

The Empire Life Insurance Company

**Management's Discussion and Analysis
For the nine months ended September 30, 2020**



MANAGEMENT'S DISCUSSION AND ANALYSIS

Dated as of October 29, 2020

This document provides Management's Discussion and Analysis (MD&A) of the unaudited operating results and financial condition of The Empire Life Insurance Company (Empire Life or the Company) for the third quarter and year to date for 2020. This MD&A should be read in conjunction with Empire Life's unaudited Condensed Interim Consolidated Financial Statements for the nine months ended September 30, 2020, as well as the MD&A and the audited Consolidated Financial Statements which form part of the Empire Life 2019 Annual Report dated February 26, 2020. Unless otherwise noted, both the unaudited Condensed Interim Consolidated Financial Statements and this MD&A are expressed in Canadian dollars. Some variances may not reconcile and analysis of components may not sum to the analysis for the grouped components due to rounding.

MD&A contains forward-looking information and involves numerous risks and uncertainties, including, but not limited to, those described in the "Risk Factors" section of the Annual Information Form which is available at www.sedar.com. No assurance can be given that results, performance or achievement expressed in or implied by any of the forward-looking information will occur or, if they do, that any benefits may be derived from them. Actual results may differ materially from those expressed or implied by such forward-looking information. See the Forward-Looking Statements and Information section in this report.

The unaudited Condensed Interim Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS), which are generally accepted accounting principles as set out in the Handbook of the Chartered Professional Accountants of Canada. This MD&A makes reference to certain non-IFRS measures. These measures are not recognized measures under IFRS and do not have a standardized meaning prescribed by IFRS. They are therefore unlikely to be comparable to similar measures presented by other companies. Rather, these measures are provided as additional information and complement IFRS measures by providing further understanding of the Company's results of operations from management's perspective. Accordingly, they should not be considered in isolation nor as a substitute for analysis of the Company's financial information under IFRS. See Non-IFRS Measures section in this report. Note that certain comparative amounts have been reclassified and restated to conform with the presentation adopted in the current period.

Although the Company is carefully monitoring the effects of the novel coronavirus (COVID-19) pandemic on the economy and financial markets, management's assessment of industry dynamics, risks and risk management, critical accounting estimates, strategy and outlook remains consistent with the disclosure in the 2019 Annual Report dated February 26, 2020.

Financial Analysis

Overview

(in millions of dollars except per share amounts)	Third quarter		Year to date	
	2020	2019	2020	2019
Common shareholders' net income (loss)	\$ 51	\$ 35	\$ 67	\$ 98
Earnings per share - basic and diluted	\$ 51.91	\$ 35.29	\$ 68.28	\$ 99.33
Return on common shareholders' equity (quarterly annualized) ¹	16.9 %	8.7 %	5.8 %	8.4 %

Empire Life reported third quarter common shareholders' net income of \$51 million for 2020, compared to net income of \$35 million for the third quarter of 2019. The increase in third quarter earnings was primarily a result of the favourable impact from changes in the investments supporting the Individual Insurance line, partially offset by increases in policy liabilities for segregated fund guarantees. Year to date common shareholders' net income was \$67 million compared to \$98 million in 2019. The decrease in year to date earnings was primarily a result of significant strengthening of policy liabilities supporting segregated fund guarantees.

¹ See Non-IFRS Measures

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The impact of COVID-19 on Canadian and international business operations, supply chains, travel, consumer confidence and business forecasts, and domestic and international securities markets, is expected to continue through the rest of 2020 and potentially beyond. The Company continues to monitor developments in equity and fixed income markets generally, and in connection with the Company's investment portfolios in particular. While the impact of COVID-19 related factors on the Company's financial results is described in the sections that follow, during a time of increased uncertainty and volatility we expect that these events will continue to have an impact on the Company's performance in the near term.

The following table provides a breakdown of the sources of earnings by line of business for the third quarter and year to date.

For the three months ended September 30 (in millions of dollars)	Wealth Management		Employee Benefits		Individual Insurance		Capital and Surplus		Total	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
Expected profit on in-force business	\$ 32	\$ 27	\$ 7	\$ 6	\$ 14	\$ 13			\$ 53	\$ 46
Impact of new business	(2)	(3)	(3)	(6)	2	(4)			(3)	(13)
Experience gains (losses)	(12)	9	(5)	2	2	(12)			(15)	(1)
Management actions and changes in assumptions	—	—	—	—	16	(1)			16	(1)
Earnings (losses) on operations before income taxes	18	33	(2)	2	34	(4)	—	—	50	30
Earnings on surplus	—	—	—	—	—	—	23	18	23	18
Income (loss) before income tax	18	33	(2)	2	34	(4)	23	18	73	49
Income taxes	4	8	—	1	9	(2)	5	4	19	11
Shareholders' net income (loss)	\$ 14	\$ 25	\$ (1)	\$ 1	\$ 25	\$ (2)	\$ 17	\$ 14	\$ 55	\$ 38
Dividends on preferred shares									(3)	(3)
Common shareholders' net income									\$ 51	\$ 35

For the nine months ended September 30 (in millions of dollars)	Wealth Management		Employee Benefits		Individual Insurance		Capital and Surplus		Total	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
Expected profit on in-force business	\$ 98	\$ 85	\$ 19	\$ 19	\$ 42	\$ 40			\$ 159	\$ 143
Impact of new business	(8)	(9)	(7)	(15)	1	3			(14)	(21)
Experience gains & losses	(167)	11	5	5	13	(27)			(148)	(11)
Management actions and changes in assumptions	—	—	—	—	40	(11)			40	(11)
Earnings (losses) on operations before income taxes	(76)	87	17	9	95	4	—	—	37	100
Earnings on surplus	—	—	—	—	—	—	62	38	62	38
Income (loss) before income tax	(76)	87	17	9	95	4	62	38	99	138
Income taxes	(22)	21	4	2	24	(2)	15	8	21	30
Shareholders' net income (loss)	\$ (54)	\$ 66	\$ 13	\$ 7	\$ 71	\$ 5	\$ 47	\$ 30	\$ 77	\$ 108
Dividends on preferred shares									(10)	(10)
Common shareholders' net income									\$ 67	\$ 98

The expected profit on in-force business increased by 15% for the third quarter and by 12% on a year to date basis.

