The Empire Life Insurance Company

Management's Discussion and Analysis

For the year ended December 31, 2016

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MANAGEMENT'S DISCUSSION AND ANALYSIS

This MD&A is dated as of February 24, 2017.

This document has been prepared for the purpose of providing Management's Discussion and Analysis ("MD&A") of the operating results and financial condition of The Empire Life Insurance Company ("Empire Life" or the "Company") for the years ended December 31, 2016 and 2015. This MD&A should be read in conjunction with the Company's December 31, 2016 consolidated financial statements, which form part of The Empire Life Insurance Company 2016 Annual Report dated February 24, 2017. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as set out in the Handbook of the Chartered Professional Accountants of Canada. Unless otherwise noted, both the consolidated financial statements and this MD&A are expressed in Canadian dollars.

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 Forward-Looking Statements and Information section in this report.

The financial statements of the Company are prepared in compliance with IFRS, which is generally accepted accounting principles ("GAAP") as set out in the Handbook of the Chartered Professional Accountants of Canada. This MD&A makes reference to certain non-GAAP 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 to 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 reported under IFRS. See Non-GAAP Measures section in this report.

Financial Analysis

Overview

	Fourth quarter		Year	
(in millions of dollars except per share amounts)	**2016**	2015	**2016**	2015
Common shareholders' net income	**$ 52.5**	$ 16.2	**$ 152.7**	$ 108.6
Earnings per share - basic and diluted	**$ 53.34**	$ 16.43	**$ 155.03**	$ 110.22
Return on common shareholders' equity (quarters annualized) ("ROE")	**17.1%**	5.9%	**13.1%**	10.2%

Empire Life reported fourth quarter common shareholders' net income of $52.5 million for 2016, compared to $16.2 million for 2015. Full year common shareholders' net income was $152.7 million compared to $108.6 million in 2015.

The following table provides a breakdown of the sources of earnings[1] for the fourth quarter and full year.

Sources of Earnings	**Fourth quarter**		**Year**	
(in millions of dollars)	**2016**	2015	**2016**	2015
Expected profit on in-force business	**$ 39.9**	$ 40.9	**$ 159.5**	$ 159.7
Impact of new business	**(5.5)**	(9.5)	**(15.2)**	(33.8)
Experience gains (losses)	**34.5**	8.0	**32.6**	(9.6)
Management actions and changes in assumptions	**5.5**	(24.9)	**40.3**	(24.9)
Earnings on operations before income taxes	**74.4**	14.5	**217.2**	91.4
Earnings on surplus	**(1.1)**	7.1	**(2.7)**	50.2
Income before income tax	**73.3**	21.7	**214.5**	141.6
Income taxes	**18.6**	5.4	**54.0**	33.0
Shareholders’ net income	**54.7**	16.2	**160.6**	108.6
Dividends on preferred shares	**2.2**	—	**7.9**	—
Common shareholders’ net income	**$ 52.5**	$ 16.2	**$ 152.7**	$ 108.6

Fourth quarter and full year common shareholders’ net income and ROE were higher relative to 2015 due to higher profit from the Individual Insurance product line primarily from improved stock market conditions in 2016, a favourable update of policy liability assumptions for the Individual Insurance product line in 2016 (compared to an unfavourable update in 2015) and management actions to improve asset/liability matching in 2016. Empire Life improved its matching position throughout 2016 by increasing its investment in real estate limited partnership units and by making changes to its bond investments. The improved matching position resulted in a gain in all four quarters of 2016.

The expected profit on in-force business was slightly lower relative to 2015 primarily due to increased premium taxes on in-force policies. This was partly offset by strong profit on the in-force Wealth Management product line due to growth in segregated fund guarantee fees and management fees and lower expenses. The impact of new business improved relative to 2015 in all quarters of 2016 primarily due to lower new business strain (resulting from lower segregated fund sales) and lower Wealth Management expenses. Earnings on surplus decreased primarily due to hedging costs which resulted from the increase in stock markets in 2016.

During the first quarter of 2016, Empire Life issued $149.5 million of preferred shares resulting in the payment of preferred share dividends in 2016 which lowered common shareholders’ net income relative to 2015. On December 16, 2016, the Company issued $200 million principal amount of unsecured subordinated debentures with a maturity date of December 16, 2026. The interest rate from December 16, 2016 until December 16, 2021 is 3.383%, and the rate from December 16, 2021 until December 16, 2026 is equal to the 3-month Canadian Bankers’ Acceptance Rate plus 1.95%. The issuance of these debentures increased Empire Life’s Minimum Continuing Capital and Surplus Requirements (“MCCSR”) ratio by 26 percentage points during the fourth quarter of 2016.

Empire Life has three major product lines (Wealth Management, Employee Benefits and Individual Insurance) and maintains distinct accounts for Capital and Surplus. A discussion of each product line’s 2016 net income compared to 2015 is shown in the Product Line Results sections later in this report.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Selected Financial Information

Income Statement Financial Information	For the years ended December 31		
(in millions of dollars)	**2016**	2015	2014
Revenue			
Net premium income	**$ 882**	$ 835	$ 867
Fees income	**228**	217	188
Investment income	**255**	259	246
Realized gain on FVTPL investments	**20**	42	74
Realized gain on available for sale investments including impairment write downs	**12**	19	13
Fair value change in FVTPL investments	**12**	(85)	538
Total Revenue	**1,409**	1,287	1,926
Expenses			
Benefits and expenses	**$ 1,178**	$ 1,139	$ 1,770
Income and other taxes	**74**	46	49
Total Expenses	**1,252**	1,185	1,819
Net income after tax	**157**	102	107
Participating policyholders' portion	**(4)**	(6)	9
Shareholders' net income	**$ 161**	$ 108	$ 98
Dividends on preferred shares	**8.0**	—	—
Common shareholders' net income	**153**	**108**	**98**
Return on shareholders' equity	**13.1%**	10.2%	10.5%

Revenue volatility was primarily driven by the impact of market interest rate movements on fair value change in fair value through profit or loss ("FVTPL") investments. The impact of this on net income is significantly reduced due to a corresponding change in insurance contract liabilities (included in Benefits and expenses in the above table).

Balance Sheet Financial Information	As at December 31		
(in millions of dollars)	**2016**	2015	2014
Assets			
Total Cash and Investments	**$ 7,605**	$ 6,859	$ 6,669
Other assets	**175**	137	112
Segregated fund assets	**8,082**	7,368	6,948
Total Assets	**$ 15,862**	$ 14,364	$ 13,729
Liabilities			
Insurance contract liabilities	**$ 5,003**	$ 4,799	$ 4,713
Reinsurance liabilities	**533**	531	491
Subordinated debt	**499**	299	299
Other liabilities	**295**	215	216
Segregated fund policy liabilities	**8,082**	7,368	6,948
Total Liabilities	**14,412**	13,212	12,667
Total Equity	**1,450**	1,152	1,062
Total Liabilities & Equity	**$ 15,862**	$ 14,364	$ 13,729

Other Financial Information	**As at December 31**		
(in millions of dollars)	**2016**	2015	2014
Assets under management[2]			
General fund assets[2]	**$ 7,780**	$ 6,996	$ 6,780
Segregated fund assets[2]	**8,082**	7,368	6,948
Mutual fund assets[2]	**189**	171	109
Subordinated debt	**499**	299	299
Preferred shares	**150**	—	—
Available regulatory capital			
Tier 1	**$ 1,206**	$ 918	$ 872
Tier 2	**707**	504	452
Total	**1,913**	1,422	1,324
Required regulatory capital	**$ 771**	$ 708	$ 671
MCCSR Ratio	**248%**	201%	197%

	2016	2015	2014
Cash dividends per share			
Preferred shares series 1	**$ 1.3183**	$ —	$ —
Common shares	**$ —**	$ —	$ 34.4985

During 2016, Empire Life’s MCCSR ratio increased by 26 percentage points from the issuance of $200 million of subordinated debentures and 20 percentage points from the issuance of $149.5 million of preferred shares.

The following table provides a summary of Empire Life results by major product line (figures in MD&A may differ due to rounding):

For the twelve months ended December 31	Wealth Management		Employee Benefits		Individual Insurance		Capital and Surplus		Total	
(in millions of dollars)	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015
Revenue										
Net premium income	**$ 176**	$ 144	**$ 339**	$ 325	**$ 367**	$ 366	**$ —**	$ —	**$ 882**	$ 835
Fee income	**217**	207	**9**	9	**2**	1	**—**	—	**228**	217
Investment income	**41**	43	**4**	4	**176**	171	**34**	41	**255**	259
Realized gain (loss) on FVTPL investments	**(1)**	1	**1**	1	**48**	38	**(28)**	2	**20**	42
Realized gain on available for sale investments including impairment write downs	**—**	—	**—**	—	**—**	—	**12**	19	**12**	19
Fair value change in FVTPL investments	**(4)**	(28)	**—**	(2)	**22**	(56)	**(6)**	1	**12**	(85)
Total Revenue	**429**	367	**353**	337	**615**	520	**12**	63	**1,409**	1,287
Expenses										
Benefits and expenses	**348**	289	**329**	322	**491**	518	**10**	10	**1,178**	1,139
Income and other taxes	**19**	19	**14**	9	**40**	4	**—**	14	**73**	46
Total Expenses	**367**	308	**343**	331	**531**	522	**10**	24	**1,251**	1,185
Net income (loss) after tax	**$ 62**	$ 59	**$ 10**	$ 6	**$ 83**	$ (2)	**$ 2**	$ 39	**$ 157**	$ 102
Participating policyholders' portion									**(4)**	(6)
Dividends on preferred shares									**8**	—
Common shareholders' net income									**$ 153**	$ 108
Assets under management[3]										
General fund assets[3]	**$ 970**	$ 959							**$ 7,780**	$ 6,996
Segregated fund assets[3]	**$ 8,061**	$ 7,347			**$ 21**	$ 20			**$ 8,082**	$ 7,367
Mutual fund assets[3]	**$ 189**	$ 171							**$ 189**	$ 171
Annualized premium sales[3]			**$ 44**	$ 44	**$ 42**	$ 51				

Total Revenue

	Fourth quarter		Year	
(in millions of dollars)	**2016**	2015	**2016**	2015
Revenue				
Net premium revenue	**$ 222**	$ 206	**$ 882**	$ 835
Investment income	**69**	67	**255**	259
Fair value change in FVTPL investments including realized amounts	**(371)**	62	**32**	(43)
Realized gain (loss) on AFS investments including impairment write downs	**(3)**	—	**12**	19
Fee and other income	**58**	56	**228**	217
Total Revenue	**$ (25)**	$ 391	**$ 1,409**	$ 1,287

For the quarter, total revenue at Empire Life decreased by $416 million to negative $25 million in 2016. On a full year basis, total revenue increased by 9% to $1,409 million compared to $1,287 million in 2015. Revenue volatility was primarily driven by the impact of market interest rate and stock market movements on Fair value change in fair value through profit and loss ("FVTPL") investments. Major revenue items are discussed below.

