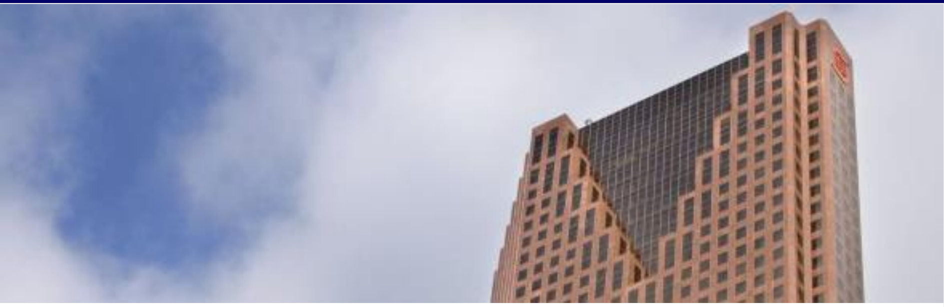
January 23, 2017

QUIC RESEARCH REPORT



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The Bank of Nova Scotia Investment Defence

A Closer Look at Canada's Most International Bank

Introduction

Purchased on QUIC's first trading day, September 21, 2010, the Bank of Nova Scotia ("Scotiabank", "BNS", "the Company") has been one of the few remaining core holdings since inception. While QUIC remains strongly in favour of Scotiabank, we feel that we need to periodically take a deep dive to re-evaluate how bullish we are on the stock.

Scotiabank has had an incredible year for growth, pleasing shareholders with extremely high returns. For context, its returns can be compared to some of the highest growth companies in North America. Alphabet rose 11%. Facebook rose 30%. Amazon rose 35%. Scotiabank outpaced all of these at 42%, share price appreciation, soaring to all-time highs and adding $28 billion to its market cap. Given this period of high growth, we take a closer to see what we can expect for 2017.

Our updated investment thesis for 2017 is as follows:

- Investment Thesis I: Industry-Leading Global Banking Platform
- Investment Thesis II: Improving Credit Quality and Energy Exposure
- Investment Thesis III: Global Banking and Markets Poised for Growth

QUIC Research Reports focus on emerging investment themes that affect current portfolio companies and companies under coverage.

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Company Overview

Introduction

Founded in 1832, over 30 years before the Confederation of Canada, Scotiabank is one of Canada's best known banks. By deposits and market capitalization, it is Canada's third largest bank. Scotiabank serves more than 23 million customers worldwide, providing financial services in more than 55 nations.

The Company has a market capitalization of $93.5 billion, and has earned revenue of $23.94 billion and net income of $7.0 billion in the last fiscal year.

The company's core business segments consist of Canadian Banking, International Banking, and Global Banking and Markets.

Canadian Banking

Canadian Banking is extremely diversified and involves providing financial advice, capital services, and wealth management services to over 10 million customers and businesses. This includes the services of Tangerine, a day-to-day banking subsidiary of Scotiabank, and those of the company's corporate banking partners and tools.

International Banking

International Banking provides a full range of financial products, solutions, and advice to retail and commercial customers outside of Canada. Scotiabank is heavily invested in the region of Latin America, more specifically, the nations of Peru, Chile, Mexico, Columbia, and the Caribbean. As a bank heavily involved in non-Canadian customers, Scotiabank holds significant exposure to Central American economic performance, and as such, often refers to itself as ' the global Canadian bank'.

Global Banking and Markets

Lastly, Scotiabank's Global Banking and Markets division provides corporate, government, and institutional investor clients with a variety of services including: Investment Banking, Corporate Banking, Capital Markets, Transaction Banking Solutions and more. Scotiabank is full-service wholesale bank and investment dealer in Canada and Mexico, and the company offers a range of financial instruments and services to select markets including Europe, Asia, and Australia.