The impact of new business was lower in the third quarter of 2020 due to lower new business strain across all lines. Strain from the Individual Insurance line was positive in the third quarter compared to negative strain in the comparative period in 2019 and positive on a year to date basis compared to a positive amount in the comparative periods in 2019 primarily due to lower sales in 2020. The impact of new business on the Individual Insurance line is positive when the present value of future profits from the new business exceeds the sum of the margins in the initial policy liabilities for that business plus the expenses incurred at the point of sale.

Experience losses increased for the third quarter and increased for the year to date in 2020 compared to the same periods in 2019, primarily due to significant strengthening of policy liabilities supporting segregated fund benefit

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guarantees. This was partially offset by improved asset liability trading gains, improved gains from increased yields on inforce assets backing the life insurance and annuity products and favourable claims experience in the Employee Benefits line.

Management actions and changes in assumptions were higher in the third quarter and year to date in 2020 relative to the same periods in 2019 primarily due to management's ongoing activities to improve the matching of assets and liabilities in the Individual Insurance line.

Earnings on surplus increased for the third quarter and year to date 2020 relative to 2019, primarily due to higher realized fair value gains on Available for Sale (AFS) bond assets in this segment.

Results by Major Product Line

The following table provides a summary of Empire Life results by major product line for the three months ended September 30 and year to date for 2020 and 2019. A discussion of results is provided in the Product Line section of the MD&A.

For the three months ended September 30 (in millions of dollars)	Wealth Management		Employee Benefits		Individual Insurance		Capital and Surplus		Total	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
Revenue										
Net premiums	\$ 28	\$ 30	\$ 90	\$ 91	\$ 104	\$ 97	\$ —	\$ —	\$ 221	\$ 218
Investment income	9	10	1	1	55	55	16	17	81	84
Fair value change in FVTPL investments	22	1	(1)	—	(21)	82	8	1	7	83
Realized gain (loss) on FVTPL investments	—	—	1	—	26	21	(2)	(2)	25	19
Realized gain (loss) on AFS investments including impairment write downs	—	—	—	—	—	—	5	6	5	6
Fee income	58	62	3	3	—	—	—	—	61	65
Total revenue	117	103	93	95	163	254	27	22	401	475
Expenses										
Net benefits and claims	40	44	62	61	40	38	—	—	142	144
Net change in insurance and investment contract liabilities	27	(6)	8	7	43	176	—	—	78	178
Policy dividends	—	—	—	—	8	8	—	—	8	8
Operating, commission and interest expenses	32	32	23	24	35	37	4	4	94	96
Income and other taxes	4	8	1	1	12	(1)	6	4	23	13
Total expenses	104	78	94	94	138	258	10	8	345	439
Net income (loss) after tax	\$ 14	\$ 25	\$ (1)	\$ 1	\$ 25	\$ (4)	\$ 17	\$ 14	\$ 56	\$ 36
Participating policyholders' portion									1	(2)
Dividends on preferred shares									3	3
Common shareholders' net income									\$ 51	\$ 35

¹ See Non-IFRS Measures

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For the nine months ended September 30 (in millions of dollars)	Wealth Management		Employee Benefits		Individual Insurance		Capital and Surplus		Total	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
Revenue										
Net premiums	\$ 74	\$ 124	\$ 264	\$ 267	\$ 301	\$ 290	\$ —	\$ —	\$ 639	\$ 681
Investment income	29	30	3	3	163	158	50	50	244	241
Fair value change in FVTPL investments	20	24	4	5	251	667	—	(5)	275	691
Realized gain (loss) on FVTPL investments	1	—	3	—	139	51	(2)	(5)	141	47
Realized gain (loss) on AFS investments including impairment write downs	(1)	—	(1)	—	(1)	—	26	11	23	12
Fee income	175	186	9	9	—	—	—	—	185	195
Total revenue	298	365	283	285	853	1,166	74	51	1,507	1,866
Expenses										
Net benefits and claims	129	156	170	186	129	119	—	—	428	461
Net change in insurance and investment contract liabilities	145	14	19	16	503	920	—	—	667	950
Policy dividends	—	—	—	—	24	24	—	—	24	24
Operating, commission and interest expenses	100	107	70	68	95	100	12	12	278	287
Income and other taxes	(22)	21	11	8	30	4	15	8	35	41
Total expenses	352	299	270	278	782	1,166	27	20	1,431	1,763
Net income (loss) after tax	\$ (54)	\$ 66	\$ 13	\$ 7	\$ 70	\$ —	\$ 47	\$ 31	\$ 76	\$ 103
Participating policyholders' portion									(1)	(5)
Dividends on preferred shares									10	10
Common shareholders' net income									\$ 67	\$ 98

Total Revenue

Net premiums were 6% lower for the year to date, primarily due to lower fixed annuity sales in the Wealth Management line compared to the same periods in 2019.