Net premium revenue for the quarter and year increased by 7.9% and 5.5% respectively, relative to 2015. The increase related primarily to the fixed interest immediate annuities portion of the Wealth Management product line, which experienced stronger demand due to improved interest rates offered by Empire Life and customer caution resulting from stock market volatility.

Fair value change in FVTPL investments including realized amounts often causes large revenue volatility. These assets experienced a loss for the fourth quarter and a net gain for the year in 2016 compared to an opposite pattern for the same periods in 2015. In 2016, the fourth quarter loss was from a decrease in bond prices (due to an increase in market interest rates). In 2015, the fourth quarter gain was primarily from an increase in bond prices (due to a decrease in market interest rates) and an increase in US stock prices. In 2016, the full year gain was primarily from an increase in stock prices and for 2015, the full year loss was from a decrease in stock prices and bond prices (due to an increase in market interest rates). For the fourth quarter and year, the impact of this on net income is significantly reduced due to a corresponding change in insurance contract liabilities (discussed in the Total Benefits and Expenses section below).

Realized gain (loss) on available for sale investments ("AFS") including impairment write downs was a gain for the year in both 2016 and 2015. The gain for both years was primarily due to the sale of AFS bonds. These gains and losses impact net income and are considered in the net income investment experience comments for each of the impacted product lines (see Product Line Results sections later in this report). The assets sold primarily backed capital and surplus.

Fee income for the quarter and year increased by 3.9% and 5.3% respectively in 2016 relative to 2015 primarily due to growth in segregated fund guarantee fees and management fees (see the Product Line Results - Wealth Management section later in this report).

Total Benefits and Expenses

	Fourth quarter		Year	
(in millions of dollars)	**2016**	2015	**2016**	2015
Benefits and expenses				
Net benefits and claims	**$ 151**	$ 162	**$ 593**	$ 642
Net change in insurance contract liabilities	**(357)**	109	**207**	126
Change in investment contracts provision	**(1)**	(1)	**—**	—
Policy dividends	**8**	7	**29**	26
Operating expenses	**40**	39	**145**	147
Net commissions	**56**	49	**195**	189
Interest expense	**3**	2	**9**	9
Total benefits and expenses	**$ (100)**	$ 367	**$ 1,178**	$ 1,139

Total benefits and expenses at Empire Life for the quarter decreased by $467 million to negative $100 million in 2016. On a full year basis, total benefits and expenses decreased by 3.5% to $1,178 million compared to $1,139 million in 2015. Expense volatility was primarily driven by the impact of market interest rate and stock market movements on net change in insurance contract liabilities. Major benefit and expense items are discussed below.

Net benefits and claims variability is dependent on the claims incurred. Generally, claims rise year over year due to growth of the insurance blocks, which was the case for the quarter and full year for the Employee Benefits line of business. Otherwise net benefits and claims for the quarter and full year were lower than last year primarily due to Wealth Management, which declined due to lower fixed interest deferred annuity withdrawals. 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 favourable or unfavourable. Claims experience is the combination of claims incurred compared to claims expected in product pricing and in insurance contract liabilities. Year over year claims experience is discussed in each of the impacted product lines (see Product Line Results sections later in this report).

Net change in insurance contract liabilities varies with many factors including new business sold, claims incurred, surrender and lapse experience, assumptions about the future, and changes in the market value of assets matching insurance contract liabilities. For the quarter and full year, the main reason for the large change from 2015 for this item was the change in insurance contract liabilities resulting from the fair value change in matching assets (described above in the Total Revenue section). Variability in the net change in insurance contract liabilities amounts does not, in isolation, impact net income as it must be looked at in concert with other lines of the statement of operations.

For the quarter and full year net commissions increased year over year primarily due to the increase in Individual Insurance participating product sales.

Product Line Results - Wealth Management

	As at December 31	
(in millions of dollars)	**2016**	2015
Assets under management[4]		
General fund annuities[4]	**$ 970**	$ 959
Segregated fund assets[4]	**8,061**	7,347
Mutual funds[4]	**189**	171

	Fourth quarter		Year	
(in millions of dollars)	**2016**	2015	**2016**	2015
Selected financial information				
Net fixed interest annuity premiums	**$ 39**	$ 32	**$ 176**	$ 144
Segregated fund gross sales[4]	**326**	279	**1,027**	1,120
Segregated fund net sales[4]	**92**	65	**157**	272
Segregated fund fee income	**54**	52	**213**	202
Mutual fund gross sales[4]	**6**	13	**33**	79
Mutual fund net sales[4]	**(1)**	7	**8**	62
Mutual fund fee income	**1**	1	**3**	2
Net income after tax	**$ 8**	$ 10	**$ 62**	$ 59

Assets in Empire Life general fund annuities increased by less than 1%, while segregated fund assets increased by 10% during the last 12 months. The increase in the last 12 months for general fund annuities is related primarily to improving demand for fixed interest immediate annuities. The increase over the last 12 months for segregated funds was attributable to increased stock markets and positive net sales.

Premium revenue for the Wealth Management product line is composed solely of new deposits on fixed interest annuities and excludes deposits on the segregated fund and mutual fund products. For the fourth quarter and full year, net fixed interest annuity premiums were up 21% and 22% respectively compared to 2015 due to improved interest rates offered by Empire Life. Management also believes that customers have chosen more conservative fixed interest products due to concerns with stock market volatility.

For the fourth quarter and full year, segregated fund gross sales were up 17% and down 8% respectively compared to 2015, primarily due to 75% maturity guarantee product sales which increased by $34 million in the fourth quarter but decreased by $56 million for the year. In the fourth quarter of 2014, Empire Life closed its existing segregated funds products to new policies effective October 31, 2014 and on November 3, 2014 launched a new suite of investment products including a new segregated funds family and a new version of its Guaranteed Minimum Withdrawal Benefit (“GMWB”) product. Fees charged to the customer on the new product line are higher than those for the former product line. The new product line’s pricing and features are Empire Life’s response to the economic, regulatory and competitive landscape in the segregated fund product marketplace. While 2016 sales were down from last year, the launch of these new segregated fund products has gone well, achieving gross sales of $281 million (2015 $227 million) and $840 million (2015 $844 million) for the fourth quarter and full year respectively, which represented 86% (2015 81%) and 82% (2015 75%) respectively of total segregated fund gross sales.

Segregated fund net sales for the quarter and full year were up 41% and down 42% respectively compared to 2015 primarily due to the above mentioned gross sales result.

Mutual fund gross sales were very weak and are still a small component of our Wealth Management assets under management. Management believes that customers have chosen more conservative fixed interest products given stock market volatility, which hurt mutual fund sales as these products offer no guarantees to customers. Empire Life continues to explore various strategic alternatives with respect to its mutual fund business.

For the quarter and full year, segregated fund fee income increased by 4% and 5% respectively in 2016 relative to 2015. The increase was primarily due to growth in segregated fund guarantee fees and management fees. Improved stock markets in the second half of 2016 resulted in higher average assets under management and management fees earned relative to 2015.

During the fourth quarter earnings from this product line decreased, while full year earnings increased relative to 2015. The following table provides a breakdown of the components of this year over year change in net income.

(in millions of dollars)	Fourth quarter	Year
Components of increase (decrease)		
2015 loss from update of policy liability assumptions	**$ 4**	**$ 4**
2016 loss from update of policy liability assumptions	**(14)**	**(14)**
Lower new business strain	**2**	**7**
Increase in inforce profit margins	**—**	**4**
Improved annuitant mortality experience	**1**	**—**
Improved investment experience	**5**	**2**
Total	**$ (2)**	**$ 3**

In both 2015 and 2016, the update of policy liability assumptions was unfavourable. In both years there were unfavourable updates for general fund annuities. In 2015, this primarily related to investment return assumptions. In 2016, this primarily related to investment return assumptions and refinements to the modelling of preferred share investment cash flows for deferred and immediate annuity business.

Higher net income from lower new business strain for the year was primarily due to the decrease in segregated fund gross sales (and the resulting sales strain) and lower expenses.

Higher net income on in-force business in 2016 was primarily due to lower expenses and improved stock markets.

