FINAL TRANSCRIPT

Canadian Western Bank

Third Quarter 2012 Financial Results

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PRESENTATION

Operator

Good afternoon, my name is Tracey (phon) and I will be your conference Operator today. At this time I would like to welcome everyone to the Canadian Western Bank Third Quarter 2012 Financial Results Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks there will be a question-and-answer session. If you would like to ask a question during this time simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question press the # key. Thank you.

And I'll now introduce and turn the call over to Miss Tracey Ball, Executive Vice President and Chief Financial Officer. Please go ahead. You may begin your conference.

Tracey Ball – Executive Vice President and Chief Financial Officer, Canadian Western Bank

Thank you very much, Tracey, and good afternoon and/or good morning to those of us on the west side of Canada, and welcome to the 2012 third quarter results conference call for Canadian Western Bank.

Before we begin, please note that the conference call slides, quarterly results news release, and supplemental financial information are available on the bank's website at www.cwbankgroup.com, in the Investor Relations section.

And also before we start I want to draw your attention to our forward-looking advisory statement on Slide 10.

The agenda for today's call is on Slide 2. Joining me today is Larry Pollock, President and Chief Executive Officer. Also in attendance are Chief Operating Officer, Chris Fowler; and Executive Vice Presidents Bill Addington, Randy Garvey, and Brian Young.

Recognizing the number of other banks reporting today, we will keep our formal commentary very brief and leave as much time as necessary for Q&A at the end of the call.

I'll begin by providing a quick summary of our third quarter and year-to-date highlights, and then I'll turn things over to Larry.

Moving to slide 3, the Bank reported record quarterly performance marking our 97th consecutive profitable quarter. The achievement of record earnings and total revenues was largely driven by the benefit of ongoing strong loan growth of 3% in the quarter, 11% year-to-date and 13% in the past year.

Loan growth also pushed total assets past the $16 billion milestone. An improvement in overall credit quality was evidenced by our ninth consecutive quarter of declines in gross impaired loans.

Net income available to common shareholders of $48.0 million was up 24% over the same quarter last year, while diluted earnings per common share increased 22% to reach 61 cents.

Adjusted cash earnings per share, which excludes the non-tax deductible change in fair value of contingent consideration and the amortization of intangible assets, was up 17% to $0.63.

Record total revenues of $138.2 million represented a 13% increase over the same quarter last year as the benefit of strong growth in both loans and other income more than offset the impact of a 14 basis point reduction in net interest margin. Other income of $22.9 million was up 28%, or $5.1 million compared to a year earlier, and included the positive impact of the settlement of contingent consideration.

For comparison purposes, the charge for the change in fair value of contingent consideration was $2.5 million in the same quarter last year and $1.2 million in the previous quarter.

Other income also reflected a $1.9 million gain from the sale of a $50 million mortgage portfolio within Optimum Mortgage, which is reflected in the other component of other income.

Gains on sale of securities of $1.9 million were up $1.0 million. A $1.0 million combined increase in net insurance revenues and credit related fee income more than offset a $0.7 million decline in trust and wealth management fees and a slight reduction in retail services fees.

Moving to the next slide, compared to the previous quarter, net income available to common shareholders and adjusted cash earnings per share increased 21% and 15%, respectively.

Results mainly reflect the positive revenue impact of a slightly improved net interest margin, two additional revenue earning days, continued loan growth and very strong other income. Non-interest expenses were also slightly lower.

Yesterday, our Board declared a quarterly cash dividend of 16 cents per common share. This dividend was unchanged from the previous quarter, when we increased the dividend by 7%, and represents a 14% increase compared to the quarterly dividend declared one year ago.

Year-to-date performance is shown on Slide 5, which confirms the Bank is well positioned to meet or surpass all of our fiscal 2012 targets.

Loan growth through the first nine months has already surpassed our annual target of 10%, and the volume in the pipeline for new loans remains encouraging. We will publish our minimum performance targets for 2013 in December with the release of our fourth quarter results.