EXHIBIT 1

Historical Share Price Performance

After a record year in 2016, BNS is trading at all-time highs

Source: Capital IQ

EXHIBIT 2

Historical Price to Book Value Trading Multiple

Despite incredible share price appreciation in 2016, we do not believe the valuation is frothy enough to sell

Source: Capital IQ

Summary of Last Twelve Months Performance

	Diluted EPS	CET1 Ratio	Operating ROE	Book Value per Share	Key Highlights
Q1/16	$1.43 (+6% YoY change)	10.1%	13.8%	$42.32	– 9% YoY revenue growth – Quarterly dividend increased by 2 cents to $0.72 per share
Q2/16	$1.46 (+3% YoY change)	10.1%	12.1%	$40.70	– YoY revenue growth of 10% outpaced 7% expense growth – Incurred restructuring charge of $278 million, expect run-rate savings of ~$550 million
Q3/16	$1.54 (+6% YoY change)	10.5%	14.8%	$42.14	– Quarterly dividend increased by 2 cents to $0.74 per share – Strong trading and banking performance
Q4/16	$1.57 (+8% YoY change)	11.0%	14.7%	$43.59	– PCL ratio improved to 45 bps, down from 47 bps YoY – Double digit growth in credit cards helped widen Canadian margins YoY
2017 Targets	+5-10% YoY change	11%+	14%+	n/a	– Management wants to maintain positive operating leverage into 2017

Source: Company Reports

Scotiabank had an extremely successful 2016, as it was able to grow revenues by 10% YoY, grow EPS by 8%, maintain a strong capital position and raise its annual dividend by 6%.

Industry Overview

Canadian banks have long been considered to be some of the safest and best-run institutions in the world. This reputation was reinforced in 2016, as Canadian banks have been awarded the title of the "world's soundest banks" for eight of the past nine years. While we do rely on the consistent performance of our Canadian bank holdings, we see a few key trends shaping the landscape of the industry into 2017.

Multiple-Driven Growth

While Canadian banks have seen their stocks rise by 26% in 2016, much of this has been due to a spike in the multiples were willing to pay. Analysts suggest that only 20% of the price gains for the sector can be attributed to changing earnings expectations, while multiple expansion was responsible for the other 80%, as investors globally have relentlessly searched for yield. NIMs have continued to be squeezed as a result of the depressed Canadian interest rate environment, hurting bank earnings across the board. While it is no secret that the U.S. is beginning a tightening cycle, Bank of Canada governor Stephen Poloz indicated that a rate cut is "on the table", proving that Canada's rate environment continues to diverge from that of the U.S. Credit Suisse estimates that Canadian banks will see EPS growth of ~5% in 2017, a slight uptick from 2016 numbers, while mortgages are expected to slow due to new qualification measures implemented by the OSFI. It is important to note that LTM P/E multiples are still slightly below the historical mean, indicating that there could still be upside potential if earnings improve.