Product Line Results - Employee Benefits

	Fourth quarter		Year	
(in millions of dollars)	**2016**	2015	**2016**	2015
Selected financial information				
Annualized premium sales[5]	**$ 9**	$ 12	**$ 44**	$ 44
Net premium revenue	**85**	82	**339**	325
Net (loss) income after tax	**$ 9**	$ (2)	**$ 10**	$ 6

For the quarter, annualized premium sales in this product line decreased by 25% and for the full year annualized premium sales were flat relative to 2015. In-force premium revenue grew 4% for the quarter and for the full year relative to the same periods in 2015. While down slightly, the 2016 level of sales is a strong achievement particularly given the weak economic conditions in Canada.

During the fourth quarter and full year, earnings from this product line increased relative to 2015. The following table provides a breakdown of the components of this year over year change in net income.

(in millions of dollars)	Fourth quarter	Year
Components of increase		
2016 gain from update of policy liability assumptions	**$ 5**	**$ 5**
Improved (worsened) claims experience	**6**	**(1)**
Total	**$ 11**	**$ 4**

In 2016, there was a favourable assumption update for the group long-term disability policy liability in the fourth quarter.

For the full year, claims experience was unfavourable in both years primarily due to health claims partly offset by group life insurance and long-term disability claims results.

Product Line Results - Individual Insurance

	Fourth quarter		Year	
(in millions of dollars)	**2016**	2015	**2016**	2015
Selected financial information				
Annualized premium sales[6]	**$ 14**	$ 11	**$ 42**	$ 51
Net premium revenue	**98**	92	**367**	366
Net income (loss) after tax				
Net income after tax shareholders' portion	**$ 38**	$ 2	**$ 90**	$ 6
Net loss after tax policyholders' portion	**(3)**	(1)	**(7)**	(8)
Net income (loss) after tax	**$ 35**	$ 1	**$ 83**	$ (2)

For the fourth quarter and full year, annualized premium sales in this product line increased by 18% and decreased by 19% respectively compared to 2015. This product line's fourth quarter sales result was attributable primarily to increased sales of participating products. Management believes this is due in part to the January 1, 2017 effective date of less favourable tax rules that deal with the exemption status of certain life insurance policies. The full year decrease in sales was due to lower universal life insurance product sales partly offset by increased sales of participating products and term products. Empire Life's recently launched EstateMax® participating product contributed to this increase in participating product sales. EstateMax® is distributed through professional financial advisors aimed at providing simple estate planning solutions to Canadian baby boomers. In recent years Empire Life has been shifting its product mix toward shorter-term products such as term life, while increasing prices on long-term products, due to the low long-term interest rate environment. During the fourth quarter of 2016 Empire Life decided to stop selling universal life insurance products but will continue to administer its in-force block of universal life insurance products.

During the fourth quarter and full year earnings from this product line increased relative to 2015. The following table provides a breakdown of the components of this year over year change in net income.

(in millions of dollars)	Fourth quarter	Year
Components of increase		
2015 loss from update of policy liability assumptions	**$ 15**	**$ 15**
2016 gain from update of policy liability assumptions	**4**	**4**
Management actions to improve asset/liability matching	**1**	**27**
Improved investment experience	**7**	**31**
Improved mortality, surrender and other experience	**8**	**11**
Decrease in inforce profit margins	**(1)**	**(3)**
Total	**$ 34**	**$ 85**

In 2015, the update of policy liability assumptions was unfavourable by $15 million.

In 2016, the update of policy liability assumptions was favourable by $4 million. The following table provides a breakdown of the components of this amount:

(in millions of dollars)	Year
Components of income increase from update of policy liability assumptions	
Lapse	**$ (19)**
Net re-investment assumptions	**(12)**
Mortality	**7**
Other	**28**
Total 2016 gain from update of policy liability assumptions	**$ 4**

The refinements to lapse rate assumptions for 2016 were primarily related to emerging lapse rate experience for increasing renewal lapse rates on renewable Term 10 business.

The update in investment return assumptions for 2016 was primarily due to regular updates to reinvestment rates and credit spreads for the Canadian Asset Liability Method ("CALM") valuation model for future reinvestment assumptions.

Other policy liability assumption updates for 2016 were primarily related to refinements to the modelling of reinsurance treaties.

Management actions to improve asset/liability matching resulted in increased profit for the fourth quarter and the full year in 2016. The improved matching position resulted in a gain from updating insurance contract liabilities. Empire Life increased its investment in real estate limited partnership units during the first nine months of 2016. This investment is used to match long-term insurance contract liabilities. In addition Empire Life made changes to its bond investments throughout 2016 to tighten matching of investments with insurance contract liabilities.

There was a gain from investment experience for the fourth quarter and full year of 2016 compared to a smaller gain for the comparable period in 2015. In 2016, the experience gain primarily resulted from favourable stock market movements during the fourth quarter and full year in 2016. In 2015, the experience gain primarily resulted from an increase in interest rate spreads on provincial and corporate bonds.

Long-term interest rate movements are demonstrated in the following table.

	Fourth quarter		Year	
	2016	2015	**2016**	2015
Interest rate movement				
30 year Canadian federal government bond yield				
End of period	**2.31 %**	2.16 %	**2.31 %**	2.16 %
Beginning of period	**1.67 %**	2.20 %	**2.16 %**	2.36 %
Change during period	**0.64 %**	(0.04)%	**0.15 %**	(0.20)%
30 year Province of Ontario spread				
End of period	**0.90 %**	1.05 %	**0.90 %**	1.05 %
Beginning of period	**1.00 %**	1.00 %	**1.05 %**	0.95 %
Change during period	**(0.10)%**	0.05 %	**(0.15)%**	0.10 %
30 year A rated corporate spread (including financials)				
End of period	**1.60 %**	1.92 %	**1.60 %**	1.92 %
Beginning of period	**1.73 %**	1.85 %	**1.92 %**	1.52 %
Change during period	**(0.13)%**	0.07 %	**(0.32)%**	0.40 %
30 year A rated financials spread				
End of period	**2.01 %**	2.19 %	**2.01 %**	2.19 %
Beginning of period	**2.26 %**	2.05 %	**2.19 %**	1.87 %
Change during period	**(0.25)%**	0.14 %	**(0.18)%**	0.32 %

Interest rate movements impact both bond asset fair values and insurance contract liabilities. In the fourth quarter and full year of 2016, the increase in interest rates (including spreads described above) caused lower bond prices, which resulted in mark to market fair value bond adjustments. These fair value adjustments are offset by changes in insurance contract liabilities.

Stock market movements are demonstrated in the following table.

	Fourth quarter		Year	
	2016	2015	**2016**	2015
Stock market movement				
S&P/TSX Composite Index				
End of period	**15,288**	13,010	**15,288**	13,010
Beginning of period	**14,726**	13,307	**13,010**	14,632
Percentage change during period	**3.80%**	(2.20)%	**17.50%**	(11.10)%
S&P 500 Index				
End of period	**2,239**	2,044	**2,239**	2,044
Beginning of period	**2,168**	1,920	**2,044**	2,059
Percentage change during period	**3.30%**	6.50 %	**9.50%**	(0.70)%

In the fourth quarter and full year of 2016 the strong increase in stock markets caused common share asset fair value gains. These gains are partially offset by increases in insurance contract liabilities.

Results - Capital and Surplus

		Fourth quarter		Year	
(in millions of dollars)		**2016**	2015	**2016**	2015
Net income (loss) after tax					
Net income (loss) after tax shareholders' portion	**$**	**(1)**	$ 5	**$ (2)**	$ 37
Net income after tax policyholders' portion		**—**	—	**4**	2
Net income (loss) after tax	**$**	**(1)**	$ 5	**$ 2**	$ 39

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.

During the fourth quarter and year, earnings from Capital and Surplus decreased relative to 2015. The following table provides a breakdown of the components of this year over year change in net income.

(in millions of dollars)	Fourth quarter	Year
Components of decrease		
Increased net loss on hedging instruments	**$ (4)**	**$ (30)**
Decreased net income from investments	**(2)**	**(7)**
Total	**$ (6)**	**$ (37)**

During the fourth quarter and full year of 2016, Empire Life experienced a loss of $5 million and $28 million after tax respectively on its hedging program primarily due to rising Canadian stock prices compared to a loss of $1 million and a gain of $2 million respectively for the comparable period in 2015 (discussed in the Risk Management section later in this report).

Decreased net income from investments was primarily due to lower gains from the sale of AFS bonds in 2016 relative to 2015.

Total Cash Flow

	Year	
(in millions of dollars)	**2016**	2015
Cash Flow provided from (used for)		
Operating activities	**$ 292**	$ 149
Investing activities	**(454)**	(179)
Financing activities	**331**	(9)
Net change in cash and cash equivalents	**$ 169**	$ (39)

Cash provided from operating activities in 2015 was close to 2014 levels.

Cash provided from operating activities in 2016 increased from 2015 levels primarily due to increased net cash flows from increases in working capital levels.

The increase in cash used for investing activities during 2016 relative to 2015 was primarily due to the investment of the proceeds from its first quarter 2016 issuance of $149.5 million of preferred shares, the investment of the increased cash flows from fixed interest annuity products into matching assets and the partial investment of the proceeds from Empire Life's fourth quarter 2016 issuance of $200 million of subordinated debt.

The increase in cash provided by financing activities during 2016 relative to 2015 was primarily due to Empire Life's issuance $200 million of subordinated debt during the fourth quarter of 2016 and its issuance of $149.5 million of preferred shares during the first quarter of 2016.

For an analysis of liquidity for Empire Life, see note 10(e) and note 28(b) to the 2016 consolidated financial statements.

