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FINAL TRANSCRIPT

Street Capital Group Inc.

Second Quarter 2016 Financial Results Conference Call

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CORPORATE PARTICIPANTS

Jonathan Ross
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Ed Gettings
Street Capital Group Inc. — Chief Executive Officer

Marissa Lauder
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CONFERENCE CALL PARTICIPANTS

Dylan Steuart
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Jaeme Gloyn
National Bank Financial — Analyst

Jeff Fenwick
Cormark Securities — Analyst

Marc Charbin
Laurentian Bank Securities — Analyst

PRESENTATION

Operator

Hi, everyone. Welcome to Street Capital Group's second quarter 2016 financial results conference call.

As a reminder, this conference is being recorded on Wednesday, August 10, 2016.

At this time, all participants are in a listen-only mode.

Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for research analysts to queue up for questions.

If anyone has any difficulty hearing the conference, please press *, 0 for Operator assistance at any time.

I will now turn the call over to Jonathan Ross, Head of Investor Relations for Street Capital Group. Please go ahead, Mr. Ross.

Jonathan Ross — Head of Investor Relations, Street Capital Group Inc.

Thanks, Sharon (phon). Good morning, everyone, and thanks for joining us today.

Street Capital Group's second quarter 2016 financial results were released this morning. The press release, financial statements, and MD&A are available on SEDAR, as well as on our website, streetcapitalgroup.ca.

Before passing the call over to Ed Gettings, we would like to remind listeners that portions of today's discussion contain forward-looking statements that reflect current views with respect to future events, such as Street Capital Group's outlook for future performance.

Any such statements involve risks and uncertainties, and undue reliance should not be placed on such statements. Certain material factors or assumptions are implied in making forward-looking statements, and actual results may differ materially from those expressed or implied in such statements.

The factors that could cause actual results or events to differ materially from current expectations include, among other things, risks related to market factors, no assurance that Street Capital will receive regulatory approvals to operate as a Schedule I bank, and other factors discussed in materials filed with applicable securities regulatory authorities from time to time, including matters discussed under Risk Factors in the Company's Annual Information Form for the year ended December 31, 2015.

Street Capital Group does not undertake to update any forward-looking statements, except as required.

I will now pass the call over to Ed Gettings, Chief Executive Officer of Street Capital Group.

Ed Gettings — Chief Executive Officer, Street Capital Group Inc.

Thank you, John. Good morning, everyone, and thank you for participating on today's call. I'm joined on the call today by Lazaro DaRocha, President of Street Capital, and Marissa Lauder, our Chief Financial Officer.

We are very optimistic regarding the future of Street Capital Group. Management is heavily invested in the future of the Company, owning almost 20 percent of the outstanding stock, and is very focused on creating shareholder value.

Since we initiated our normal course issuer bid in March, we have been active in the market and to July 31st have repurchased 327,106 common shares. We will continue to be active in the market at these prices.

This year we are focused on putting the pieces in place to drive revenue growth starting in 2017. We have three primary objectives in 2016.

Our first objective is to advance our Schedule I bank application through to completion. The bank platform allows the transition from a single product lender to a multi-channel, multi-product financial services entity. We continued to advance this application during the quarter, and Lazaro will update you later on on the call with more details.

Our second objective is to grow mortgages under administration and hold our market share in the mortgage broker channel. Originations were lower than what we would have liked during the quarter, as the underwriting adjustments we made in Q1 2016 had some spillover effects into the second quarter of 2016.

Mortgage commitments issued in Q1 2016 for closing and Q2 2016 were lower and affected Q2 new originations. However, in the latter part of the quarter we were back on track, and our market position in the broker channel reflects this as we improved to fourth position from sixth last quarter.

We are looking forward to a continual recovery during the second half of the year and are targeting to remain number three or four in the broker channel.

We expect Q3 and Q4 of 2016 to be stronger than the comparable periods in 2015; however, the disruption caused by the underwriting changes we implemented back in Q1 will cause earnings to be lower this year than we had originally expected.