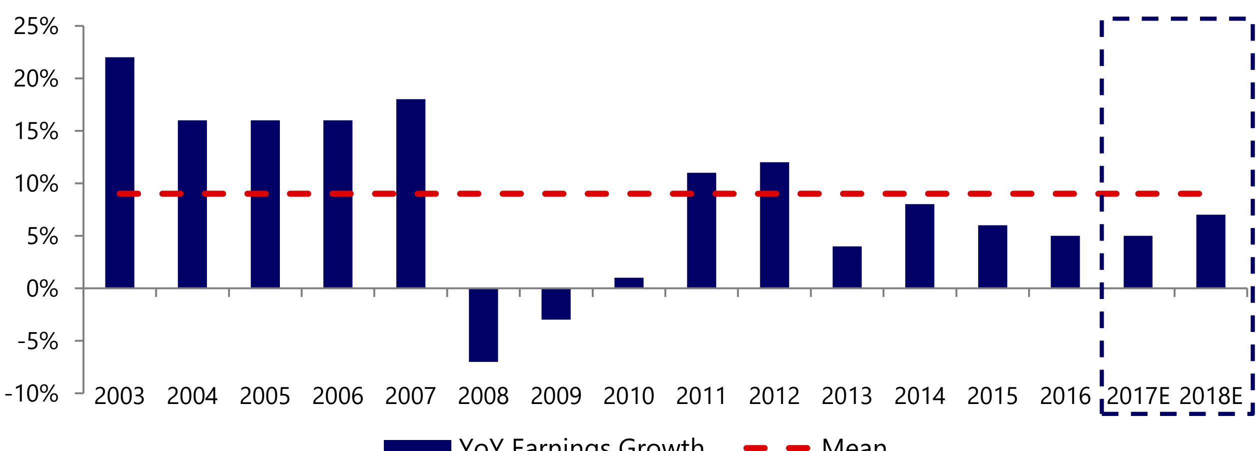
Areas for Improvement

Canadian banks will continue to make expense management a priority in hopes of spurring bottom line growth. Non-interest expense ratios have declined steadily over the past two years, and this trend is expected to continue into 2018. A changing regulatory environment and the imminent threat of a downturn in the real estate market pose challenges for Canadian banks into 2017. However, we believe that moderate loan growth and careful expense management will help Canadian banks to see upside in 2017.

EXHIBIT 3

Historical YoY EPS Growth of Canadian Banks

2016, 2017E and 2018E earnings growth estimates are all below long-term median of 9%



Source: Credit Suisse

Investment Thesis I: Industry-Leading Global Banking Platform

Investment Thesis I: Industry-Leading Global Banking Platform

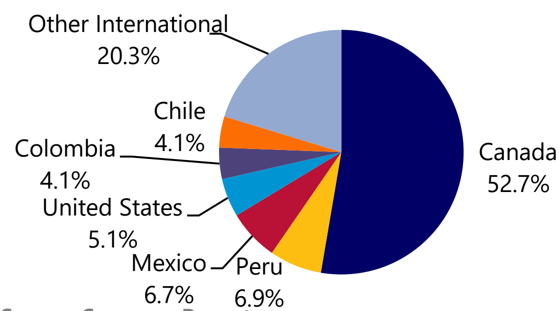
Compared to all other Big 5 Canadian banks, Scotiabank offers the most unique geographic profile from international operations. While large Canadian banks such as TD and BMO have exposure to the United States in varying degrees, no other bank generates meaningful and significant portions of earnings from high growth international markets other than Scotiabank. Favourable emerging markets exposure offers increased upside potential versus a slower-growing peer set.

Scotiabank has an incredible global banking platform, with a strong focus on Central and Latin America. BNS has a global footprint in over 55 countries, with over 50,000 international employees across over 1,800 branches. It has been operating in Canada, the U.S. and the Caribbean for over 125 years, establishing a strong presence in a wide variety of international markets. Scotiabank focuses its international operations in Peru, Mexico, the U.S., Colombia, Chile and other international markets, as shown in the following segmented revenue graph.

EXHIBIT 5

Revenue Breakdown by Geography (FY2016)

Scotiabank earns half of its revenue internationally



Source: Company Reports

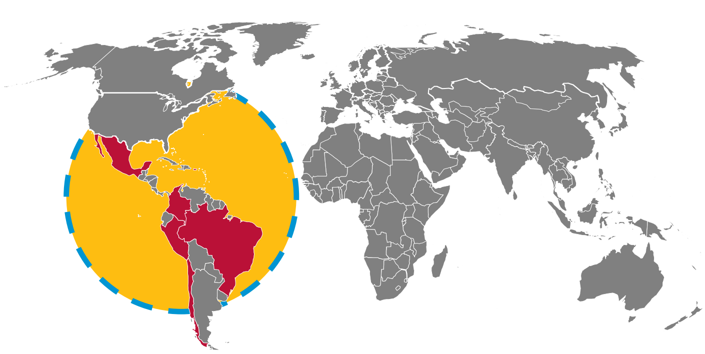
Over the past two years with relatively flat NIMs, the bank has grown international banking net income and total assets in excess of 10% each year. This highly successful international performance was primarily driven by revenue growth rather than increased operating profitability. In 2016, BNS also expanded operating leverage.