Financial Instruments

Empire Life buys investment quality bonds to support, to a very large extent, the liabilities under the insurance and annuity policies of Empire Life. Empire Life's investment strategy also includes the use of publicly-listed "large cap" common stocks to support the liabilities under its insurance policies. Cash flows arising from these financial instruments are intended to match the liquidity requirements of Empire Life's policies, within the limits prescribed by Empire Life. Empire Life is subject to market risk on these financial instruments.

Empire Life 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. Empire Life manages market risk exposure 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. Empire Life manages credit risk by applying its 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 issuer of such debt instruments. Management and Board committees review credit quality relative to investment purchases and also monitor the credit quality of invested assets over time. Management reports regularly to the Investment Committee of Empire Life's Board on the credit risk to which the portfolio is exposed.

Empire Life 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, with total credit exposure limited to $100 million. Additional information regarding financial instruments is included in notes 2(d), 3, 10(c), and 28 to the audited consolidated financial statements for the year ended December 31, 2016.

Capital Resources

	Dec 31 2016	Sep 30 2016	Jun 30 2016	Mar 31 2016	Dec 31 2015
MCCSR Ratio	**248%**	213%	213%	219%	201%

Empire Life continues to maintain a strong balance sheet and capital position. Empire Life's debentures and preferred shares are rated by DBRS Limited ("DBRS") and A.M. Best Company, Inc. ("A.M. Best"). On May 27, 2016, DBRS confirmed its ratings of Empire Life including its issuer rating of "A" (sixth highest of 20 categories), its subordinated debt rating of "A (low)" (seventh highest of 20 categories), its financial strength rating of "A" (sixth highest of 22 categories) and its Preferred Share rating of Pfd-2 (fifth highest of 18 categories). All ratings have a stable trend. According to DBRS, the assigned ratings reflect Empire Life's smaller scale, full suite of products, participation in niche markets that reward company strengths and improved and consistent levels of profitability and fixed charge coverage. On December 16, 2016, Empire Life issued $200 million principal amount of unsecured subordinated debentures due December 16, 2026 by way of private placement in Canada. On December 15, 2016 DBRS assigned a subordinated debt rating of "A (low)" with a stable trend to these debentures.

MANAGEMENT'S DISCUSSION AND ANALYSIS

On May 27, 2016, A.M. Best confirmed its ratings of Empire Life including its issuer rating of “a” (sixth highest of 21 categories), its subordinated debt rating of “bbb+” (eighth highest of 21 categories), its financial strength rating of “A (Excellent)” (third highest of 16 categories) and its Preferred Share rating of “bbb” (ninth highest of 21 categories). All ratings have a stable trend. According to A.M. Best, the ratings reflect Empire Life's favourable risk-adjusted capital position, continued earnings growth and sustainable market presence in Canada with multiple lines of business. On December 16, 2016, A.M. Best assigned a subordinated debt rating of “bbb+” with a stable trend to Empire’s December 16, 2016 subordinated debenture issue.

Empire Life’s risk-based regulatory capital ratio, as measured by MCCSR, of 248% as at December 31, 2016 continued to be above the requirements set by the Office of the Superintendent of Financial Institutions Canada (“OSFI”) as well as Empire Life’s minimum internal targets.

The MCCSR ratio increased 35 percentage points from the previous quarter and increased by 47 percentage points for the full year. The increase for the fourth quarter and full year was primarily due to increases in available regulatory capital. For the year this was partly offset by increases in required regulatory capital, as shown in the table below. The increase for the fourth quarter and full year 2016 was primarily due to Empire Life’s issuance of $200 million principal amount of unsecured subordinated debentures on December 16, 2016 (as described below) which increased Empire Life’s MCCSR ratio by 26 percentage points. The increase for the full year was also due to Empire Life’s issuance of $149.5 million of preferred shares in the first quarter of 2016 (as described below) which increased Empire Life’s MCCSR ratio by 20 percentage points.

(millions of dollars)	**Dec 31 2016**	Sep 30 2016	Jun 30 2016	Mar 31 2016	Dec 31 2015
Available regulatory capital					
Tier 1	**$ 1,206**	$ 1,123	$ 1,089	$ 1,078	$ 918
Tier 2	**707**	541	535	528	504
Total	**$ 1,913**	$ 1,664	$ 1,624	$ 1,606	$ 1,422
Required regulatory capital	**$ 771**	$ 781	$ 762	$ 734	$ 708

The increase in Tier 1 available regulatory capital from the previous quarter was primarily due to net income. The increase in Tier 1 available regulatory capital for the year was primarily due to net income and Empire Life’s issuance of $149.5 million of Preferred Shares in the first quarter of 2016.

Tier 2 available regulatory capital increased from the previous quarter and for the full year primarily due to Empire Life’s issuance of $200 million principal amount of unsecured subordinated.

Regulatory capital requirements decreased from the previous quarter but increased for the full year. The decrease for the quarter was primarily due to decreased requirements related to lapses and interest rate risk, both of which benefited from rising long-term interest rates during the fourth quarter. The increase for the full year was primarily due to increased requirements related to asset default and segregated fund guarantees.

During the first quarter of 2016, Empire Life completed a Canadian public offering of $149.5 million of Preferred Shares. Empire Life is using the net proceeds from the offering for regulatory capital and general corporate purposes. The offering closed during the first quarter and commenced trading on the Toronto Stock Exchange under the ticker symbol EML.PR.A. Holders of the Preferred Shares will be entitled to receive fixed non-cumulative quarterly dividends yielding 5.75% annually, as and when declared by the Board of Directors of Empire Life, for the initial period ending on and including April 17, 2021. Thereafter, the dividend rate will be reset every five years at a rate equal to the 5-year Government of Canada bond yield plus 4.99%.

On December 16, 2016, the Company issued $200 million principal amount of unsecured subordinated debentures with a maturity date of December 16, 2026. The interest rate from December 16, 2016 until December 16, 2021 is 3.383%, and the rate from December 16, 2021 until December 16, 2026 is equal to the 3-month Canadian Bankers’ Acceptance Rate plus 1.95%.

Other Comprehensive Income

(in millions of dollars)	Fourth quarter 2016	Fourth quarter 2015	Year 2016	Year 2015
Other comprehensive income (loss)	**$ (16)**	$ 3	**$ 3**	$ (13)
Less: Participating Policyholders	**—**	(1)	**(2)**	1
Other comprehensive income (loss), attributable to shareholders	**$ (16)**	$ 3	**$ 1**	$ (12)

Other comprehensive income (OCI) decreased in the fourth quarter but increased for the full year of 2016 relative to the comparable periods of 2015. For the fourth quarter, this was primarily due to unrealized fair value decreases relating to AFS bonds in 2016, primarily due to interest rate movements (interest rates increased during the fourth quarter of 2016). This was partly offset by a large gain in the fourth quarter on the re-measurement of the liability component of post-employment defined benefit ("DB") plans resulting from increased interest rates. For the full year 2016, the increase in OCI was primarily due to re-measurement of the asset component of post-employment defined benefit ("DB") plans (described below) and lower realized gains reclassified to net income relating to AFS bonds.

OCI includes the re-measurement of DB plans which had a gain for the full year in 2016 compared to a loss in 2015. The 2016 result for DB plans was primarily due to stock market increases in 2016, compared to stock market decreases in 2015.

Unrealized fair value increases and decreases on AFS bonds in OCI do not impact MCCSR. Re-measurement of DB plans does not immediately impact MCCSR as each quarter's re-measurement gain or loss is amortized over 12 quarters for MCCSR purposes.

Industry Dynamics and Management's Strategy

Empire Life's operations are organized by product line with each line of business having responsibility for product development, marketing, distribution and customer service within their particular markets. This structure recognizes that there are distinct marketplace dynamics in each of the three major product lines. Management believes this structure enables each line of business to develop strategies to achieve the enterprise-wide objectives of business growth and expense management while recognizing the unique business environment in which each operates. The lines of business are supported by corporate units that provide product pricing, administrative and technology services to the lines of business, manage invested assets, and oversee enterprise risk management policies.

Based on general fund and segregated fund assets, Empire Life is among the 10 largest life insurance companies in Canada. Empire Life has approximately six per cent or less market share in all three of its product lines. To be priced competitively in the marketplace while simultaneously providing acceptable long-term financial contribution to shareholders, Empire Life, as a mid-sized company, must find a way to continue to be cost competitive with the larger companies that have some natural economy of scale advantages. In order to improve its unit expenses, management's enterprise-wide strategic focus has been on achieving profitable growth in its selected markets and on expense management. Empire Life has focused exclusively on the Canadian marketplace and, within it, on particular market segments where management feels there are opportunities to build solid, long-term relationships with independent distribution partners by offering competitive products and more personal service. By focusing on particular market segments and by being seen by these independent advisors as a viable alternative to broadly focused competitors, management believes these solid relationships will enable profitable growth.

The Wealth Management product line at Empire Life is comprised of segregated fund products, guaranteed interest products and mutual funds. These products compete against products offered by a variety of financial institutions. A key element of any competitive strategy in this market is providing a competitive rate of return to clients. The value-oriented equity investment strategy used by Empire Life has focused on developing long-term performance in the fund marketplace. Management will continue to improve competitiveness by focusing on long-term performance, providing low cost products to customers along with broadened distribution reach. Although industry sales and Empire Life sales were down in 2016, Empire Life achieved strong growth in assets under management from its segregated fund business as a result of equity market appreciation. Empire Life is continuing to monitor and manage GMWB risk exposure and the competitive landscape for this product The fourth quarter 2014 product launch by Empire Life included a new version of its GMWB product which commands a higher price and reduces the amount of risk to Empire Life while still offering a competitive guaranteed income solution to customers

Within the broader employee benefits marketplace in Canada, Empire Life continues to focus on the small group employer market with fewer than 200 employees representing the majority of Canadian companies. This niche strategy coupled with an ongoing focus on balancing growth and profit has enabled Empire Life to be cost competitive within this market segment and is expected to enable this product line to grow its market share while generating acceptable returns.