Gains from assets classified as Fair Value Through Profit and Loss (FVTPL) were lower in the third quarter reflecting increased long-term bond yields and lower equity markets gains relative to the same period in 2019. On a year to date basis, gains from assets valued at FVTPL were lower than the same period in 2019, primarily due to lower gains on bonds. The TSX Composite Index increased by 3.9% in the third quarter, and has declined by 5.5% on a year to date basis. Yields on 30-year Government of Canada bonds increased by 12 basis points in the third quarter and have declined by 65 basis points for the year to date. Assets classified as FVTPL also include the fair value change in assets backing index-linked products. Changes in the value of these assets are largely offset by changes in the related liabilities which are reflected in Net change in insurance and investment contract liabilities. The fair value change in assets backing other non-index linked policy liabilities in the Individual Insurance line is also partially offset by corresponding changes in the Net change in insurance and investment contract liabilities in the Expenses section of the results.

Fee income for the third quarter declined by 5% and by 5% for the year to date primarily due to lower segregated fund assets under management as a result of poor equity market experience for the year to date.

¹ See Non-IFRS Measures

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Total Expenses

A substantial portion of Total expenses is driven by the impact that equity market movements and market interest rate movements have on the Net change in insurance contract liabilities. This change in expenses is significantly offset by corresponding changes in the Fair value change in FVTPL investments, as noted in the Revenue section. The net change in insurance and investment contract liabilities includes a \$7 million strengthening of policy liabilities supporting segregated fund benefit guarantees for the quarter and \$154 million for the year to date.

Net benefits and claims for the year to date were lower than the comparative period in 2019, primarily from lower claims in the Employee Benefits line due to closures of most dental and paramedical offices in accordance with COVID-19 regulations. Net benefits and claims variability is dependent on the claims incurred. Generally, claims rise year over year due to growth of the insurance blocks. Variability in claims amounts does not, in isolation, impact net income as insurance contract liabilities are released when claims occur. The insurance contract liabilities released may be larger or smaller than the claims incurred depending on whether claims experience has been more or less than what was estimated in the insurance contract liabilities. Claims experience gains and losses are a combination of claims incurred compared to claims expected in product pricing and in insurance contract liabilities.

Product Line Results - Wealth Management

Key Operating Results

(in millions of dollars)	Third quarter		Year to date	
	2020	2019	2020	2019
Fixed Annuities				
Assets under management ¹	\$ 951	\$ 959	\$ 951	\$ 959
Gross sales ¹	28	30	74	124
Net sales ¹	2	1	(11)	13
Segregated Funds				
Assets under management ¹	7,918	8,344	7,918	8,344
Gross sales ¹	152	203	526	613
Net sales ¹	(73)	(54)	(178)	(246)
Fee income	58	61	173	183
Mutual Funds				
Assets under management ¹	120	141	120	141
Gross sales ¹	1	2	6	6
Net sales ¹	(4)	(8)	(15)	(21)
Fee income	—	1	1	2
Net Premiums	\$ 28	\$ 30	\$ 74	\$ 124
Benefits and Expenses	99	70	374	277
Net income (loss) after tax	\$ 14	\$ 25	\$ (54)	\$ 66

Fixed annuities assets under management were lower reflecting decreased sales of these products for the year to date. Gross sales in the third quarter were 7% lower and 40% for the year to date compared to the same periods in 2019.

Segregated fund assets under management are lower relative to the same period in 2019, reflecting the equity market declines experienced in late March this year. While equity markets have rebounded from their March lows,

¹ See Non-IFRS Measures

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the TSX is still below its December 2019 levels. For the third quarter of 2020, gross sales were 25% lower than the same period in 2019 and 14% lower on a year to date basis.

Segregated fund fee income was 5% lower compared to the third quarter of 2019 and 5% lower on a year to date basis as lower average assets impacted fee revenues. Fee income from segregated funds and mutual funds is calculated daily for most products.

Mutual fund assets under management decreased during the last 12 months due to lower mutual fund sales. Empire Life continues to explore various strategic alternatives with respect to its mutual fund business.

This line had net income of \$14 million for the quarter and a net loss of \$54 million for the year to date compared to net income of \$25 million and \$66 million for the third quarter and year to date in 2019, respectively, primarily as a result of an increase in policy liabilities for segregated fund guarantees. These guarantees are only payable if fund values are below the guaranteed values when the insurable event occurs.

Product Line Results - Employee Benefits

Key Operating Results

(in millions of dollars)	Third quarter		Year to date	
	2020	2019	2020	2019
Selected financial information				
Annualized premium sales ¹	\$ 8	\$ 31	\$ 54	\$ 83
Net premiums	90	91	264	267
Net income (loss) after tax	\$ (1)	\$ 1	\$ 13	\$ 7

Annualized premium sales decreased in the third quarter and year to date compared to the same periods in 2019, primarily due to a large block transfer from a new strategic distribution partner in 2019. The Company continues to increase sales of its core products in the small to medium-sized business market and to enter into strategic partnerships to expand market share.

Net premiums for the third quarter and year to date decreased by 1%, relative to the same periods in 2019 as premium rebates were offered to customers to reflect lower health claims experience, as many health care providers were either closed or operating at a limited capacity and offering emergency services only, due to the COVID-19 pandemic. The Company continues to focus on profitable sales in the employee benefits market where price competition continues for all major product lines.

Net income for the third quarter declined on lower net premiums and higher claims relative to the same period in 2019. For the year to date, net income has increased, primarily due to favourable claims experience for dental and extended health benefits, driven by COVID-19 related closures of dental and paramedical offices.

¹ See Non-IFRS Measures

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Product Line Results - Individual Insurance

Key Operating Results

(in millions of dollars)	Third quarter		Year to date	
	2020	2019	2020	2019
Shareholders'				
Shareholders' annualized premium sales ¹	\$ 7	\$ 5	\$ 17	\$ 16
Shareholders' net premiums	71	67	207	205
Net income (loss) after tax	25	(2)	71	5
Policyholders'				
Policyholders' annualized premium sales ¹	3	4	9	12
Policyholders' net premiums	33	30	94	85
Net income (loss) after tax	—	(2)	(1)	(6)
Net income (loss) after tax	\$ 25	\$ (4)	\$ 70	\$ —

Shareholders' annualized premium sales increased by 33% in the third quarter and 4% for the year to date compared to the same periods in 2019, while policyholders' annualized premium sales declined 25% in the third quarter and 24% for the year to date as the impact of COVID-19 lockdowns and physical distancing made underwriting of sales more challenging. Shareholders' net premiums were 5% higher in the quarter and 1% higher for the year to date compared to the prior periods. Policyholders' net premiums increased by 12% in the third quarter and by 11% for the year to date compared to the same periods in 2019, reflecting recent strength in policyholders' new premium sales.