Our third objective for 2016 is to continue to generate renewal volumes of 75 to 80 percent of loans eligible for renewal. Year to date, we have renewed $710 million of mortgages, which is close to the 75 percent of those available for renewal.

Moving into next year and 2018, we will drive solid earnings growth as loans underwritten in the past years come up for renewal.

We have built a substantial brand in the industry. With our 130,000 customers and key broker relationships as a base, we see a bank platform as the optimal foundation to leverage our leading brand into a multiproduct, multichannel opportunity.

And we are looking forward to using this platform to drive significant value for our shareholders in the coming years.

I'll now turn the call over to Marissa for some additional commentary.

Marissa Lauder — Chief Financial Officer, Street Capital Group Inc.

Thank you, Ed, and good morning, everyone. I'm pleased to present the second quarter 2016 key financial highlights.

Adjusted earnings per share were $0.05 in the quarter compared to $0.09 last year. While we did anticipate lower EPS this year given our expectations for lower renewal volumes and higher expenses, new originations were below our targets for the quarter for the reason Ed already described.

We sold 2.54 billion of mortgages in Q2 compared to 3 billion last year. Of this total, 380 million were renewals compared to 407 million last year.

Net gains on sale of mortgages were 19.8 million compared to 26.2 million last year. Gains as a percentage of mortgages sold was 185 basis points in the quarter, above our normally expected range of 178 to 182 basis points. This was lower than the 190 basis points in Q2 2015 when spreads were higher than normal.

We continue to expect that on a full year basis gains as a percentage of loans sold will be in the range of 178 to 182 basis points.

Our acquisition expense ratio was 106 basis points in the quarter. This compares to 102 basis points last year. The increase reflects lower relative renewal volume year over year and a broker incentive program we launched late in Q1 2016 that increased acquisition costs in the quarter.

Moving into the remainder of the year, we continue to expect 2016 renewal volumes that are approximately 15 percent lower compared to the 1.77 billion renewed in 2015. But in 2017, as we've discussed previously, we expect the upward trend in renewal volumes to resume, with renewal volumes expected to exceed 2015 renewal volumes by 10 to 15 percent, and 2018 renewal volumes are expected to increase by 30 to 40 percent over a strong 2017, providing a real revenue boost in these years.

While expenses were managed tightly in the quarter, as anticipated, they were up sequentially from Q1. This reflects the growth in our people from 187 to 241 year over year and from 215 in Q1 2016.

As we continue to advance our Schedule I bank application, this also reflects staff additions to support the operational changes that we made in Q1 and into Q2.

Given our current primary business model of originate to sell, we measure our expense efficiency by the ratio of operating expenses as a percentage of mortgages originated and renewed.

In Q2 2016, this ratio was 48 basis points, and as expected, this is up from 37 basis points last year. Given the seasonal nature of mortgage originations and renewals, this measure will vary by quarter. On a 12-month basis, we expect this ratio to be in the range of 46 to 52 basis points through to 2018, with 2016 coming in at the high end of this range.

Before I close, I'd also like to draw your attention to our tax loss carry-forward balance, which was 315 million at the end of June. This represents a real and sustainable advantage for the Company.

For us, this means that right now we're not paying any cash taxes, and we don't expect to pay cash taxes for many years to come. As a result, the net income after-tax measure underestimates the true earnings available to the Company.

With that, I'll pass the call to Lazaro.

Lazaro DaRocha — President, Street Capital Group Inc.

Thanks, Marissa. Good morning. As you know, at Street Capital we are focused on credit quality as our number one priority.

Our credit quality continues to be strong. At June 30th, the serious arrears rate on our portfolio of mortgages was 11 basis points, well below the CBA performance. This is also well below last year, which at 16 basis points was also a very good rate on a well-seasoned portfolio.

At the end of June at time of origination, the average beacon score on our profit was 749, the average loan to value ratio was 81.2, and the average total debt service ratio was 36.1 percent.