Individual Insurance products are very long-term in nature and consequently can be subject to new business strain. New business strain occurs when the provision for adverse deviation included in the actuarial policy liabilities exceeds the profit margin in the product pricing. At current reinsurance price levels in the Canadian market place, a company may reduce new business strain and improve profitability in the short term by opting to increase the amount of insurance risk reinsured to third parties. Mortality trends continue to be favourable for life insurance products. Rather than give up the future earnings that would emerge if the trend in mortality improvement witnessed in recent decades continues, Empire Life continues to utilize lower than average levels of reinsurance with the resultant negative impact on short-term earnings. Low long-term interest rates continue to have an unfavourable impact on this product line. In the past few years, industry prices for longer term life insurance products have increased. Empire Life has also increased prices for these products and has focused its growth efforts on shorter term products, such as 10 year renewable term life insurance. Because of the reasonable long-term returns of this product line, management continues to focus on steady growth, technology development and process improvement in order to continue to have a cost structure that allows us to compete while generating an acceptable long-term financial contribution. Empire Life is continuously reviewing its Individual Insurance product mix to improve profitability, reduce interest rate risk, reduce required regulatory capital, develop web-based products and processes, and improve the customer and advisor experience.

Risk Management

Empire Life is a financial institution offering Wealth Management, Employee Benefits and Individual Insurance products. The Company is exposed to a number of risks as a result of its business activities. The goal of the Company’s risk management process is to ensure that the operations that expose it to risk are consistent with the Company’s strategy, business objectives and risk philosophy while maintaining an appropriate risk/reward balance and enhancing stakeholder value. When making decisions about risk taking and risk management, Empire Life considers:

- The need to meet the expectations of its customers, shareholders and creditors and to protect the commitments that have been made to them;
- The need to be adequately compensated for the capital deployed to support business activities and strategic objectives;
- The need to protect its brand; and
- The need to maintain its targeted financial strength rating.

Empire Life’s risk appetite defines the aggregate level of risk the Company is willing to take to achieve its business strategies. The risk appetite supports the pursuit of shareholder value but does not compromise the Company’s ability to pay claims and fulfil policyholder commitments.

Empire Life's risk management framework is structured based on a number of guiding principles:

- Due to the long term nature of the majority of its commitments, the Company accepts capital market risk provided it is managed within specific risk tolerances and limits. The Company takes a low risk, value-oriented approach to managing its investments - it accepts credit and alternative asset risk provided it is rewarded through appropriately enhanced returns;
- The Company manages liquidity across the business to provide a high level of confidence that all obligations (to customers, creditors and shareholders) will be met when they fall due;
- The Company accepts insurance risks provided they are properly priced and managed in order to deliver value to its customers and shareholders;
- The Company is forward-looking in its business planning and takes a prudent approach to capital management. It strives to have a high level of confidence that capital is sufficient to support planned activities into the future;
- Management is active in industry committees and, through a network of oversight functions, monitors the landscape so that the Company is appropriately positioned to manage regulatory, tax, accounting and actuarial changes;
- The Company accepts that operational risks are a part of doing business and knows that risk management is a key part of decision-making. It protects its business and customers by engaging in cost effective risk mitigation; and
- The Company expects ethical conduct by all of its employees and acts with integrity at all times.

The Board of Directors oversees and monitors the Company's risk management framework, processes and practices and reviews and approves the Company's Enterprise Risk Management Framework and overall risk appetite. Senior management shares responsibility and accountability for risk management across the organization. This enables a cross-functional perspective on risk management, enhanced by the frequency of contact across the management team. The Company has an Asset Management Committee with responsibility for overseeing the management of corporate policies established by both the Investment Committee and Risk and Capital Committee of the Board. More information related to governance can be found under the Corporate Governance over Risk Management section of Empire Life's 2016 annual report. Risk management policy development is centralized under the leadership of the Chief Risk Officer and applies to all business units. The Chief Risk Officer is a member of the Asset Management Committee and has Board reporting responsibility with respect to risk and capital management. All risk management policies and procedures are regularly reviewed for relevance and changes in the risk environment. Accountability, application, day-to-day management and procedural elements are the responsibility of area management, supported by business unit compliance officers and the risk management department. There is senior management representation and oversight on various interdisciplinary risk control committees. The Company formally establishes and documents its values and risk tolerances through several company-wide policies including a Code of Business Conduct, Corporate Disclosure principles, enterprise risk management, capital management and whistleblower policies. The Company's strategic risk management policies (including those related to product design and pricing, investment policies and capital management) are also approved by its Board, or a Board committee.

Caution Related to Sensitivities

In the sections that follow, the Company 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 the Company'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 the Company's future net income, OCI, and capital sensitivities. Changes in risk variables in excess of the ranges illustrated may result in other than proportionate impacts.

Market Risk

Empire Life has equity market risk related to its segregated fund products and from equity assets backing life insurance liabilities. Empire Life has a semi-static hedging program. The objective of the hedging program is to partially protect Empire Life from possible future MCCSR ratio declines that might result from adverse stock market price changes. The hedging program currently employs put options and short positions on key equity indices. The extent of options 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 MCCSR purposes related to segregated fund guarantees, but does not have policy liabilities related to these guarantees on its balance sheet. Therefore a by-product of hedging MCCSR exposure is income statement volatility, as the gains or losses from hedging instruments are not offset by changes in policy liabilities related to segregated fund guarantees on the income statement. During the fourth quarter and full year of 2016 Empire Life experienced a loss of $5 million and $28 million after tax respectively on its hedging program primarily due to rising Canadian stock prices compared to a loss of $1 million and a gain of $2 million respectively for the comparable period in 2015.

Empire Life's MCCSR ratio is also sensitive to stock market volatility, due primarily to liability and capital requirements related to segregated fund guarantees. As of December 31, 2016, Empire Life had $8.1 billion of segregated fund assets and liabilities. Of this amount, approximately $7.8 billion have guarantees. The following table provides a percentage breakdown by type of guarantee:

	Dec 31 2016	Dec 31 2015
Percentage of segregated fund liabilities with:		
75% maturity guarantee and a 75% death benefit guarantee	**1.2%**	0.4%
75% maturity guarantee and a 100% death benefit guarantee	**49.7%**	51.5%
100% maturity and death benefit guarantees (with a minimum of 15 years between deposit and maturity date)	**6.1%**	5.9%
100% maturity and death benefit guarantees (guaranteed minimum withdrawal benefit (GMWB))	**43.0%**	42.2%

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 ignores all the deposits in the customer's policy where the fund value is above the guaranteed amount. Therefore, generally policy-based guarantees 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 were issued, the sensitivity is reduced. If period-end stock markets are low relative to market levels at the time that segregated fund policies were issued, the sensitivity is increased.

The segregated fund regulatory capital and liability framework includes the use of "zero floors" (i.e. negative 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. Generally as stock markets and interest rates rise the magnitude of the negative liabilities will also rise. In the first table below, Empire Life discloses the sensitivity of net income to changes in segregated fund guarantee insurance contract liabilities. There is a net loss resulting from a 20% and a 30% decrease at December 31 for 2016 and 2015, but otherwise the amounts shown in the table are nil. These liabilities (present value of future benefits and expenses minus the present value of future fee revenue) are calculated using stochastic modeling techniques based on a range of future economic scenarios. The liabilities are the greater of: (i) the average of the amounts determined in the worst 20% of the scenarios; and (ii) zero. For the nil amounts shown in this table, the liability for Empire Life was negative. Therefore, the alternative level of zero is applied in these tests (zero floor) resulting in a net income impact of nil. Based on stock market levels at December 31 for 2016 and 2015, the sensitivity of Empire Life shareholders' net income to changes in segregated fund guarantee insurance contract liabilities resulting from stock market increases and decreases is as follows:

Sensitivity to segregated fund guarantees:	**Increase**		**Decrease**		
(in millions of dollars after tax)	**20%**	**10%**	**10%**	**20%**	**30%**
December 31, 2016 Shareholders' net income	**$ nil**	**$ nil**	**$ nil**	**$ (10)**	**$ (117)**
December 31, 2015 Shareholders' net income	$ nil	$ nil	$ nil	$ (10)	$ (109)

As per the sensitivity table, the impact of stock market changes on the segregated fund guarantee liabilities is not linear. As noted earlier, Empire Life also has equity market risk related to its equity assets backing life insurance liabilities. Based on stock market levels as at December 31, 2016 and 2015, the sensitivity of Empire Life shareholders' net income (including changes in segregated fund guarantee insurance contract liabilities) resulting from stock market increases and decreases is as follows (excluding the effect of Empire Life's equity risk hedging program):

Sensitivity excluding equity risk hedge	**Increase**		**Decrease**		
(in millions of dollars after tax)	**20%**	**10%**	**10%**	**20%**	**30%**
December 31, 2016 Shareholders' net income	**$ 51**	**$ 25**	**$ (25)**	**$ (60)**	**$ (196)**
December 31, 2015 Shareholders' net income	$ 44	$ 22	$ (22)	$ (54)	$ (207)

The equity risk hedging program provides relief in adverse scenarios, but incurs losses in positive scenarios.

