risk is the risk of loss associated with a borrower, guarantor, or counterparty's inability or unwillingness to fulfill its contractual obligations. The Bank is exposed to credit risk primarily as a result of its lending activities but also as a result of investing in securities. As a result of the material deterioration in the Canadian economy, precipitated by the COVID-19 pandemic, the Bank's credit risk department has taken a number of steps to increase the frequency and comprehensiveness of its review and assessment of the credit risk profile of the Bank's lending portfolio as well as in its monitoring of the general activity within each of the Bank's lending portfolios, including annual and interim reviews, risk rating adjustments, new credit volumes, funding requirements, requests for deferrals, concessions or restructurings and any risk rating adjustments precipitating from same, and further, has tightened its oversight of general adherence to the Bank's credit adjudication policies. In the current quarter, management continued to consider available information related to the number of active COVID-19 cases in Canada as well as the associated infection rate of the virus, the expected duration, scope and impact of active monetary and fiscal policy stimulus programs, and available market data in its interpretation of current and expected macroeconomic conditions and, ultimately, in its assessment of the credit risk profile of its lending portfolio.

The Bank manages its lending activity credit risk using policies that have been recommended by the Chief Credit Officer and the Chief Risk Officer to the Risk Oversight Committee, which then recommends the policies to the Board of Directors for approval. These policies consist of approval procedures and limits on loan amounts, portfolio concentration, geographic concentration, industry concentration, asset category, loans to any one entity and associated groups, a risk rating policy that assigns a risk rating to each asset in its lending portfolio, and early recognition of problem accounts with an action plan for each account. The Risk Oversight Committee reviews these policies on an ongoing basis.

The Bank manages credit risk associated with securities included in its Treasury portfolio by applying policies that have been recommended by the Chief Credit Officer and the Chief Risk Officer to the Risk Oversight Committee, which then recommends the policies to the Board of Directors for approval. These policies consist of approval procedures and restrictions in the selection of security dealers, restrictions in the nature of securities selected, and in setting securities portfolio concentration limits. The Risk Oversight Committee reviews these policies on an ongoing basis.

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Notes to Interim Consolidated Financial Statements (Unaudited)

Three month & nine month periods ended July 31, 2020 and 2019

The Risk Oversight Committee, comprised entirely of independent directors, performs the following functions related to credit risk:

- Recommends policies governing management of credit risks to the Board of Directors for approval and reviews credit risk policies on an ongoing basis to ensure that they are prudent and appropriate given possible changes in market conditions and corporate strategy;
- Concurs with credits exceeding the levels delegated to management, prior to commitment;
- Reviews, on a regular basis, watchlist accounts, impaired loans and accounts that have gone into arrears and expected credit loss analysis on a quarterly basis.

Liquidity Risk

Liquidity risk is the risk that the Bank is unable to meet the demand for cash to fund obligations as they come due. The Bank is exposed to liquidity risk as a result of timing differences in the cash flows of its lending activities, security investment activities and deposit taking activities. The Bank has established policies to ensure that its cash outflows and inflows are closely matched and that its sources of deposits are diversified between funding sources and over a wide geographic area. In the current quarter management considered the general activity and trends in its key deposit markets, the expected duration, scope and impact of active monetary and fiscal policy stimulus programs and the anticipated impact of same on its future cashflow requirements in its assessment of its liquidity risk profile. In the current quarter the Bank continued to maintain elevated liquidity levels as a prudent liquidity practice in response to the persisting economic uncertainty resulting from the impact of COVID-19.

The Risk Oversight Committee recommends policies governing management of liquidity risk to the Board for approval and reviews liquidity policies on an ongoing basis. It receives and reviews quarterly securities portfolio reports and liquidity risk reports from management relating to its liquidity position. Additionally, an Asset Liability Committee, consisting of members of senior management, monitors liquidity risk, reviews compliance with policies and discusses strategies in this area.