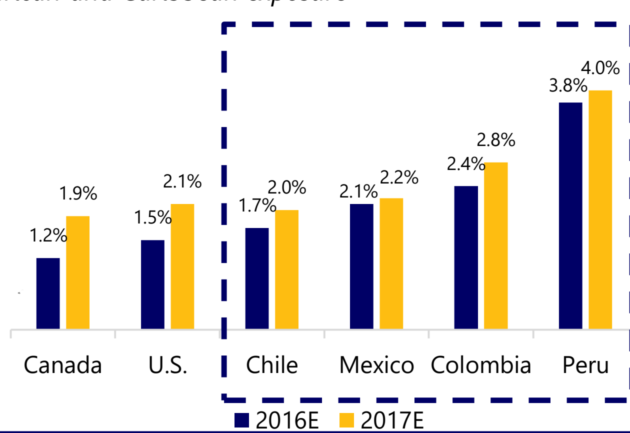
Following an incredible year across Canadian and international segments, BNS has outpaced its peers in growth, and has returned over 40% in the past year.

EXHIBIT 4

Highlighted Latin American and Caribbean Operational Footprint & Real GDP Forecasts

While Scotiabank has international operations in the U.S., Europe, Asia, Australia and beyond, its key distinguishing factor stems from its significant Latin American and Caribbean exposure





Source: Scotiabank Economics

Investment Thesis II: Improving Credit Quality and Energy Exposure

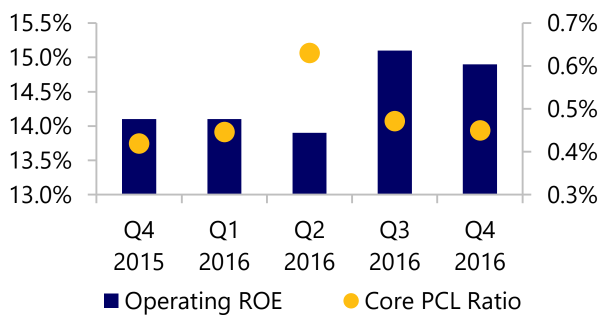
Investment Thesis II: Improving Credit Quality and Energy Exposure

While Scotiabank is often seen as one of the faster-growing large banks in Canada, this is not without any offsetting factors. Scotiabank's above-average growth is largely derived from international earnings. In the context of banks, this is seen through higher net interest margins at the expense of higher provision for credit losses.

EXHIBIT 6

Recent Operating Profitability and Credit Quality

BNS's last three quarters show the story of de-risking its loan portfolio to drive ROE expansion



Source: Company Reports

As seen above, PCLs peaked in Q2 2016. Since then, BNS has seen a period with continued mean reversion, with core PCLs at 0.449% in the latest reported quarter. This has ultimately helped BNS achieve improved return on equity in excess of 100bps over Q2 2016 in the following quarters.

Scotiabank derives much of its international income from Latin America and the Caribbean. Strong risk management has kept PCLs down in international markets, with a slight decrease in 2016 relative to 2015.

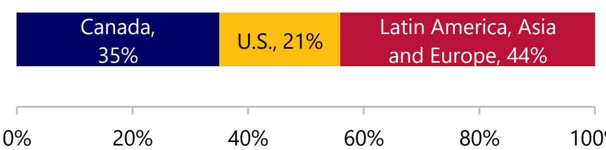
Energy Exposure

As of Q4 2016, BNS had $15.6 billion in loan exposure to companies in the energy sector – about 3.1% of the total loan portfolio, down 40 bps year-over-year. Of these commitments, 59% were investment grade, leaving 41% subject to significant risk-reward upside in an improving oil market.

EXHIBIT 7

Drawn Energy Exposure by Geography

Scotiabank's energy exposure is geographically diverse



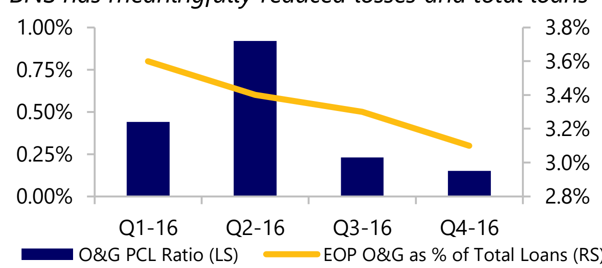
Source: Company Reports

From Q1 2015 to Q4 2016, Scotiabank has seen cumulative PCLs of $338 million. BNS has seen a cumulative energy loan loss ratio of 2.1% over this period, and expects to operate below guidance in the 3.0-3.5% range, in line with prior guidance in 2017.