Shareholders' net income for this product line was \$25 million for the third quarter of 2020 compared to a loss of \$2 for the same period in 2019, primarily due to the favourable impact on policy liabilities from asset mix changes in the portfolio of investments supporting this line, as well as improved experience on non-economic assumptions. On a year to date basis, net shareholders' net income was \$71 million for the year to date compared to \$5 million in 2019 primarily due to gains from asset mix improvements and favourable experience gains. As of September 30, 2020, this product line has not had a significant increase in mortality experience due to COVID-19 related claims.

Results - Capital and Surplus

Key Operating Results

(in millions of dollars)	Third quarter		Year to date	
	2020	2019	2020	2019
Income from investments	\$ 31	\$ 24	\$ 71	\$ 61
Gains (losses) on hedging instruments	(4)	(1)	3	(12)
Interest and other expenses	(4)	(4)	(12)	(12)
Earnings before income taxes	23	18	62	38
Income taxes	5	4	15	8
Net income (loss) after tax shareholders' portion	17	14	47	30
Net income (loss) after tax policyholders' portion	—	—	—	1
Net income (loss) after tax	\$ 17	\$ 14	\$ 47	\$ 31

¹ See Non-IFRS Measures

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In addition to the three major lines of business, Empire Life maintains distinct accounts for the investment income attributable to Shareholders' Capital and Surplus and to Policyholders' Surplus.

Income from investments in the third quarter of 2020 was higher than the same period in 2019, primarily due to unrealized gains on assets valued as FVTPL in this line. For the year to date, income from investments was higher than the prior year, primarily due to higher realized gains on assets classified as AFS. Losses on the hedging program (discussed in the Risk Management section) in the third quarter were greater than the third quarter of 2019, primarily related to unrealized losses on the Company's hedging instruments as equity markets continued to rebound in the third quarter from the lows experienced in March. On a year to date basis, the Company had a gain on its hedging program relative to a loss in the prior year.

Shareholder Dividends

The declaration and payment of common shareholder dividends and the amounts thereof are at the discretion of the Board of Directors.

Common shareholder dividends are reviewed on a quarterly basis and depend upon various factors, including the results of operations, the economic environment and the financial condition of Empire Life, taking into account regulatory restrictions on the payment of shareholder dividends, as well as any other factors deemed relevant by the Board of Directors.

On October 29, 2020, the Board of Directors declared a dividend of \$22.0723 per common share of Empire Life. The following table provides details of the amounts and dates for Empire Life's per share dividends.

	Amount of Dividend per share	Payable Date	Record Date
Common shares	\$ 22.0723	8 December 2020	13 November 2020
Non-Cumulative Rate Reset Preferred Shares, Series 1 (TSX: EML.PR.A)	\$ 0.359375	17 January 2021	18 December 2020
Non-Cumulative Rate Reset Preferred Shares, Series 3	\$ 0.306250	17 January 2021	18 December 2020

Empire Life advises that the above-referenced dividends are eligible dividends for the purposes of the Income Tax Act, Canada and any similar provincial tax legislation.

Total Cash Flow

(in millions of dollars)	Year to date	
	2020	2019
Cash flow provided from (used for)		
Operating activities	\$ 241	\$ 292
Investing activities	34	(205)
Financing activities	(176)	(72)
Net change in cash and cash equivalents	\$ 99	\$ 15

Cash flows from operating activities include insurance premiums, net investment income and fee income. These funds are primarily used to pay policy benefits, commissions, operating expenses and policyholder dividends. Cash flows from investing activities primarily relate to purchases and sales of investments supporting policy liabilities and the capital and surplus accounts. Cash flows related to financing activities include issuance and redemption of capital instruments and related dividend and interest payments.

For the year to date, cash and cash equivalents increased by \$99 million. Cash flows provided by operating activities decreased by \$51 million primarily due to lower net premiums for the period, partially offset by lower claims

¹ See Non-IFRS Measures

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activity. Cash provided for investing activities increased by \$239 million compared the same period in 2019. Cash used for financing activities was higher than the corresponding period in 2019, primarily due to the payment of common share dividends declared in the first quarter of 2020, including a special dividend of \$90 million.

For an analysis of liquidity for Empire Life, see note 10(e) and note 27(b) to the 2019 consolidated financial statements.

Financial Instruments

Empire Life's investment strategy includes the purchase of investment quality bonds to support, to a very large extent, insurance and annuity policy liabilities and the use of equity investments to support insurance policy liabilities. Cash flows arising from these financial instruments are intended to match the liquidity requirements of the underlying customer obligation. Investment strategies are subject to prescribed limits outlined in various corporate policies. Empire Life is subject to market risk on these financial instruments.

The Company is also subject to credit risk on these financial instruments which could result in a financial loss should the other party fail to discharge an obligation. This credit risk is derived primarily from investments in bonds, debentures, preferred shares, short-term investments and mortgages. Market risk exposure is managed mainly through investment limits and oversight of its in-house investment managers and external investment firms by the Chief Investment Officer, Asset Management Committee and Investment Committee of the Board. The Investment Committee actively monitors the portfolio size and asset mix. Empire Life has a semi-static hedging program as part of its approach to managing this risk. Credit risk is managed by applying investment guidelines established by the Investment Committee of the Board of Directors. The investment guidelines establish minimum credit ratings for issuers of bonds, debentures and preferred share investments, and provide for concentration limits by issuers of such debt instruments. Management reviews credit quality relative to investment purchases and also monitors the credit quality of invested assets over time. Management reports regularly to the Investment Committee of the Board on the credit risk to which the portfolio is exposed.