Going to the next slide, our Basel II capital ratios at July 31st remained well above both regulatory minimums and our internal targets. On a pro forma basis, the all-in Basel III capital position using the standardized approach for calculating risk-weighted assets, shows a Common Equity Tier 1 ratio of 8.0%, a Tier 1 ratio of 9.6% and a total ratio of 12.8%. All of the pro forma Basel III ratios are above the required regulatory minimums of 7.0%, 8.5% and 10.5%, respectively, which has the Bank well positioned for the forthcoming transition effective January 1, 2013.

The next slide shows the long-term trend of net interest margin, spread on loans and the prime lending interest rate. The margin and spread on loans for periods prior to the fourth quarter of 2010 have not been restated for either IFRS or the change in accounting for loan fees that commenced in the first quarter of 2011.

Third quarter net interest margin (teb) of 2.85% improved four basis points compared to the prior period largely reflecting the benefit of higher interest recoveries on impaired loans.

Reduced debenture expense and slightly lower deposit costs also helped offset the impact of overall lower lending yields.

Margin was down 14 basis points from the same period last year with the difference mainly reflecting lower yields on loans and preferred shares, partially offset by a reduction in fixed term deposit costs, reduced debenture expense and higher interest recoveries.

Year-to-date net interest margin of 2.81% was down 22 basis points compared to the same period in 2011 reflecting the factors already noted.

Looking forward, and based on the current environment of very low interest rates, strong competition and other factors, it's unlikely we will realize any improvement in net interest margin compared to what was achieved on a year-to-date basis.

While higher interest rates and a steepening of the yield curve would have a meaningful positive impact on net interest margin, the prevalence of ongoing macroeconomic uncertainties suggests this will not be the case within the foreseeable future.

I will now turn things over to Larry to provide additional comments on our overall outlook and strategy.

Larry Pollock – President and Chief Executive Officer, Canadian Western Bank

Thank you Tracey. Slide 8 shows our historical level of gross impaired loans and write-offs measured as a percentage of total loans. Overall credit quality continued to improve with the dollar level of gross impaired loans decreasing for a ninth straight quarter. As a result, the current period represents the first time since 2008 that the collective allowance for credit losses has exceeded the total balance of impaired loans, net of specific allowances.

The total number of accounts classified as impaired was also down significantly compared to a year earlier. Based on our current view of credit quality, we expect the balance of gross impaired loans will likely fluctuate around the current level moving forward.

Future write-offs are also expected to remain within the Bank's range of acceptable levels.

We are regularly asked about our view of Canadian real estate markets, and what the Bank's exposure would be in the event of a meaningful pullback in prices. We continue to believe Canada's overall market for residential real estate remains healthy.

This view is supported by affordability levels in most markets that are generally within historical ranges, largely owing to very low interest rates.

Higher relative prices in specific markets, an increased level of Canadian consumer debt and the potential for higher interest rates within the foreseeable future are among many things we consider to ensure our underwriting standards reflect current market risks.

We regularly stress our portfolios and results show that in the event of a 30% decline in real estate values, our expected provision for credit losses would remain manageable.

The primary impact of this scenario on near-term performance would most likely be a decrease in loan growth resulting from the combination of lower demand and tighter credit criteria.

We also stress our loan portfolios for the expected impact of a rapid increase in interest rates, and believe this is another manageable scenario.

This is confirmed by the excess debt service capacity required through our underwriting processes, as well as an increasing number of clients choosing fixed interest rates.

Our total exposure to project loans on condominiums currently represents about 5% of total loans, and the average loan-to-value for this portfolio is approximately 61%. About 2/3rds of this exposure is concentrated in BC, with the bulk of the balance split between major centres in Ontario and Alberta.

Total loans within Optimum Mortgage at quarter end were just over $1 billion, and about 67% of this portfolio is comprised of alternative mortgages carrying a weighted average loan-to-value at initiation of approximately 72%.

The average deal size for this business is in the mid- two hundred thousand range, which has been the case for quite some time. As with all of our businesses, we are very confident in our underwriting processes, and also remain comfortable with Optimum's overall risk profile.

Our *Homeworks* residential mortgage product, which is offered in CWB branches, represents about 5% of total loans. Of this amount, approximately 2/3rds is represented by the equivalent of a home equity line of credit, with balance being advanced on a term reducing basis. Utilization of the line of credit component is typically within the range of 70 to 75%.