The December 31, 2016 and 2015 amounts in the following table include the effect of Empire Life's equity risk hedging program (described above):

Sensitivity including equity risk hedge	**Increase**		**Decrease**		
(in millions of dollars after tax)	**20%**	**10%**	**10%**	**20%**	**30%**
December 31, 2016 Shareholders' net income	**$ 36**	**$ 18**	**$ (16)**	**$ (36)**	**$ (148)**
December 31, 2015 Shareholders' net income	$ 27	$ 12	$ (7)	$ (19)	$ (149)

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.

Based on stock market levels on the dates indicated below the sensitivity of Empire Life's MCCSR ratio to stock market increases and decreases for all Empire Life stock market exposures, including segregated fund guarantees, is as follows (excluding the effect of Empire Life's equity risk hedging program):

Excluding Equity Risk Hedge MCCSR	**Increase**		**Decrease**		
Sensitivity to stock markets	**20%**	**10%**	**10%**	**20%**	**30%**
December 31, 2016 MCCSR Ratio	**(0.7)**	**(0.2)**	**(12.1)**	**(35.3)**	**(40.1)**
December 31, 2015 MCCSR Ratio	1.2	0.7	(13.9)	(31.6)	(50.0)

The December 31, 2016 and 2015 amounts in the following table include the effect of Empire Life's equity risk hedging program (described below):

Including Equity Risk Hedge MCCSR	**Increase**		**Decrease**		
Sensitivity to stock markets	**20%**	**10%**	**10%**	**20%**	**30%**
December 31, 2016 MCCSR Ratio	**(5.4)**	**(2.6)**	**(9.7)**	**(30.4)**	**(30.2)**
December 31, 2015 MCCSR Ratio	(3.0)	(1.8)	(10.6)	(24.8)	(40.0)

The amount at risk related to segregated fund maturity guarantees and segregated fund death benefit guarantees and the resulting actuarial liabilities and MCCSR required capital for Empire Life segregated funds is as follows:

Segregated Funds	**Withdrawal Benefit > Fund Value**		**Maturity Guarantee > Fund Value**		**Death Benefit > Fund Value**		**Actuarial**	**MCCSR**
(in millions of dollars)	**Fund Value**	**Amount At Risk**	**Fund Value**	**Amount At Risk**	**Fund Value**	**Amount At Risk**	**Liabilities**	**Required Capital**
December 31, 2016	**$ 2,530**	**$ 627**	**$ 37**	**$ 1**	**$ 324**	**$ 4**	**$ nil**	**$ 150**
December 31, 2015	$ 2,343	$ 593	$ 124	$ 4	$ 1,415	$ 17	$ nil	$ 130

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 December 31, 2016, the aggregate amount at risk for these three categories of risk (reported in the above table) was $632 million, an increase from the aggregate amount at risk of $614 million as at December 31, 2015.

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 actuarial 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. The amounts at risk in December 2016 decreased from the December 2015 levels for GMWB withdrawal benefit exposure primarily due to GMWB sales volume in 2016. The quarterly update of segregated fund policy data on our stochastic model resulted in an increase in required regulatory capital.

In addition, Empire Life's MCCSR ratio is sensitive 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 assumed initial reinvestment rate ("IRR") for nonparticipating insurance business and segregated fund guarantees, is shown in the table below. This assumes no change in the ultimate reinvestment rate ("URR"). The first column below excludes the impact of market value changes in AFS bonds. The AFS bonds provide a natural economic offset to the interest rate risk arising from our product liabilities. The second column below shows the impact if the AFS bonds were sold to realize the gains from a 50 basis point decrease in interest rates.

	Before The Sale of AFS Assets	After The Sale of AFS Assets
	50 bps Decrease	**50 bps Decrease**
Sensitivity To Market Interest Rates:		
December 31, 2016 MCCSR Ratio	**(20)%**	**(15)%**
December 31, 2015 MCCSR Ratio	(17)%	(13)%

Operational Risk

Operational risk relates to the uncertainty arising from larger than expected losses or damages as a result of inadequate or failed internal processes, people and systems, or from external events. Operational risk is naturally present in all of the Company's business activities and encompasses a broad range of risks, including legal disputes, regulatory compliance failures, technology failures, business interruption, information security and privacy breaches, human resources management failures, processing errors, modelling errors, theft and fraud, and damage to physical assets. The following is a further description of key operational risks and their associated risk management strategies.

(1) Legal and Regulatory Risk

The Company is governed by the Insurance Companies Act ("ICA") and supervised by OSFI and is also subject to various requirements imposed by legislation and regulation in each of the provinces and territories of Canada applicable to insurance companies and companies providing other financial services. Material changes in the regulatory framework could have an adverse effect on the Company. Failure to comply with regulatory requirements or public expectations could adversely impact the Company's reputation and ability to conduct business. The Company is subject to litigation from time to time, in the normal course of business, and currently has a number of outstanding lawsuits. There can be no assurance that the present or any future litigation will not have a material adverse effect on the Company.

The Company's corporate compliance department, headed by the Chief Compliance Officer, oversees the regulatory compliance framework. This framework promotes risk-based management of compliance and regulatory risk and includes Company-wide policies, operating guidelines, programs to promote awareness of laws and regulations impacting the Company, ongoing monitoring of emerging legal issues and regulatory changes and employee education programs that include anti-money laundering and anti-terrorist financing, privacy and information security risk management as well as reporting breaches and the Company's code of business conduct. The framework is supported by a network of business unit compliance officers as well as the corporate legal services department. The Chief Compliance Officer reports regularly to the Conduct Review Committee of the Board on the state of compliance, key compliance risks and emerging regulatory trends. General Counsel reports regularly to the Audit Committee of the Board on litigation activity.

(2) Model Risk

The Company uses models to support many business functions including investment analysis, product development and pricing, valuation of policy liabilities, planning, asset/liability management, capital management, project management and risk management. The risk of inappropriate use or interpretation of the Company's models or their output, or the use of deficient models, data or assumptions could result in financial losses or inappropriate decision making. The Company has developed management and mitigation processes related to model use and oversight of models to limit financial, operational and strategic impacts from an error or misinterpretation of model results. Senior management has overall responsibility and accountability for models in use to support activities within their business area.

(3) Human Resources Risk

Competition for qualified employees, including executives, is intense both in the financial services industry and non-financial industries. If the Company is unable to retain and attract qualified employees and executives, the results of its operations and financial condition, including its competitive position, could be adversely affected. To mitigate this risk, the Company has a number of human resources policies, processes and practices in place. Management reports regularly to the Human Resources Committee of the Board on succession planning and employee development programs as well as compensation practices and programs, all of which are designed to attract, motivate and retain high-performing and high-potential employees.

(4) Third-party Risk

The Company obtains many different types of services from a number of third-party services providers and has outsourced certain business functions or processes to third parties. Should these third parties fail to deliver services in compliance with contractual or other service arrangements, the Company's business may be adversely impacted. To mitigate this risk, the Company has established a Company-wide outsourcing policy that provides guidance when considering, entering into or managing existing outsourcing arrangements commensurate with the risks associated with the service provider and the nature of the arrangement. Annually, management reports to the Conduct Review Committee of the Board on outsourcing activities including details on those arrangements deemed to be most material to the Company.

(5) Technology, Information Security and Business Continuity Risk

The Company relies on technology in virtually all aspects of its business and operations including the creation and support of new products and services, and the nature of life insurance business necessitates a substantial investment in technology. Operational integrity, data integrity and security of information and systems infrastructure are all relied upon for normal business operations. Disruptions due to system failure, information security breaches, privacy breaches, cyber-attacks, human errors, natural disasters, criminal activity, fraud or the loss of certain software licensing agreements could have a material adverse impact on the Company.

The Company has an enterprise-wide business continuity and disaster recovery program overseen by the Business Continuity Planning Team and the Chief Technology Officer. The program includes policies, plans and procedures designed so that, to the extent practically possible, key business functions can continue and normal operations can resume effectively and efficiently should a major disruption occur. Each business unit is accountable for preparing and maintaining detailed business continuity plans and processes. The Company establishes and regularly tests business continuity and disaster recovery plans and maintains off-site backup facilities and failover capability designed to minimize downtime and accelerate system recovery.

Information security breaches, including various forms of cyber-attack, could occur and may result in inappropriate disclosure or use of personal or confidential information. To mitigate this risk, the Company has an information security program overseen by the Chief Technology Officer. This program consists of a number of standards, procedures and guidelines focused on protecting information and computer systems. An incident management process is in place for monitoring and managing security events.

Privacy breaches could occur and may result in unauthorized disclosure or use of private and confidential information. To manage this risk, the Company has a privacy program overseen by the Chief Privacy Officer. The program includes policies and standards, ongoing monitoring of emerging privacy legislation and a network of business unit privacy officers. Processes have been established to provide guidance to employees on the handling of personal information and the reporting of privacy incidents and issues to appropriate management for response and resolution.

Business and Strategic Risk

Business and strategic risk relates to the uncertainty in future earnings and capital related to the potential inability to implement appropriate business plans and strategies, make decisions, allocate resources, manage distribution or adapt to changes in business environment, such as the competitive landscape, regulatory and tax changes or changes in accounting and actuarial standards. The Company regularly reviews and adapts its business strategies and plans in consideration of changes in the external business environment, economic, political and regulatory environment. The Company's financial performance is dependent upon its ability to implement and execute business strategies and plans for growth.

The Company's business strategies and plans are designed to align with risk appetite, capital position and financial performance objectives. The Company periodically reassesses risk appetite taking into consideration the economic, regulatory and competitive environments in which it operates. The current environment requires the Company to adapt rapidly to new opportunities and challenges and to refine its strategies accordingly. If the Company fails to revise its strategies on a timely basis or adapt to the changing environment, it may not be able to achieve its growth objectives.