The Company manages credit risk with respect to derivatives by applying limits and credit rating restrictions established by the Investment Committee in its investment guidelines, which set out permitted derivatives and permitted uses for derivatives, as well as limits to the use of these instruments. In particular, no leverage is permitted in the use of derivatives and strict counterparty credit restrictions are imposed. Additional information regarding financial instruments is included in notes 2(d), 3, 10(c), and 27 to the audited consolidated financial statements for the year ended December 31, 2019.

Sources of Capital

Empire Life has issued private and public securities to strengthen its capital position and fund new business growth. The securities outstanding are summarized in the following table.

(in millions of dollars)	As at	
	30 September 2020	31 December 2019
Subordinated debentures	\$ 400	\$ 400
Equity		
Preferred shares	\$ 250	\$ 250
Common shares	\$ 1	\$ 1
Total equity	\$ 251	\$ 251

¹ See Non-IFRS Measures

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Details of the Company's outstanding subordinated debt and preferred shares are as follows:

Subordinated Debentures				As at	
(in millions of dollars)	Date Issued	Earliest Redemption Date	Interest Rate	30 September 2020	31 December 2019
Subordinated debentures ⁽¹⁾	December 2016	16 December 2021	3.383 % \$	200 \$	200
Subordinated debentures ⁽²⁾	September 2017	15 March 2023	3.664 % \$	200 \$	200

⁽¹⁾ Series 2016-1 Subordinated 3.383% Unsecured Debentures due 2026. From December 16, 2021, interest is payable at 1.95% over the 3-month Canadian Deposit Offering Rate (CDOR).

⁽²⁾ Series 2017-1 Subordinated 3.664% Unsecured Debentures due 2028. From March 15, 2023, interest is payable at 1.53% over the 3-month CDOR.

Preferred Shares				As at	
(In millions of dollars)	Date Issued	Earliest Redemption Date	Yield	30 September 2020	31 December 2019
Preferred shares	January 2016	17 April 2021	5.75 % \$	150 \$	150
Preferred shares	November 2017	17 January 2023	4.90 % \$	100 \$	100

Empire Life's debentures and preferred shares are rated by DBRS Limited (DBRS) and A.M. Best Company, Inc. (A.M. Best).

Empire Life's DBRS issuer rating is "A" (sixth highest of 20 categories), its subordinated debt rating is "A (low)" (seventh highest of 20 categories), its financial strength rating is "A" (sixth highest of 22 categories) and its Preferred Share rating is Pfd-2 (fifth highest of 18 categories). All ratings have a stable trend. According to DBRS, the assigned ratings reflect Empire Life's position as a consistently performing life insurer with a proven track record of generating stable earnings while maintaining a conservative risk profile.

A.M. Best ratings of Empire Life are "A Excellent" financial strength rating (third highest of 16 categories), "a" long-term issuer credit rating (sixth highest of 21 categories), "bbb+" Subordinated Debt rating (eighth highest of 21 categories), and "bbb" Preferred Share rating (ninth highest of 21 categories). All ratings have a stable trend. According to A.M. Best, the ratings reflect Empire Life's balance sheet strength, which A.M. Best categorizes as very strong, as well as its strong operating performance, neutral business profile and appropriate enterprise risk management.

Regulatory Capital

The Life Insurance Capital Adequacy Test (LICAT) is intended to improve the measurement of the life insurer's solvency position by recognizing the long-term economics of the life insurance business. Empire Life had a strong capital position under MCCR and continues to have a strong capital position under the LICAT framework. Empire Life is required to maintain a minimum Core Ratio of 55% and a Total Ratio of 90%. OSFI has established supervisory target levels of 70% for Core and 100% for Total capital.

As of September 30, 2020, the Total Ratio and Core Ratio reduced significantly from December 31, 2019 primarily due to the significant strengthening of policy liabilities and regulatory capital supporting segregated fund benefit guarantees.

¹ See Non-IFRS Measures

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LICAT	30 Sep.	30 Jun.	31 Mar.	31 Dec.	30 Sep.
(in millions of dollars)	2020	2020	2020	2019	2019
Available capital					
Tier 1	\$ 1,544	\$ 1,527	\$ 1,435	\$ 1,616	\$ 1,562
Tier 2	703	710	671	669	681
Total	\$ 2,247	\$ 2,237	\$ 2,106	\$ 2,285	\$ 2,243
Surplus allowance and eligible deposits	1,111	1,094	1,029	1,109	944
Base solvency buffer	2,542	2,510	2,371	2,191	2,133
LICAT total ratio	132 %	133 %	132 %	155 %	149 %
LICAT core ratio	91 %	91 %	91 %	109 %	104 %

Other Comprehensive Income

(in millions of dollars after tax)	Third quarter		Year to date	
	2020	2019	2020	2019
OCI, attributable to shareholders	\$ —	\$ 4	\$ 36	\$ 64
OCI, attributable to policyholders	1	1	3	4
Total other comprehensive income	\$ 1	\$ 5	\$ 39	\$ 68

Other comprehensive income (OCI) decreased in the third quarter of 2020 primarily due to lower unrealized fair value gains on AFS investments and a larger loss on the remeasurement of the post-employment defined benefit plans. On a year to date basis, OCI decreased relative to the same period in 2019 primarily due to lower unrealized gains on AFS investments and a larger loss on the remeasurement of post-employment defined benefit plans. The loss on these components of OCI was primarily due to fluctuations in interest rates and credit spreads during the third quarter and year to date in 2020.