Overall, our outlook for both consolidated loan growth and credit quality remains encouraging.

Refer to Slide 9. The next slide highlights our strategic priorities and outlook. The Bank's strategy remains focused on continued investment in our people, infrastructure and technology to support future growth.

Our overriding goal to expand market share is based on further enhancing client services, developing additional synergies between our businesses and building awareness of CWB Group's offerings.

While there are opportunities to further improve operating leverage, constrained growth in revenues owing to the very low interest rate environment, coupled with increased investment in certain areas, will likely limit our capacity to achieve meaningful improvement in the efficiency ratio compared to the current level. That being said, we will maintain our efforts to effectively control costs while ensuring CWB Group is positioned to deliver sustained, long-term growth.

As Tracey mentioned, the Bank's capital position using the standardized approach for calculating risk-weighted assets exceeds all minimum requirements under Basel III. We highlight the standardized approach because the advanced approach used by many other financial institutions results in reported capital ratios that are not directly comparable with CWB's. This circumstance is partly evidenced by our much lower leverage measured by total assets-to-equity.

The Bank's eventual transition to an advanced approach will be a multi-year process, but our preliminary analysis indicates this could have a significant positive impact on our businesses looking forward. Although any future transition would be subject to regulatory approval, if we apply the average of the risk-weightings used by other Canadian banks to our business loan portfolio, our current pro forma CET1 capital ratio would be well north of 10%. This would not only allow the Bank to support a higher level of growth with internally generated capital, it would provide us increased flexibility to raise our target dividend payout ratio for shareholders.

Economic activity remains relatively strong throughout our core geographic markets, but we remain cautious in light of what we believe is still a fragile global economy. We continue to closely monitor global economic headwinds to assess the potential impacts on CWB.

We will also continuously evaluate our liquidity strategies to ensure the Bank remains well positioned in the event of any unexpected economic or market fallouts.

All of our operating affiliates have excellent potential to further develop and grow, including National Leasing, Canadian Direct Insurance and our trust services companies. National Leasing is particularly well positioned for significant expansion over time, as our capabilities in this business are highly scalable in terms of both volume and geography.

Our third quarter and year-to-date performance has the Bank positioned for another year of record results. We are confident we can effectively execute on our strategies and continue building on the Bank's long history of success.

As part of this, we will also continue to evaluate the potential for strategic acquisitions that may become available. As Tracey mentioned earlier, we will provide an updated outlook and discuss our 2013 performance targets with the release of our fourth quarter and annual results in December.

I'll now turn things back to Tracey.

Tracey Ball

Okay. Thanks, Larry. And that does conclude our formal presentation for today's call. At this time, I'll ask Tracey to begin the question-and-answer period.

Q&A

Operator

At this time, I would like to remind everyone in order to ask a question press *, then the number 1 on your telephone keypad.

Your first question comes from the line of Scott Chan with Canaccord Genuity. Please go ahead.

Scott Chan – Canaccord Genuity

Good afternoon.

Tracey Ball

Hello.

Scott Chan

Just on National Leasing, I guess just prior to the conference call I saw they purchased Globale FC. Maybe you could just describe that transaction.

And also can you just remind me of the business synergies that you kind of quoted in the press release, potential across all the business units as well?

Larry Pollock

Yeah. On Globale, it's a small acquisition, but it enhances our ability to grow in Quebec. We really took a key strategic broker that we used and acquired them. And we'll use that as our growth platform in Quebec. And I believe National have about 7 percent of their total book in Quebec at this time.

Scott Chan

Okay.

Larry Pollock

So that's an important market for us. Was there another part to your question Scott?

Scott Chan

No. No, that's fine. Just a second question, just on the core banking system. I think the last time we spoke you had a budget of about 50 million. I'm just wondering how much is spent so far? I know it looks like it's on track to hit 2015, and if the remaining is more frontend or backend loaded, and if I can remember I think most of it's going to be capitalized and amortized at the end of the project?

Larry Pollock

Yeah. That's a bit of an accounting question, but…

Tracey Ball

Yeah. Scott; Tracey. Yeah, the 50 million will primarily, absolutely be capitalized and amortized once we start the process in 2015 or once we get to the—to start to operate it. Right now, there will be some backfilling of individuals so we could see a little creep-up in staff costs but I don't think it will be material.