Market Risk

Market risk is the risk of a negative impact on the balance sheet and/or income statement resulting from changes or volatility in market factors such as interest rates or market prices. The Bank's principal market risk arises from interest rate risk as the Bank does not undertake any material foreign exchange or trading activities. The Risk Oversight Committee is charged with recommending policies that govern market risk to its Board of Directors for approval and with reviewing the policies on an ongoing basis.

Interest rate risk is the risk that a movement in interest rates could negatively impact spread, net interest income and the economic value of assets, liabilities and shareholders' equity. The Bank manages interest rate risk by employing a number of methods including income simulation analysis and interest rate sensitivity gap and duration analysis.

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Management prepares regular reports to the Board to allow for ongoing monitoring of the Bank's interest rate risk position. The Asset Liability Committee reviews the results of these analyses on a monthly basis and monitors compliance with limits set by corporate policy.

The management of interest rate risk also includes stress testing the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios.

15. Capital management:

a) Overview:

The Bank's policy is to maintain a strong capital base so as to retain investor, creditor and market confidence as well as to support future development of the business. The impact of the level of capital on shareholders' return is an important consideration and the Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater leverage and the advantages and security afforded by a more robust capital position.

OSFI sets and monitors capital requirements for the Bank. Capital is managed in accordance with policies and plans that are regularly reviewed and approved by the Board of Directors and take into account forecasted capital requirements and financial market conditions.

The goal is to maintain adequate regulatory capital for the Bank to be considered well capitalized, protect consumer deposits and provide capacity to support organic growth as well as to capitalize on strategic opportunities that do not otherwise require accessing the public capital markets, all the while providing a satisfactory return to shareholders. The Bank's regulatory capital is comprised of share capital, retained earnings and unrealized gains and losses on fair value through other comprehensive income securities (Common Equity Tier 1 capital), preferred shares (Additional Tier 1 capital) and the qualifying amount of subordinated notes (Tier 2 capital).

The Bank monitors its capital adequacy and related capital ratios on a daily basis and has policies setting internal maximum and minimum amounts for its capital ratios. These capital ratios consist of the leverage ratio and the risk-based capital ratios.

The Bank makes use of the Standardized Approach for credit risk as prescribed by OSFI and, therefore, may include eligible ECL allowance amounts in its Tier 2 capital, up to a maximum of 1.25% of its credit risk-weighted assets calculated under the Standardized Approach. Further to this, and as a result of the onset of the COVID-19 pandemic and the economic uncertainty associated with same, OSFI introduced guidance over the course of the previous quarter, that set out transitional arrangements pertaining to the capital treatment of expected loss provisioning which allows for a portion of eligible ECL allowances to be included in CET1 capital, on a transitional basis over the course of the period ranging between 2020 and 2022 inclusive. The portion of ECL allowances that is eligible for inclusion in CET1 capital is calculated as the increase in the sum of Stage 1 and Stage 2 ECL allowances estimated in the current quarter relative to the sum of Stage 1 and Stage 2 ECL allowances estimated for the baseline period, which has been designated by OSFI to be the three months ended January 31st, 2020, adjusted for tax effects and

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multiplied by a scaling factor. The scaling factor has been set by OSFI at 70% for fiscal 2020, 50% for fiscal 2021 and 25% for fiscal 2022. The impact of the capital treatment of expected loss provisioning on the Bank's capital levels and associated capital ratios is presented in the table below.

b) Risk-Based Capital Ratios:

The Basel Committee on Banking Supervision has published the Basel III rules on capital adequacy and liquidity ("Basel III").

OSFI requires that all Canadian banks must comply with the Basel III standards on an "all-in" basis for the purpose of determining their risk-based capital ratios. Required minimum regulatory capital ratios are a 7.0% Common Equity Tier 1 capital ratio ("CET1"), an 8.5% Tier 1 capital ratio and a 10.5% total capital ratio, all of which include a 2.50% capital conservation buffer.

OSFI also requires banks to measure capital adequacy in accordance with guidelines for determining risk adjusted capital and risk-weighted assets including off-balance sheet credit instruments as specified in the Basel III regulations. Based on the deemed credit risk for each type of asset, assets held by the Bank are assigned a weighting ranging between 0% to 150% to determine the Bank's risk weighted equivalent assets and its risk-based capital ratios.