Now turning to the status of our bank application. As you know, we are in the pre-commencement review phase of our application to the Minister of Finance to continue as a Schedule I bank.

As discussed last quarter, in Q1 the Company implemented various operational changes in order to address the OFSI observations from their on-site review in Q4 of 2015. In Q1 we informed you that we expected OSFI to return on site during the summer to confirm that the changes made by the Company have been adequately implemented.

We are pleased to confirm that OSFI did, in fact, return in July, and we are now awaiting the results of that visit. We continue to fully expect to receive approval to operate as a Schedule I bank in fiscal 2016; however, we have not built any meaningful contribution of profitability into our expectations until 2017.

At this point, I'd like to ask the Operator to open the lines for questions. Thank you.

Q&A

Operator

If you'd like to ask a question at this time, please press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, press the # sign. We will pause for a moment to compile the Q&A roster.

Your first question comes from Dylan Steuart from Industrial Alliance. Your line is open.

Dylan Steuart — Industrial Alliance Securities

Good morning, everybody.

Ed Gettings

Good morning, Dylan.

Marissa Lauder

Good morning, Dylan.

Dylan Steuart

A quick question. You guys reiterated your view that new originations for 2016 should match 2015; obviously the first half a little bit light. So just maybe a bit more colour in what you're seeing out there that gives you the confidence in that outlook?

Ed Gettings

Dylan, we're looking at our current pipeline and we're feeling good about the fact that we think we have turned the corner on those operational issues that we were dealing with in Q1 and Q2. Market share during the quarter went up as well from 7.6 percent in Q1 to 8.4 percent, placing us in the number four position, so we believe that we are building momentum, and we're clearly headed in the right direction.

Marissa Lauder

And, Dylan…

Dylan Steuart

Just looking at the market—sorry, go ahead.

Marissa Lauder

Sorry, Dylan. Also compared to 2015, we expect the second half of this year to be stronger than 2015.

Dylan Steuart

Okay. And I guess just maybe just a general market commentary, just given the affordability issues in Toronto and Vancouver. Are you seeing any less demand from first-time buyers? Are they being squeezed out of the market? Are you still seeing, I guess, a healthy pipeline overall?

Ed Gettings

What I read in industry reports, Dylan, is that we still have a very healthy pipeline. The broker channel itself is growing at about between 4 and 5 percent year over year on a year-to-date basis.

First-time buyers, yes, the price points are being stretched for them. And what I understand is happening is that instead of buying houses they're focusing on condominiums because the price point's more attractive for them.

Dylan Steuart

Okay. And just one final question just on the new bodies added, and I believe it went up to 241 from 215 last quarter. Just wondering what area of hires that you made on the increased body count?

Lazaro DaRocha

They were primarily, if not all, within our underwriting and QA areas. They are all in response to the actions we took, given OSFI's visit back in Q4 of last year.

Dylan Steuart

Okay. That's sort of what I figured. And you remain pretty confident at these staffing levels? Or will there be any more expansion required do you think in the near future here?

Lazaro DaRocha

I don't envision having any sort of material expansion for any significant operational changes. I think that's behind us. Any increases would be nominal at this point.

Dylan Steuart

Okay. Great. That's it for me, everybody, but thanks very much.

Ed Gettings

Thank you.

Marissa Lauder

Thanks.

Operator

Your next question comes from Jaeme Gloyn from National Bank Financial. Your line is open.

Jaeme Gloyn — National Bank Financial

Hi. I was just hoping you could provide a little bit more colour on the broker incentive program and some details around that and how much of a contribution was that to the increase in acquisition costs?

Marissa Lauder

Oh, Jamie, thank you for the question. We had a broker incentive program out there that basically increased the acquisition costs on a net basis by about 5 basis points on certain products. And so given that, the contribution is anywhere between 3 and 4 basis points on the acquisition cost.

That program was discontinued; however, there are some mortgages in the pipeline that will come through in the third quarter with that promo on it.