Scott Chan

Okay. And just a last question. How much of the NIM quarter-over-quarter increase related to the recovery of the impaired loan.

Tracey Ball

Scott, I looked at it. We had about 8 basis points altogether, but on an average we run about 4. So I would say 4 basis points is as good as I can guess, which would really put us back to our second quarter margin of 281.

Scott Chan

Okay. That's perfect. Thanks, guys.

Operator

Your next question comes from Gabriel Dechaine with Credit Suisse. Please go ahead.

Gabriel Dechaine – Credit Suisse

Right. Just reading your MD&A, it almost sounds like the guidance for your margins is to stay flat, not necessarily go down, so I think if you can confirm that, we're at kind of trough levels now with no change in rates. And then, on the—I've got a follow-up.

Tracey Ball

Oh. Hello.

Gabriel Dechaine

Yeah, I've got a follow-up, but I'll wait.

Tracey Ball

Okay. So on the margin, yeah, we expect it to be fairly stable at the—really the quarter two level since the quarter three level had a little bit of a bump-up with the interest recoveries.

Gabriel Dechaine

Yeah. So no grind down or anything like that. Just kind of bump…

Tracey Ball

Bump along. Bump along.

Gabriel Dechaine

Okay...

Larry Pollock

If we had an increasing rate environment though, Gabriel, I think you'd start to see it improve again.

Gabriel Dechaine

I hear you, Larry. Okay. Then the commercial lending or lending overall, I guess the commercial, general commercial and equipment leasing off that, pretty much flat growth in real estate construction lending. That's obviously positive. If you can kind of talk about the capital impact of that kind of mix shift, how beneficial that could be with your kind of average risk wait for those types of loans versus the real estate constructions loans.

And then also what's the potential for, and you allude to the slowdown in the housing market as a source of headwind for loan growth in that portfolio as one would expect, what's the potential for real estate construction lending to actually turn negative if originations don't keep pace with paydowns.

Larry Pollock

Well, so far this year they're not negative. They're still increasing, but not increasing as rapidly as some of our other portfolios.

On the capital side and that part of your question, we've been driving the growth in the equipment business both through National Leasing and our big ticket group, Equipment Finance Group, because most of those loans would be classified as small business loans and they require about 25 percent less capital than say a real estate construction loan would be. So effectively we could grow at a more rapid pace with our Equipment Group and National Leasing by about 25 percent and use the same amount of capital.

Gabriel Dechaine

Right. Okay, that's straight forward. So you don't anticipate maybe seeing some negative growth in the real estate construction portfolio, because if projects really slow down and the stuff that's on the books now gets paid off, I mean it's not hard to...

Larry Pollock

Yeah.

Gabriel Dechaine

Imagine that taking place...

Larry Pollock

Yeah, we may see some slowdown of course in the Toronto and Vancouver markets, but what we're seeing in Edmonton and Calgary...

Gabriel Dechaine

Mm-hmm.

Larry Pollock

And the Alberta markets, it's ramping up and...

Gabriel Dechaine

Okay.

Larry Pollock

The City of Edmonton just did a presentation this week announcing within a 16 block radius of the core of the downtown alone $4.8 billion worth of new projects.

Gabriel Dechaine

Okay.

Larry Pollock

So we're seeing Alberta ramping up. So we should see a bit of an offset there...

Gabriel Dechaine

Okay.

Larry Pollock

And we're anticipating to still see growth in the real estate construction.

Gabriel Dechaine

Okay. Thanks a lot.

Larry Pollock

Okay.

Operator

Your next question comes from John Reucassel with BMO Capital Markets. Please go ahead.

John Reucassel – BMO Capital Markets

Thank you. Just on—Tracey? Question. I just want to make sure I understood the impact of the interest recoveries on previously impaired loans. You think it's about 4 basis points in the quarter.

Tracey Ball

Yeah. It was—total recovery was 8 basis points, but we have them all the time.

John Reucassel

Yes.

Tracey Ball

So an average run rate would be 4.

John Reucassel

Okay. Okay.

Tracey Ball

But I'm saying 4 is unusual.