Remeasurement of defined benefit pension plans does not immediately impact LICAT as each quarter's remeasurement gain or loss is amortized over 12 quarters for LICAT purposes.

Risk Management

Caution Related to Sensitivities

In the sections that follow, Empire Life provides sensitivities and risk exposure measures for certain risks. These include sensitivities due to specific changes in market prices and interest rates, based on market prices, interest rates, assets, liabilities and business mix in place as at the calculation dates. The sensitivities are calculated independently for each risk factor, assuming that all other risk variables remain constant. Actual results can differ materially from these estimates for a variety of reasons, including the interaction among these factors when more than one factor changes; changes in actuarial and investment return and future investment activity assumptions; actual experience differing from the assumptions; changes in business mix, effective tax rates and other market factors; and the general limitations of Empire Life's internal models used for purposes of these calculations. Changes due to new sales or maturities, asset purchases/sales, or other management actions could also result in material changes to these reported sensitivities. For these reasons, the sensitivities should only be viewed as directional estimates of the underlying sensitivities for the respective factors based on the assumptions outlined, and should not be viewed as predictors for Empire Life's future net income, OCI, and capital sensitivities. Given the nature of these calculations, Empire Life cannot provide assurance that actual impact will be consistent with the estimates provided. Changes in risk variables in excess of the ranges illustrated may result in other than proportionate impacts.

¹ See Non-IFRS Measures

MANAGEMENT'S DISCUSSION AND ANALYSIS

Significant Developments

Commencing in the first quarter of 2020, the spread of the COVID-19 pandemic, given its severity and scale, continues to affect Empire Life's business, some of our clients and also continues to pose risks to the Canadian economy. The Company continues to adjust operations as government restrictions and measures evolve. As the impacts of the COVID-19 pandemic continue to materialize, management is monitoring the effects of the disruption on the Company's business strategies and initiatives and the effects on its financial results.

The COVID-19 pandemic has and may continue to result in disruptions to clients and the way in which business is conducted, including prolonged duration of employees working from home. To date, Empire Life has taken proactive measures through business continuity plans, carefully planning the return to premise for some employees, and management teams have increased their efforts to preserve the well-being of employees and our ability to serve clients. Processes supporting ongoing systems availability, stability and security are operating effectively and the Company continues to monitor the threat landscape.

The duration and impacts of the COVID-19 outbreak cannot currently be determined. If the COVID-19 pandemic is prolonged, or further diseases emerge that give rise to similar effects, there may be further negative effects on the Canadian economy as well as increased volatility in equity and fixed income markets. Unexpected developments in financial markets, regulatory environments, or consumer behaviour and confidence may also have adverse impacts on the Company's financial results and condition, and business.

Market Risk

Empire Life has equity market risk related to its segregated fund products and from equity assets backing life insurance liabilities. The Company has a semi-static hedging program. The hedging program may employ derivative positions including put options and futures. The extent of derivatives used is monitored and managed on an ongoing basis, giving consideration to equity risk and the level of available capital.

There is income statement volatility from this hedging program. Based on current equity market levels, Empire Life has required capital for LICAT purposes and has insurance contract liabilities on the statement of financial position related to segregated fund guarantees. Therefore, a by-product of hedging LICAT exposure is net income volatility, as the gains or losses from hedging instruments are not necessarily offset by changes in policy liabilities related to segregated fund guarantee risk. The equity risk hedging program provides some relief in adverse scenarios, but may incur losses in positive scenarios. For the third quarter, Empire Life experienced a loss of \$3 million after tax, and a gain of \$2 million after tax on its hedging program for the year to date, primarily due to volatile Canadian equity markets. This compares to a hedge cost of \$1 million and \$9 million after tax, respectively, for the comparable periods in 2019.

Empire Life's LICAT ratio is also sensitive to stock market volatility, due primarily to liability and capital requirements related to segregated fund guarantees. As of September 30, 2020, Empire Life had \$7.9 billion of segregated fund assets and liabilities. Of this amount, approximately \$7.7 billion have guarantees. The following table provides a percentage breakdown by type of guarantee:

	30 September 2020	31 December 2019
Percentage of Segregated Fund Liabilities with:		
75% maturity guarantee and a 75% death benefit guarantee	5 %	4 %
75% maturity guarantee and a 100% death benefit guarantee	45 %	46 %
100% maturity and death benefit guarantee (with a minimum of 15 years between deposit and maturity date)	7 %	7 %
Guaranteed minimum withdrawal benefit (GMWB)	43 %	43 %

All Empire Life segregated fund guarantees are policy-based (not deposit-based), thereby generally lowering Empire Life's stock market sensitivity relative to products with deposit-based guarantees. Policy-based guarantees consider all of the deposits in the customer's policy (whether the fund value is below or above the guaranteed amount) to arrive at an overall net guarantee payment, whereas deposit-based guarantees consider only the deposits where the fund value is below the guaranteed amount and ignore all the deposits in the customer's policy

¹ See Non-IFRS Measures

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where the fund value is above the guaranteed amount. Therefore, policy-based guarantees generally pay less than deposit-based guarantees. For segregated fund guarantee insurance contract liabilities, the level of sensitivity is highly dependent on the level of the stock market at the time of performing the estimate. If period-end stock markets are high relative to market levels at the time that segregated fund policies are issued, the sensitivity is reduced. If period-end stock markets are low relative to market levels at the time that segregated fund policies are issued, the sensitivity is increased.

The segregated fund regulatory capital and liability framework includes the use of "zero floors" (i.e., negative liability amounts are not permitted so zero is used instead, as described below) and other regulatory constraints, and this often makes the sensitivity impacts non-linear. The liabilities are the greater of: (i) the average of the amounts determined by averaging the results from adverse economic scenarios; and (ii) zero.