The Company's business strategies and plans are dependent on the successful execution of organizational and strategic initiatives designed to support the growth of its business. The ability to effectively manage these changes and prioritize initiatives directly affects the Company's ability to execute these strategies. Identifying and implementing the right set of initiatives is critical to achieving the Company's business plan targets. Failure to implement these initiatives could also lead to cost structure challenges.

Successful execution of the Company's business strategies and plans depends on a number of factors including its ability to (i) generate sufficient earnings to maintain an adequate level of capital; (ii) generate sustained investment performance; (iii) meet regulatory requirements; (iv) manage risk exposures effectively; (v) attract and retain customers and distributors;(vi) have the right set of products; and (vii) reduce operating expenses while maintaining the ability to hire, retain and motivate key personnel. The Company's business and strategic plans are reviewed and discussed by its senior management team and are subject to approval by the Board of Directors, which also receives regular updates on implementation progress against key business plan objectives. The Board and its subcommittees receive regular updates on key risks.

In addition to the discussion of risks included in this MD&A, a comprehensive discussion of the material risks that impact Empire Life is included in Empire Life's Annual Information Form available at www.sedar.com. Additional disclosures of Empire Life's sensitivity to risks are included in note 28 to the 2016 consolidated financial statements.

Disclosure Controls and Procedures

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company under Canadian securities laws is recorded, processed, summarized and reported within the specified time periods, and include controls and procedures that are designed to ensure that information is accumulated and communicated to management on a timely basis to allow appropriate decisions regarding public disclosure. Under the supervision of management, an evaluation was carried out on the effectiveness of the Company's disclosure controls and procedures as of December 31, 2016. Based on that evaluation, management concluded that the Company's disclosure controls and procedures were effective as at December 31, 2016.

Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS. Under the supervision of management, an evaluation of the Company’s internal control over financial reporting was carried out as at December 31, 2016. Based on that evaluation, management concluded that the Company’s internal control over financial reporting was effective as at December 31, 2016. No changes were made in the Company’s internal control over financial reporting during the year ended December 31, 2016, that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Critical Accounting Estimates

Empire Life’s significant accounting policies are described in note 2 to the consolidated financial statements. Certain of these policies require management to make estimates and assumptions about matters that are inherently uncertain. The most critical of these accounting estimates for Empire Life are the valuation of policy liabilities, financial instrument classification, pension and other employee future benefits and the determination of allowances for impaired investments.

Policy Liabilities

The determination of policy liabilities requires best estimate assumptions that cover the remaining life of the policies for mortality, morbidity, investment returns, persistency, expenses, inflation and taxes and include consideration of related reinsurance effects. Due to the long-term risks and measurement uncertainties inherent in the life insurance business, a margin for adverse deviation from best estimates is included in each assumption. These margins allow for possible deterioration in future experience and provide for greater confidence that policy liabilities are adequate to pay future benefits. The resulting provisions for adverse deviations have the effect of increasing policy liabilities and decreasing the income that otherwise would have been recognized at policy inception. A range of allowable margins is prescribed by the Canadian Institute of Actuaries. Assumptions are reviewed and updated at least annually and the impact of changes in those assumptions is reflected in earnings in the year of the change. Empire Life’s sensitivity to risks related to policy liabilities are included in note 28 to the consolidated financial statements.

Financial Instrument Classification

Management judgment is used to classify financial instruments as fair value through profit or loss (FVTPL), available for sale (AFS) or loans and receivables. Most financial assets supporting insurance contract liabilities and investment contract liabilities are designated as FVTPL. Most financial assets supporting capital and surplus and participating accounts are classified as AFS. Loans and receivables support both contract liabilities and capital and surplus. The designation of a financial instrument as FVTPL or AFS dictates whether unrealized fair value changes are reported in net income or other comprehensive income. Additional information regarding financial instrument classification is included in notes 2(d), 3(a), 3(b), and 10(c).

Pension and Other Employee Future Benefits

Pension and other employee future benefits expense is calculated by independent actuaries using assumptions determined by management. The assumptions made affect the pension and other employee future benefits expense included in net income. If actual experience differs from the assumptions used, the resulting experience gain or loss is recorded in OCI. Additional information regarding pension and other employee future benefits is included in notes 2(j), and 12.

Provision for Impaired Investments
Empire Life maintains a prudent policy in setting the provision for impaired investments. When there is no longer reasonable assurance of full collection of loan principal and loan interest related to a mortgage or policy contract loan, management establishes a specific provision for loan impairment and charges the corresponding reduction in carrying value to income in the period the impairment is identified. In determining the estimated realizable value of the investment, management considers a number of events and conditions. These include the value of the security underlying the loan, geographic location, industry classification of the borrower, an assessment of the financial stability of the borrower, repayment history and an assessment of the impact of current economic conditions. Changes in these circumstances may cause subsequent changes in the estimated realizable amount of the investment and changes in the specific provision for impairment.

Available for sale securities are subject to a regular review for losses that are significant or prolonged. Objective evidence of impairment exists if there has been a significant or prolonged decline in the fair value of the investment below its cost or if there is a significant adverse change in the technological, market, economic or legal environment in which the issuer operates or the issuer is experiencing financial difficulties.

Outlook

The Canadian economy continued to experience slow growth in 2016. Much of the weakness came from low investments in the oil industry and disruption in the output in Alberta oil sands. Unemployment hovered near 7% for most of the year. The sluggishness in Canada reflected the uncertainty in the Global economy. The momentum in the US in 2015 didn’t spill over into 2016 as expected. Growth in China for most of 2016 was sluggish compared to prior years while the economy shifts to a more market driven consumer based economy. Business confidence in the UK and the Euro zone was damaged by the potential impact from the Brexit referendum. The headwinds from the global economy was partially offset by increased consumer spending, an increase in infrastructure spending, and continued growth in the residential housing market in Canada. The Canadian economy picked up momentum in the second half of 2016. The Canadian long-term interest rates increased from 1.72% at the end of the second quarter to 2.31% at the end of fourth quarter 2016. While corporate and provincial bond spreads decrease slightly during this period, the increase in yields brought some relief after a significant decrease in interest rates that occurred in 2014. Interest rates have generally been lower than typical levels for several years. 2016 Global stock markets rallied in 2016. Stock market conditions mainly impact in-force profit margin results and new business growth for the segregated fund and mutual fund portions of Empire Life’s Wealth Management product line. The Canadian resource heavy stock market rose by 17.5% in 2016 compared to a decrease of 11.1% in 2015. The U.S. S&P 500 stock index rose by 9.5% in 2016 compared to a decrease of 0.7% in 2015. The increase in the Canadian and U.S. stock markets has a positive impact on Empire Life’s fees from the segregated funds in the wealth management business. The strengthening of the Canadian dollar resulted in a slightly weaker performance for assets denominated in U.S. dollars which contributed to the performance of many of Empire Life’s segregated funds. Looking forward, consumers continue to be cautious about stock market exposure and Empire Life is well positioned with segregated fund, mutual fund and fixed interest annuity product offerings to satisfy demand for lower risk investments.

While Canada fared well during the 2008 financial crisis compared to many other countries, Canada’s economy has experienced modest growth in the past few years and there continues to be uncertainty resulting in mixed economic indicators. Consumers are the primary stimulus for growth and home sales continue to rise particularly in central Canada and the far western regions of Canada. The recession in parts of western Canada caused by the drop in the oil price appears to have run its course. With recent stability in oil prices and progress in the approval of key pipelines, Alberta’s economy is expected to expand in 2017. Overall the Canadian economy is expected to grow by 2% depending on the contribution the federal fiscal stimulus will provide to growth. With the new administration in the U.S, the uncertainty surrounding Canada’s trade with its largest trading partner could have a material impact on growth in Canada in 2017. This could ultimately have a negative impact on all of Empire’s lines of business.

The Individual Insurance product line has been challenged by a persistent low long-term interest rate environment that followed the financial crisis. This has impacted the entire industry resulting in price increases for individual insurance products by Empire Life and many of our competitors. While market long-term interest rates recovered somewhat in 2015 and 2016, interest rate volatility continued in 2016. Empire Life has decreased its emphasis on long-term life insurance products in favor of shorter term products, such as 10 year renewable term life insurance. Long-term interest rates, product mix and product pricing are expected to continue to be issues for Empire Life's Individual Insurance product line in 2017.

Regulatory changes related to segregated fund guarantees continues to evolve. OSFI is reviewing the overall approach for determining capital requirements for segregated fund guarantee risks. Changes to the capital required for products with guaranteed income may ultimately impact the industry's ability to offer these products at reasonable prices to the consumer.

On September 12, 2016, OSFI released its final version of 2018 guideline - Life Insurance Capital Adequacy Test. This new Guideline, effective January 1, 2018, will establish a new regulatory capital framework for life insurance companies, which will replace the current MCCSR Guideline. This new Guideline was developed in consultation with the Life Insurance industry and OSFI does not expect that it will have a material impact on the capital required by the industry as a whole, in comparison to MCCSR. Empire life is assessing the impact of the new framework and will provide further information once the assessment is completed and OSFI concurs with Empire's application of the new Guidelines.