John Reucassel

And that gets you back to the 281.

Tracey Ball

Correct.

John Reucassel

Gotcha. Okay. On the loan growth, Larry. Could you try and break it down a little bit on how much is an increase in your own (phon) exposure? Or these are new accounts? Or how much has been purchased portfolios?

Larry Pollock

Very little of it would be purchased, and purchased portfolios are a regular event for us. We have vendors, large equipment vendors, as an example, that give us product constantly. So every quarter we seem to have some of that. So that's not abnormal anymore.

John Reucassel

Yup.

Larry Pollock

The fastest growing markets that we have in our portfolio are the general commercial, and your growth there is really driven by both new customers and the expansion of existing customers. So we're able to grow as our customers grow, and we've seen extremely rapid growth, especially in the Alberta market, driven by the oil patch and mainly the oil sands.

John Reucassel

Okay. So that's why you remain confident, because you're getting good balance between increased in drawn and new customers. Is that right?

Larry Pollock

Yes.

John Reucassel

Okay. And then just back to you, Tracey. The sale of the mortgage loan portfolio?

Tracey Ball

Yes.

John Reucassel

Is that—maybe I'm too tired today—but is that an unusual event for CWB? Or is that...

Tracey Ball

It's the second time, John. So when we're developing our—growing our optimum mortgage portfolio, which is broker generated, we're offering both Alt-A and insured product because that's what our brokers want. We don't make a lot of money on the insured product, so we have done one loan sale previous to this, and this second loan sale is with the same company or same financial institution that bought it. So it would be nice to have a continuing program of it but we're not quite there yet. So it's…

John Reucassel

Okay. When was the last time you did this?

Tracey Ball

I think it was September, last year?

Unknown Speaker

2011

Unknown Speaker

Q4 2011.

Tracey Ball

Q4 2011.

John Reucassel

Okay. Okay. And then on the negative net impaired loans, I mean you talk about a 20 to 25 basis point provisioning level, but I mean aren't we getting a little too conservative given the environment we're In?

Tracey Ball

Yes.

John Reucassel

What would you—how would you guide us on that? Or provide us some comfort that that's...

Tracey Ball

Well I don't...

John Reucassel

Not too conservative?

Tracey Ball

You're not going to see—you won't see much change for this year.

John Reucassel

Yes.

Tracey Ball

So we expect to be at the low end of the 20 to 25 basis points. We might even be a tick under. But we do have to take another look at our model and make sure it works all the way around, but we're not uncomfortable with our level of a collective allowance because we do grow more quickly than our peer group. So we're cognizant of that, and we don't think that we're over capitalized or over...

Unknown Speaker

Reserved.

Unknown Speaker

Reserved.

Tracey Ball

Reserved.

John Reucassel

Okay. Thank you.

Operator

Your next question comes from the line of Shubha Khan with National Bank Financial. Please go ahead.

Shubha Khan – National Bank Financial

Thanks. Good afternoon. Just curious about the sequential drop in commercial mortgage balances. Was it in any way driven by sort of more aggressive underwriting by your larger peers this quarter? Or were other factors at play?

Larry Pollock

That would certainly be part of it, Shubha. We've seen some sort of irrational pricing out there by some of our competitors. It makes us wonder why they should be lending long-term fixed money at 3 percent or 3.07 and that sort of thing. So what—our discipline is such that for our shareholders we're going to make money. We're not going to do business to be able to beat our chest at the next conference and say we took market share from somebody else. The question that should follow that up is at what cost? So we value liquidity and every deal that we've put on the books has to meet our criteria with both a return and credit quality, and if we can't achieve that because we've got competitors that are doing deals that wouldn't meet that, we're not going to enter that game. We're going to adjust our focus to more industrial business or focus on growth in the Fort McMurray area or something like that or another geographic area. And we are looking at expanding geographically a little bit in some of our product lines.

Tracey Ball

And, Shubha, it's not a surprise that this is happening because when we went through the crisis that was a sector in the market that a lot of lenders backed out of, so we got a lot more opportunity and we were lending. So we kind of built that book up. But frankly, previous to the crisis we weren't a big player in that market and ran into the competition regularly. So it's really going back to normal.

