

TO OUR SHAREHOLDERS

This year was another record year for Chesswood Group by almost all measures! Portfolio size, originations, operating income and pre-tax earnings were all records for Chesswood, once again. If not for the “Trump Bump” which generated a tax recovery and increased earnings by \$9.4 million in 2017, as a one-time effect, our net income would also have hit a new milestone. Furthermore, our pre-tax return on equity increased to almost 20% for 2018, from 17.2% in 2017.

We earned \$32.7 million before tax in 2018, compared to \$27.8 million for 2017, for an increase of 18%, while our operating income totaled \$33.7 million versus \$32.1 million in 2017. This \$1.6 million improvement in operating income would have been larger by approximately \$900,000 had we not retired our convertible debenture at the start of 2018 by using our bank debt. Interest expense on our bank debt is deducted in the calculation of operating income whereas interest on our now retired convertible debenture was not part of operating income in prior years.

This past year included two important accomplishments for Chesswood’s treasury resources and future growth. We completed our second U.S. securitization in June, followed by completing our new U.S.\$250 million warehouse facility in the second half of the year. This new warehouse facility provides us with appropriate treasury for our U.S. prime originations by improving our advance rates and cost of funds to better match our treasury resources with our prime originations activity. The warehouse line will hold most of our prime originations before they are bundled together and securitized.

Our shareholders have relied on us for sustainable dividends, for more than a decade. In 2018 we paid out \$15.1 million in dividends, providing our shareholders with an annual yield of 7.65% based on our average share price in 2018 of \$10.98. Just as importantly, our payout ratio - the percentage of our permitted free cash flow that we pay out in dividends - is approximately 65% following the release of these year-end financial statements. Our share price in 2018 provided us with an opportunity to repurchase some of our shares through our normal course issuer bid at values we considered to be

advantageous for shareholders. We purchased 499,436 shares at an average cost of \$10.41 per share.

Late in 2018 we began the work necessary to launch our new equipment finance business, Tandem Finance Inc. Headquartered in Houston, Texas, Tandem provides equipment financing programs to equipment vendors and distributors in the U.S. and offers a truly unique value proposition to this largest channel of equipment finance - direct funding for most credit tiers. In this channel, we will be the only funder that can approve, fund, hold and administer equipment finance contracts for small and medium sized businesses with credit profiles from “A” through “C”, using our decades of experience with these multiple credit segments. Today, other funders in this space generally resell transactions that are not prime as they do not have the expertise or treasury necessary to fund this type of business. This results in poorer service, lower approval rates and less equipment sales for the equipment sellers. Tandem is led by an experienced team from this channel, who are focused on bringing our proven expertise in small-ticket equipment finance in most credit categories, to the much larger vendor channel, in 2019.

Lastly, our decade long record of success in the growth of our earnings and portfolio is a testament to the great team members we have in the U.S. and Canada. Money is ubiquitous but a consistent commitment to the customer is hard to find and we are very grateful to our team of more than 130 employees for their passion, dedication and delivery of superior service, each and every day.



Barry Shafran
President & CEO

MANAGEMENT'S DISCUSSION AND ANALYSIS

This management’s discussion and analysis (this “MD&A”) is provided to enable readers to assess the financial condition and results of operations of Chesswood Group Limited (“Chesswood” or the “Company”) as at and for the year ended December 31, 2018. This discussion should be read in conjunction with the 2018 audited consolidated financial statements and accompanying notes of the Company. Unless otherwise indicated, all financial information in this MD&A has been prepared in accordance with

Generally Accepted Accounting Principles ("GAAP") and International Financial Reporting Standards ("IFRS"), and all amounts are expressed in Canadian dollars, unless specifically denoted otherwise. This MD&A is dated March 5, 2019.

Additional information relating to the Company, including its Annual Information Form, is available: on SEDAR at www.sedar.com, at the www.chesswoodgroup.com website, by email to investorrelations@chesswoodgroup.com, or via phone at 416-386-3099.

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FORWARD-LOOKING STATEMENTS

In this document and in other documents filed with Canadian regulatory authorities or in other communications, the Company may from time to time make written or oral forward-looking statements within the meaning of applicable securities legislation. Forward-looking statements include, but are not limited to, statements regarding the Company's business plan and financial objectives. The forward-looking statements contained in this MD&A are used to assist readers in obtaining a better understanding of the Company's financial position and the results of operations as at and for the periods ended on the dates presented and may not be appropriate for other purposes.

Forward-looking statements typically use the conditional, as well as words such as prospect, believe, estimate, forecast, project, expect, anticipate, plan, may, should, could and would, or the negative of these terms, variations thereof or similar terminology. By their very nature, forward-looking statements are based on assumptions and involve inherent risks and uncertainties, both general and specific in nature. The Company operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond its control and which could have an effect on the Company's business, revenues, operating results, cash flow and financial condition. It is therefore possible that the forecasts, projections and other forward-looking statements will not be achieved or will prove to be inaccurate. Although the Company believes the expectations reflected in these forward-looking statements are reasonable, it can give no assurance that these expectations will prove to be correct.

The Company cautions readers against placing undue reliance on forward-looking statements when making decisions, as actual results could differ considerably from the opinions, plans, objectives, expectations, forecasts, estimates and intentions expressed in such forward-looking statements due to various material factors. Among others, these factors include: continuing access to required financing; continuing access to products that allow the Company and its subsidiaries to hedge exposure to changes in interest rates; risks of increasing default rates on leases, loans and advances; the adequacy of the Company's provisions for credit losses; increasing competition (including, without limitation, more aggressive risk pricing by competitors); increased governmental regulation of the rates and methods we use in financing and collecting on our equipment leases or loans; dependence on key personnel; disruption of business models due to the emergence of new technologies; fluctuations in the Canadian dollar and U.S. dollar exchange rate; and general economic and business conditions. The Company further cautions that the foregoing list of factors is not exhaustive.

For more information on the risks, uncertainties and assumptions that would cause the Company's actual results to differ from current expectations, please also refer to "Risk Factors" in this MD&A and in the Company's Annual Information Form, as well as to other public filings of the Company available at www.sedar.com. The Company does not undertake to update any forward-looking statements, whether oral or written, made by itself or on its behalf, except to the extent required by securities regulations.

NON-GAAP MEASURES

This MD&A makes reference to certain non-GAAP measures as supplementary information and to assist in assessing the Company's financial performance.

Management believes EBITDA and Adjusted EBITDA, as defined below, are useful measures in evaluating the performance of the Company. EBITDA and Adjusted EBITDA are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Adjusted EBITDA may not be comparable to similarly titled measures presented by other issuers. Readers are cautioned that EBITDA and Adjusted EBITDA should not be construed as an alternative to net income determined in accordance with GAAP as indicators of performance, or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows.

"Adjusted EBITDA" is EBITDA further adjusted for (i) interest on debt facilities, (ii) non-cash gain (loss) on interest rate derivatives, investments and convertible debentures, (iii) non-cash unrealized gain (loss) on foreign exchange, (iv) non-cash share-based compensation expense, (v) non-cash change in finance receivable allowance for credit losses (effective Q1 2018), (vi) acquisition costs, (vii) contingent consideration accretion or reduction, (viii) any unusual and material one-time gains or expenses and (ix)

actual interest attributable to the period in respect of the convertible debentures.

"EBITDA" is defined as net income adjusted to exclude interest, income taxes, depreciation and amortization.

"Free Cash Flow" ("FCF") is defined as Adjusted EBITDA less maintenance capital expenditures, tax effect of the non-cash change in the allowance for credit losses (effective Q1 2018) and tax expense.

"FCF L4PQ" is defined as FCF for the most recently completed four financial quarters for which the Company has publicly filed its consolidated financial statements (including its annual consolidated financial statements in respect of a fourth quarter).

"Maximum Permitted Dividends" is defined under Chesswood's credit facility as the maximum amount for cash dividends and purchases under its normal course issuer bid that the Company is permitted to pay in respect of a month, being 1/12 of 90% of the FCF L4PQ.

"Operating Income" is defined as "income before undernoted items" as presented in the consolidated statement of income.

COMPANY OVERVIEW

Chesswood is North America's only public company focused exclusively on commercial equipment finance for small and medium-sized businesses. As at December 31, 2018, its primary operations consisted of two wholly-owned subsidiaries:

- Pawnee Leasing Corporation ("Pawnee"), which finances micro and small-ticket commercial equipment for small and medium-sized businesses in the U.S.; and
- Blue Chip Leasing Corporation ("Blue Chip"), which provides commercial equipment financing to small and medium-sized businesses across Canada.

In early 2019, the Company launched Tandem Finance Inc., which will provide small and medium sized businesses of all credit profiles with financing for their equipment purchases through equipment vendors and distributors in the U.S.

PAWNEE

The Company's U.S. operations are primarily conducted by Pawnee, which accounted for 83.9% of consolidated revenue and 80.8% of consolidated operating income from continuing operations before corporate overhead in the year ended December 31, 2018.

Established in Fort Collins, Colorado in 1982, Pawnee specializes in providing equipment financing of up to U.S. \$250,000 to small and medium-sized businesses in the U.S., with a wide range of credit profiles from start-up

entrepreneurs to more established businesses, in prime and non-prime market segments, through a network of approximately 600 independent equipment finance broker firms. At December 31, 2018, approximately 52% of Pawnee's gross finance receivables were in the prime market segment.

As of December 31, 2018, Pawnee employed 94 full-time equivalent employees.

Pawnee Key Portfolio Statistics (in U.S.\$ thousands except # of leases/loans and %'s)

	Mar 31 2017	June 30 2017	Sep 30 2017	Dec 31 2017	Mar 31 2018 ⁽⁵⁾	June 30 2018	Sep 30 2018	Dec 31 2018
Number of leases and loans outstanding (#)	14,943	15,616	16,226	16,627	17,037	17,604	17,974	18,179
Gross lease and loan receivable ("GLR") ⁽¹⁾	\$309,120	\$337,276	\$362,846	\$398,053	\$427,100	\$465,526	\$493,370	\$515,439
Residual receivable	\$16,041	\$16,512	\$16,849	\$16,977	\$17,101	\$17,617	\$18,175	\$18,725
Net investment in leases and loans receivable, before allowance ⁽⁴⁾	\$248,557	\$273,390	\$296,655	\$327,608	\$352,431	\$384,643	\$408,957	\$426,065
Security deposits (nominal value) ⁽⁴⁾	\$11,135	\$11,510	\$11,915	\$12,325	\$12,734	\$13,330	\$13,763	\$13,787
Allowance for credit losses ⁽⁵⁾	\$6,555	\$6,848	\$8,602	\$8,482	\$15,309	\$15,895	\$15,489	\$15,904
Over 31 days delinquency (% of GLR) ⁽²⁾	2.19%	2.21%	2.69%	2.30%	2.10%	1.97%	1.83%	1.89%
Net charge-offs for the three-months ended ⁽³⁾	\$3,698	\$2,962	\$3,101	\$3,912	\$3,765	\$3,131	\$3,208	\$3,986
Provision for credit losses for the three-months ended ⁽⁵⁾	\$3,229	\$3,334	\$4,923	\$3,857	\$3,379	\$3,717	\$2,802	\$4,059

Notes:

(1) Excludes residual receivable.

(2) Over 31-days delinquency includes non-accrual gross lease and loan receivables.

(3) Excludes the "charge-offs" of interest revenue on finance leases and loans on non-accrual leases recognized under IFRS prior to 2018.

(4) Excludes adjustment for discounting security deposits and increasing unearned income for interest savings on security deposits.

(5) Provision for credit losses and allowance for credit losses included in the key portfolio statistics for the three months ended and as at March 31, 2018 and subsequent periods, were prepared in accordance with IFRS 9, Financial Instruments ("IFRS 9"). Prior period comparatives were prepared in accordance with IAS 39, Financial Instruments: Recognition and Measurement ("IAS 39") and have not been restated. Refer to Note 2 and Note 7 of the consolidated financial statements for further details.

Pawnee defines "start-up" businesses as those with less than two years of operating history. Start-up businesses do not fall into traditional credit categories because of their lack of business credit history. "B" credit businesses are those with two or more years of operating history that have some unique aspect to their overall credit profile such that they are not afforded an A-rated credit score, and/or that the business owner(s) do not have an A-rated personal or business/commercial credit history. "C" rated businesses have a credit profile that is weaker than "B" credit businesses. Pawnee further limits the transaction size for "C" businesses as one measure of mitigating risk.

These non-prime market niches are not usually considered by most conventional financing sources, and generally have a higher risk profile. To manage the incremental risk associated with financing businesses in these niches, Pawnee's management has built a stringent operating model that has historically enabled Pawnee to achieve higher net margins than many typical finance companies.

In September 2008, prior to the financial crisis and in pursuit of growth, Pawnee leveraged its existing sales channel of equipment finance brokers by expanding its range of products to include the B credit market. This market consists of higher

quality credits than Pawnee's historical market segment and is also a significantly larger segment. This was the first meaningful expansion from Pawnee's "core" suite of products.

As the financial crisis took hold in late 2008, Pawnee's portfolio also experienced more stress; however, it remained profitable by having maintained risk-adjusted pricing in the years leading up to the crisis that were in excess of most of its competitors. A large majority of Pawnee's competitors in both its traditional and B markets were gone by January 2009 having either retreated to their core markets, lost their funding and/or closed their operations.

Pawnee was fortunate, therefore, to be able to take advantage of its strong market position and continued access to capital to grow significantly while building a portfolio which, in each product "bucket", enjoyed unprecedented credit quality due to the also unprecedented contraction in credit markets, especially from 2009 through 2013. With the gradual normalization of credit markets, loss rates in Pawnee's higher yielding market segments are returning to more typical levels. Pawnee continues to generate excellent risk-adjusted returns, but at levels below the years immediately following the crisis, the same pattern seen in past economic cycles.

Beginning in 2015, Pawnee expanded its product line once more, by entering the prime or A-rated equipment finance market. Just as in 2008, when Pawnee entered the "B" market, this new market segment is much larger than the markets Pawnee had served previously. Pawnee now offers equipment financing to small and medium sized businesses across America in all credit classes with transactions up to U.S. \$250,000, and it may in the future finance equipment costing up to U.S.\$500,000 in the prime market.

These gradual expansions in Pawnee's product offerings have allowed it to become a much more important source of funding to its broker customers as well as expanding its overall market to include brokers with whom it did not have a prior business relationship. Many brokers concentrate on prime equipment finance customers, and therefore did not consider Pawnee as a source for the funding of leases and loans prior to its entry into the prime market.

Funding

Pawnee's leases and loans are presently funded through the following facilities:

- Chesswood's revolving corporate credit facility allows borrowings of up to U.S.\$250.0 million subject to, among other things, threshold levels of eligible

finance receivables, and is renewed to December 8, 2020.

- On October 16, 2017, Pawnee closed its first non-recourse U.S.\$75 million asset-backed facility, which is secured by a portfolio of Pawnee's prime equipment leases and loans. A second U.S.\$50 million facility was closed during 2018. The repayment terms are based on the cash flow of the underlying portfolio. The proceeds from these non-recourse facilities were applied to Chesswood's revolving corporate credit facility.
- In August 2018, Pawnee closed its new U.S.\$250 million warehouse facility with a syndicate of three major banks which expires in August 2023. The warehouse facility is used to fund most of Pawnee's prime originations before they are securitized.

