

CLARKE
Halifax, Canada

MD&A & Financial Statements
2018

Management's Discussion & Analysis

Clarke Inc.

December 31, 2018 and 2017

MANAGEMENT'S DISCUSSION & ANALYSIS

Management's Discussion & Analysis ("MD&A") presents management's view of the financial position and performance of Clarke Inc. ("Clarke" or the "Company") for the year ended December 31, 2018 compared with the year ended December 31, 2017. The following disclosures and associated consolidated financial statements are presented in accordance with International Financial Reporting Standards ("IFRS"). This MD&A should be read in conjunction with the information disclosed within the consolidated financial statements and notes thereto for the year ended December 31, 2018 and the Company's Annual Information Form ("AIF"), including the risk factors described therein, available on SEDAR at www.sedar.com. This MD&A provides an overall discussion, followed by analyses of the performance of the Company's major investments. The MD&A is prepared as at February 13, 2019 (unless otherwise stated). All dollar amounts are shown in millions of Canadian dollars unless otherwise indicated.

OVERVIEW & STRATEGY

Clarke is an investment company. Our objective is to maximize shareholder value. While not the perfect metric, we believe that Clarke's book value per share, together with the dividends paid to shareholders, is an appropriate measure of our success in maximizing shareholder value over time.

We attempt to maximize shareholder value by allocating capital to investments that we believe will generate high returns and reallocating capital over time as needed. In doing this, Clarke's goal is to identify investments that are either undervalued or are underperforming and may be in need of positive change. These investments may be companies, securities or other assets such as real estate, and they may be public entities or private entities. We do not believe in limiting ourselves to specific types of investments. From time to time, Clarke will invest passively in a security where it believes the security is undervalued and there is no need for change or where it believes the security is undervalued but that the management team in place at the underlying company is doing an appropriate job to reduce the undervaluation. More often, Clarke will seek active involvement in the governance and/or management of the company in which it invests. In these cases, Clarke will have acquired the security with a view of changes that could be made to improve the underlying company's performance and maximize the company's value. When Clarke believes that an investee company has implemented appropriate changes and/or the value of the investee company has reached or exceeded its intrinsic value, Clarke may sell its investment. Clarke generally invests in industries that have hard assets, including manufacturing, industrial, energy and real estate businesses.

FULL YEAR REVIEW AND OUTLOOK

During 2018, the Company's book value per share increased by \$1.50 or 14.0%. The increase can be ascribed to (i) positive \$1.31 per Clarke common share ("Common Share") resulting from the recognition of additional surplus in one of our pension plans, (ii) positive \$0.23 per Common share due to repurchasing Common Shares at prices below our book value per share, offset by (iii) negative \$0.04 per Common Share of investment performance. Our book value per Common Share at the end of the year was \$12.21 while our Common Share price was \$12.50.

Two thousand eighteen was a year of mixed performance for Clarke. First, the positive.

We continued to monitor and work with our largest investees, Holloway Lodging Corp. ("Holloway") and TerraVest Industries Inc. ("Terravest"). We believe each company performed well during the year and continued to increase its intrinsic value per share, especially given the challenges each company faced during the year.

We expect that Holloway increased its net operating income compared to the prior year with a rebound in certain Western Canadian hotel markets. Holloway launched a third party management platform, which is a capital-light, high-margin business. Holloway also sold three hotels from October 2018 to January 2019 generating significant gains on sale. As a result of these and other activities, Holloway was able to repay approximately \$48.0 million of debt or 23% of its total debt and repurchase 15.1% of its shares since January 1, 2018. Clarke did not sell any shares of Holloway during the year and now owns 51% of Holloway's shares. Accounting rules require that, beginning in the first quarter of 2019, Clarke consolidate Holloway's financial results into its own results and deduct a non-controlling interest for the 49% of Holloway's shares Clarke does not own. Of course, this does not reflect the way we view or treat our investment in Holloway. We will do our best to provide supplementary disclosure to show Clarke's performance on a non-consolidated basis. We believe Holloway remains undervalued. With a much lower debt balance and cost of debt than in prior years, Holloway has the ability to generate significant cash flows. As well, we believe the value of Holloway's hotels is understated on its financial statements, which should lead to growth in book value per share if Holloway sells additional hotels.