The Bank's risk-based capital ratios are calculated as follows:

(thousands of Canadian dollars)

	July 31 2020 "Transitional"	July 31 2020 "All in"	October 31 2019 "All in"
Common Equity Tier 1 (CET1) capital			
Directly issued qualifying common share capital	\$ 152,757	\$ 152,757	\$ 152,757
Retained earnings	69,518	69,518	58,069
CET1 before regulatory adjustments	222,275	222,275	210,826
Regulatory adjustments applied to CET1	(8,003)	(8,230)	(13,281)
Common Equity Tier 1 capital	\$ 214,272	\$ 214,045	\$ 197,545
Additional Tier 1 capital			
Directly issued qualifying Additional Tier 1 instruments	\$ 29,337	\$ 29,337	\$ 29,337
Total Tier 1 capital	\$ 243,609	\$ 243,382	\$ 226,882
Tier 2 capital			
Directly issued capital instruments	\$ 5,000	\$ 5,000	\$ 5,000
Tier 2 capital before regulatory adjustments	5,000	5,000	5,000
Eligible stage 1 and stage 2 allowance	2,130	2,357	-
Total Tier 2 capital	\$ 7,130	\$ 7,357	\$ 5,000
Total regulatory capital	\$ 250,739	\$ 250,739	\$ 231,882
Total risk-weighted assets	\$ 1,518,918	\$ 1,518,918	\$ 1,501,435
Capital ratios			
CET1 ratio	14.11%	14.09%	13.16%
Tier 1 capital ratio	16.04%	16.02%	15.11%
Total capital ratio	16.51%	16.51%	15.44%

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c) Leverage Ratio:

The leverage ratio, which is prescribed under the Basel III Accord, is a supplementary measure to the risk-based capital requirements and is defined as the ratio of Tier 1 capital to the Bank's total exposures. The Basel III minimum leverage ratio is 3.0%. The Bank's leverage ratio is calculated as follows:

(thousands of Canadian dollars)

	July 31 2020 "Transitional"	July 31 2020 "All-in"	October 31 2019
On-balance sheet assets	\$ 1,930,256	\$ 1,930,256	\$ 1,785,381
Assets amounts adjusted in determining the Basel III Tier 1 capital	(8,003)	(8,230)	(13,281)
Total on-balance sheet exposures	1,922,253	1,922,026	1,772,100
Off-balance sheet exposure at gross notional amount	\$ 308,061	\$ 308,061	\$ 309,440
Adjustments for conversion to credit equivalent amount	(197,874)	(197,874)	(190,023)
Off-balance sheet exposures	110,187	110,187	119,417
Tier 1 capital	243,609	243,382	226,882
Total exposures	2,032,440	2,032,213	1,891,517
Leverage ratio	11.99%	11.98%	11.99%

The Bank was in compliance with the leverage ratio prescribed by OSFI throughout the periods presented.

16. Interest rate position:

The Bank is subject to interest rate risk which is the risk that a movement in interest rates could negatively impact net interest margin, net interest income and the economic value of assets, liabilities and shareholders' equity. The following table provides the duration difference between the Bank's assets and liabilities and the potential after-tax impact of a 100 basis point shift in interest rates on the Bank's earnings during a 12 month period as well as the potential after-tax impact of a 100 basis point shift in interest rates on the Bank's shareholders' equity over a 60 month period if no remedial actions are taken.

	July 31, 2020		October 31, 2019	
	Increase 100 bps	Decrease 100 bps	Increase 100 bps	Decrease 100 bps
Increase (decrease):				
Impact on projected net interest income during a 12 month period	\$ 3,178	\$ (1,851)	\$ 1,621	\$ (1,613)
Impact on reported equity during a 60 month period	\$ (1,764)	\$ 1,253	\$ (3,669)	\$ 3,780
Duration difference between assets and liabilities (months)	0.4		1.3	

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17. Fair Value of Financial Instruments:

Fair values are based on management's best estimates of market conditions and valuation policies at a certain point in time. The estimates are subjective and involve particular assumptions and matters of judgment and as such, may not be reflective of future fair values. The Bank's loans and deposits lack an available market as they are not typically exchanged and, therefore, they are not necessarily representative of amounts realizable upon immediate settlement. See Note 21 to the October 31, 2019 audited Consolidated Financial Statements for more information on fair values.