Key Aspects of Business Model

Management believes Pawnee's long track-record of success is attributable to several key aspects of its business model, including:

1. credit underwriting parameters designed to mitigate risk;
2. a relationship-driven approach to origination through a well-established and trained network of reputable broker firms;
3. portfolio diversification across geographies, industries, equipment classes, origination source, vendors, equipment cost, and credit classes; and
4. risk management resources that include credit analyst reviews of all applications, a proprietary credit scorecard to guide consistent analysis and decision-making, and effectively price for risk; and a dedicated and efficient servicing and collection effort.

These four aspects are discussed in greater detail below.

1. Asset quality at Pawnee begins with underwriting parameters that define a conservative approach to doing business and mitigating risk. Generally:

- Pawnee finances equipment that is fundamental to the core operations of the lessee/borrower's business, reflecting management's view that payments on "business essential" equipment are among the least susceptible to default except in the case of business failure;
- Pawnee operates only in select market segments, excluding certain industries such as agriculture and hazardous materials;
- A personal guarantee of at least the major shareholder(s)/owner(s) and generally all owners

are obtained for non-prime credits, with acceptable personal credit profiles a prerequisite for credit approval;

- Business owners are interviewed by Pawnee for verification purposes prior to the commencement of the lease or loan, with site inspections conducted for financings as low as U.S.\$15,000 or more (U.S. \$100,000 for A-rated credits); and
- All scheduled payments for non-prime financings are paid by direct debit from the lessee's/borrower's account, allowing Pawnee's collection team to take immediate action on delinquencies.

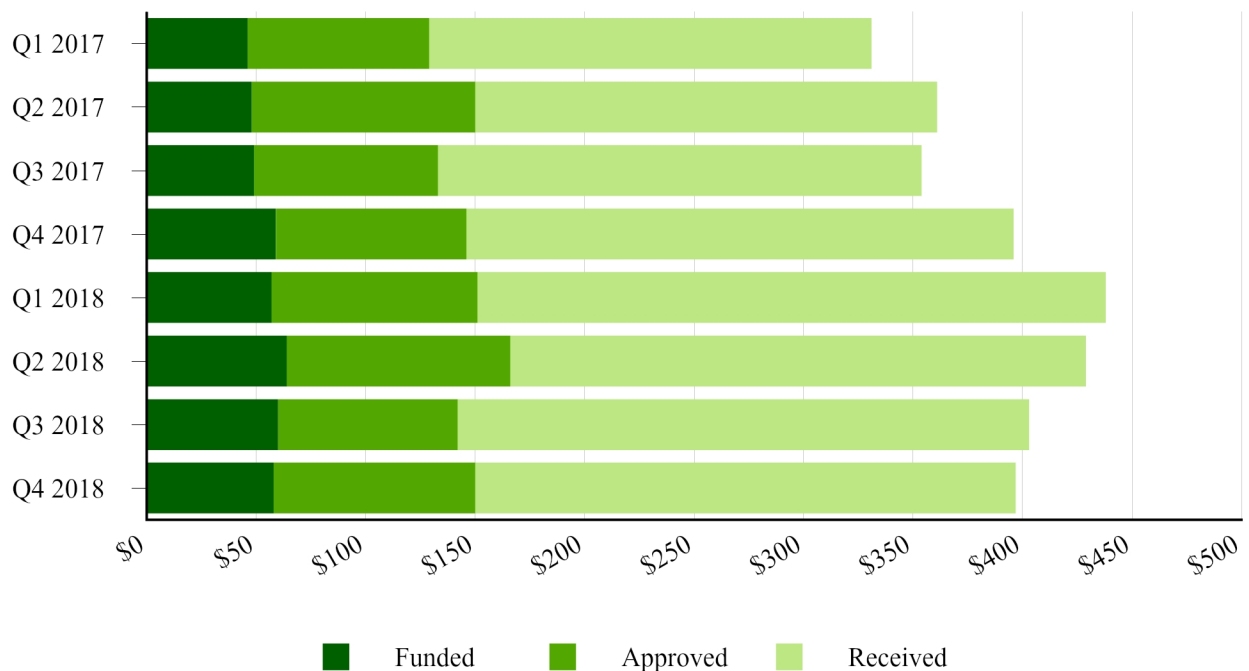
2. Pawnee originates finance receivables through a network of over 600 independent broker firms across the U.S., with a relationship-driven approach and service capabilities that have distinguished it as first-choice funder.

acceptable personal credit profile, industry references, and preferably a minimum one-year track record in the equipment finance industry. Pawnee's Business Development managers train new and existing brokers and their staff, and develop a knowledge base on Pawnee's underwriting policies and procedures. The training process is instrumental in reducing broker and Pawnee's time spent reviewing applicants unable to meet Pawnee's credit qualifications. Business Development managers also monitor broker efficiencies in credit application reviews and closings, including applications submitted, approved and ultimately funded.

Pawnee's service-driven focus strengthens the relationships with its customers, helping to support and expand origination volumes. It has become a funder of choice as a result of unique capabilities that improve efficiency and save time for its broker customers, such as consistent credit decisions; rapid response time, a customized broker portal (for application submissions, tracking of lease and loan status and documentation) and one-stop shopping for all credit-classes.

Risk management begins with the selection and training of broker firms and their staff. Broker principals must have an

Pawnee Lease and Loan Application, Approval and Origination Volume (in U.S.\$ millions)



3. Pawnee's portfolio of leases and loans is well diversified across geography, equipment types, industries, brokers, vendors, equipment cost, and credit classes.

As of December 31, 2018, Pawnee's portfolio of 18,179 leases and loans, representing U.S.\$515.4 million in gross finance receivables (excluding residual receivable), was diversified, with:

- over 86 equipment categories, with the five largest - restaurant, titled trucks, construction, medical and trailers - accounting for 47.0% of the total number of active leases and loans;
- over 229 industry segments, with no industry representing more than 15.1% of the number of active financings;
- no lessee/borrower accounting for more than 0.07% of the total;
- 48 U.S. states, with no state representing more than 10.0% of the number of total active leases and loans (with the exception of California and Texas, which represented 16.9% and 12.8%, respectively); and
- the largest originator accounting for 8.3% of gross lease and loan receivables, and the ten largest accounting for 39.1%.

Portfolio diversification is maintained, and rebalanced as necessary, through management's regular review of Pawnee's portfolio performance and lease and loan application, approval and origination volumes, for trends that may indicate changes in the economic or competitive landscape and that may necessitate adjustments in Pawnee's approach to doing business in specific market segments. Significant changes in these and other metrics may result in a detailed review of specific brokers, industry or equipment type, equipment cost, and/or geographic areas.

4. Risk management resources include a credit analyst's personal review of all applications, a proprietary credit scorecard to guide consistent decision-making and effectively pricing for risk, efficient servicing and collection processes, and other risk management tools.

Pawnee's credit process is not the automated scoring procedure typical of high volume equipment finance companies. Its success in selecting credit-worthy businesses is based on a model that engages both human expertise and the latest technology to meet clearly defined standards for asset quality in an efficient manner. A credit analyst personally reviews all applications and completes a proprietary scorecard designed to ensure all analysts are consistent in their credit reviews and to provide guidance in reaching prudent credit decisions.

Additionally, analysts are available to directly assist brokers submitting applications and personally communicate credit decisions, including information on how to improve the likelihood of approval, such as obtaining a business owner's personal credit information and/or guarantee.

Given the importance of limiting defaults to the greatest extent possible, Pawnee emphasizes the employment and retention of experienced personnel, and clearly delineated collection and portfolio servicing processes.

- Pawnee had 94 full-time equivalent employees at 2018 fiscal year-end, of which more than a third were engaged in the collection and servicing processes. Collection and servicing activities are structured to systematically and quickly resolve delinquent leases and loans whenever possible, mitigate losses, and collect post-default recovery dollars.
- Because of Pawnee's requirement that most lease and loan payments be made by direct debit, it can immediately recognize a delinquent account when a direct debit payment is not received on the required due date.
- Generally, when a payment falls 31 days past due, or earlier if investigation reveals an underlying issue at the borrower/lessee level, the account is referred to the appropriate negotiation, repossession/remarketing, bankruptcy or legal specialist on Pawnee's Advanced Collection Team. Through a combination of collecting payments, issuing forbearances, repossessing and selling financed equipment, initiating lawsuits and negotiating settlements, Pawnee regularly remediates a high percentage of past due accounts.
- After 154 days of delinquency, or earlier if Pawnee deems the account uncollectible, the debt is written off. However, collection efforts continue when prospects for recovery through a personal guarantor, sale of equipment or other remedy warrant. Otherwise, the account is normally assigned to an independent collection agency for further collection efforts, where the primary sources of recovery include payments on restructured accounts, settlements with guarantors, equipment sales, litigation, and bankruptcy court distributions.

Risk management tools and processes are continually monitored and improved to address changes in portfolio performance and in the equipment finance industry, and

periodically assessed by outside professionals with statistical expertise.

Pawnee's static pool loss analysis measures finance receivable loss performance by identifying a finite pool of transactions and segmenting it into quarterly or annual vintages according to origination date. Performance by

brokers, geographic area, equipment type, industry, transaction size, and product type are among the characteristics examined in these analyses. Underperforming portfolio segments are further examined to identify areas for underwriting adjustment and/or a change in funding guidelines or for other identifiable causes on which corrective action can be taken.

BLUE CHIP

Chesswood's Canadian operations are conducted by Blue Chip, a specialist in micro and small-ticket equipment finance for small and medium-sized businesses since 1996. Blue Chip accounted for 16.1% of consolidated revenue and 18.0% of consolidated operating income from continuing operations before corporate overhead in the year ended December 31, 2018.

Located in Toronto, Blue Chip provides equipment financing across Canada, through a nationwide network of more than 50 independent equipment finance broker firms and through direct, in-house origination efforts via equipment vendors.

Blue Chip's portfolio risk is mitigated by its diversification across geographies, industries, equipment types, equipment cost and credit classes. Blue Chip had 32 full-time equivalent employees at December 31, 2018.

Blue Chip Portfolio Statistics (in \$ thousands except # of leases/loans and %)

	Mar 31 2017	June 30 2017	Sep 30 2017	Dec 31 2017	Mar 31 2018 ⁽¹⁾	June 30 2018	Sep 30 2018	Dec 31 2018
Number of leases and loans outstanding (#)	12,278	12,910	13,345	13,781	14,188	14,587	14,494	14,253
Gross lease and loan receivable ("GLR")	\$152,502	\$162,164	\$166,505	\$170,183	\$175,681	\$190,466	\$191,365	\$189,917
Net investment in leases and loans receivable ("NIL"), before allowance	\$134,777	\$143,310	\$147,436	\$150,951	\$155,930	\$168,745	\$169,657	\$168,631
Allowance for credit losses ⁽¹⁾	\$1,438	\$1,621	\$1,702	\$1,284	\$1,731	\$1,974	\$2,127	\$2,233
Over 31 days delinquency (% of NIL)	0.66%	0.46%	0.36%	0.16%	0.34%	0.46%	0.19%	0.25%

(1) Allowance for credit losses as at March 31, 2018 and subsequent periods (included in the portfolio statistics above) were prepared in accordance with IFRS 9. Prior period comparatives were prepared in accordance with IAS 39 and have not been restated. Refer to Note 2 and Note 7 of the consolidated financial statements for further details.

Key Aspects of Business Model

Management believes Blue Chip's track record of success is attributable to several key aspects of its business model, including those described below.

Blue Chip has successfully grown originations and earnings by filling a market void created by the tendency of Canadian bank competitors to have slower small ticket processes and a preference to finance larger-ticket equipment, and by Blue Chip's nimbleness in addressing customer needs as an efficient and consistent "one-stop" funding source.

- The micro-ticket segment is a high-volume, low-touch business. Blue Chip has an application,

approval and funding process designed to speed up credit decisions and automate the preparation of secure documents to meet market demand for rapid funding and customer service excellence.

- Blue Chip also has the expertise in financial analysis and detailed documentation to meet the underwriting requirements of the small-ticket segment.
- Like Pawnee, Blue Chip's value proposition to originators is relationship and service based, with fast and predictable credit decision-making and the convenience of one-stop shopping for commercial equipment financing needs across all credit classes.

Blue Chip's portfolio risk is mitigated by its diversification across geography, origination sources, industry, equipment type, equipment cost and credit class.

As at December 31, 2018, Blue Chip's gross finance receivables portfolio of \$189.9 million (2017: \$170.2 million) consisting of 14,253 leases and loans (2017: 13,781) was well diversified:

- Ontario represented 45.4% of net finance receivables, Alberta represented 20.9% and 33.7% were from the other provinces;
- the five largest equipment categories by volume - industrial, construction, photographic, truck and trailers - accounted for 55.8% of net finance receivables;
- of its network of more than 50 originators, the largest originator by dollar volume during 2018 accounted for 15% originations; and
- the four largest brokers by dollars financed accounted for approximately 52% of originations during 2018.

Effective risk management has made Blue Chip a solid performer in its markets throughout business cycles.

- In line with Pawnee, Blue Chip has an intense focus on thorough credit analysis, consistent decision-making, risk-based pricing, careful broker selection and education, a strong collection effort, and management's continual evaluation of portfolio performance against key performance indicators.

Blue Chip's performance has been enhanced by its success in negotiating a competitive cost of funds.

- The majority of Blue Chip's leases and loans are financed by securitization and bulk lease financing facilities, whereby it sells or assigns the future payment stream of a tranche of leases/loans, on a discounted basis, to a third-party such as a life insurance company or bank. A small percentage of the proceeds is held back in a loss reserve pool or supported by Blue Chip through a letter of guarantee in favour of the funder.
- Blue Chip's multiple funding partners have rigorous monitoring and audit processes, including thorough initial portfolio reviews; site visits; file audits to validate credit decisions, documentation accuracy and security perfection; and monthly compliance certificates attesting to the correctness of portfolio and financial statistics.
- Blue Chip also uses Chesswood's revolving credit facility to provide some operational and warehouse funding.
- Blue Chip recognizes its revenue over the full-term of its finance receivables and not through "gain-on-sale" accounting.

DISCONTINUED OPERATIONS AND WINDSET

WINDSET

For accounting purposes, Windset Capital Corporation ("Windset") is not considered a discontinued operation and its results continue to be grouped with Pawnee in the segment reporting note to the consolidated financial statements (see Note 27 - *Segment Information*).

Windset ceased accepting loan applications in September 2016, but continued to service its existing portfolio for the full-term of the loans. Almost all of the portfolio was collected in 2017, with the remaining \$107,000 collected in 2018.

DISCONTINUED OPERATIONS

Case Funding Inc. ("Case Funding"), a specialty provider of loans and funding solutions to attorneys and law firms, sold its assets in 2015, except for a small portfolio of receivables. At December 31, 2018, there were 110 advances and loans outstanding totaling \$1.9 million (December 31, 2017 - 180 advances and loans totaling \$3.4 million).