Terravest increased its EBITDA by \$14.2 million or 56% compared to the prior year. This was despite weak oil and gas conditions in Western Canada and significant steel tariffs imposed by Canadian and US governments. Terravest acquired MaXfield Group Inc. early in 2018, which we believe will contribute greatly to Terravest’s product line, manufacturing capabilities and financial results. Terravest also completed two substantial issuer bids, repurchasing a total of 9.5% of its shares since January 1, 2018. Clarke sold 363,560 shares in Terravest’s first substantial issuer bid. We do not intend to sell additional shares for the foreseeable future and currently own 31.6% of Terravest. We also believe Terravest is materially undervalued, trading at approximately 7x 2018 EBITDA. We believe Terravest can continue to grow organically and through smart acquisitions; assuming only modest EBITDA growth over last year, Terravest likely trades at or less than 6x EBITDA.

Our ferry business, led by Serge-Martin Denis, continues to operate safely and reliably while contributing to Clarke’s cash flow. We look forward to another successful season in 2019.

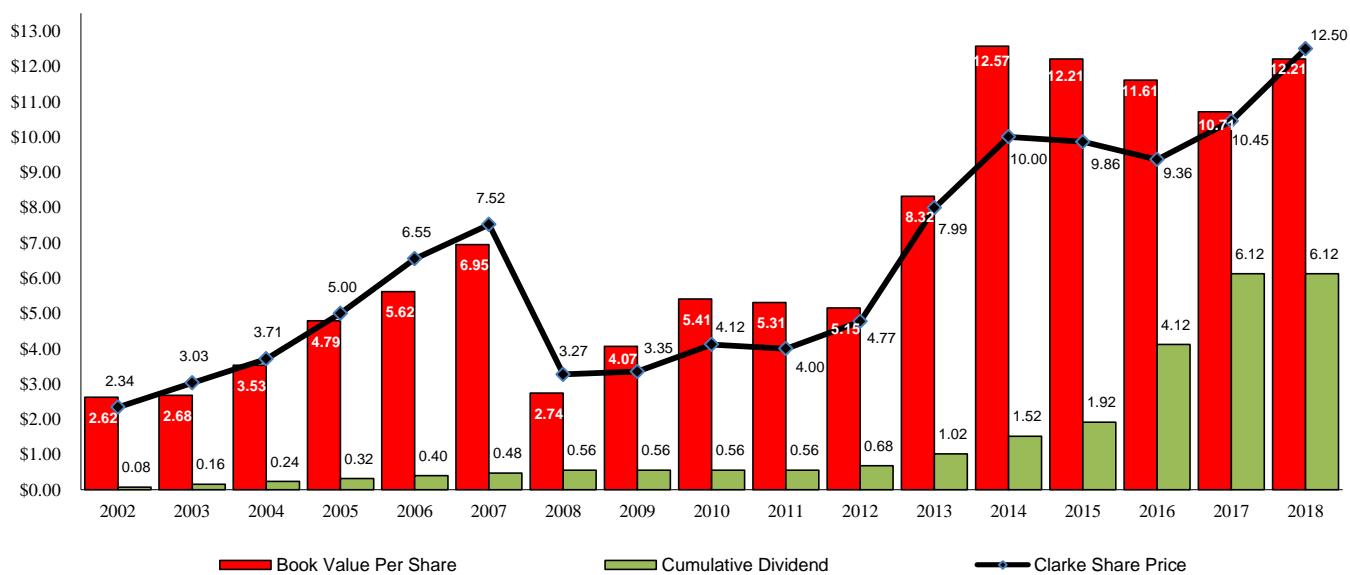
Finally, we repurchased a total of 2,315,079 Common Shares or 15.9% of our outstanding Common Shares during the year. We believe this purchase price will prove to be a bargain as the true value of Holloway, Terravest and our other investments are realized over time.

Now for the negative. Our energy basket investments performed dismally in 2018. We have spent considerable time reflecting on the investments we made, where we made mistakes and what we should do differently if similar investment situations arise in the future. We believe the three energy investments we own are undervalued, but the degree of undervaluation varies among the three companies.