EXHIBIT 8

LTM Oil & Gas Loan Exposure and PCLs

BNS has meaningfully reduced losses and total loans



Source: Company Reports

Comparing BNS to other Canadian banks, Scotiabank has the lowest gross impaired loans ratio, indicating that its loan portfolio has optimized its risk tolerance as well as risk diversification.

With WTI above $50 vs. a sub-$30 trough last January, BNS stands to benefit in a continued upswing in the oil market and Albertan economy.

Investment Thesis III: Global Banking and Markets Poised for Growth

Investment Thesis III: Global Banking and Markets Poised for Continued Growth

Scotiabank's Global Banking and Markets segment encompasses two main divisions: Business / Wholesale Banking and Capital Markets. In 2016 it grew at a very impressive pace, and Scotiabank's platform is positioned to continue rapid (albeit lower) periods of double-digit growth into 2017.

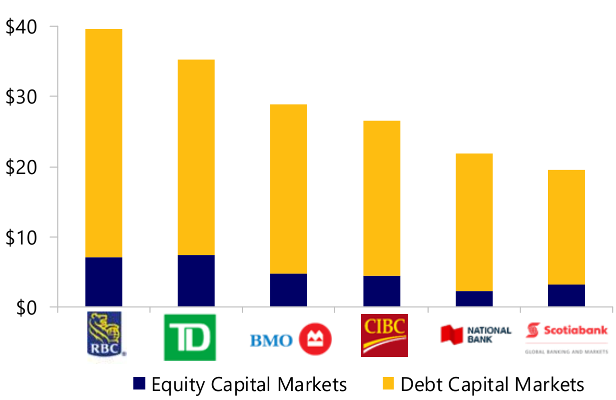
On the investment banking side, M&A advisory revenue can be highly volatile due to high variance in transaction size and frequency in Canada. Given that the debt capital markets space in Canada is heavily led by major federal and provincial debt raises, it is much more stable. Scotiabank's strong balance sheet should help it pick up a larger share of financing deal flow going forward.

Scotiabank has a very small presence, but as a result has been able to generate incredible growth in its business, rapidly stealing share from larger competitors and establishing itself as a legitimate force. With BNS's past growth, their trajectory in the coming years could propel the bank to capital markets deal flow levels in line with BMO and CIBC.

EXHIBIT 9

Domestic Financing Transaction Value (2016)

BNS currently has the smallest capital markets presence of any big six bank exclusively within Canada



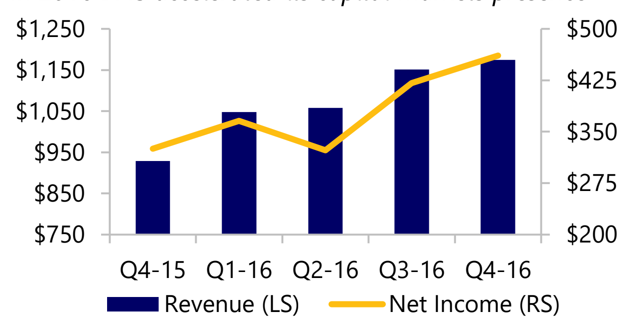
Source: Company Reports

Scotiabank's Global Banking and Markets segment has performed very well in 2016. Looking at the most recent quarter in isolation, BNS posted earnings up 10% QoQ and up 42% YoY, resulting from strong revenue growth up 26% YoY paired with increased efficiency and profitability.

EXHIBIT 10

Global Banking and Markets Recent Performance

In 2016 BNS accelerated its capital markets presence



Source: Company Reports

Industry-Leading Capital Position

As of Q4 2016, Scotiabank boasted a Basel III CET1 ratio of 10.98%, growing 45 bps since Q3 2016.