SELECTED FINANCIAL INFORMATION

(\$ thousands, except per share figures)

	2016 ⁽⁵⁾	2017 ⁽⁶⁾	2018 ⁽⁷⁾
Average foreign exchange rate for the year	1.3248	1.2986	1.2957
Revenue ⁽¹⁾	\$ 91,583	\$ 95,324	\$ 110,586
Finance margin	\$ 55,940	\$ 58,972	\$ 64,516
Income before tax and other items (Operating Income) ⁽²⁾	\$ 30,310	\$ 32,075	\$ 33,704
Income from continuing operations	\$ 17,317	\$ 25,751	\$ 23,343
Net income	\$ 24,278	\$ 25,431	\$ 22,885
Basic earnings per share - continuing operations ⁽¹⁾⁽³⁾	\$0.97	\$1.43	\$ 1.31
Diluted earnings per share - continuing operations ⁽¹⁾⁽³⁾	\$0.95	\$1.39	\$ 1.28
Basic earnings per share ⁽³⁾	\$1.36	\$1.41	\$ 1.28
Diluted earnings per share ⁽³⁾	\$1.33	\$1.37	\$ 1.25
Foreign exchange rate as at year end	1.3427	1.2545	1.3642
Total assets	\$ 527,937	\$ 643,612	\$ 818,187
Long-term financial liabilities	\$ 354,800	\$ 447,412	\$ 639,092
Adjusted EBITDA ⁽²⁾	\$ 31,031	\$ 31,860	\$ 35,013
Dividends declared ⁽⁴⁾⁽⁵⁾	\$ 22,963	\$ 15,147	\$ 15,044
Dividends declared per share ⁽⁴⁾⁽⁵⁾	\$1.29	\$0.84	\$0.84

(1) It was determined that Case Funding meets the criteria of discontinued operations for each of the years displayed above. See Note 5 - *Discontinued Operations* in the 2018 audited consolidated financial statements. EcoHome Financial Inc. ("EcoHome"), a consumer financing company, was sold in February 2016 for approximately \$35.0 million resulting in a gain of \$6.7 million (net of taxes and costs). The gain on sale and its operating results for a month and half are included in 2016 income from discontinued operations, see the 2016 Annual Report for more details.

(2) Adjusted EBITDA and Operating Income are non-GAAP measures. See "Non-GAAP Measures" above for the definitions.

(3) Based on weighted average shares outstanding during the period for income attributable to common shareholders.

(4) Includes dividends on Exchangeable Securities (non-controlling interest, as described below under "Statement of Financial Position").

(5) In Q1 2016, a special dividend of \$0.50 per share, or \$8.9 million in total, was declared following the sale of EcoHome and was paid on March 15, 2016.

(6) As a result of the 2017 U.S. Tax Cuts and Jobs Act, the U.S. subsidiaries' net deferred tax liabilities were revalued, resulting in a \$9.4 million reduction in future taxes expense and deferred tax liabilities.

(7) Provision for credit losses and allowance for credit losses included in the selected financial information for 2018 were prepared in accordance with IFRS 9. Prior period comparatives were prepared in accordance with IAS 39, and have not been restated. Refer to Note 2 - *New Accounting Standards* and Note 7 - *Finance Receivables* of the consolidated financial statements for further details.

As at and for the quarter-ended (\$ thousands, except per share figures)	2017				2018 ⁽⁵⁾			
	Q1	Q2	Q3	Q4 ⁽⁴⁾	Q1	Q2	Q3	Q4
Revenue ⁽⁶⁾	\$ 23,051	\$ 24,286	\$ 23,355	\$ 24,632	\$ 25,185	\$ 27,012	\$ 28,898	\$ 29,491
Finance margin before expenses	14,859	16,130	13,014	14,969	15,409	15,736	17,574	15,797
Income before tax and other items (Operating Income) ⁽¹⁾	8,049	9,290	6,718	8,018	8,339	8,046	9,415	7,904
Income before tax	7,452	7,026	5,527	7,806	8,427	8,221	9,280	6,788
Provision for taxes ⁽⁴⁾	2,768	3,080	2,220	(6,008)	2,529	2,572	3,007	1,265
Income from continuing operations	4,684	3,946	3,307	13,814	5,898	5,649	6,273	5,523
Income from discontinued operations	12	(197)	(119)	(16)	2	(33)	(181)	(246)
Net income	\$ 4,696	\$ 3,749	\$ 3,188	\$ 13,798	\$ 5,900	\$ 5,616	\$ 6,092	\$ 5,277
Basic EPS - continuing operations ⁽²⁾	\$0.26	\$0.22	\$0.19	\$0.76	\$0.33	\$0.31	\$0.35	\$0.32
Diluted EPS - continuing operations ⁽²⁾	\$0.25	\$0.21	\$0.19	\$0.74	\$0.32	\$0.31	\$0.34	\$0.31
Basic earnings per share ⁽²⁾	\$0.26	\$0.21	\$0.18	\$0.76	\$0.33	\$0.31	\$0.34	\$0.30
Diluted earnings per share ⁽²⁾	\$0.25	\$0.20	\$0.18	\$0.74	\$0.32	\$0.31	\$0.33	\$0.29
Total assets	\$ 547,686	\$ 573,414	\$ 593,065	\$ 643,612	\$ 685,593	\$ 748,732	\$ 766,310	\$ 818,187
Long-term liabilities	\$ 377,735	\$ 404,784	\$ 428,752	\$ 447,412	\$ 515,590	\$ 575,289	\$ 589,702	\$ 639,092
<u>Other Data</u>								
Adjusted EBITDA ⁽¹⁾	\$ 8,092	\$ 9,089	\$ 6,669	\$ 8,010	\$ 8,033	\$ 9,476	\$ 9,224	\$ 8,280
Dividends declared ⁽³⁾	\$ 3,779	\$ 3,787	\$ 3,790	\$ 3,791	\$ 3,784	\$ 3,764	\$ 3,759	\$ 3,737
Dividends declared per share	\$0.21	\$0.21	\$0.21	\$0.21	\$0.21	\$0.21	\$0.21	\$0.21

(1) Adjusted EBITDA and Operating Income are non-GAAP measures. See “Non-GAAP Measures” above for the definitions.

(2) Based on weighted average shares outstanding during the period for income attributable to common shareholders.

(3) Includes dividends on Exchangeable Securities (non-controlling interest, as described below under "Statement of Financial Position").

(4) As a result of the 2017 U.S. Tax Cuts and Jobs Act, the U.S. subsidiaries' net deferred tax liabilities were revalued, resulting in a \$9.4 million reduction in future taxes expense and deferred tax liabilities which was recorded in Q4 2017.

(5) Provision for credit losses and allowance for credit losses included in the selected financial information for 2018 were prepared in accordance with IFRS 9. Prior period comparatives were prepared in accordance with IAS 39, and have not been restated. Refer to Note 2 and Note 7 of the consolidated financial statements for further details.

ADJUSTED EBITDA, FREE CASH FLOW, MAXIMUM PERMITTED DIVIDENDS ⁽¹⁾

For the quarter-ended (\$ thousands)	2017				2018 ⁽⁵⁾			
	Q1	Q2	Q3	Q4 ⁽⁴⁾	Q1	Q2	Q3	Q4
Net income ⁽⁵⁾	\$ 4,696	\$ 3,749	\$ 3,188	\$ 13,798	\$ 5,900	\$ 5,616	\$ 6,092	\$ 5,277
Interest expense	3,131	3,538	3,868	4,731	5,257	6,211	7,213	7,966
Provision for taxes ⁽⁴⁾	2,768	3,080	2,220	(6,008)	2,529	2,572	3,007	1,265
Amortization and depreciation	421	449	626	636	632	450	458	478
EBITDA ⁽¹⁾	11,016	10,816	9,902	13,157	14,318	14,849	16,770	14,986
Interest expense	(3,131)	(3,538)	(3,868)	(4,731)	(5,257)	(6,211)	(7,213)	(7,966)
Non-cash change in finance receivables allowance for credit losses ⁽⁶⁾					(628)	982	(368)	242
Share-based compensation expense	266	206	280	213	262	364	233	235
Financing costs - convertible debenture	(20)	710	(100)	540	(29)	—	—	—
Interest expense on convertible debenture	(321)	(324)	(328)	(328)	(61)	—	—	—
Contingent consideration reduction	—	—	—	(538)	—	—	—	—
Unrealized loss (gain) on investments	544	1,117	876	332	151	—	—	30
Foreign exchange unrealized loss (gain)	(11)	3	31	95	36	52	58	(117)
Unrealized loss (gain) – interest rate derivatives	(251)	99	(124)	(730)	(759)	(560)	(256)	870
Adjusted EBITDA ⁽¹⁾	8,092	9,089	6,669	8,010	8,033	9,476	9,224	8,280
Maintenance capital expenditures	(7)	(102)	(6)	(68)	(69)	(10)	(56)	(50)
Tax impact of change in allowance for credit losses ⁽⁶⁾					166	(263)	98	(53)
Provision for taxes	(2,768)	(3,080)	(2,220)	6,008	(2,529)	(2,572)	(3,007)	(1,265)
Free Cash Flow ⁽¹⁾	\$ 5,317	\$ 5,907	\$ 4,443	\$ 13,950	\$ 5,601	\$ 6,631	\$ 6,259	\$ 6,912
FCF L4PQ divided by 4 ⁽¹⁾⁽³⁾	\$ 5,268	\$ 4,912	\$ 4,871	\$ 4,824	\$ 5,666	\$ 7,452	\$ 7,596	\$ 7,959
Maximum Permitted Dividends ⁽¹⁾⁽³⁾	\$ 4,741	\$ 4,421	\$ 4,384	\$ 4,342	\$ 5,100	\$ 6,707	\$ 6,837	\$ 7,163
Dividends declared ⁽²⁾	\$ 3,779	\$ 3,787	\$ 3,790	\$ 3,791	\$ 3,784	\$ 3,764	\$ 3,759	\$ 3,737

(1) Adjusted EBITDA, EBITDA, Free Cash Flow, FCF L4PQ (Free Cash Flow for the last four published quarters) and Maximum Permitted Dividends are non-GAAP measures. See “Non-GAAP Measures” above for the definitions.

(2) Includes dividends on Exchangeable Securities (non-controlling interest, as described below under "Statement of Financial Position").

(3) The FCF L4PQ is calculated on a monthly basis as required by the terms of Chesswood's revolving credit line. This calculation uses Chesswood's most recent four quarters' published results at any one point in time, divided by twelve. The FCF L4PQ, in any one quarter, is the basis for the Maximum Permitted Dividends in that quarter (90% of FCF L4PQ) and will not include the FCF for the currently published quarter as they are released/published after the final month of the respective reporting period.

(4) As a result of the 2017 U.S. Tax Cuts and Jobs Act, the U.S. subsidiaries' net deferred tax liabilities were revalued, resulting in a \$9.4 million reduction in future taxes expense and deferred tax liabilities which was recorded in Q4 2017.

(5) Provision for credit losses included in the net income for 2018 was prepared in accordance with IFRS 9. Prior period comparatives were prepared in accordance with IAS 39 and have not been restated. Refer to Note 2 and Note 7 of the consolidated financial statements for further details.

(6) Effective for Q1 2018, and in keeping with the revised calculation of Free Cash Flow as agreed upon with our lenders, the formulas for Consolidated Adjusted EBITDA and Free Cash Flow have been amended to adjust for the non-cash change in finance receivables' allowance for credit losses included in the provisions for credit losses in the income statement as well as the related tax effect of this non-cash change. As a result of this, on a go-forward basis since the first quarter of 2018, Consolidated Adjusted EBITDA and Free Cash Flow includes only the actual net credit losses incurred in the quarter. Management believes that this change enhances the usefulness of Adjusted EBITDA and Free Cash Flow as performance measures and is a more appropriate method of calculation as it removes the volatility associated with the effect of estimates and assumptions for a non-cash item.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2018 AND 2017

The Company reported consolidated net income of \$5.3 million for the three months ended December 31, 2018 compared to \$13.8 million in the same period of 2017, a decrease of \$8.5 million year-over-year. The Q4 2017 results includes a one-time future tax recovery of \$9.4 million resulting from the revaluation of our U.S. subsidiaries' net deferred tax liabilities due to the U.S. Tax Cuts and Jobs Act passed in December 2017, which accounts for the majority of the decrease in net income for the three month period year-over-year. Net unrealized fair value adjustments and other items also decreased \$904,000 compared to 2017, quarterly operating income decreased \$114,000 year-over-year, and tax expense (other than the one-time item in Q4 2017) was down \$2.1 million due to the decreased in tax rates in the U.S. year-over-year. U.S. dollar results for the three months ended December 31, 2018 were converted at an exchange rate of 1.3204, which was the average exchange rate for Q4 2018 (Q4 2017 - 1.2713).

	Three months ended December 31, 2018				
	Equipment Financing - U.S.	Equipment Financing - Canada	Discontinued Operations (Note 5)	Corporate Overhead - Canada	Total
(\$ thousands)					
Interest revenue on leases and loans	\$ 22,823	\$ 3,484		\$ —	\$ 26,307
Ancillary finance and other fee income	2,104	1,001		79	3,184
Interest expense	(6,586)	(1,380)		—	(7,966)
Provision for credit losses	(5,626)	(102)		—	(5,728)
Finance margin	12,715	3,003		79	15,797
Personnel expenses	2,673	647		394	3,714
Share-based compensation expense	64	5		166	235
Other expenses	2,682	548		569	3,799
Depreciation - property and equipment	144	1		—	145
Income before undernoted items	7,152	1,802		(1,050)	7,904
Amortization - intangible assets	—	(333)		—	(333)
Fair value adjustments - investments	—	—		(30)	(30)
Unrealized loss on interest rate derivatives	(380)	—		(490)	(870)
Unrealized gain on foreign exchange	—	—		117	117
Income before taxes	6,772	1,469		(1,453)	6,788
Tax expense	802	274		189	1,265
Income from continuing operations	5,970	1,195		(1,642)	5,523
Loss from discontinued operations	—	—	\$ (246)	—	(246)
Net income	\$ 5,970	\$ 1,195	\$ (246)	\$ (1,642)	\$ 5,277
Net cash used in operating activities	\$ (22,499)	\$ 1,965	\$ 62	\$ (908)	\$ (21,380)
Net cash used in investing activities	\$ (50)	\$ —	\$ —	\$ —	\$ (50)
Net cash from financing activities	\$ 63,286	\$ 1,166	\$ —	\$ (45,347)	\$ 19,105
Property and equipment expenditures	\$ 50	\$ —	\$ —	\$ —	\$ 50

	Three months ended December 31, 2017				
	Equipment Financing - U.S.	Equipment Financing - Canada	Discontinued Operations (Note 5)	Corporate Overhead - Canada	Total
(\$ thousands)					
Interest revenue on leases and loans	\$ 18,642	\$ 2,926		\$ —	\$ 21,568
Ancillary finance and other fee income	1,877	1,040		147	3,064
Interest expense	(3,610)	(1,121)		—	(4,731)
Provision for credit losses	(4,666)	(266)		—	(4,932)
Finance margin	12,243	2,579		147	14,969
Personnel expenses	2,435	770		300	3,505
Share-based compensation expense	64	(37)		186	213
Other expenses	2,124	408		578	3,110
Depreciation - property and equipment	117	6		—	123
Income before undernoted items	7,503	1,432		(917)	8,018
Amortization - intangible assets and contingent consideration reversal	—	(513)		538	25
Fair value adjustments - convertible debentures and investments	—	—		(872)	(872)
Unrealized gain on interest rate derivatives	192	—		538	730
Unrealized loss on foreign exchange	—	—		(95)	(95)
Income before taxes	7,695	919		(808)	7,806
Tax expense (recovery)	(6,596)	35		553	(6,008)
Income from continuing operations	14,291	884		(1,361)	13,814
Loss from discontinued operations	—	—	\$ (16)	—	(16)
Net income	\$ 14,291	\$ 884	\$ (16)	\$ (1,361)	\$ 13,798
Net cash used in operating activities	\$ (39,640)	\$ (1,233)	\$ 482	\$ (4,786)	\$ (45,177)
Net cash used in investing activities	\$ (144)	\$ —	\$ —	\$ —	\$ (144)
Net cash from financing activities	\$ 87,826	\$ 3,128	\$ —	\$ (51,648)	\$ 39,306
Property and equipment expenditures	\$ 144	\$ —	\$ —	\$ —	\$ 144

In the three months ended December 31, 2018, consolidated operating income (“income before undernoted items”) from continuing operations was \$7.9 million, compared to \$8.0 million in the same period in the prior year, a decrease of \$114,000, or 1.4%.