Empire Life also has equity market risk related to its equity assets backing life insurance liabilities. Based on stock market levels as at September 30, 2020 and December 31, 2019, the sensitivity of Empire Life shareholders' net income and LICAT ratio resulting from stock market increases and decreases is provided in the following table.

Sensitivity to equity risk: Impact on net income (in millions of dollars after tax)	Increase			Decrease		
	20 %	10 %	10 %	20 %	30 %	
As at September 30, 2020						
Segregated fund guarantees	\$ 113	\$ 61	\$ (18)	\$ (127)	\$ (255)	
Other equity risk	32	15	(14)	(25)	(89)	
Equity hedge	(10)	(5)	7	16	28	
Total	\$ 135	\$ 71	\$ (25)	\$ (136)	\$ (317)	

As at December 31, 2019

Segregated fund guarantees	\$ —	\$ —	\$ (10)	\$ (76)	\$ (229)
Other equity risk	33	15	(12)	(20)	(65)
Equity hedge	(2)	(1)	4	16	38
Total	\$ 31	\$ 14	\$ (18)	\$ (80)	\$ (256)

Sensitivity to equity risk: Impact on LICAT	Increase			Decrease		
	20 %	10 %	10 %	20 %	30 %	
As at September 30, 2020						
Segregated fund guarantees	7 %	4 %	(1)%	(9)%	(16)%	
Other equity risk	— %	— %	— %	— %	(1)%	
Equity hedge	(1)%	— %	— %	1 %	1 %	
Total	6 %	4 %	(1)%	(7)%	(16)%	

As at December 31, 2019

Segregated fund guarantees	3 %	— %	(6)%	(16)%	(22)%
Other equity risk	(1)%	(1)%	— %	1 %	1 %
Equity hedge	(3)%	(2)%	1 %	3 %	3 %
Total	(1)%	(2)%	(4)%	(12)%	(18)%

Empire Life's equity market sensitivity in a 20% and 30% stock market decline increased primarily as a result of the significant decline in equity markets during the first quarter of 2020. The segregated fund guarantee liability was strengthened during the quarter as the value of withdrawal and guarantee benefits increases when there is a decline in equity markets. This increases net income sensitivity as any changes to the liability when it is above the zero floor will flow through net income.

¹ See Non-IFRS Measures

MANAGEMENT'S DISCUSSION AND ANALYSIS

Empire Life also has a reinsurance agreement to cede a portion of Empire Life's segregated fund death benefit exposure. All Empire Life segregated fund policyholders with death benefit guarantees of at least \$2 million are included in this agreement. Empire Life does not reinsure any other insurer's segregated fund products.

The amount at risk related to segregated fund maturity guarantees and segregated fund death benefit guarantees, and the resulting policy liabilities and LICAT base solvency buffer for Empire Life's segregated funds, is provided in the following table.

Segregated Funds (in millions of dollars)	Withdrawal Benefit > Fund Value		Maturity Guarantee > Fund Value		Death Benefit > Fund Value		Policy Liabilities	LICAT Capital
	Fund Value	Amount At Risk	Fund Value	Amount At Risk	Fund Value	Amount At Risk		
30 September 2020	\$ 2,664	\$ 993	\$ 201	\$ 12	\$ 2,827	\$ 80	\$ 154	\$ 696
31 December 2019	\$ 2,701	\$ 882	\$ 51	\$ 2	\$ 650	\$ 6	\$ —	\$ 465

The first six columns of the above table show all segregated fund policies where the future withdrawal benefit, future maturity guarantee, or future death benefit guarantee is greater than the fund value. The amount at risk represents the excess of the future withdrawal benefit, future maturity guarantee or future death benefit guarantee amount over the fund value for these policies. The withdrawal benefit amounts in the above table relate to GMWB products. The GMWB withdrawal benefit amount at risk represents the amount that could be paid by Empire Life to GMWB policyholders if the net return on each GMWB policyholder's assets is zero for the remainder of each GMWB policyholder's life, based on life expectancy. As at September 30, 2020, the aggregate amount at risk for all three categories of risk was \$1.1 billion. As at December 31, 2019, the aggregate amount at risk for these three categories of risk was \$890 million. For these three categories of risk, the amount at risk is not currently payable. Payment is contingent on future outcomes, including fund performance, deaths, deposits, withdrawals and maturity dates.

The level of policy liabilities and required regulatory capital in the above table is calculated based on the probability that Empire Life will ultimately have to make payment to the segregated fund policyholders for any fund value deficiency that may exist on future payments to GMWB policyholders, or upon future maturity of the segregated fund policies, or upon future death of the segregated fund policyholders.

In addition, Empire Life considers the sensitivity of its LICAT ratio to changes in market interest rates. The impact of an immediate 50 basis point decrease in interest rates and a 50 basis point decrease in the assumed initial reinvestment rate (IRR) for non-participating insurance business and segregated fund guarantees for September 30, 2020 and December 31, 2019, is shown in the table below. This assumes no change in the ultimate reinvestment rate (URR). The AFS bonds provide a natural economic offset to the interest rate risk attributable to Empire Life's product liabilities.