While Scotiabank does not have a relatively large capital markets presence, it has a sizeable balance sheet, significantly larger than many peers with larger investment banking operations. This underutilized balance sheet creates a bounty of risk-weighted assets currently unused by the bank.

Post-crisis, banks with strong capital positions are best positioned to grow their trading, underwriting and commercial lending segments. Tightening capital constraints can be a setback to banks, however BNS is well-positioned to have the balance sheet capacity necessary to sustain high growth in capital-intensive areas such as trading and underwriting. Of all Canadian banks, QUIC believes that BNS has the greatest upside potential in capital markets given its underutilized balance sheet, relatively small size and international exposure.

Catalysts & Risks

Catalysts

1. Capital Deployment Flexibility

Scotia's Q4/2016 CET1 ratio came in at 10.98%, an increase of 45bps, which was well ahead of analyst expectations. Having excess regulatory capital gives Scotia the ability to deploy capital much more freely than its competitor, given it is able to identify lucrative lending opportunities. Having sufficient core capital will allow the bank to pursue riskier segments of their loan book more aggressively, such as cards and corporate, thereby increasing their risk-weighted assets, should they so choose.

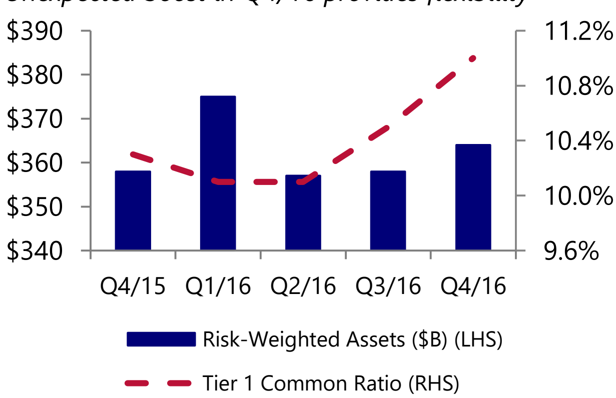
2. Financial Deregulation in the U.S.

The Trump administration has indicated several times that it intends to loosen regulatory oversight on financial institutions by making amendments to Dodd-Frank. Lessened regulation would be a tailwind for U.S. banks, allowing them to lend and trade more freely in hopes of driving top line growth over the coming year. Canadian banks with U.S. operations are poised to receive "spillover effects" from this growth if changes in regulation are to eventually be approved.

EXHIBIT 11

Steady Increase in CET1 Ratio

Unexpected boost in Q4/16 provides flexibility



Source: Dundee Capital Markets

Risks

1. International Exposure

As Scotia is more exposed than its peers to international markets, it is more subject to geopolitical risk than its competitors. Specifically, its exposure to Mexico and Latin America subject the company to downside risk if Trump imposes unfavourable policy (towards Mexico specifically). However, management feels that these exposures have led to an excessive discount of the company, and strong Q4 international results (7% decrease in PCL, 1.5% growth in average loans) should help to dampen this rhetoric.

2. Regulatory Changes

The OSFI recently imposed new regulation heightening the requirements to qualify for a mortgage. These actions are intended to help cool Toronto's scorching real estate market, and more difficulty in qualifying for mortgages could lead to a natural slowdown in mortgage lending for Scotia. However, the company has shifted its loan book towards card and auto loans in hopes of mitigating this risk, which has so far increased margins by +13 bps YoY.

3. Canadian Real Estate Market Exposure

As Canadian real estate valuations continue to soar, many fear that a correction in housing prices may be on the horizon in 2017. This could impair borrowers' abilities to pay their mortgages, which has led the OSFI and CMHC to take action to raise mortgage qualification standards.

4. Potential Canadian Interest Rate Cut

While not likely, an interest rate cut by the Bank of Canada would further squeeze NIMs, hurting the profitability of banks across the nation.