By segment, Pawnee and Windset's operating income for the quarter decreased by \$351,000 compared to the same period in the prior year. Pawnee's revenue totaled \$24.9 million in the three months ended December 31, 2018, an increase of \$4.4 million compared to the same period in the prior year, due to growth in the finance receivables. As part of the process of reviewing and adopting IFRS 15, *Revenue from Contracts with Customers*, we have reclassified \$1.0 million of certain revenue items from Ancillary finance and other fee income to Interest revenue on leases and loans in 2018 and \$1.1 million in 2017.

Pawnee's interest expense totaled \$6.6 million in the three months ended December 31, 2018, compared to \$3.6 million in the same period of the prior year, an increase of \$3.0 million. The increased interest expense is as a result of three factors: a much larger portfolio of finance receivables and a corresponding increase in debt, rising interest rates and some significant fees incurred in the execution of Pawnee's first securitizations and warehousing facilities. Higher fees are expected when initially entering the securitization markets, in order to build out the structures and processes needed to support this type of treasury activity.

The change in Pawnee's portfolio delinquency rate from the third quarter was very modest for what is usually a cyclically weak quarter due to the holiday season (Q4 2018 1.89% vs Q3 2018 1.83%). Actual net charge-offs in the three month period were relatively flat year-over-year, even though our finance receivable portfolio was much larger. Of the

\$960,000 increase in provision for credit losses, \$365,000 was the result of an increase in the foreign exchange rate year-over-year. Pawnee's provision for credit losses, prepared under IFRS 9, would have been \$190,000 higher in the three months ended December 31, 2018 if it were prepared in accordance with the IAS 39 standard used in the 2017 comparative results.

Personnel and other expenses at Pawnee increased by \$796,000 in the quarter compared to the same period last year due to increased headcount (approx. 10 more employees year-over-year) and other expenses related to the growth in the finance receivables. Of the \$558,000 increase in other expenses, collection related costs increased by \$200,000 in the three month period; however, the increased funds recovered is netted against the provision for credit losses.

Blue Chip generated operating income of \$1.8 million in the quarter compared to \$1.4 million in the same period last year, an increase of \$370,000. Blue Chip's provision for credit losses in the three months ended December 31, 2018 would have been \$155,000 higher if using the same accounting method that was used in the 2017 comparative results.

Corporate overhead before other items increased by \$133,000 year-over-year, mainly from a \$94,000 increase in personnel expenses, a \$68,000 decrease in interest income on loans to EcoHome offset by a \$9,000 decrease in general and administrative expenses and a \$20,000 decrease in share-based compensation.

The market value of the Company's investment in Dealnet Capital Corp. ("Dealnet") common shares decreased \$30,000 in the three months ended December 31, 2018 compared to a decrease in value of \$332,000 in the same period of 2017 resulting in an increase in net income of \$302,000 year-over-year.

As the Company's convertible debentures were redeemed in January 2018, there was no non-cash unrealized mark-to-market adjustment in Q4 2018 compared to an unrealized loss of \$540,000 in the same period in the prior year, translating to an increase in net income of \$540,000 year-over-year.

The non-cash unrealized mark-to-market adjustment on interest rate derivatives for the three months ended December 31, 2018 totaled a loss of \$870,000 compared to a gain of \$730,000 in the same period in the prior year, translating to a decrease in net income of \$1.6 million year-over-year.

The provision for taxes for the three months ended December 31, 2018 totaled \$1.3 million compared to the recovery of taxes of \$6.0 million in the same period in the

prior year. The Q4 2017 tax expense includes a future tax recovery of \$9.4 million resulting from the revaluation of our U.S. subsidiaries' net deferred tax liabilities due to the U.S. Tax Cuts and Jobs Act passed in December 2017. The \$1.3 million for the three months ended December 31, 2018 is comprised of current tax expense of \$856,000, future tax expense of \$232,000, and \$177,000 in withholding tax expense on inter-company dividends. The effective tax rate differs from the Canadian statutory tax rate due to permanent differences between accounting and taxable income, which primarily include share-based compensation expense.

The loss from discontinued operations in the three months ended December 31, 2018 totaled \$246,000 compared to a loss of \$16,000 recorded in the same period in 2017. The loss from discontinued operations relates to the wind-down of Case Funding's remaining legal finance receivables.

RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

The Company reported consolidated net income of \$22.9 million in the year ended December 31, 2018 compared to \$25.4 million in 2017, a decrease of \$2.5 million year-over-year. The decrease is mostly comprised of a \$7.3 million increase in tax expense, the 2017 results included a future tax recovery of \$9.4 million as a result of the revaluation of our U.S. subsidiaries' net deferred tax liabilities due to the U.S. Tax Cuts and Jobs Act passed in December 2017; without that one-time recovery, tax expense is actually down \$2.1 million year-over-year. The increase in taxes was partially offset by a \$3.3 million increase in net unrealized fair value adjustments and other items compared to 2017 and a \$1.6 million increase in operating income.

The adoption of IFRS 9, the repayment of our convertible debentures and the change in exchange rates have significantly impacted our results from a comparative perspective, and therefore the table below adjusts for these factors for a more meaningful comparison of our operating income for 2018:

Average FX rate	1.2957	1.2986	
	For the years ended		
	December 31,		
<i>(\$ thousands)</i>	2018	2017	Change
Operating income	\$ 33,704	\$ 32,075	\$ 1,629
IFRS 9 impact <i>(a)</i>	573	—	573
Impact of FX rate <i>(b)</i>	100	—	100
Interest exp on conv deb <i>(c)</i>	(61)	(1,300)	1,239
Operating income normalized	\$ 34,316	\$ 30,775	\$ 3,541

For 2018, consolidated operating income ("income before undernoted items") from continuing operations was \$33.7 million, compared to \$32.1 million in the same period in the prior year, an increase of \$1.6 million, or 5.1%, before considering the items noted in the chart above.

(a) While the provision for credit losses is down \$1.7 million year-over-year, the Company's provision for credit losses would have been a further \$573,000 lower in the year ended December 31, 2018 if the same accounting guidelines used in the prior year had been used in 2018. The provision for credit losses for the year ended December 31, 2018 was calculated in accordance with IFRS 9. Prior period comparatives were prepared in accordance with IAS 39, and have not been restated.

(b) U.S. dollar results for the year ended December 31, 2018 were converted at an exchange rate of 1.2957, which was the average exchange rate for the period (2017 - 1.2986). This lower exchange rate compared to 2017 understates the improvement in 2018 U.S. operating results compared in 2017 by \$100,000.

(c) Prior to redemption in January 2018, convertible debenture interest expense was not part of operating income whereas the interest expense on the funds used to repay the debentures (from Chesswood's corporate revolving credit facility) is deducted as an expense in calculating operating income in 2018.

By segment, Pawnee and Windset's operating income increased by \$1.1 million compared to the same period in the prior year. Pawnee's revenue totaled \$92.5 million, an increase of \$13.1 million year-over-year. A \$14.0 million growth in Pawnee's revenue due to growth in its portfolio was offset by an \$893,000 decrease in Windset's revenue as Windset's portfolio completes its wind down. As part of the process of reviewing and adopting IFRS-15, *Revenue from Contracts with Customers*, we have reclassified \$4.4 million of certain revenue items from Ancillary finance and other fee income to Interest revenue on leases and loans in 2018 and \$4.1 million in 2017.

Pawnee's interest expense totaled \$21.6 million in the year ended December 31, 2018, compared to \$11.1 million in the same period of the prior year. The increased interest expense is as a result of three factors: a much larger portfolio of finance receivables and a corresponding increase in debt, rising interest rates and some significant fees incurred in the execution of Pawnee's first securitizations and warehousing facilities. Higher fees are expected when initially entering the securitization markets, in order to build out the structures and processes needed to support this type of treasury activity.

The delinquencies in Pawnee's non-prime portfolio improved at December 31, 2018 compared to the prior year, which helped contribute to a \$1.9 million decrease in the provision for credit losses year-over-year. Windset's provision for credit losses was \$532,000 lower in 2018 compared to the prior year, due to the wind down of its portfolio. Pawnee's provision for credit losses, prepared under IFRS 9, would have been \$172,000 higher in 2018 if it were prepared in accordance with the IAS 39 standard used in the 2017 comparative results.

Personnel and other expenses at Pawnee and Windset increased by \$3.4 million year-over-year, reflecting support for the growth in new business volumes and size of the portfolio. Pawnee had approximately 10 more staff during the year ended December 31, 2018, compared to the prior year, when Pawnee was still building out its resources to support its very strong growth and customer service levels. Year-over-year therefore, the increased staffing level resulted in an increase in personnel expenses of \$1.4 million. The largest increase in other expenses was collection related costs, which increased \$640,000 in the year ended December 31, 2018 compared to the prior year; however, the increased funds recovered is netted against the provision for credit losses. The effects of a lower foreign exchange rate this year lowered operating income by \$100,000 year-over-year.

Blue Chip generated operating income of \$6.8 million in the year ended December 31, 2018, compared to \$5.9 million in the prior year, an increase of \$872,000 due to growth in the finance receivable portfolio while maintaining effective cost controls, and after being impacted by the effects of IFRS 9 adoption. Blue Chip's provision for credit losses is \$745,000 higher in the year ended December 31, 2018 as a result of the new requirements under IFRS 9.

Corporate overhead before other items increased by \$345,000 year-over-year, as a result of a \$246,000 increase in personnel expenses, an \$83,000 increase in share-based compensation expense, and a \$23,000 increase in general and administrative expenses, offset by a \$7,000 increase in interest income on Chesswood's loan to EcoHome.

The Company's investment in Dealnet common shares decreased in market value by \$181,000 in the year ended December 31, 2018 compared to a \$2.9 million decrease in the prior year resulting in an increase in net income of \$2.7 million year-over-year.

The non-cash unrealized mark-to-market adjustment gain on the Company's convertible debentures was an unrealized gain of \$29,000 compared to an unrealized loss of \$1.1 million in the prior year, translating to an increase in net income of \$1.2

million year-over-year. The convertible debentures were redeemed in January 2018.

The non-cash unrealized mark-to-market adjustment on interest rate derivatives for the year ended December 31, 2018 totaled a gain of \$705,000 compared to a gain of \$1.0 million in the prior year, translating to a decrease in net income of \$301,000 year-over-year.

The provision for taxes for the year ended December 31, 2018 totaled \$9.4 million, compared to \$2.1 million in the prior year. The 2017 tax expense included a one-time future tax recovery of \$9.4 million resulting from the revaluation of our U.S. subsidiaries' net deferred tax liabilities due to the U.S. Tax Cuts and Jobs Act passed in December 2017. Without that one-time recovery in 2017, tax expense would have been lower by \$2.1 million year-over-year. The \$9.4 million provision for taxes for the year ended December 31, 2018 is comprised of \$6.4 million in current tax expense, future tax expense of \$2.2 million, and \$795,000 in withholding tax expense on inter-company dividends. The effective tax rate differs from the Canadian statutory tax rate due to withholding taxes and permanent differences between accounting and taxable income, which include share-based compensation expense.

See Note 27 - *Segment Information* in the notes to the Company's consolidated financial statements for a breakdown of operating results and other information by industry segment and geographic location.

STATEMENT OF FINANCIAL POSITION

The total consolidated assets of the Company at December 31, 2018 were \$818.2 million, an increase of \$174.6 million from December 31, 2017. The U.S. dollar exchange rate on December 31, 2018 was 1.3642, compared to 1.2545 at December 31, 2017. The increase in the foreign exchange rate represents an increase of \$38.2 million in assets.

Cash totaled \$2.3 million at December 31, 2018 compared to \$3.6 million at December 31, 2017, a decrease of approximately \$1.3 million. The Company's objective is to maintain low cash balances, investing any free cash in finance receivables as needed and using any excess to pay down debt on the primary financing facilities. Please see the Liquidity and Capital Resources overview section of this MD&A for a discussion of cash movements during the periods ended December 31, 2018 and 2017.

Assets held for sale consist of Case Funding's legal finance receivables for funds advanced to plaintiffs, attorneys, and for the purchase of medical liens relating to plaintiff cases. At December 31, 2018, there were 110 advances and loans outstanding totaling \$1.9 million (December 31, 2017 - 180 advances and loans totaling \$3.4 million). The advances and loans are due when the underlying cases are settled. The number of days the receivable is outstanding does not necessarily indicate the likelihood of impairment. It is normal for receivables in the legal finance industry to be outstanding anywhere from six months to 48 months (or longer). The collectability of loans and/or advances made by Case Funding depends on litigation outcomes in the form of judgments and/or settlements. Once an advance/loan is made, the timing of the collection cycle is out of Case Funding's control. Therefore, the timing of actual collections will be irregular.

Other assets totaled \$8.8 million at December 31, 2018, a decrease of \$8.8 million from December 31, 2017. The receipt of \$4.7 million in tax refunds in 2018 account for approximately half of the decrease year-over-year. Other assets included in this total relate to the sale of EcoHome in 2016 and totaled \$5.4 million at December 31, 2018 compared to \$10.3 million at December 31, 2017. In relation to the sale of EcoHome, the non-cash consideration received included a \$2.5 million convertible note (repaid in Q1 2018) and 6,039,689 Dealnet common shares. The fair value of the common shares represents the trading price at each reporting date, and the value at December 31, 2018 totaled \$453,000. Other assets also includes a loan receivable from EcoHome representing the inter-company warehouse funding for leases and loans that had not yet been securitized with EcoHome funders. The value at December 31, 2018 totaled \$4.9 million. This loan matures in October 2020 and is secured by specific leases and loans as well as a general security agreement over all of the assets of EcoHome. The loan has fixed monthly principal payments, and related interest based on a floating interest rate plus a fixed margin. See Note 6 - *Other Assets* in the consolidated financial statements for further details.