Shubha Khan

Okay. But in terms of the competition, have you seen pricing pressures that are persistent to the current quarter? Or have things levelled off? Or have they reversed? What's transpired since the end of last…

Larry Pollock

We've actually seen—we've seen both. We've seen some covenant light lending, because a customer won't always move just for rates. So they're looking for looser conditions and terms on loans. So we've seen some of that, and low pricing as well.

You'll probably hear that from the other banks and that. It's very difficult to grow in the Canadian market for them because they hold most of the market share now. So they're just trading positions with each other, and doing it with low rates.

Shubha Khan

Okay. That's helpful. And if I can just switch gears sort of to the Optimum portfolio. You saw fairly strong growth there, adjusted for the portfolio sale. So geographically, I'm just wondering, was the growth broad based? Or did you see any evidence that the housing market is perhaps levelling off or slowing in Western Canada and so most of the growth is being sort of generated elsewhere?

Larry Pollock

I would say it is broad based, Shubha. Looking at the volume that we had last quarter, we did have the mortgage sale but our volume was up, and that had to do with the exit of a couple of the larger banks in Alt-A side. So we had very strong volume. And Ontario remains to be strong, as the west is too. So it is fairly broad based.

Shubha Khan

Okay. That's helpful. Thank you.

Operator

Your next question comes from the line of Darko Mihelic with Cormark Securities. Please go ahead.

Darko Mihelic – Cormark Securities

Hi. I guess good morning over there. Couple of questions. Larry, the growth in the branch-generated deposits is impressive at 12.5, but still lacks the growth rate of your loan book. Is there anything you can do on that front with respect to the deposit book for branch-generated I mean? Or is it just a function of you just have so many branches and there's only so much you can do?

Larry Pollock

We do supplement with agent funding. And we have in the last couple of years initiated senior deposit notes that we've been issuing, and we'll continue to issue on a regular basis.

And we also have started an Internet bank called Canadian Direct Financial, and it operates in Canada. The back room is here in Alberta. And it has shown us that we can generate fairly material retail deposit growth directly with clients using this vehicle. We've had it in the testing phase for the last year or so. We've seen about, I think 65 percent growth this year, something in that area. So that's a vehicle that I think you'll see us out on the airwaves more with.

And we saw a purchase today of ING, which is a similar type platform; ours is much smaller of course, but it replicates what that one does and it does work. And we can, being concentrated with our branch network in Western Canada, access those markets through the Internet without having to build out bricks and mortar.

Darko Mihelic

And so the testing phase is over and now it's ready for some sort of a big strong launch? Would that be the...

Larry Pollock

Yeah. We've only been offering, what is it two products, Randy?

Randy Garvey

Pretty much.

Larry Pollock.

Yeah, pretty much just two products. We can expand the product offering. We can adjust pricing. What we don't want to end up facing, because we still have a limited platform, is driving too much business through that area, sort of like drinking out of a fire hose. So we have to be a bit careful. So we're targeting, what is it London, Ontario, Ottawa as well?

Randy Garvey

Kind of (phon) smaller markets in Ontario

Larry Pollock

Yeah. And that's worked quite well. I mean stay tuned on that one. We'll keep you informed.

Darko Mihelic

Yeah. I might follow-up on that. That sounds interesting.

And then I guess, just generally speaking Larry, I mean I've followed your company for a long time and I've watched you do a lot of things, but you still can't seem to break away from having a very large reliance on spread income. You've added a couple trust companies. You've added an insurance company, and asset manager. But now it seems as though we're going down the National Leasing route, which would once again further up the dependence on spread. Is there anything that can be done elsewhere? Or is it just a function of whenever you do deals they tend to be just opportunistic when things come your way. And we simply haven't seen anything that would be more fee income related in the last 12 months or so.

Larry Pollock

Well, of course our trust businesses and our insurance business all fall into that fee income category. And the wealth management business, which we acquired a few years ago, we're looking at trying to expand that. So stay tuned on that.

And the trust businesses, especially Valiant Trust, has been quite constrained in growth in the last little while because the capital markets activity hasn't been very brisk, as you've seen with the results of the other banks. And that income can be quite large and lumpy. We made in one particular transaction 50 percent of our purchase price on the Company on an after-tax basis. So if the market perks up here we'll see more fee income. But we do like—interest income is not a bad thing to us, and I believe we are the only bank that could continue to earn a profit with no fee income, and you can check that, Darko.