Valuation

EXHIBIT 12

Residual Income Valuation Model

On an intrinsic basis, Scotiabank seems to trade closely to fair value prior to its dividend

The Bank of Nova Scotia - Residual Income Model

($ in Millions Except Per Share Data)

	Historical	Projected				
December 31,	**2016**	2017	2018	2019	2020	2021
Normalized Net Income to Common:	**$ 7,368**	**$ 8,060**	**$ 8,939**	**$ 9,654**	**$ 10,176**	**$ 10,587**
% Growth:	**3.8%**	9.4%	10.9%	8.0%	5.4%	4.0%
Common Dividends:	**3,468**	**4,833**	**3,810**	**4,493**	**5,258**	**6,280**
% Growth:	**5.4%**	39.4%	(21.2%)	17.9%	17.0%	19.4%
Payout Ratio:	**47.1%**	60.0%	42.6%	46.5%	51.7%	59.3%
Beginning Common Equity:	**$ 50,545**	$ 54,227	$ 61,403	$ 70,480	$ 79,590	$ 88,458
Plus: Net Income to Common:		8,060	8,939	9,654	10,176	10,587
Plus: Stock Issuances:		3,919	3,919	3,919	3,919	3,919
Less: Common Dividends:		(4,833)	(3,810)	(4,493)	(5,258)	(6,280)
Plus: Other Considerations:		30	28	30	31	34
Ending Common Equity:	**$ 54,227**	**$ 61,403**	**$ 70,480**	**$ 79,590**	**$ 88,458**	**$ 96,718**
Avg. Risk-Weighted Assets:	**364,048**	385,891	409,044	429,497	450,971	469,010
% Growth:	**1.7%**	6.0%	6.0%	5.0%	5.0%	4.0%
Tier 1 Common Ratio:	18.3%	17.8%	19.0%	20.2%	21.2%	22.2%
Return on Common Equity:	13.6%	13.1%	12.7%	12.1%	11.5%	10.9%
Tier 1 Common Capital Calculation:						
Ending Common Equity:	**$ 54,227**	$ 61,403	$ 70,480	$ 79,590	$ 88,458	$ 96,718
Less: Disallowed Intangibles:	12,233	7,271	7,271	7,271	7,271	7,271
Plus: Other Adjustments:	-	-	-	-	-	-
Total Tier 1 Common Capital:	**$ 66,460**	**$ 68,674**	**$ 77,751**	**$ 86,861**	**$ 95,729**	**$ 103,989**
Residual Income / Excess Returns:		**$ 4,487**	**$ 4,864**	**$ 5,017**	**$ 4,983**	**$ 4,866**
Discount Period:	**0.0**	1.0	2.0	3.0	4.0	5.0
Mid-Year Discount Period:		0.5	1.5	2.5	3.5	4.5
PV of Residual Income:		$ 4,355	$ 4,446	$ 4,319	$ 4,040	$ 3,715

Valuation

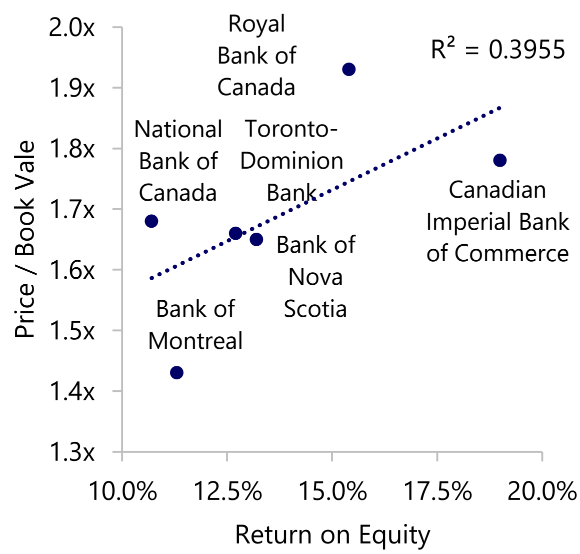
EXHIBIT 13

Residual Income Model Assumptions

Residual Income Assumptions		
Mid-Year Convention:		0.50
Minimum Tier 1 Common Ratio:		13.0%
Annual Stock Repurchases:	$	100
Cost of Equity:		6.18%
Present Value of Equity Calculations:		
Current Value of Common Equity:	$	54,227
Sum of PV of Residual Income:		20,874
Terminal NI Growth Rate:		2.5%
PV of Res. Inc. Terminal Value:		20,071
Present Value of Equity:	**$**	**95,172**
Diluted Shares:		1,214.0
Implied Share Price:	**$**	**78.39**
Dividend Yield:		6.64%
Implied Upside:		**7.94%**
Options: 19.8 $ 54.55		6.0