The IASB has set January 1, 2021 for the adoption of IFRS 17 Accounting for Insurance Contracts. IFRS 17 will include fundamental differences from the CALM method (equivalent to IFRS 4 Insurance Contracts) that Empire Life currently applies for the valuation of insurance contracts and revenue recognition. The IASB has also granted a temporary exemption from the application of IFRS 9 Financial Instruments to allow insurance companies the option of implementing both IFRS 17 and IFRS 9 effective 2021. IFRS 9 applies to the measurement of financial assets, the expected credit loss model and hedge accounting. For Insurance Contracts and Financial Instruments accounting the goal is global consistency under IFRS as opposed to the differing approaches in each country that exist today. In 2014 OSFI issued the Capital Adequacy Guidelines for Banks in Canada based on the Basel III capital standards for Banks worldwide. The Guidelines include requirements that ensure that investors in non-common regulatory capital instruments will bear the loss in the event that the bank may become non- viable as a going concern. These new financial instruments issued by banks must comply with new regulations in order to be included in the banks' capital ratios. OSFI has indicated that they are exploring the applicability of these rules for insurance companies. Empire Life is not aware of any immediate plans by OSFI to make similar changes for life insurance companies.

For capital adequacy standards the goal is consistent treatment of risk within insurance companies from a capital adequacy perspective regardless of the type of business. These two items could have a material impact on the measurement of Empire Life's net income in the future and capital ratios.

The Canadian Securities Administrators ("CSA") has increased disclosure requirements for mutual fund companies, including point of sale requirements and customer relationship model initiatives. Mutual fund fees continue to be an area of interest for Canadian securities regulators. The CSA commissioned independent third-party research that will assess the impact of commissions and embedded (trailer) fees on mutual fund flows. This research will support CSA policy decisions concerning Canada's current mutual fund fee structure. Empire Life continues to monitor these developments and assess the possible impact to the insurance industry at some future date.

Regulatory change is also occurring for Managing General Agents ("MGAs"). Life insurance companies, including Empire Life, commonly contract with MGAs as a key component of the distribution chain for insurance and wealth management products. In 2013, the Canadian Life and Health Insurance Association ("CLHIA") developed a new Insurer-MGA Relationship guideline (effective January 1, 2015). The Guideline describes desired outcomes and related practices in five general areas, stating that insurers should: perform due diligence prior to entering into a contract with an MGA, clearly set out roles and responsibilities in the contract, commit to a culture of treating customers fairly, monitor the performance of the MGA and retain ultimate responsibility.

Government pension reform including the Federal Pooled Registration Pension Plan program and the proposed Ontario Registered Pension Plan are expected to reduce future demand for private sector retirement savings products, having an adverse impact on banks, mutual fund companies, life insurance companies and advisors.

In 2016 changes to tax rules that deal with the exemption status of certain life insurance policies effective on January 1, 2017. The exemption test aims to distinguish between (and tax differently) policies that are designed as protection versus those that are primarily investments. The new exempt test represent a significant change to the tax regime that has existed over the past 30 years. These changes required all life insurance companies to review the design and the pricing of their life insurance product offerings. Empire Life has either modified or withdrawn certain product offerings to comply with the new tax rules.

Quarterly Results

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

(in millions of dollars, except earnings per share)	**Dec 31 2016**	Sep 30 2016	Jun 30 2016	Mar 31 2016	Dec 31 2015	Sep 30 2015	Jun 30 2015	Mar 31 2015
Revenue	**$ (25)**	$ 453	$ 564	$ 416	$ 391	$ 212	$ 41	$ 643
Common shareholders' net income	**$ 53**	$ 38	$ 25	$ 37	$ 16	$ 22	$ 44	$ 26
Earnings per share - basic and diluted	**$ 53.34**	$ 38.67	$ 25.21	$ 37.81	$ 16.43	$ 22.49	$ 45.34	$ 25.97

For the fourth quarter of 2016, total revenue at Empire Life decreased to negative $25 million compared to $391 million in the fourth quarter of 2015. The decrease was primarily due to a large loss in the fourth quarter on FVTPL investments in 2016 compared to a net gain for the same period in 2015. In 2016, the loss was from a decrease in bond prices (due to an increase in market interest rates). In 2015, the net gain was primarily from an increase in bond prices (due to a decrease in market interest rates) and an increase in US stock prices (see Total Revenue section earlier in this report). Revenue volatility during the most recent eight quarters was primarily driven by the impact of market interest rate movements and stock market movements on Fair value change in FVTPL investments. The impact of this on net income is significantly reduced due to a corresponding change in insurance contract liabilities.

For the fourth quarter of 2016, net income was higher relative to 2015 due to higher profit from the Individual Insurance product line primarily attributable to improved stock market conditions in 2016, a favourable update of policy liability assumptions for the Individual Insurance product line in 2016 (compared to an unfavourable update in 2015) and management actions to improve asset/liability matching in 2016. See Product Line Results sections earlier in this report for further information on quarterly results.

Empire Life improved its matching position throughout 2016 by increasing its investment in real estate limited partnership units during the first nine months of 2016 and by making changes to its bond investments. The improved matching position resulted in a gain in all four quarters of 2016 from updating insurance contract liabilities.

Net income variability during the most recent eight quarters was often driven by long-term interest rate movements. Long-term interest rates decreased resulting in unfavourable net income in the individual insurance product line during the quarters ending June 30, 2016, March 31, 2015 and December 31, 2014 quarters. Long-term interest rates increased, resulting in favourable net income in the individual insurance product line during the second, third and fourth quarters of 2015. In addition, unfavourable Individual Insurance mortality, surrender and lapse experience lowered net income in the first, second and third quarters of 2016 and the third quarter of 2015. The annual update of Individual Insurance policy liability assumptions lowered net income in the fourth quarter of 2015. During the first and third quarters of 2016, the first three quarters of 2015 and the fourth quarter of 2014, Empire Life achieved strong year over year growth in the Wealth Management product line net income. This product line’s strong result was primarily due to the growth in segregated fund management fees and growth in segregated fund guarantee fees related to GMWB products. Strong fee income was primarily due to the positive impact of favourable stock market conditions on management fees earned, strong segregated fund sales and higher GMWB prices.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Forward-looking Statements and Information

Certain statements in this MD&A about the Company'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 risks including equity risks, hedging risks, interest rate risks, foreign exchange rate risks; liquidity risks; credit risks including counterparty risks; insurance risks including mortality risks, policyholder behaviour risks, expense risks, morbidity risks, product design and pricing risks, underwriting and claims risks, reinsurance risks; operational risks, including legal and regulatory risks, model risks, human resources risks, third-party risks, technology, information security and business continuity risks; and business risks, including risks with respect to competition, risks with respect to financial strength, capital adequacy risks, risks with respect to distribution channels, risks with respect to changes to applicable income tax legislation, risks with respect to litigation, risks with respect to reputation, risks with respect to risk management policies, risks with respect to intellectual property, risks 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 the Company; 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 the Company'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. The Company 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-GAAP Measures

The Company uses non-GAAP measures including source of earnings, annualized premium sales, assets under management, mutual fund gross and net sales and segregated fund gross and net sales 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. The Company also believes that securities analysts, investors and other interested parties frequently use non-GAAP measures in the evaluation of issuers. The Company's management also uses non-GAAP measures in order to facilitate operating performance comparisons from period to period, to prepare annual operating budgets and to determine components of management compensation.

Sources of earnings breaks down Empire Life 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 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 twelve 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. Empire Life believes that these measures provide information useful to its shareholders and policyholders in evaluating Empire Life's underlying financial results.

Assets under management is a non-GAAP measure of the assets managed by Empire Life, which includes general fund assets, mutual fund assets and segregated fund assets. They represent the total assets of Empire Life and the assets its customers invest in. Empire Life believes that these measures provide information useful to its shareholders and policyholders in evaluating Empire Life's underlying financial results.

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 December 31	
(in millions of dollars)	**2016**	2015
Assets under management		
General fund assets	**$ 7,780**	$ 6,996
Segregated fund assets	**8,082**	7,368
Total assets per financial statements	**15,862**	14,364
Mutual fund assets	**189**	171
Assets under management	**$ 16,051**	$ 14,535

The above table includes the following amounts held by Empire Life's DB plans.

	As at December 31	
(in millions of dollars)	**2016**	2015
DB Plan Assets		
Segregated fund assets	**$ 195**	$ 183
Mutual fund assets	**13**	11

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MANAGEMENT'S DISCUSSION AND ANALYSIS 2016

The Empire Life Insurance Company (Empire Life) is a proud Canadian company that has been in business since 1923. We offer individual and group life and health insurance, investment and retirement products, including mutual funds through our wholly-owned subsidiary Empire Life Investments Inc.

Empire Life is among the top 10 life insurance companies in Canada[1] and is rated A (Excellent) by A.M. Best Company[2]. Our mission is to make it simple, fast and easy for Canadians to get the investment, insurance and group benefits coverage they need to build wealth, generate income, and achieve financial security.

Follow Empire Life on Twitter @EmpireLife or visit our website, www.empire.ca for more information.

[1] Based on general fund and segregated fund assets in Canada as at December 31, 2015 as reported in regulatory filings
[2] As at May 27, 2016

Transfer Agent and Registrar
CST Trust Company
320 Bay Street, 3rd Floor
Toronto, Ontario, M5H 4A6
Phone: 416-682-3860
Toll Free: 800-387-0825
www.canstockta.com

Stock Exchange Listing
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Reporting Procedure for Accounting and Auditing Matters
If you have a complaint regarding accounting, internal controls or auditing matters or a concern regarding questionable accounting or auditing matters, you should submit your written complaint or concern to:

Mr. John Brierley
The Empire Life Insurance Company
259 King Street East
Kingston, ON, K7L 3A8
Email: jfbrierley@sympatico.ca
Phone: 905-338-7290

You may submit your complaint or concern anonymously. Your submission will be kept confidential and will be treated in accordance with the Company's policy for reporting accounting and auditing matters.

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www.empire.ca info@empire.ca

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