For most of the year, we commented that we found it challenging to find investments that meet our investment criteria. We started to get excited about new opportunities in December 2018 as markets declined precipitously, although there remains a dearth of opportunities in the small-cap real estate and industrial sectors that have proven to be good hunting grounds for us in the past. We used the opportunity the markets presented beginning in December to materially increase the size of one of our energy basket investments. We believe this company is undervalued and could benefit from new value-creating ideas. We will say more about this when we can.

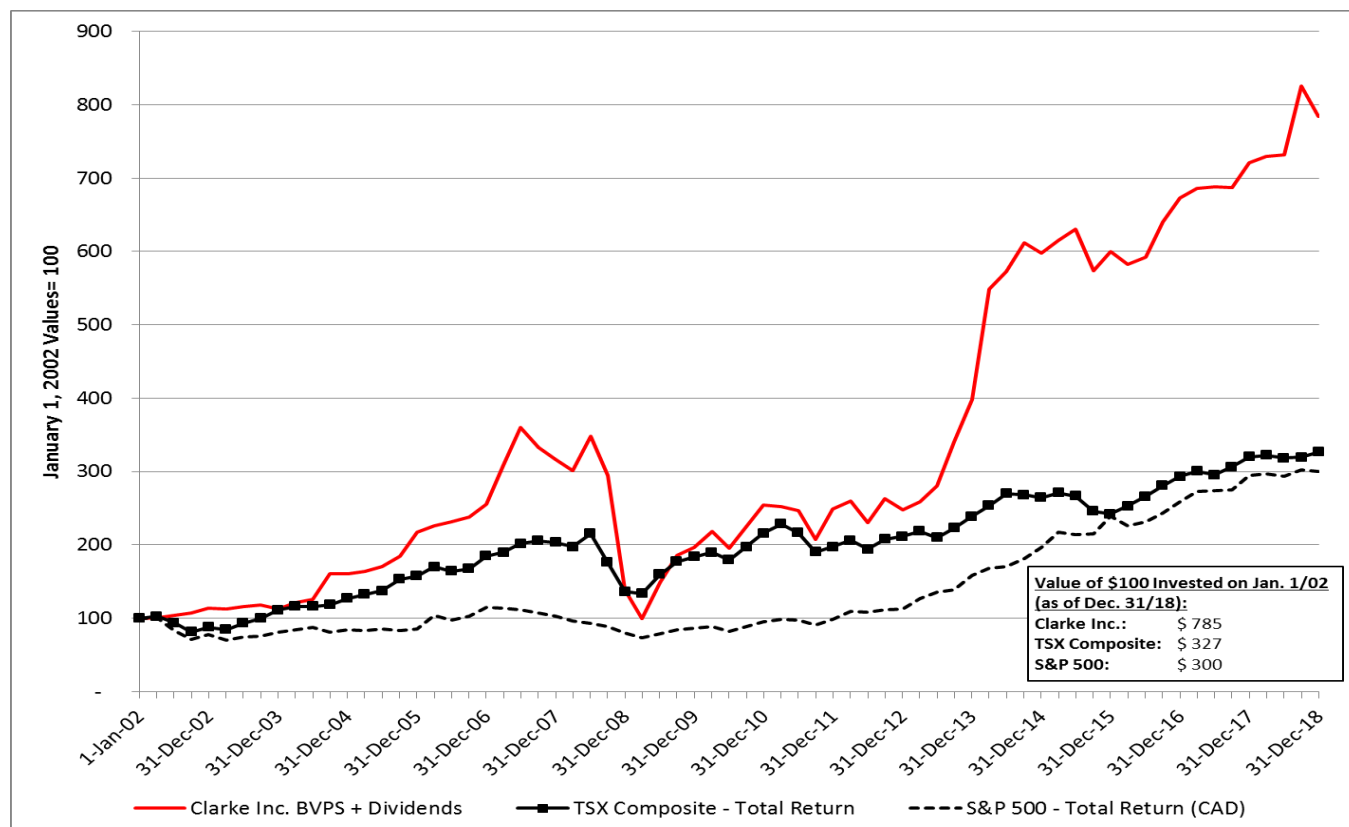
BOOK VALUE PER SHARE

The Company’s book value per share at December 31, 2018 was \$12.21, an increase of \$1.50 per Common Share since December 31, 2017. The following graph shows Clarke’s book value per share, share price and cumulative dividends paid since 2002 (the year the present Executive Chairman joined the Company).