Darko Mihelic

Yeah. I will.

Larry Pollock

You probably will. But we like businesses that are still making money while you're sleeping. And certainly the spread income business falls into that category.

Darko Mihelic

Okay. So strategically then, just to sort of sum that up, there isn't really anything driving you to make an acquisition that would focus in on fees. Really what you're doing right now is focusing on your bread and butter, and if something came along on the leasing side you'd happily go after that and not even worry about the fee-income component?

Larry Pollock

Absolutely. We would really like to expand National Leasing. And we had a constraint because we didn't own all of the company up till June of this year. We completed the acquisition, and now we own 100 percent. So any acquisition we would have done before that period of time would have had to been shared with our partners. And what we're able to do is swap CWB common shares for the preferred share component of that company, which equated to about 30 percent of National Leasing.

So that really cleaned up a situation that was hindering us. And there are some opportunities in that area and we are aggressively looking for them. We're not sitting back waiting for something to fall through the door. But these things aren't easy to do, and we're pretty fussy about what we add to our portfolios. But we are looking for both portfolios and smaller leasing companies, or larger- or medium-sized ones, that would be a good cultural fit with anything that we're doing today.

And we've had spectacular growth in our heavy equipment side, as we talked about earlier. And we're going to be a little bit more aggressive in expanding that area because it's got both good margins and it's not a business that we trip across the major banks in very much. Our main competitors tend to be other lenders, CAT Finance, GE Capital, and those folks; John Deere Finance. And so we can compete very nicely head-oh with them, and we get excellent margins and it's a low loss type business. So stay tuned on all those areas. We're going to be more aggressive.

Darko Mihelic

Yeah. I can appreciate all that and I don't want to take up too much more on the conference call, but one last thought as we go down that route, which is you seem to be on a path towards an advanced internal ratings based methodology for your RWA. You're happily growing the asset side of the balance sheet, at double-digit territory. Under Basel III though, the AIRB methodology is quite procyclical and we could get into a situation where your RWA would grow rather fast under that. And I appreciate you have a lot of capital, but I'm just wondering have you taken that—I mean you obviously must of thought of this, but it just seems like an almost somewhat risky route to take when you have excess capital to try and keep growing the asset side of the balance sheet, particularly lending which can turn procyclical on you.

Larry Pollock

Right. And we are quite aware of that. We have had discussions with our regulator, OSFI, and our Board, and we're not necessarily of the view that we would go as far as AIRB would allow you to. We are of the standardized approach today. We carry about 40 percent more capital than our competitors do and we still earn a 15, 15.5 ROE, so we don't think that's such a bad business model. So we could take on a lot more business, even with the capital we have today. I think one of the other banks announced that they were satisfied at 7 percent under AIRB and we're at 8 under the standardized approach, and if we were under AIRB today, we would probably be north of 10 on CET1.

Darko Mihelic

Okay. All right. Thanks very much for your comments.

Larry Pollock

You're welcome.

Operator

Ladies and gentlemen, if you would like to ask a question please press *, then the number 1 on your telephone keypad. Your next question comes from the line of Brad Smith with Stonecap Securities. Please go ahead.

Brad Smith – Stonecap Securities

Thank you very much. Yes, I had a quick question with respect to the third party mortgage broker channel and how that's changing in the last number of months; what changes you've seen in terms of the quality of the product that's coming your way now that some of the previous participants in that market have pulled out. And perhaps maybe some comments, just generally, on the pricing and the margin directions that you're seeing.

Larry Pollock

Well so far, I mean the rules are just in the process of changing now and the banks will be adjusting their own internal policies on booking these things, but what we have seen is, you're right, Brad, about some of the competitors withdrawing. The comments coming out of the pure players like Home Capital and Equitable have been quite positive on recent events. So we're optimistic that we will see continued strong volumes. I think Chris mentioned earlier that we had our strongest volumes in this last quarter.

Chris Fowler

To date. Yeah.

Larry Pollock

To date. So we would very much like to continue to grow this business.