Jaeme Gloyn

Okay. So some in Q3, but Q4 we shouldn't expect to see anything from (unintelligible) program.

Marissa Lauder

Well, we react to competitive nature of commissions, so I can't say we wouldn’t introduce another promo.

Jaeme Gloyn

Okay. And this was just sort of like a onetime quick promo that you can turn on and off at any time?

Lazaro DaRocha

Yes. And Marissa alluded to the fact that it was a reaction by what was in the market by our competitors. So that's what she means by if—we always need to be competitive. We're never the lowest rate or the highest commission, but we need to be competitive. So this was a reaction to others' moves.

Jaeme Gloyn

Great. Thank you. And just talking about the 2018 renewal pipeline that's going to—or your expectation that it's going to increase 30 percent to 40 percent over 2017 renewals…

Marissa Lauder

Mm-hmm.

Jaeme Gloyn

What's driving that number? And I'm trying to base this off of a origination growth in 2013 versus 2012 of 30 percent, so it's kind of like a one-for-one, whereas in 2017 we're not getting that kind of one-for-one versus the origination year. So if you could just provide a little bit more colour on the 30 to 40?

Marissa Lauder

Okay. I'll have to look into the numbers in a little more detail, but generally speaking, the 2017 numbers still had some spillover effects from the three to four-year promos that we had talked about that reduced the 2016 renewals.

So it's the mix—it's the mix of the book.

Jaeme Gloyn

Okay.

Marissa Lauder

Whereas the mortgages coming up for renewal in 2018 were primarily five-year.

Jaeme Gloyn

Okay. And how is the mix currently with respect to mortgages originated? Is it back to primarily five-year, would you say, sort of above the 90 percent level?

Ed Gettings

Yeah. We're typically originating five-year terms, Jamie, as a rule of thumb, but from time to time there might be some promotions, but our pattern has typically led as a five-year cycle.

Jaeme Gloyn

Okay. Great. And then just last one for me; in Alberta, could you provide a little bit more colour around the performance of originations? Is it a decline of X percent year over year? And what you're seeing in that market specifically?

Ed Gettings

It's a slight decline on year-to-date originations. We would have had 15 percent of the book in Alberta last year; it's dropped down to 14 percent. So it's definitely a function of the market in Alberta, as well as some of our underwriting guidelines.

Jaeme Gloyn

Okay. Great. I'll re-queue.

Operator

Your next question comes from Jeff Fenwick from Cormark Securities. Your line is open.

Jeff Fenwick — Cormark Securities

Hi. Good morning, everybody. Just wanted to follow up on the questions around renewals; you mentioned in your opening comments that you're approaching 75 percent of renewals, and you hope to achieve that number or higher going forward. Can you just give us some colour around what allows you to get there or enables you to get there? Is it a question of customer service? Or data analytics? Or some combination of factors such as that?

Ed Gettings

Yeah. So our target range is 75 to 80 percent, Jeff, and we definitely have a retention team in place that if we see a customer calling in that has a desire like for a payout statement or something like that, we'll immediately flip them to an in-house retention team and we'll have a dialogue with the customer to understand what their needs are.

If they're looking to negotiate a bit on rate, we'll take that into account. But our goal is to try to renew in the 75 to 80 percent range.

Jeff Fenwick

Okay. And are you proactively reaching out to customers then as they're approaching the end of the term on the mortgage then to make sure you do that?

Ed Gettings

We're mailing out a standard renewal 90 days in advance. If we haven't heard from that customer within 30 days we are calling them, re-contacting them to open up a dialogue with them.

Also what we are doing is also going out throughout the term of the mortgage with communications to our portfolio. And again, the objective behind that communication strategy is just to let them know that we're here if they have a refinancing need or other sort of financial need that they can call Street directly, and we'll work with them to solve their issues.