EXHIBIT 14

Return on Equity compared to Price / Book Value Multiple for Canadian Banks



Valuation

EXHIBIT 15

Comparable Companies Analysis

Scotiabank trades favourably to its peers given its growth profile

	Market	P / TBV		P / B		P / E			ROE	Div. Yield	CET 1
Canadian Commercial Banks	Cap ($MM)	Current	5-yr	Current	5-yr	LTM	2017E	2018E	2016E	(%)	Ratio
Royal Bank of Canada	$139,870	2.9x	3.9x	2.2x	2.9x	13.8x	11.8x	12.2x	15.9%	3.5%	11.9%
The Toronto-Dominion Bank	$125,294	2.6x	3.5x	1.8x	2.4x	14.4x	13.0x	11.9x	13.6%	3.3%	10.4%
The Bank of Nova Scotia	$93,524	2.3x	3.0x	1.8x	2.2x	13.3x	11.9x	11.1x	13.9%	3.8%	12.4%
Bank of Montreal	$63,893	2.1x	2.7x	1.7x	2.1x	14.2x	11.7x	11.8x	11.9%	3.6%	10.1%
Canadian Imperial Bank of Commerce	$44,421	2.3x	3.1x	2.0x	2.6x	10.4x	10.5x	10.2x	17.0%	4.4%	11.8%
Mean		**2.4x**	**3.2x**	**1.9x**	**2.4x**	**13.2x**	**11.2x**	**11.4x**	**14.5%**	**3.7%**	**11.3%**
Median		**2.3x**	**3.1x**	**1.8x**	**2.4x**	**13.8x**	**11.7x**	**11.8x**	**13.9%**	**3.6%**	**11.8%**

EXHIBIT 16

Sensitivity Analysis

Cost of Equity

Terminal Net Income Growth Rate	4.7%	5.2%	5.7%	6.2%	6.7%	7.2%	7.7%
4.0%	$ 161.09	$ 118.33	$ 100.14	$ 89.64	$ 82.55	$ 77.26	$ 73.06
3.5%	121.07	102.48	91.75	84.49	79.09	74.80	71.23
3.0%	104.88	93.91	86.49	80.96	76.57	72.92	69.78
2.5%	96.12	88.54	82.88	78.39	74.66	71.45	68.62
2.0%	90.63	84.85	80.26	76.44	73.15	70.26	67.66
1.5%	86.87	82.17	78.26	74.90	71.94	69.28	66.85
1.0%	84.13	80.13	76.69	73.66	70.94	68.46	66.17

Commentary

Through the Residual Income Valuation, the FIG team has arrived at an implied share price of $78.39, implying 7.9% upside from the current share price of $77.39 after dividend. This price is in line with analyst estimates, falling in the mid-range in comparison to brokered analyst valuations.

When comparing Scotiabank to its peers, it is evident that it is closest in line with the linear trend when comparing the top Canadian banks on return on equity and price / tangible book value multiples.

Moreover, the bank is currently in line with the mean in regards to earnings per share, likely trading at a premium multiple in the projected future. The same is generally held true for in regards to tangible book value per share. The Core Tier 1 (CET1) Ratio for Scotiabank is above the mean and median, indicating solvency and decreased funding risk, both beneficial for the future.

The FIG team is comfortable with this valuation and Scoitabank's position in the portfolio going forward.

References

1. Bloomberg
2. Capital IQ
3. Company Reports
4. Credit Suisse
5. Deloitte
6. Dundee Capital Markets
7. Financial Post
8. Scotiabank Global Markets