On the question of margin, I think the margins have been quite stable. We did see some people that were in this business pricing closer to A (phon) product, and I don't think that's the case today. Do you know?

Chris Fowler

Certain markets are more competitive than others, depending on the players in those markets, but the pricing has been—it's beating our expectations. We're not out there undercutting. It's an area that we do focus on the margins, so we do—83 percent of our originations in this last quarter were in the Alt-A side, so that is a better yield.

Brad Smith

Terrific. Thanks. Now on the acquisitions front, it seems that most of your discussion so far in acquisitions is really focused on the left-hand side of the balance sheet. What about on the funding side? Do you have an appetite here for acquired deposit capacity? And things like that in terms of branches, other opportunities to expand that footprint?

Larry Pollock

Yes. Historically, you go back into the 90s, we have historically been one of the largest acquirers. I can probably name about five trust companies that we acquired to get the branch network, and we consolidated them, picked up the deposits.

One of the most valuable components of banking today is the ability to raise funding inexpensively on your own balance sheet rather than using other sources, so we would be very interested in an acquisition. Certainly, we salivate over credit unions' ability to raise deposits. We have the ability to run that left-hand side of the balance sheet extremely well. You marry those two entities up and you've got a real winner on your hands.

Brad Smith

And you raised an interesting point, which was going to be my next question. If you could just comment on from your perspective what these sort of draft rule changes with respect to the oversight of credit unions and the flexibility that they'll have—may have in your markets.

Larry Pollock

Yeah. There is a provision in the Act that they can go federal. They would then be susceptible to OSFI regulations as we are and also have CDIC insurance. So that would change their insurance levels because in Alberta and British Columbia, for sure, the deposits are guaranteed 100 percent by the provinces. So they would then move to $100,000 per deposit, which changes a lot of things for them. There are corporations depositing with these credit unions now that probably wouldn't if they only had $100,000 in insurance, and scrutiny from OSFI I think would be more robust than the provincial regulations. So they're going to have to change a lot of things. And the constraint they have in going federal is if they do encounter some growth opportunities, they do not have the ability to raise capital as easily as a publicly traded bank would, as we saw today with Scotia.

So if I were the head of a credit union I would be thinking long and hard on that prospect. The other issue, of course, is that as these credit unions have grown and the provinces have offered 100 percent guarantees, the provinces are really taking on a liability much larger than I think they had originally anticipated. So I think there will be some heightened scrutiny from the provinces on those institutions and maybe some adjustments in their deposit insurance.

Tracey Ball

And I think one of the interesting things that's in those draft rules though is the ability for a federal credit union to become a bank. So that certainly does potentially change the landscape in the future, should a credit union decide to go federal and then determine that it's in their best interest to become a bank and get that access to capital that Larry was talking about. So it could be a game changer. We just—we're not sure how far along the credit unions are.

Brad Smith

One last question. I don't want to belabour this, but we're really talking about some of the larger credit unions I think at that point, but what about the smaller players in the credit union marketplace? Do you think—how does this potential change or game changing affect them? I'm thinking in terms of your acquisition appetite.

Larry Pollock

Well, the smaller ones have been consolidated into the larger ones so there's a lot less of them around than there used to be. And with the regulatory costs and rigour that they have to face today, even at the provincial level, makes it very difficult to keep your costs in line. So what you're seeing are very higher cost operations, very high efficiency ratios in those organizations that will, over time, probably render them non-competitive in the marketplace, and we see some of that now. And you can look at their results. They do have, some of them, efficiency ratios in the 70-plus percent range.

Brad Smith

Right.

Larry Pollock

And the banks are all sort of in the 50s, and we're 44. So it's going to be difficult for them to compete.

Brad Smith

Perfect. Thanks so much.

Operator

At this time, there are no further questions in queue. I turn the call back over to Miss Tracey Ball.

Tracey Ball

Okay. Thank you, Tracey, and thank you very much everybody on the call. I know it's a busy day and—but we're happy to talk to you about Canadian Western Bank, of course, and if you have any follow-up questions or comments, please call us or contact us by email. Thank you, and have a good day.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for joining Canadian Western Bank's third quarter 2012 financial results conference call. You may now disconnect.

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