Jeff Fenwick

Okay. And I noticed in your MD&A you've provided us with a table here on the MUA maturities expected going forward. I'm just wondering, does that number factor in amortization off of those mortgages or prepayment patterns? Or should we just be looking at that number and taking 75 percent of it as your target?

Marissa Lauder

I wouldn't take 75 percent of it. Those are contractual maturities, so they reflect a balance today and the contractual maturities that equal to that balance. So you would have to consider both midterm liquidations, amortization, and renewal rates.

Jeff Fenwick

Okay. That's great. That's what I was wondering. And then with respect to the bank, you do give us some sort of pro forma capital ratios that you would expect if you were to look at it—or it to become a bank today. Can you give us an estimate of what the gross value of the regulatory capital would be that you'd have on commencement as a bank? Is it effectively your shareholders' equity today? Or what's the adjustment there?

Lazaro DaRocha

It would be what is disclosed on our Street Capital financial corporation legal entity shareholders' equity, which is different than the parent company's shareholder equity.

Marissa Lauder

So the shareholders' equity in the parent includes a higher amount of shareholders' equity than would be in the sub. We haven't disclosed that yet, unfortunately.

Jeff Fenwick

Okay. And…

Lazaro DaRocha

I can tell you that OSFI is satisfied with the capital in the subsidiary that is going to become the bank.

Jeff Fenwick

Gotcha. Okay. And then maybe just one last question here. There was a question earlier about Alberta, but I noticed a lot of your origination growth here seems to be focusing on the BC market, which is obviously very hot. Can you just give us some thoughts about how you're approaching that market, given how the prices have shot so much higher this year and all the concerns about that market?

Ed Gettings

Yeah. So two things; I want to remind everybody that 100 percent of our loans are insured. That doesn't mean that we ignore the credit risk. We operate as if we own it, reflected in our 11 basis points of serious arrears.

But the other aspect is that we are really not targeting that high-end segment of the marketplace. Like other lenders, we have a sliding scale. So as you go up in loan amount we reduce the loan to value that we'll lend to you as a customer. You have to have more skin in the game.

Two examples: if it's a $1 million home and you're looking forward you have to put 20 percent down. Because it's over $1 million you have to put in 200 million and you might be looking to Street for $800,000. We might consider lending you that full amount, depending on a number of underwriting criteria.

If it's a $3 million home you have to have $600,000 in as a down payment, and you're looking for 2.4. I'm not—the maximum that I will lend is in the 1.8, 1.9 range which takes our loan to value down into the 60 to 65 percent range. So we've got lots of capital protection in case of a default or a downturn in the marketplace.

Our average loan size is in the $375,000 range.

Jeff Fenwick

Okay. Great. All right. That's all I had. Thank you very much.

Operator

Once again, if you would like to ask a question, press *, then the number 1 on your telephone keypad.

Your next question comes from Marc Charbin from Laurentian Bank Securities. Your line is open.

Marc Charbin — Laurentian Bank Securities

Good morning. Just a quick question on your targeted expense ratio; does that also apply to the incremental revenue you'd expect from a successful bank application?

Marissa Lauder

Yes. It does. So the range of 46 to 52 applies on that as well.

Marc Charbin

Okay. And in terms of nominal expense growth looking at 2017, would you say it would be above or below 8 percent?

Marissa Lauder

Well, as we move through our planning cycle this year and think about our strategy and growing the business and taking advantage of the banking platform, we're going to balance our operating leverage improvement with the need to invest in the future. So I've given the range; that's the range that we expect to operate in to improve our profitability.

But as we move through I can't really give you guidance that is that specific.

Marc Charbin

Okay. Thank you.

Operator

Once again, if you'd like to ask a question, please press *, then the number 1 on your telephone keypad.

We do not have any questions at this time. I will turn the call over to the presenters.

Jonathan Ross

Thanks, everyone, for participating on today's call and for your support. Just feel free to reach out anytime today if you have any other questions.

Thanks, and talk to you next quarter. Bye-bye.

Operator

This concludes today's conference call. You may now disconnect.

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