* Information for the years ended 2002 and 2003 is as at March of the following year. In 2004 the Company’s year-end was changed to December. All other information is for the years ended December 31.

The following graph compares the yearly change in the value of \$100 invested since 2002 (the year the present Executive Chairman joined the Company) in (i) the TSX Composite Total Return Index, (ii) the S&P 500 Total Return Index, and (iii) the Company based on the change in book value per share (“BVPS”) and cumulative dividends paid.



RESULTS OF OPERATIONS

Highlights of the consolidated financial statements for the last three completed fiscal years are as follows:

<i>(in millions, except per share amounts)</i>	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
	\$	\$	\$
Realized and unrealized gains (losses) on investments	(5.2)	3.2	20.2
Dividend income	3.7	3.6	3.5
Interest income	0.2	0.8	1.7
Revenue and other income*	8.2	5.6	7.3
Net income (loss)	(0.6)	3.5	25.4
Comprehensive income (loss)	18.6	15.9	22.9
Basic and diluted earnings (loss) per share (“EPS”)	(0.04)	0.24	1.66
Total assets	164.1	160.6	177.8
Long-term financial liabilities	2.4	0.4	1.1
Cash dividends declared per share	—	2.00	2.20
Book value per share	12.21	10.71	11.61

*Revenue and other income include gains on sale of fixed assets, foreign exchange gains/losses, and service revenue.

Net loss of the Company for the year ended December 31, 2018 was \$0.6 million compared with net income of \$3.5 million in 2017. During the year ended December 31, 2018, the Company had unrealized losses on its investments of \$9.2 million compared to unrealized gains of \$30.4 million in 2017. The Company had realized gains on its investments of \$4.0 million for the year ended December 31, 2018 compared with realized losses of \$27.2 million in 2017.

INVESTMENT HOLDINGS

The Company owns securities and a ferry business. The Company's equity holdings generated dividends of \$3.7 million in the year ended December 31, 2018 and \$3.5 million in 2017. The Company's debt and cash holdings generated interest income of \$0.2 million in the year ended December 31, 2018, compared to \$0.8 million in 2017. This decrease is due to the sale of debenture investments during the prior year.

Securities Portfolio

The Company's securities portfolio consisted of the following investments:

	December 31, 2018				December 31, 2017			
	Shares	Market Price \$	Market value \$'000	%	Shares	Market Price \$	Market value \$'000	%
Energy Securities Portfolio	N/A	N/A	11,552	9.6	N/A	N/A	15,503	13.0
Holloway	7,952,715	6.30	50,102	41.7	7,952,715	5.70	45,330	38.0
Keck Seng Investments Ltd.	4,292,000	0.86	3,686	3.1	4,292,000	1.12	4,823	4.0
Terravest	5,386,440	10.18	54,834	45.6	5,750,000	9.35	53,763	37.3
Carrying value of securities			120,174	100.0			119,419	100.0

The breakdown of the change in the Company's securities portfolio is as follows:

	Year ended December 31, 2017 \$
Securities – beginning of year	119.4
Purchases	9.4
Proceeds on sale	(4.0)
Net realized and unrealized losses on securities (net of foreign exchange gains on securities)	(4.6)
Securities – end of year	120.2

Other Investments

During the year, we sold our interest in a private equity fund. We continue to own a receivable of nominal value from a second private equity fund, which is classified with our marketable securities for accounting purposes. We also own a passenger/car ferry operating on the St. Lawrence River under contract with the Government of Québec since 1973. There were no material developments with the ferry during the quarter.

OUTSTANDING SHARE DATA

At February 13, 2019, the Company had:

- An unlimited number of Common Shares authorized and 12,283,688 Common Shares outstanding; and
- An unlimited number of First and Second Preferred Shares authorized and none outstanding.
- 250,000 options to acquire Common Shares outstanding, all of which are vested and exercisable.