Finance receivables consist of the following:

	December 31, 2018	December 31, 2017
	(\$ thousands)	
U.S. equipment - Pawnee	\$ 559,542	\$ 398,969
Canada equipment - Blue Chip	169,382	151,574
Working capital loans - Windset	—	107
	<u>\$ 728,924</u>	<u>\$ 550,650</u>

Finance receivables increased by \$178.3 million, or 32%, during the year ended December 31, 2018. The increase in

the foreign exchange rate led to a \$34.9 million increase in finance receivables since December 31, 2017. In U.S. dollars, Pawnee's finance receivables increased by U.S.\$92.1 million, or 29.0%, since December 31, 2017. Blue Chip's finance receivables increased by \$17.8 million, or 11.7%, during the year ended December 31, 2018.

The \$728.9 million in net investment in leases and loans is net of \$23.9 million in allowance for credit losses based on IFRS 9 (compared to \$11.9 million in allowance for credit losses at December 31, 2017). The allowance for credit losses at December 31, 2017 is calculated based on IAS 39 and has not been restated.

On January 1, 2018, the Company adopted the new impairment and measurement requirements under IFRS 9. Upon the adoption of IFRS 9, the allowance for credit losses increased by \$10.0 million. IFRS 9 introduces an expected credit loss impairment ("ECL") model in determining the appropriate allowance for credit losses for finance receivables. Application of the ECL model will depend on the following credit stages of the financial assets:

- (i) Stage 1 - for new leases and loans recognized and for existing leases or loans that have not experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the net credit losses expected to result from defaults occurring in the next 12 months;
- (ii) Stage 2 - for those leases or loans that have experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the net credit losses expected over the remaining life of the lease or loan; and
- (iii) Stage 3 - for leases or loans that are considered to be credit-impaired, a loss allowance equal to full life time expected net credit losses is recognized.

Finance receivables at Pawnee and Blue Chip are composed of a large number of homogenous leases and loans, with relatively small balances. Thus, the evaluation of the allowance for credit losses is performed collectively for the lease and loan receivable portfolios.

The Company determined the previous methodology under IAS 39 covered Stages 2 and 3 and retained that methodology for those stages. For Stage 2, the Company considers leases and loans to have experienced a significant increase in credit risk since initial recognition if they are delinquent for over 30 days and further includes approximately 15% of the non-prime 1-30 day delinquent leases and loans.

For Stage 3, the Company considers leases and loans to be credit impaired if they are delinquent for more than 90 days or if the individual leases and loans are classified as non-accrual.

For Stage 1, the Company utilized static pool loss data applied to recent origination levels along with forward-looking macroeconomic assumptions under the ECL methodology.

The measurement of expected credit losses for Stage 1 and the assessment of significant increase in credit risk considers information about past events and current conditions, as well as reasonable and supportable forecasts of future events and economic conditions. The estimation and application of forward-looking information will also require judgment.

Pawnee charges off leases and loans when they become 154 days contractually past due, unless information indicates that an earlier charge-off is warranted. A high percentage of charge-offs are recognized before the subject leases/loans reach 154 days contractually past due. Blue Chip charges off leases and loans on an individual basis when there is no realistic prospect of recovery. Financial receivables that are charged-off could still be subject to collection efforts, with future recoveries possible.

Intangible assets totaled \$18.8 million at December 31, 2018. Of the \$919,000 decrease in intangible assets from December 31, 2017, \$1.5 million reflects amortization and \$593,000 relates to the increase in the foreign exchange rate. The significant intangible assets of broker relationships and trade names do not require any outlay of cash to be maintained, as the creation of lease and loan receivables does not require an outlay of cash, other than commissions, which are separately expensed over the terms of the lease and loan receivables.

Goodwill totaled \$41.0 million at December 31, 2018 compared to \$39.9 million at December 31, 2017. The \$1.18 million increase in goodwill relates to the increase in the foreign exchange rate. Goodwill is typically tested annually for impairment unless certain circumstances arise that would require an assessment prior to an annual review. The Company's annual goodwill impairment assessment did not indicate any impairment as at December 31, 2018.

Accounts payable and other liabilities totaled \$15.6 million at December 31, 2018 compared to \$14.9 million at December 31, 2017, an increase of \$711,000. See Note 11 - *Accounts Payable and Other Liabilities* in the consolidated financial statements for more detail on the balances that comprise accounts payable and other liabilities.

On December 16, 2013, the Company issued a total of \$20.0 million principal amount of convertible debentures. The debentures were to mature on December 31, 2018, and bore interest at a rate of 6.5% per annum, paid semi-annually. The Company announced on December 12, 2017 that it would exercise its right to early redemption of the debentures. On January 17, 2018, Chesswood paid, in cash, the \$20 million outstanding principal and the accrued and unpaid interest to the debenture holders as the redemption amount.

The debentures had several embedded derivative features which were determined to not meet the criteria for treatment as equity components and would otherwise be required to be recognized as separate financial instruments, measured at fair value through profit or loss. The Company elected under *IAS 39.11A* to designate the entire debentures (and all the embedded derivatives) as a combined financial liability at fair value through net income or loss. The fair value of the debentures was based on their trading price on the Toronto Stock Exchange as at the end of each reporting period.

Borrowings totaled \$601.5 million at December 31, 2018 compared to \$412.2 million at December 31, 2017, an increase of \$189.4 million. The \$189.4 million increase in borrowings is supporting \$178.3 million of growth in our net finance receivables, and the Company utilized \$20.0 million of its credit facility to redeem the convertible debenture in January 2018. The increase in the foreign exchange rate since December 31, 2017, led to a \$32.0 million increase in the borrowing amount.

Chesswood was utilizing U.S.\$178.7 million of its U.S. \$250.0 million revolving credit facility at December 31, 2018 compared to U.S.\$165.0 million at December 31, 2017. The corporate credit facility allows Chesswood to internally manage the allocation of capital to its various financial services businesses in Canada and the United States. The credit facility supports growth in finance receivables, provides for Chesswood's working capital needs and for general corporate purposes. The facility, available in U.S. or Canadian dollars, also improves the Company's financial flexibility by centralizing treasury management and making the provision of capital to individual businesses more efficient. The facility matures in December 2020.

The Company's borrowings under the corporate credit facility are subject to, among other things, adhering to certain percentages of eligible gross lease/loan receivables. The credit facility is secured by substantially all of the Company's assets and contains covenants (including the maintaining of leverage and interest coverage ratios). Chesswood was in full compliance with all its bank covenants at December 31, 2018 and December 31, 2017 (and throughout the periods).

On October 16, 2017, Pawnee announced that it had closed its first U.S. non-recourse U.S.\$75.0 million asset-backed facility secured by a portion of Pawnee's prime equipment finance receivable portfolio. On June 4, 2018, Pawnee obtained another U.S. non-recourse U.S.\$50.0 million asset-backed facility with the same financial institution secured by a portion of Pawnee's prime equipment finance receivable portfolio. The repayment terms are based on the cash flow of the underlying leases and loans. Proceeds from these non-recourse facilities were applied to Chesswood's corporate credit facility. As part of the servicing agreements related to Pawnee's non-recourse facilities, Pawnee is to comply with leverage ratio, interest coverage ratio, and tangible net worth covenants. At December 31, 2018 and throughout the period from October 2017 to December 31, 2018, Pawnee was in compliance with its covenants. The non-recourse facilities interest rate risk is mitigated by interest rate caps for an amount that is not less than 80% of the aggregate outstanding balance. The interest rate caps are tied to the repayment terms of the underlying finance receivables portfolios supporting the facilities, through the maturity dates, with a floating index rate which is subject to a capped fixed rate. At December 31, 2018, the fair value of the interest rate caps was an asset of \$441,000 (December 31, 2017 - \$185,000).

On August 20, 2018, Pawnee announced that it had closed a U.S.\$250 million warehouse facility specifically to fund its growing prime portfolio. The warehouse facility will hold Pawnee's prime receivables before they are securitized and provides an improved cost of capital and better advance rate than the Company's revolving facility, which was primarily structured for non-prime commercial leases and loans and will continue to be utilized for those originations. At December 31, 2018, Pawnee was utilizing U.S.\$83.0 million of this facility.

Blue Chip has entered into master purchase and servicing agreements and bulk lease financing facilities with various financial institutions and life insurance companies (referred to collectively as the "Funders"). Funds under each securitization facility are advanced to Blue Chip on a tranche-by-tranche basis, with each tranche collateralized by a specific group of underlying finance receivables and any related security provided thereunder. Interest rates are fixed at the time of each advance and are based on Government of Canada Bond yields with maturities comparable to the term of the underlying leases plus a premium. Blue Chip maintains either certain cash reserves as credit enhancements or provides letters of guarantee in return for release of cash reserves. Blue Chip continues to service these finance receivables on behalf of the Funders. As at December 31, 2018, Blue Chip had access to at least \$93.8 million of committed bulk financing lines of funding from both financial and insurance companies, in addition to access to

Chesswood's revolving facility. Blue Chip must meet certain financial covenants to support these securitization and bulk lease financing facilities. As at December 31, 2018 and December 31, 2017 (and throughout the periods), Blue Chip was in compliance with all covenants.

The \$16.8 million (December 31, 2017 - \$14.0 million) in customer security deposits relates to security deposits predominantly held by Pawnee. Pawnee's non-prime contracts require that the lessees/borrowers provide two payments as security deposit (not advance payments), which are held for the full term of the lease/loan and then returned or applied to the purchase option of the equipment at the lessee's/borrower's request, unless the contract is in default (in which case the deposit is applied against the receivable). Historically, a very high percentage of such deposits are either applied to the purchase option of the leased equipment at the end of the lease term or used to offset charge-offs.

The Company entered into interest rate swap agreements that provide for payment of an annual fixed rate, in exchange for a LIBOR-based floating rate amount. The interest rate swaps are intended to offset a portion of the variable interest rate risk on the credit facility. If the Company had terminated the swaps at December 31, 2018, the Company would have realized a gain of \$455,000 compared to a cost to terminate of \$43,000 at December 31, 2017.

Pawnee's non-recourse asset-backed facility requires Pawnee to mitigate interest rate risk by entering into an interest rate cap for a notional amount of not less than 80% of the aggregate outstanding balance. The interest rate cap is tied to the repayment terms of the underlying finance receivables portfolio supporting the Pawnee facility, through the maturity date, with a floating index rate based on USD-LIBOR-BBA, but subject to a capped fixed rate. At December 31, 2018, the fair value of the interest rate caps was an asset of \$441,000 (2017 - \$185,000).

Future taxes payable at December 31, 2018 totaled \$20.8 million compared to \$21.2 million at December 31, 2017, a decrease of \$408,000. The tax impact of the IFRS 9 and 15 adoption led to a decrease of \$3.5 million in future taxes payable. Offsetting this decrease was a \$1.3 million increase in future taxes payable due to the change in the foreign exchange rate, and a \$1.8 million increase in future tax expense. Taxes at Pawnee, Windset and Blue Chip are provided for using the asset and liability method of accounting. This method recognizes future tax assets and liabilities that arise from differences between the accounting basis of the subsidiary's assets and liabilities and their corresponding tax basis.

At December 31, 2018, there were 16,229,066 common shares outstanding (excluding the shares issuable in exchange for the Exchangeable Securities, as defined below) with a book value of \$103.6 million. Including the Exchangeable Securities, Chesswood would have had 17,707,603 common shares outstanding.

In August 2017, the Company's Board of Directors approved the repurchase for cancellation of up to 1,085,981 of the Company's outstanding common shares for the period commencing August 25, 2017 and ending on August 24, 2018. During the period from January 1, 2018 to August 24, 2018, the Company repurchased 293,096 of its common shares under this normal course issuer bid at an average cost of \$10.5277 per share.

In August 2018, the Company's Board of Directors approved the repurchase for cancellation of up to 1,043,895 of the Company's outstanding common shares for the period commencing August 25, 2018 and ending on August 24, 2019. From August 25, 2018 to December 31, 2018, the Company repurchased 206,340 of its common shares under this normal course issuer bid at an average cost of \$10.2412 per share.

Subsequent to December 31, 2018 (up to and including March 5, 2019), the Company repurchased 48,360 of its shares under the normal course issuer bid at an average cost of \$10.7452 per share.

The Company has entered into an automatic share purchase plan with a broker for the purpose of permitting us to repurchase our common shares under the normal course issuer bid at times when we would not be permitted to trade in our own shares during internal blackout periods, including during regularly scheduled quarterly blackout periods. Such purchases will be determined by the broker in its sole discretion based on parameters the Company has established.

Non-controlling interest consists of 1,274,601 Class B common shares and 203,936 Class C common shares (the "Exchangeable Securities") of Chesswood US Acquisitionco Ltd. ("U.S. Acquisitionco"), which were issued as partial consideration for the acquisition of Pawnee and are fully exchangeable at any time for the Company's common shares, on a one-for-one basis, through a series of steps. Attached to the Exchangeable Securities are Special Voting Shares of the Company which provide the holders of the Exchangeable Securities voting equivalency to holders of common shares. Under IFRS, the Exchangeable Securities must be shown as non-controlling interest because they are equity in a subsidiary not attributable, directly or indirectly, to the parent (even though they have no voting powers in the subsidiary, have voting powers only in the parent company, and are fully

exchangeable into the equity of the parent for no additional consideration and receive the same dividends as the common shares of the parent company). When the non-controlling interest was moved from Other Liabilities back to the shareholders' equity section on January 1, 2011 (the date Chesswood Income Fund was converted into the Company), per IFRS, the value attributed to the non-controlling interest was just the fair value of the equivalent common shares (closing value of the units of Chesswood Income Fund on the Toronto Stock Exchange on December 31, 2010) as the Exchangeable Securities are fully exchangeable into the Company's common shares. Their portion of the cumulative income and dividends from May 2006 to January 1, 2011 was not allocated to non-controlling interest; however, their portion of income and dividends has since been allocated to non-controlling interest.

On January 1, 2018, the Company was required to adopt IFRS 9. The IFRS 9 transition amount reduced retained earnings and non-controlling interest by \$7.6 million after-tax. Please see Note 2 - *New Accounting Standards* and Note 7 - *Finance Receivables* in the consolidated financial statements for the year ended December 31, 2018. As part of the process of reviewing and adopting IFRS-15, *Revenue from Contracts with Customers*, we have reclassified certain revenue items from Ancillary finance and other fee income on the Statement of Income to the Interest revenue on leases and loans. These revenue items will also now be recognized on an effective interest basis versus our historical method of recognizing items as revenue when received. As part of this transition, unearned income, included in finance receivables, was increased by \$3.4 million and a reduction in shareholders' equity and non-controlling interest of approximately \$2.7 million, on an after-tax basis, was recorded.

Reserves represent the accumulated share-based compensation expensed over the vesting term for options and restricted share units unexercised at December 31, 2018. There were 2,384,354 options and 44,000 restricted share units outstanding at December 31, 2018.

Accumulated other comprehensive income is the cumulative translation difference between the exchange rate on January 1, 2010, the IFRS adoption date, and the exchange rate on December 31, 2018 of self-sustaining foreign operations net assets.

LIQUIDITY AND CAPITAL RESOURCES

The primary sources of cash for the Company and its subsidiaries have been cash flows from operating activities, and borrowings under its, and its various subsidiaries' credit

and securitization and bulk lease financing facilities. The primary uses of cash for the Company and its subsidiaries are to fund business operations, equipment leases and loans, support working capital, long-term debt principal repayments, share repurchases and dividends.