(thousands of Canadian dollars)	July 31, 2020		October 31, 2019	
	Book Value	Fair Value	Book Value	Fair Value
Assets				
Cash and cash equivalents	\$ 353,794	\$ 353,794	\$ 139,145	\$ 139,145
Securities	-	-	10,061	10,061
Loans	1,547,761	1,548,260	1,594,288	1,593,277
Other financial assets	3,799	3,799	17,510	17,510
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Liabilities				
Deposits	\$ 1,565,334	\$ 1,605,552	\$ 1,399,889	\$ 1,403,816
Subordinated notes payable	4,887	5,000	4,881	5,000
Securitization liabilities	9,053	9,151	33,366	33,469
Other financial liabilities	99,370	99,370	107,082	107,082

CORPORATE INFORMATION

DIRECTORS

The Honourable Thomas A. Hockin, P.C., B.A, M.P.A., Ph.D., ICD.D
Chairman of the Board
Retired, former Executive Director of the International Monetary Fund

Gabrielle Bochynek, B.A. CHRL
Principal, Human Resources and Labour Relations, The Osborne Group

Robbert-Jan Brabander, M.Sc. and B.Sc. (Economics)
Managing Director of Bells & Whistles Communications, Inc.

David A. Bratton, B.A.(Hons), M.B.A., CHRP, FCMC
Retired, former President of Bratton Consulting Inc.

R.W. (Dick) Carter, FCPA, FCA, C. Dir
Retired, former Chief Executive Officer of the Crown Investments Corporation of Saskatchewan

Art Linton, JD
Barrister and Solicitor

Colin Litton, FCPA, FCA, ICD.D.
Retired, former senior partner of KPMG LLP

Susan T. McGovern, B.Sc.
Vice-President, External Relations and Advancement
Ontario Tech University

Paul G. Oliver, FCPA, FCA, ICD.D.
Retired, former senior partner of PricewaterhouseCoopers LLP

David R. Taylor, B.Sc. (Hons), M.B.A., F.I.C.B.
President & Chief Executive Officer, VersaBank

OFFICERS AND SENIOR MANAGEMENT

David R. Taylor, B.Sc. (Hons), M.B.A., F.I.C.B.
President & Chief Executive Officer

Shawn Clarke, M.Eng., P.Eng., M.B.A.
Chief Financial Officer & Corporate Secretary

Michael Dixon, B.Comm., M.B.A.
Senior Vice President, e-Commerce

Ross P. Duggan
Senior Vice President, Commercial Lending

Nick Kristo, B.Comm., M.B.A.
Chief Credit Officer

Jonathan F.P. Taylor, B.B.A., CHRP
Senior Vice President, Deposits & Chief HR Officer

Jean-Paul Beker, B.A. (Economics), CFA
Vice President, Commercial Lending

Steve Creery, B.A. (Economics)
Vice President, Credit

Barbara Hale, LL.B.
Chief Compliance Officer & Chief Anti-Money Laundering Officer

Joanne Johnston, B.Comm, CPA, CA, CIA
Chief Internal Auditor

Wooi Koay, B.Comm., B.Sc.
Chief Information Officer

Aly Lalani, B.A., M.B.A., CPA, CA
Chief Risk Officer & Treasurer

Tel Matrundola, Hons. B.A., M.A., Ph.D.
Chief Strategy Officer, Cyber Security

Andy Min, B.A., CPA, CA
Vice President, Finance & Corporate Accounting

Scott A. Mizzen, B.A., LL.B.
Vice President, Commercial Lending

Gurpreet Sahota, CISSP, CCSP
Chief Architect, Cyber Security

David Thoms, B.A., M.B.A.
Vice President, Structured Finance

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