Sensitivity to market interest rates LICAT	Impact of 50 bps Decrease
September 30, 2020 LICAT total ratio	(1)%
December 31, 2019 LICAT total ratio	1 %

Quarterly Results

The following table summarizes various financial results on a quarterly basis for the most recent eight quarters:

	30 Sep. 2020	30 Jun. 2020	31 Mar. 2020	31 Dec. 2019	30 Sep. 2019	30 Jun. 2019	31 Mar. 2019	31 Dec. 2018
(in millions of dollars, except per share amounts)								
Revenue	\$ 401	\$ 1,105	\$ 2	\$ 249	\$ 475	\$ 603	\$ 788	\$ 289
Common shareholder's net income	\$ 51	\$ 48	\$ (32)	\$ 76	\$ 35	\$ 20	\$ 43	\$ 6
Earnings per share - basic and diluted	\$ 51.91	\$ 48.42	\$ (32.05)	\$ 77.25	\$ 35.29	\$ 20.45	\$ 43.59	\$ 6.36

¹ See Non-IFRS Measures

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Forward-Looking Statements and Information

Certain statements in this MD&A about Empire Life's current and future plans, expectations and intentions, results, market share growth and profitability, strategic objectives or any other future events or developments constitute forward-looking statements and information within the meaning of applicable securities laws. The words "may", "will", "would", "should", "could", "expects", "plans", "intends", "trends", "indications", "anticipates", "believes", "estimates", "predicts", "likely" or "potential" or the negative or other variations of these words or other comparable words or phrases, are intended to identify forward-looking statements and information. Although management believes that the expectations and assumptions on which such forward-looking statements and information are based are reasonable, undue reliance should not be placed on the forward-looking statements and information because there can be no assurance that they will prove to be correct. By their nature, such forward-looking statements and information are subject to various risks and uncertainties, which could cause the actual results and expectations to differ materially from the anticipated results or expectations expressed. These risks and uncertainties include, but are not limited to, market risk including equity risk, hedging risk, interest rate risk, foreign exchange rate risk; liquidity risk; credit risk including counterparty risk; insurance risk including mortality risk, policyholder behaviour risk, expense risk, morbidity risk, product design and pricing risk, underwriting and claims risk, reinsurance risk; operational risk, including legal and regulatory compliance risk, model risk, human resources risk, third-party risk, technology, information security and business continuity risk; and business risk, including risk with respect to competition, risk with respect to financial strength, capital adequacy risk, risk with respect to distribution channels, risk with respect to changes to applicable income tax legislation, risk with respect to litigation, risk with respect to reputation, risk with respect to risk management policies, risk with respect to intellectual property, risk with respect to significant ownership of common shares. Please see the section titled "Risk Factors" in Empire Life's Annual Information Form available at www.sedar.com for more details on these risks.

Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking statements and information include that the general economy remains stable; assumptions on interest rates, mortality rates and policy liabilities; and capital markets continue to provide access to capital. These factors are not intended to represent a complete list of the factors that could affect Empire Life; however, these factors should be considered carefully, and readers should not place undue reliance on forward-looking statements made herein or in the documents reproduced herein.

To the extent any forward-looking information in this MD&A constitutes future-oriented financial information or financial outlooks within the meaning of securities laws, such information is being provided to demonstrate potential benefits and readers are cautioned that this information may not be appropriate for any other purpose. Future-oriented financial information and financial outlooks are, without limitation, based on the assumptions and subject to the risks set out above.

The forward-looking information contained herein is expressly qualified in its entirety by this cautionary statement. When relying on Empire Life's forward-looking statements and information to make decisions, investors and others should carefully consider the foregoing factors, assumptions and other uncertainties and potential events. Readers are cautioned not to place undue reliance on this forward-looking information, which is given as of the date hereof or the date indicated, and to not use such forward-looking information for anything other than its intended purpose. Empire Life undertakes no obligation to update publicly or revise any forward-looking statements and information, whether as a result of new information, future events or otherwise after the date of this document, except as required by law.

Non-IFRS Measures

Empire Life uses non-IFRS measures including return on common shareholders' equity, source of earnings, assets under management, annualized premium sales, gross and net sales for mutual funds, segregated funds and fixed annuities to provide investors with supplemental measures of its operating performance and to highlight trends in its core business that may not otherwise be apparent when relying solely on IFRS financial measures. Empire Life also believes that securities analysts, investors and other interested parties frequently use non-IFRS measures in the evaluation of issuers. Empire Life's management also uses non-IFRS measures in order to facilitate operating performance comparisons from period to period, to prepare annual operating budgets and to determine components

¹ See Non-IFRS Measures

MANAGEMENT'S DISCUSSION AND ANALYSIS

of management compensation. Empire Life believes that these measures provide information useful to its shareholders and policyholders in evaluating Empire Life's underlying financial results.

Return on common shareholders' equity is a profitability measure that presents the net income available to common shareholders as a percentage of the average capital deployed to earn the income.

Sources of earnings breaks down Empire Life's earnings into several categories which are useful to assess the performance of the business. These categories include expected profit from in-force business, impact of new business, experience gains and losses, management actions and changes in assumptions, and earnings on surplus. The sources of earnings components are reconciled to net income. See the Overview section earlier in this report.

Annualized premium sales is used as a method of measuring sales volume. It is equal to the premium expected to be received in the first 12 months for all new individual insurance and employee benefit policies sold during the period. Mutual fund gross and net sales and segregated fund gross and net sales are also used as measures of sales volume.

Assets under management is a non-IFRS measure of the assets managed by Empire Life, which includes general fund assets, mutual fund assets and segregated fund assets. It represents the total assets of Empire Life and the assets its customers invest in.

The following table provides a reconciliation of assets under management to total assets in Empire Life's financial statements.

Reconciliation of Assets Under Management

As at (in millions of dollars)	30 September 2020	31 December 2019
Assets Under Management		
General fund assets	\$ 10,129	\$ 9,462
Segregated fund assets	7,934	8,499
Total assets per financial statements	18,063	17,961
Mutual fund assets	120	139
Assets under management	\$ 18,183	\$ 18,100

The above table includes the following amounts held by Empire Life's defined benefit (DB) pension plans.

As at (in millions of dollars)	30 September 2020	31 December 2019
DB plan assets		
Segregated fund assets	\$ 193	\$ 203
Mutual fund assets	15	14

¹ See Non-IFRS Measures