At December 31, 2018, the Company's continuing operations had approximately U.S.\$71.3 million in additional borrowings available under the corporate credit facility, U.S. \$167.0 million under Pawnee's warehouse facility and at least \$93.8 million under Blue Chip's securitization and bulk lease financing facilities to fund business operations.

The Chesswood corporate credit facility allows borrowings up to U.S.\$250.0 million. The Chesswood credit facility is used to provide funding for operations (i.e. to provide financing for the purchase of assets that are to be the subject of leases and loans and support working capital). The financing facilities are not intended to directly fund dividends by the Company. Under the facility, the maximum amount of cash dividends and purchases under its normal course issuer bid in respect of a month is 1/12 of 90% of Free Cash Flow (see Dividend Policy below) for the most recently completed four financial quarters for which Chesswood has publicly filed its consolidated financial statements (including its annual consolidated financial statements in respect of a fourth quarter). Free Cash Flow is defined as the consolidated Adjusted EBITDA less maintenance capital expenditures, and tax expense, plus or minus the tax effect of change in the allowance for credit losses (effective Q1 2018). Please refer to the definitions of Non-GAAP Measures provided in this MD&A.

Cash Sources and Uses

The statement of cash flows, which is compiled using the indirect method, shows cash flows from operating, investing, and financing activities, and the Company's cash at the beginning and end of the period. Cash flows in foreign currencies have been translated at the average exchange rate for the period. Cash flow from operating activities comprises net income (loss) adjusted for non-cash items, changes in working capital and operational net assets. IFRS deems changes in finance receivables as operating assets for financial companies. Receipts and payments with respect to tax are included in cash from operating activities. Interest revenue and interest expense are included in operating activities and not investing or financing activities. Cash flow from investing activities comprises payments relating to the acquisition of companies, net of cash proceeds from the sale of discontinued operations, and payments relating to the purchase of property and equipment. Cash flow from financing activities comprises changes in borrowings,

payment of dividends, proceeds from stock issues, exercise of stock options, and the purchase and sale of treasury stock.

For the year ended December 31, 2018

In the year ended December 31, 2018, there was a decrease in cash of \$1.3 million compared to a decrease in cash of \$7.8 million in the prior year as a result of reasons discussed below.

The Company's continuing operations utilized \$117.4 million of cash during the year ended December 31, 2018 compared to \$126.9 million in the prior year, a decrease in the utilization of cash of \$9.5 million.

The net cash utilized to fund the growth in finance receivables (funds advanced, origination costs, security deposits, restricted cash, less principal payments) totaled \$207.2 million in the year ended December 31, 2018 compared to \$196.3 million in the prior year, an increase of \$10.9 million. The Company funded the growth in finance receivables from excess opening cash, cash from operations and \$158.5 million in net borrowings (included in finance activities) in the year ended December 31, 2018 (2017 - \$137.7 million).

In the year ended December 31, 2018, the Company made tax payments of \$3.6 million compared to \$12.5 million in the year ended December 31, 2017, a decrease of \$8.9 million year-over-year. The decrease in taxes paid, year-over-year, is predominantly a result of the \$3.5 million in taxes paid in Q1 2017 on the gain on sale of EcoHome which was sold in Q1 2016, and \$3.5 million in net tax refunds received in Q3 2018.

If the cash utilized to fund the growth in finance receivables and net tax payments (discussed above) is excluded from cash from operating activities, the continuing operations generated \$93.5 million in cash from net income, non-cash items and other working capital changes compared to \$81.9 million in the prior year, an increase of \$11.5 million from the prior year.

Capital expenditures totaled \$212,000 (2017 - \$943,000) during the year ended December 31, 2018.

The Company repurchased 499,436 of its common shares under normal course issuer bids at an average cost of \$10.4094 during the year ended December 31, 2018 totaling \$5.2 million (2017 - nil).

The Company paid dividends to the holders of its common shares and Exchangeable Securities in the amount of \$15.1 million during the year ended December 31, 2018 relatively unchanged from the prior year. The Company received

\$571,000 (2017 - \$162,000) from the exercise of options by employees during the year ended December 31, 2018.

For the three months ended December 31, 2018

In the three months ended December 31, 2018, there was a decrease in cash of \$2.3 million compared to a decrease in cash of \$5.7 million in the same period in the prior year as a result of reasons discussed below.

The Company's continuing operations utilized \$21.4 million of cash during the three months ended December 31, 2018 compared to \$45.7 million in the same period in the prior year, a decrease in the utilization of cash of \$24.2 million.

The net cash utilized to fund the growth in finance receivables (funds advanced, origination costs, security deposits, restricted cash, less principal payments) totaled \$42.5 million in the three months ended December 31, 2018 compared to \$61.1 million in the same period in the prior year, a decrease of \$18.5 million. The Company funded the growth in finance receivables from excess opening cash, cash from operations and \$25.4 million in net borrowings (included in finance activities) in the three months ended December 31, 2018 (Q4 2017 - \$46.5 million).

In the three months ended December 31, 2018, the Company made net tax payments of \$1.4 million, compared to net tax payments of \$3.1 million in the same period in the prior year.

If the cash utilized to fund the growth in finance receivables and net tax payments (discussed above) is excluded from cash from operating activities, the continuing operations generated \$22.5 million in cash from net income, non-cash items and other working capital changes compared to \$18.5 million in the same period in the prior year, an increase of \$4.0 million from the prior year.

Capital expenditures totaled \$50,000 (Q4 2017 - \$144,000) during the three months ended December 31, 2018.

The Company repurchased 206,340 of its common shares under its normal course issuer bid at an average cost of \$10.2412 during the three months ended December 31, 2018 totaling \$2.1 million (2017 - nil).

The Company paid dividends to the holders of its common shares and Exchangeable Securities in the amount of \$3.8 million during the three months ended December 31, 2018 relatively unchanged from the same period in the prior year. The Company received \$nil (2017 - \$39,000) from the exercise of options by employees during the three months ended December 31, 2018.

Chesswood expects that current operations and planned capital expenditures for the foreseeable future of its subsidiaries will be financed using funds generated from operations, existing cash, and funds available under existing and/or new credit and financing facilities. Chesswood may require additional funds to finance future acquisitions and support significant internal growth initiatives relating to finance receivable portfolio growth. It will seek such additional funds, if necessary, through public or private equity, debt financings or securitizations from time to time, as market conditions permit.

Financial Covenants, Restrictions and Events of Default

The Company and its operating subsidiaries are subject to bank and/or funder covenants relative to leverage and/or working capital.

The Company's ability to access funding at competitive rates through various economic cycles enables it to maintain the liquidity necessary to manage its businesses, and its ability to continue to access funding is an important condition to its future success.

The Company's secured borrowing agreement and its subsidiaries' warehousing, securitization and bulk lease financing facility agreements have financial covenants and other restrictions which must be met in order to obtain continued funding and avoid default.

Advances on the Chesswood revolving corporate credit facility may be drawn at any time, subject to compliance with borrowing base calculations and compliance with the covenants set out therein. As of December 31, 2018, U.S. \$178.7 million was outstanding under the U.S.\$250.0 million facility and the Company had capacity to draw another U.S.

\$28.5 million and remain within the borrowing base under the facility. The Company had U.S.\$7.7 million of letters of credit outstanding under the Chesswood corporate credit facility.

Dividends to Shareholders

The Company declared monthly cash dividends of \$0.07 per common share from January 2018 to December 31, 2018.

Dividend Policy

The Company's policy is to pay monthly dividends to shareholders of record on the last business day of each month by the 15th of the following month (or the next business day thereafter if the 15th is not a business day).

Under the Chesswood credit facility, the maximum amount of monthly cash dividends and repurchases under its normal course issuer bid is 1/12 of 90% of Free Cash Flow (as defined under Non-GAAP Measures in this MD&A) for the most recently completed four financial quarters for which Chesswood has publicly filed its consolidated financial statements.

The amount of any dividends payable by Chesswood is at the discretion of its Board of Directors, is evaluated on an ongoing basis, and may be revised subject to business circumstances and expected capital requirements depending on, among other things, Chesswood's earnings, financial requirements for its operating entities, growth opportunities, the satisfaction of applicable solvency tests for the declaration and payment of dividends and other conditions existing from time to time.

Minimum Payments The following are the contractual payments and maturities of financial liabilities and other commitments as at December 31, 2018 (including interest):

(\$ thousands)	2018	2019	2020	2021	2022	2023 and beyond	Total
Accounts payable and other liabilities	\$ 15,600	\$ —	\$ —	\$ —	\$ —	\$ —	15,600
Borrowings (a)	123,815	353,368	95,544	56,416	26,746	91	655,980
Customer security deposits (b)	3,884	4,655	4,678	3,293	2,296	58	18,864
	143,299	358,023	100,222	59,709	29,042	149	690,444
Other financial commitments (c)	805	717	739	748	757	790	4,556
Total commitments	\$ 144,104	\$ 358,740	\$ 100,961	\$ 60,457	\$ 29,799	\$ 939	\$ 695,000

a. Borrowings are described in Note 13 - *Borrowings* in the consolidated financial statements, and include Chesswood's corporate

credit facility and Pawnee's warehousing facility which are lines-of-credit; as such the balances can fluctuate. The amount above includes fixed interest payments on Pawnee and Blue Chip's facilities and estimated interest payments on the Chesswood corporate credit facility, assuming the interest rate, debt balance and foreign exchange rate at December 31, 2018 remain the same until its expiry date of December 2020.

- b. The Company's experience has shown the actual contractual payment streams will vary depending on a number of variables including: prepayment rates, charge-offs and modifications. Accordingly, the scheduled contractual payments of customer security deposits shown in the table above are not to be regarded as a forecast of future cash payments.
- c. The Company and its subsidiaries are committed to future minimum rental payments under existing leases for premises, excluding occupancy costs and property tax, with expirations up to 2025, which represent the bulk of other financial commitments.

The Company has no material "off-balance sheet" financing obligations, except for long-term premises lease agreements and U.S. \$7.7 million in letters of guarantee. Other commitments are disclosed in Note 18 - *Contingent liabilities and other financial commitments* in the 2018 audited consolidated financial statements.

OUTLOOK

As we cautioned at the end of our third quarter, it is our view that market behavior has once again become irrational. Led by many bank owned equipment finance companies that have lower cost of funds and balance sheets that allow them to be less sensitive to the risk-reward balance while in pursuit of volume, the market today is very aggressive.

As a non-bank independent finance company, we have passed on more of the recent rate increases to our customers than have our bank-owned competitors, which puts some pressure on our originations. We are focused more on the quality of those originations rather than the volumes we are generating at this later stage in the economic cycle when conventional wisdom holds that we are closer to a correction. We believe this is a prudent approach.

We are excited by the launch of Tandem Finance, which is a long-term investment in our future. Tandem operates in a market segment that is much larger than the market served by our equipment brokers, while sales cycles are longer than in our traditional channel. Therefore, we have modest expectations for Tandem in its first year and accordingly we will incur net operating expenses in that business in 2019 that will be significant and could total as much as \$2.0 - \$3.0 million.

RISK FACTORS

An investment in the Company's common shares entails certain risk factors that should be considered carefully.

Chesswood operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond our control and which could have an effect on our business,

revenues, operating results, cash flow and financial condition. Readers should carefully review the risk factors in the Company's annual information form filed with various Canadian securities regulatory authorities through SEDAR (the System for Electronic Document Analysis and Retrieval) at www.sedar.com, a summary of which are set out below.

Dependence on Key Personnel

Our operating companies depend to a large extent upon the abilities and continued efforts of their key operating personnel and senior management teams.

Relationships with Brokers and Other Origination Sources

Pawnee and Blue Chip have formed relationships with hundreds of origination sources, comprised primarily of equipment finance brokerage firms. They rely on these relationships to generate applications and originations. The failure to maintain effective relationships with their brokers and other origination sources or decisions by them to refer transactions to, or to sign contracts with, other financing sources could impede their ability to generate transactions, including Canada where Blue Chip gets a substantial portion of its origination volume from a few large equipment brokerage firms.

Risk of Future Legal Proceedings

Our operating companies are threatened from time to time with, or are named as defendants in, or may become subject to, various legal proceedings, fines or penalties in the ordinary course of conducting their respective businesses. A significant judgment or the imposition of a significant fine or penalty on an operating company (or on a company engaged in a similar business, to the extent the operating company operates in a similar manner) could have a material

adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Interest Rate Fluctuations

The Company and our operating companies are exposed to fluctuations in interest rates under their borrowings. Increases in interest rates (to the extent not mitigated by interest hedging arrangements or fixed rate securitizations) may have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

The leases and loans are written at fixed interest rates and terms. Generally, the Company finances the activities of its operating companies with both fixed rate and floating rate funds. To the extent the operating companies finance fixed rate leases and loans with floating rate funds, they are exposed to fluctuations in interest rates such that an increase in interest rates could narrow or eliminate the margin between the yield on a lease and loan and the effective interest rate paid by the borrower.

At the customer level, non-prime segments of the micro and small-ticket equipment finance market have historically and typically been, and continue to be, more sensitive to monthly lease/loan payment amounts than to the effective rates of interest charged.

Portfolio Delinquencies; Inability to Underwrite Lease and Loan Applications

Pawnee's receivables consist primarily of lease and loan receivables originated under programs designed to serve small and medium-sized, often owner-operated, businesses that have limited access to traditional financing. There is a high degree of risk associated with equipment financing for such parties. A portion of Pawnee's portfolio are start-up businesses that have not established business credit or a more established business that has experienced some business or personal credit difficulty at some time in its history. As a result, such leases or loans entail a relatively higher risk and may be expected to experience higher levels of delinquencies and loss levels. Pawnee cannot guarantee that the delinquency and loss levels of its receivables will correspond to the historical levels Pawnee has experienced on its portfolio and there is a risk that delinquencies and losses could increase significantly.

Analogous risks are faced by Blue Chip in its business.

In addition, since defaulted leases and loans and certain delinquent leases and loans cannot be used as collateral under our financing facilities, higher than anticipated lease defaults

and delinquencies could adversely affect our liquidity by reducing the amount of funding available to us under our financing arrangements. Furthermore, increased rates of delinquencies or loss levels could result in adverse changes to the terms of future financing arrangements, including increased interest rates payable to lenders and the imposition of more burdensome covenants and increased credit enhancement requirements.

Deterioration in Economic or Business Conditions; Impact of Significant Events and Circumstances

The results of the Company's subsidiaries may be negatively impacted by various economic factors and business conditions, including the level of economic activity in the markets in which they operate. To the extent that economic activity or business conditions deteriorate, delinquencies and credit losses may increase. Delinquencies and credit losses generally increase during economic slowdowns or recessions such as that experienced in the United States from 2008-2013. As our operating companies extend credit primarily to small businesses, many of their customers may be particularly susceptible to economic slowdowns or recessions, and may be unable to make scheduled lease or loan payments during these periods. Unfavourable economic conditions may also make it more difficult for our operating companies to maintain new origination volumes and the credit quality of new leases and loans at levels previously attained. Unfavourable economic conditions could also increase funding costs or operating cost structures, limit access to credit facilities, securitizations and other capital markets or result in a decision by lenders not to extend further credit.

In addition, the equipment finance industry generally may be affected by changes in accounting treatment for leases and loans, and negative publicity with respect to, among other things, fraud or deceptive practices by certain participants in the industry. Greater governmental scrutiny is also a risk, especially as to the tax treatment of certain transaction structures or other aspects of these transactions that, if changed, could result in additional tax, fee or other revenue to that governmental authority. Any of these factors may make leasing or loaning less attractive or diminish the profitability of the existing financing alternatives offered by our operating companies.

In addition to being impacted by factors or conditions in the United States or Canada, political, economic or other significant events or circumstances outside of North America (whether political unrest which impacts upon the prices of oil and other commodities or otherwise) can ultimately significantly impact upon North American economic conditions which, in turn, could result in the adverse implications described in the first paragraph under this

heading. Similarly, natural disasters in any part of the world may directly (through impact on supplies of goods or equipment to our businesses) or indirectly impact Chesswood's operations or results. Further, tariffs or duties imposed by a country could adversely impact upon industries in which companies to which our operating companies have provided financing or seek to provide financing which may impact Chesswood's operations or results.

Losses from Leases and Loans; The Risk/Yield Trade-off

Losses from leases and loans in excess of our operating companies' expectations would have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Changes in economic conditions, the risk characteristics and composition of the portfolio, bankruptcy laws, and other factors could impact our operating companies' actual and projected net credit losses and the related allowance for credit losses. Should there be a significant change in the above noted factors, then our operating companies may have to set aside additional reserves which could have a material adverse impact on their respective business, financial condition and results of operations and on the amount of cash available for dividends to our shareholders.

Determining the appropriate level of the allowance is an inherently uncertain process and therefore the determination of this allowance may prove to be inadequate to cover losses in connection with a portfolio of leases and loans. Factors that could lead to the inadequacy of an allowance for credit losses may include the inability to appropriately underwrite credit risk of new originations, effectively manage collections, or anticipate adverse changes in the economy or discrete events adversely affecting specific customers, industries or geographic areas.

Pawnee began offering its prime product in 2015 - financing for higher credit rated lessees and borrowers, and this product represents an increasing part of the composition of Pawnee's portfolio. While it is expected that the losses and allowance for credit losses in respect of this part of Pawnee's portfolio will be lower - commensurate with the prime credit rating of the lessees/borrowers - the spread between the rates that Pawnee can charge over our cost of funds is also considerably smaller.

Adverse Events or Legal Determinations in Areas with High Geographic Concentrations of Leases or Loans

If judicial or other governmental rulings or actions or interpretations of laws adverse to the equipment finance industry and/or the working capital loan industry in general

or to business practices engaged in by our operating companies, or adverse economic conditions or the occurrence of other significant events such as natural disasters and terrorist attacks, were to occur in a geographic region with a high concentration of leases/loans or equipment financed from our operating companies, there could be a material adverse impact on our business, financial condition and results of operations, and the amount of cash available for dividends to our shareholders.

"Characterization" Risks

If an applicable court or regulatory authority were to make an adverse finding, or take an adverse action on the basis that one of Pawnee's form of lease is not a true lease for commercial law, tax law, or other legal purposes, adverse consequences could result with respect to leases entered into in such form including the loss of preferred creditor status (which would impact upon Pawnee's rights to recover on its claim), limitations on finance charges and other fees that can be enforced, and additional federal, state and other (income or sales) taxes payable by Pawnee.

Case Funding's non-recourse advances may be re-characterized in certain jurisdictions as loans, or determined to be improper fee-splitting, which would adversely affect the collectability of the advances.

Defenses to Enforcement of a Significant Number of Leases and Loans

Certain defenses and recovery impediments are more common in micro and small-ticket equipment finance transactions than with respect to equipment finance providers in other segments of the equipment finance industry. Management believes that certain of these risks are sufficiently addressed in the existing documentation and related business practices of our operating companies. However, there are other risks that they have not addressed for various reasons, including that certain of these risks are not susceptible to being addressed either at all or without incurring cost inefficiencies or taking other measures deemed unacceptable by management based on a risk-reward assessment. Our operating companies have never experienced any material occurrence of these risks nor have these risks historically had a material adverse impact on them. However, there is no assurance that these risks will not have a material adverse impact on their business, financial condition and results of operations in the future.

Origination, Funding and Administration of Transactions

Our operating companies' origination, funding and transaction administration practices could result in certain

vulnerabilities in their enforcement rights. For example, certain leases and loans are assignments of transactions already documented by brokers. Acquiring leases/loans by this “indirect” process subjects our operating companies to various risks, including risks that might arise by reason of the broker’s insolvency, administrative inadequacies or fraudulent practices, as well as any third party claims against the broker or its rights with respect to the assigned lease or loan. Our operating companies may be subject to risks related to broker practices, whether or not our operating companies have actual legal responsibility for broker conduct. Any of these broker related risks can impair our operating companies’ rights with respect to recovering the rents and/or property under leases and loans. Pawnee has not been involved in any claims or litigation in relation to such risks and Pawnee does not conduct lien searches in the name of, require lien releases from, or file financing statements against the lease broker.

If the lessee/borrower or broker is the party to whom the vendor of the equipment has agreed to sell the property at the time of its delivery, then under applicable commercial law, the lessee/borrower or broker, as applicable, may be deemed to have acquired title to the property prior to our operating companies having funded the transaction. It has not been their practice to ensure that the title to the leased property has not already passed or to obtain assurances that it is acquiring good title to that property free of liens and other third party claims. The manner in which our operating companies purchase the equipment is typical in this market segment, especially with respect to similarly situated equipment financing providers. They have not yet faced any meaningful challenge or adverse consequence from this practice, but there can be no assurance that such a challenge or consequence will not occur in the future.

In most circumstances where the equipment is less than U.S. \$15,000 (or U.S.\$10,000 if for a home business) for Pawnee’s core product and U.S.\$35,000 for the “B” product, and U.S. \$100,000 for “A”, Pawnee’s practice of requiring only a verbal confirmation that the property has been delivered and irrevocably accepted under the subject lease or loan, and/or inspecting the property to confirm the same, could make Pawnee vulnerable to certain defenses. By way of example, Pawnee’s deemed failure to deliver conforming property under the lease or loan documents could be a defense to a lessee/borrower’s “unconditional” obligation to pay the rents and certain other amounts. Pawnee has not suffered any material losses relating to these practices, however, there can be no assurance that it would not in the future.

Analogous risks are faced by Blue Chip.

Changes in Governmental Regulations, Licensing and Other Laws and Industry Codes of Practice

Finance companies are subject to laws and regulations relating to extending financing generally and are also members of industry associations which have adopted, among other things, codes of business practice. Laws, regulations and codes of business practice may be adopted with respect to existing leases and loans or the leasing, marketing, selling, pricing, financing and collections processes which might increase the costs of compliance, or require them to alter their respective business, strategy or operations, in a fashion that could hamper the ability to conduct business in the future.

Licensing Requirements

If an applicable court or regulatory authority were to make an adverse finding or otherwise take adverse action with respect to our operating companies based on their failure to have a finance lender’s or other license or registration required in the applicable jurisdiction, our operating companies would have to change business practices and could be subject to financial or other penalties. Further, certain jurisdictions may enact or change administrative practices in respect of licensing requirements for our operating companies or their referring brokers. For example, California requires that referring brokers have a lenders’ license, which may impact loan referrals from certain brokers for funding to California residents.

Fees, Rates and Charges

Some of our operating companies’ documents require payment of late payment fees, late charge interest, and other charges either relating to the non-payment under, or enforcement, of their leases and loans. It could be determined that these fees and/or the interest rates charged exceed applicable statutory or other legal limits. If the charges are deemed to be punitive and not compensatory, or to have other attributes that are inconsistent with, or in violation of, applicable laws, they could be difficult to enforce. A number of charges payable with respect to equipment finance transactions in the micro and small-ticket equipment finance market have been the subject of litigation by customers against financing parties in the past. Although our subsidiaries are not currently the subject of any such litigation, there can be no assurance that a lessee/borrower or a group of lessees/borrowers will not attempt to bring a lawsuit against our subsidiaries in relation to fees and charges, which our subsidiaries may or may not be successful in defending.

Our operating companies believe that their fee programs are designed and administered so as to comply with legal

requirements and are within the range of industry practices in their market segments. Nevertheless, certain attributes of these fees or charges, and their practices, including that their leases and loans typically provide for several different fees and charges resulting in a substantial amount of fee income and the possibility that the fees and charges may exceed actual costs involved or may otherwise be deemed excessive, could attract litigation, including class actions, that would be costly even if our subsidiaries were to prevail and as to which no assurance can be given of their successful defense. In addition to the risk of litigation, fee income is important to our subsidiaries and the failure of our subsidiaries to continue to collect most of these fees could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Insurance

To ensure that the lessor or lender of the leased or financed property suffering a loss receives the related insurance proceeds, the lease or loan also requires that the lessor or lender be named as a loss payee under the requisite casualty coverage. However, each lessee/borrower is ultimately relied upon to obtain and maintain the required coverage for financed equipment but there is no certainty that they will obtain the requisite coverage either conforming to the requirements of the lease or loan, or at all. Additionally, there are often policy provisions including exclusions, deductibles and other conditions that by their terms, or by reason of a breach, could limit, delay or deny coverage. There can be no assurance that any insurance will protect our operating companies interests in the equipment, and the failure by the lessee/borrower to obtain insurance or the failure by the operating companies to receive the proceeds from such insurance policies could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Lessor Liability

There is a risk that a lessor, such as Pawnee or Blue Chip, could be deemed liable for harm to persons or property in connection with, among other things, the ownership or leasing of the leased property, or the conduct or responsibilities of the parties to the lease relating to that property. The liability may be contractual (such as warranties regarding the equipment), statutory (such as federal, state or provincial environmental liability) or pursuant to various legal theories (such as negligence). There have been cases in which a lessor has been held responsible for damage caused by leased property without a showing of negligence or wrongdoing on the lessor's part. Even if a lessor ultimately succeeds

in defending itself or settling any related litigation, the related costs and any settlement amount could be significant.

Liability for Misuse of Leased Equipment

There is no practical manner to ensure that leased equipment or a leased vehicle will be used, maintained or caused to comply with applicable law. Pawnee and Blue Chip require its lessees to deliver evidence of compliance with same as a condition to funding but have no assurance that a lessee will take the appropriate actions during the lease term to address any use, maintenance or compliance issues which may arise. A lessee's conduct (or lack thereof) could subject Pawnee or Blue Chip, as applicable, to liability to third parties.

Estimates Relating to Value of Leases

Based on the particular terms of a lease, equipment finance companies estimate the residual value of the financed equipment, which is recorded as an asset on its statement of financial position. At the end of the lease term, equipment finance companies seek to realize the recorded residual for the equipment by selling the equipment to the lessee or in the secondary market or through renewal of the lease by the lessee. The ultimate realization of the recorded residual values depends on numerous factors, including: accurate initial estimate of the residual value; the general market conditions and interest rate environment at the time of expiration of the lease; the cost of comparable new equipment; the obsolescence of the leased equipment; any unusual or excessive wear and tear on or damage to the equipment; and the effect of any additional or amended government regulations.

If Pawnee or Blue Chip (in connection with those leases where the lessee is not obligated to either purchase the equipment or guarantee the residual value of the equipment at the end of the term of the lease) is unable to accurately estimate or realize the residual values of the leased equipment subject to their leases, the amount of recorded assets on its statement of financial position will have been overstated.

Competition from Alternative Sources of Financing

The business of micro and small-ticket equipment finance in the United States is highly fragmented and competitive. Pawnee focuses some its business on the segment of the micro and small-ticket equipment finance market involving start-up businesses that have not established business credit or established businesses that have experienced some credit difficulty in their history that do not meet the credit standards of more traditional financing sources. Pawnee's main competition comes from equipment finance companies, banks, commercial lenders, home equity loans, and credit cards.

As Pawnee expands its suite of products and targets potential lessees/borrowers with better credit scores, it faces competition from more traditional financing sources, including: national, regional and local finance companies; captive finance and equipment finance companies affiliated with major equipment manufacturers; and financial services companies, such as commercial banks, thrifts and credit unions.

Many of the firms and institutions providing financing alternatives are substantially larger than Pawnee and Blue Chip and have considerably greater financial, technical and marketing resources. Some of them may have a lower cost of funds and access to funding sources that are unavailable to Pawnee and Blue Chip. A lower cost of funds could enable a competitor to offer leases and loans with pricing lower than that of Pawnee and/or Blue Chip, potentially forcing Pawnee and Blue Chip to decrease its prices or lose origination volume. In addition, some financing sources may have higher risk tolerances or different risk assessments, which could allow them to establish more origination sources and customer relationships to increase their market share.

Further, because there are fewer barriers to entry with respect to the micro and small-ticket equipment finance market, new competitors could enter this market at any time, especially if an improvement in the economy leads to a greater ability of small and medium-sized businesses to establish improved levels of creditworthiness.

With the ever advancing improvements in technology, financial-technology ("Fintech") firms have been emerging with new business models, based on new technology that often includes an internet component, for offering financial services to businesses and consumers. It is possible that advancements by Fintech firms could negatively impact Pawnee and/or Blue Chips' business in a significant manner.

Fraud by Lessees, Borrowers, Vendors or Brokers

While our operating companies make every effort to verify the accuracy of information provided to them when making a decision whether to underwrite a lease or loan and have implemented systems and controls to protect against fraud, in a small number of cases in the past our operating companies have been a victim of fraud by lessees/borrowers, vendors and brokers. In cases of fraud, it is difficult and often unlikely that our operating companies will be able to collect amounts owing under a lease or loan or repossess the related equipment. Our operating companies may be subject to risks related to broker practices whether or not our operating companies have actual legal responsibility for broker conduct. Increased rates of fraud could have a material

adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Protection of Intellectual Property

Chesswood's operating subsidiaries continually develop and improve their brand recognition and proprietary systems and processes, which is an important factor in maintaining a competitive market position. No assurance can be given that competitors will not independently develop substantially similar branding, systems or process. Despite the efforts of our operating subsidiaries to protect their proprietary rights, unauthorized parties may attempt to obtain and use information the subsidiaries regard as proprietary. Preventing unauthorized use of such proprietary rights may be difficult, time-consuming and costly, and without any assurance of success.

Uncertainty of Outcome of Cases

The returns on loans and/or advances made by Case Funding, and thus the returns for Chesswood, depend on litigation outcomes in the form of judgments or settlements. Litigation of individual cases entails a large degree of uncertainty. It is also possible that a claimant may die or abandon his or her case, that the lawyer may abandon the plaintiff's case, or that the defendant, the law firm, or the defendant's insurance carrier may declare bankruptcy. Case Funding is also reliant on the capabilities of the attorneys handling the cases in which it provides funding to effectively litigate claims with due skill and care. Although Case Funding sought to weigh such uncertainties in the due diligence conducted before making its funding decisions, and intended to reduce risk by funding in a broad array of cases, there can be no assurance that the outcome of any given litigated claim or basket of claims can be predicted, whether or not the probabilities were correctly assessed by Case Funding.

Uncertainty in the Timing of Litigation Settlements and Awards

The nature of litigation recoveries, including the timing and amounts recovered, are outside the control of Case Funding. Individual claims may be resolved over drastically varying times: for example, as short as one month, or longer than three years. Case Funding will be required to wait for an indeterminate period of time after an advance/loan is made to fully collect money from judgment recoveries.

Case Funding May Have Difficulty Collecting on its Investments

If plaintiffs or law firms to which Case Funding has advanced or loaned funds do not pay Case Funding pursuant to the terms

of the advances/loans made, Case Funding may be required to pursue costly legal actions to collect. It is also possible that a plaintiff's attorney or a law firm may attempt to renegotiate the ultimate amount owed to Case Funding or that there is not enough proceeds from the case to repay Case Funding in full. In these situations, Case Funding may have to accept a smaller return than anticipated in order to accommodate and maintain business relationships or avoid litigation. In either event, the inability of Case Funding to collect or the necessity of legal action to collect, could harm or reduce the potential cash flow.

Failure of Computer and Data Processing Systems

Our operating companies are dependent upon the successful and uninterrupted functioning of their computer and data processing systems. The failure of these systems could interrupt operations or materially impact the ability of our operating companies to originate and service their lease and loan portfolio and broker networks. If sustained or repeated, a system failure could negatively affect these operations. Our operating companies maintain confidential information regarding lessees and borrowers in their computer systems. This infrastructure may be subject to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. A security breach of computer systems could disrupt operations, damage reputation and result in liability.

Security Risks

Despite implementation of network security measures, the infrastructure of our subsidiaries' websites and our management network is potentially vulnerable to computer break-ins and similar disruptive problems.

Risks Related to our Structure and Exchange Rate Fluctuations

The dividends expected to be paid to our shareholders will be denominated in Canadian dollars. However, a significant percentage of our revenues are expected to be derived from the revenues of our U.S. operations, which are received in U.S. dollars. Changes in the value of the U.S. dollar could have a negative impact on our Canadian dollar results, and in turn, on the amount in Canadian dollars available for dividends to our shareholders.

Unpredictability and Volatility of Share Price

A publicly-traded company will not necessarily trade at values determined by reference to the underlying value of its business. The prices at which our common shares will trade cannot be predicted. The market price of the common shares could be subject to significant fluctuations in response to variations in quarterly operating results and other factors. The

annual yield on the common shares as compared to the annual yield on other financial instruments may also influence the price of common shares in the public trading markets. In addition, the securities markets have experienced significant price and volume fluctuations from time to time in recent years that often have been unrelated or disproportionate to the operating performance of particular issuers. These broad fluctuations may adversely affect the market price of the common shares.

Leverage, Restrictive Covenants

The Company and its subsidiaries have third party debt service obligations under their respective credit and securitization and bulk lease financing facilities. The degree to which our subsidiaries are leveraged could have important consequences to our shareholders, including: (i) the ability to obtain additional financing for working capital in the future may be limited; (ii) a portion of the cash flow from the assets of such subsidiaries may be dedicated to the payment of the principal of and interest on their respective indebtedness, thereby reducing funds available for distribution to the Company; and (iii) certain of the respective borrowings of such subsidiaries will be at variable rates of interest, which will expose them to the risk of increased interest rates. The ability of such subsidiaries to make scheduled payments of the principal of or interest on, or to refinance, their indebtedness will depend on their future cash flow, which is subject to their respective assets, prevailing economic conditions, prevailing interest rate levels, and financial, competitive, business and other factors, many of which are beyond their control.

Possible Acquisitions

Acquisitions, if they occur, may increase the size of the operations as well as increase the amount of indebtedness that may have to be serviced by Chesswood and its subsidiaries. There is no assurance that such acquisitions can be made on satisfactory terms, or at all. The successful integration and management of acquired businesses involve numerous risks that could adversely affect the growth and profitability of Chesswood and its subsidiaries. There is no assurance that such acquisitions will be successfully integrated.

Restrictions on Potential Growth

The payout by our operating companies of a significant portion of their earnings available for distribution will make additional capital and operating expenditures dependent upon increased cash flow or additional financing in the future. Lack of those funds could limit the future growth of our operating companies and their cash flow.

Canadian Income Tax Matters

The income of the Company's operating companies must be computed in accordance with applicable Canadian, U.S. or foreign tax laws, and the Company is subject to Canadian tax laws, all of which may be changed in a manner that could adversely affect the amount of distributable cash.

United States Income Tax Matters

There can be no assurance that U.S. federal and state income tax laws and administrative policies will not develop or be changed in a manner that adversely affects our shareholders.

On December 22, 2017, the U.S. government enacted new tax legislation effective January 1, 2018. The legislation made broad and complex changes to the U.S. tax code. The tax provision recorded by the Company in our financial statements may change in the future following a more comprehensive review of the legislation, including implementation of the associated rules and regulations and supporting guidance from the Internal Revenue Service and other bodies, and as a result of any future changes or amendments to this legislation.

Environmental risk

Chesswood and its activities have no direct significant impact on the environment.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Understanding the Company's accounting policies is essential to understanding the results of the Company's operations and financial condition. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our consolidated financial statements. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

Net Investment in Leases

The leases entered into are considered to be finance leases in nature, based on an evaluation of all the terms and conditions and the determination that substantially all the risks and rewards of legal ownership of the asset has been transferred

to the lessee. Interest revenue on finance leases is recognized under the effective interest method. The effective interest method of income recognition applies a constant rate of interest equal to the internal rate of return on the lease.

Allowance for Credit Losses

The carrying value of net investment in leases and loans is net of allowance for credit losses. Quantifying the impairment is based on the estimates of the carrying value that will ultimately not be collected where there is objective evidence of impairment.

The finance receivables are each composed of a large number of homogenous leases and loans, with relatively small balances made to inherently risky borrowers. Pawnee charges-off leases and loans when they become 154 days contractually past due, unless information indicates that an earlier charge-off is warranted. A high percentage of charge-offs are made before the subject leases and loans reach 154 days contractually past due.

As of January 1, 2018, the Company adopted IFRS 9 which introduces a new expected credit loss impairment method for calculating allowance for credit losses. Please see Note 2(a) - *New Accounting Standards* in the 2018 audited consolidated financial statements for further disclosure.

At December 31, 2017, Pawnee's allowance for credit losses on Chesswood's consolidated financial statements was comprised of the net investment in leases and loans value that were over 30 days delinquent, plus any leases or loans identified as impaired less than 30 days delinquent and approximately 15% of the 1-30 day delinquent leases (those considered most likely to fall into the over 30 days delinquent category by the next month). A similar approach was taken for Windset and Blue Chip.

In 2017 and prior, under IFRS, an allowance could only be set up if there was objective evidence that the impairment has already occurred; potential losses expected as a result of future events, no matter how likely based on past historical evidence, were not allowed to be recognized. As only a small percentage of the total lease and loan receivable portfolio have monthly payments that are past due at any one reporting date, the portion of the lease and loan receivables that shows observable objective evidence of impairment at any one reporting date is quite small, despite long-term historical experience that indicates that future charge-offs with respect to the current lease and loan receivable will typically exceed the level of observable impairment, in a matter of months.

Projections of probable net credit losses are inherently uncertain, and as a result we cannot predict with certainty the

amount of such losses. Changes in economic conditions, the risk characteristics and composition of the portfolio, bankruptcy laws, and other factors could impact the actual and projected net credit losses and the related allowance for credit losses.

Legal Finance Receivables

Attorney loans and medical lien financing are deemed to be a financial asset as they are a contractual right to receive cash from another entity and are considered to be loans and receivables for accounting purposes, based on an evaluation of all the terms and conditions of the contracts. The contracts are deemed to have fixed or determinable payments, in that the payments are due when the underlying cases are settled however the date as to which that will happen is not known and is estimated. Loans and receivables are accounted for at amortized cost using the effective interest method; however the effective interest rate is calculated using estimated cash flows based on an estimated settlement dated.

Plaintiff advances are deemed to be a financial asset as they are a contractual right to receive cash from another entity and are considered to be available-for-sale financial assets for accounting purposes, based on an evaluation of all the terms and conditions of the contracts. The terms of the plaintiff advances are on a non-recourse basis, and payment depends on the success and potential claim size. Thus, the terms may limit the expected cash flows and other than for credit deterioration, they are deemed not to be loans and receivables. Available-for-sale financial assets are valued at fair value, the accretion or reduction in value is recognized based on the effective interest method and recognized into finance income.

Once an advance/loan is made, the timing of the collection cycle is out of Case Funding's control. Therefore, the timing of actual collections will be irregular.

Impairment of Goodwill

Goodwill is evaluated for impairment on an annual basis, or more frequently if certain events or circumstances exist. The Company's impairment test of goodwill is based on the value-in-use which is estimated using a discounted cash flow model. The cash flows are derived from budgets for the next five years, excluding restructuring activities and future investments. Impairment testing is applied on an individual asset basis unless an asset does not generate cash inflows that are largely independent of the cash inflows generated by other assets or groups of assets. None of the Company's non-financial assets generate independent cash inflows and therefore all non-financial assets are allocated to cash generating units ("CGU") for purposes of assessing impairment.

CGUs are defined as the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Impairment losses are recognized when the carrying amount of a CGU exceeds the recoverable amount, which is the greater of the CGU's fair value less cost to sell and its value in use. Value-in-use is the present value of the estimated future cash flows from the CGU discounted using a pre-tax rate that reflects current market rates and the risks inherent in the business of each CGU. If the recoverable amount of the CGU is less than its carrying amount, the CGU is considered impaired and is written down to its recoverable amount. The impairment loss is allocated to reduce the carrying amount of the assets of the CGU, first to reduce the carrying amount of the CGU's goodwill and then to the other assets of the CGU allocated pro-rata on the basis of the carrying amount of each asset. Other than the cash flow estimates, the value-in-use is most sensitive to the discount rate used and the growth rate applied beyond the five year estimate. Changes in these estimates and assumptions could have a significant impact on the value-in-use and/or goodwill impairment.

Convertible Debentures

The convertible debentures had several embedded derivative features which were determined to not meet the criteria for treatment as equity components and would otherwise be required as separate financial instruments, measured at fair value through the profit or loss. The Company had elected under IAS 39.11A to designate the entire convertible debentures (and all the embedded derivatives) as a combined financial liability at fair value through profit or loss. As the convertible debentures were fair valued based on the trading price on the Toronto Stock Exchange every reporting period, there may have been increased volatility in our reported net income. As result of the election to value the convertible debentures at fair value, the expenses related to the issuance of the convertible debenture were expensed when incurred.

Share-based Payments

The Black-Scholes model is used to fair value options issued by the Company. The model requires the use of subjective assumptions including the expected share price volatility. In addition, the options issued have characteristics different from those of traded options so the Black-Scholes option-pricing model may not provide a reliable single measure of the fair value of options issued. Changes in the subjective assumptions can have a material effect on the fair value estimate.

Interest rate derivatives

Financial instruments accounting requires recognition of the fair value of all derivative instruments on the statement of financial position as either assets or liabilities. Changes in a derivative's fair value are recognized currently in earnings unless specific hedge accounting criteria are met. Gains and losses on derivative hedging instruments must be recorded in either other comprehensive income or current earnings, depending on the nature and designation of the instrument.

Interest rate derivatives are not considered trading instruments as the Company intends to hold them until maturity. Nonetheless, interest rate derivatives do not qualify as a hedge for accounting purposes, and are therefore recorded as separate derivative financial instruments. Accordingly, the estimated fair value of interest rate derivatives is recorded as an asset or a liability on the accompanying consolidated statement of financial position. Payments made and received pursuant to the terms of the interest rate derivatives are recorded as an adjustment to interest expense, and adjustments to the fair value of the interest rate derivatives are recorded as gain or loss on interest rate derivatives. The fair value of interest rate derivatives is based upon the estimated net present value of cash flows.

Taxes

Pawnee and Blue Chip use the asset and liability method to account for taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for future tax benefits for which realization is not considered more likely than not. Pawnee and Blue-Chip account for their lease arrangements as operating leases for federal tax reporting purposes. This results in temporary differences between financial and tax reporting for which deferred taxes have been provided.

Significant management judgment is required in determining the provision for taxes, deferred tax assets and liabilities and any necessary valuation allowance recorded against net deferred tax assets. The process involves summarizing temporary differences resulting from the different treatment of items, for example, leases for tax and accounting purposes. These differences result in deferred tax assets and liabilities,

which are included within the consolidated statements of financial position. Management must then assess the likelihood that deferred tax assets will be recovered from future taxable income or tax carry-back availability and, to the extent management believes recovery is not probable, a

FUTURE ACCOUNTING STANDARDS

A listing of the recent accounting pronouncements not yet adopted by the Company is included in Note 2(b) - *New Accounting Standards* in the audited consolidated financial statements for the year ended December 31, 2018.

RELATED PARTY TRANSACTIONS

See Note 25 - *Related Party Transactions* in the audited consolidated financial statements for the disclosure of key management compensation.

CONTROLS AND PROCEDURES**Disclosure Controls and Procedures**

The Chief Executive Officer and the Director of Finance (the "Certifying Officers"), along with other members of management, have designed, or caused to be designed under their supervision, Disclosure Controls and Procedures ("DC&P") to provide reasonable assurance that (i) material information relating to the Company is made known to them by others, particularly during the period in which the annual filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

The Certifying Officers have assessed the design effectiveness of the Company's DC&P as at December 31, 2018 and have concluded that the design of the Company's DC&P is effective as at that date.

The Certifying Officers have also evaluated the operating effectiveness of the Company's DC&P and have concluded that the Company's DC&P was effective as at December 31, 2018.

Internal Control over Financial Reporting

The Certifying Officers, along with other members of management, have also designed, or caused to be designed under their supervision, Internal Control over Financial Reporting (“ICFR”) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes prepared in accordance with IFRS. The Certifying Officers have used the Internal Control - Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”), to design the Company’s ICFR.

The Certifying Officers have also evaluated the operating effectiveness of the Company’s ICFR and have concluded that the Company’s ICFR was effective as at December 31, 2018.

During the quarter ended December 31, 2018, there has been no significant change in the Company’s ICFR that would have materially affected, or would be reasonably likely to materially affect, the Company’s ICFR.

Limitations of an Internal Control System

The Certifying Officers believe that any DC&P or ICFR, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs.

Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues, including instances of fraud, if any, within the Company have been prevented or detected. These inherent limitations include, amongst other items: (i) that management’s assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; (ii) breakdowns could occur because of undetected errors; and (iii) controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override.

The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

Accordingly, because of the inherent limitations in a cost effective control system, misstatements due to error or fraud

may occur and not be detected. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

MARKET FOR SECURITIES

The Company’s common shares are traded on the Toronto Stock Exchange under the symbol CHW. The following table summarizes the high and low sales prices of the common shares and the average daily trading volume for each month in the year ended December 31, 2018.

	Common Shares		Average Daily Volume
	High	Low	
January	\$12.49	\$11.33	13,221
February	\$11.60	\$9.83	17,700
March	\$11.45	\$9.04	32,225
April	\$10.88	\$10.49	19,643
May	\$10.80	\$10.01	20,146
June	\$11.20	\$10.30	15,396
July	\$11.75	\$11.00	11,558
August	\$12.59	\$11.64	19,662
September	\$12.25	\$11.56	12,601
October	\$12.14	\$9.96	22,665
November	\$10.93	\$9.95	17,135
December	\$10.66	\$8.81	25,582
	<u>\$12.59</u>	<u>\$8.81</u>	<u>18,961</u>