SUBSTANTIAL ISSUER BIDS (“SIB”)

In December 2017, the Company initiated a SIB, pursuant to which the Company offered to purchase for cancellation up to 1,250,000 of its issued and outstanding Common Shares at a price of \$10.50 per common share. The offer was open for acceptance until January 2018 at which time 1,851,579 Common Shares were tendered and taken up by the Company and cancelled.

NORMAL COURSE ISSUER BIDS (“NCIB”)

The directors and management are of the opinion that, from time to time, the prices of the Company’s Common Shares may not reflect their intrinsic value and, therefore, purchasing such Common Shares may be a worthwhile use of funds and in the best interests of the Company and its shareholders.

In May 2017, Clarke announced that it had received approval from the TSX to conduct a NCIB to purchase for cancellation up to 742,243 Common Shares, representing 5% of the issued and outstanding Common Shares as at that date. The NCIB commenced on June 2, 2017 and Clarke repurchased 243,900 Common Shares by the end of 2017 and 199,100 Common Shares in 2018 prior to the expiry date of June 1, 2018.

In June 2018, Clarke announced that it had received approval from the TSX to conduct a NCIB to purchase for cancellation up to 627,514 Common Shares, representing 5% of the issued and outstanding Common Shares as at that date. The NCIB commenced on June 8, 2018 and Clarke repurchased 264,400 Common Shares by the end of 2018.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2018, the Company’s cash position was \$7.0 million compared to \$20.8 million at December 31, 2017. This decrease in cash is mainly a result of the repurchase of Common Shares.

Cash flow from operating activities

Cash provided by operating activities was \$12.0 million for the year ended December 31, 2018 and \$4.8 million for 2017. The cash from operating activities is driven mainly by the dividends and interest received during the year as well as the ferry operations.

At December 31, 2018, working capital excluding securities was \$6.2 million, compared to \$25.0 million at December 31, 2017. The Company’s working capital needs are minimal and the Company has the ability to fund any working capital needs through its cash on hand and its existing credit facilities.

Cash flow from investing activities

Net cash of \$3.1 million was used in investing activities during the year ended December 31, 2018, compared to \$41.9 million provided in 2017. Net cash used investing activities during the year was mainly a result of net purchases of investments of \$5.3 million and dry dock costs of \$0.8 million in the ferry operation, offset by an after-tax pension surplus distribution of \$1.2 million and proceeds of \$1.7 million on the sale of a private equity investment. Net cash provided by investing activities during 2017 was mainly a result of the after-tax pension surplus distributions of \$23.4 million and net sales of investments in the amount of \$17.6 million.

Cash flow from financing activities

Net cash used in financing activities was \$22.6 million for the year ended December 31, 2018, compared to \$32.7 million in 2017. Net cash used in financing activities during the year was related to the repurchase of Common Shares of \$25.0 million, offset by long-term debt proceeds of \$3.1 million. Cash used in financing activities during 2017 was mainly related to the payment of a special dividend in the amount of \$29.3 million and the repurchase of Common Shares of \$2.7 million.

Available capital under credit facilities

The Company has access to credit facilities where certain of the Company’s securities are pledged as collateral. At December 31, 2018, \$20.0 million was available under these facilities and nil was drawn on these facilities. Declines in the market value of pledged securities may have an adverse effect on the amount of credit available under these facilities.

Contractual obligations and capital resource requirements

The effects of commitments, events, risks and uncertainties on future performance are discussed in the sections relating to Contractual Obligations and Capital Resource Requirements.

The table below summarizes Clarke’s maximum contractual obligations by due date:

Contractual obligations	Total	Less than			
		1 year	1 – 3 years	3 - 5 years	After 5 years
	\$	\$	\$	\$	\$
Long-term debt	3.4	1.0	2.0	0.4	—
Operating leases	0.9	0.9	—	—	—
	4.3	1.9	2.0	0.4	—

Clarke expects to be able to fund all working capital requirements, contractual obligations, and capital expenditures from a combination of operating cash flows, existing credit facilities, and its current cash and cash equivalents position.

Clarke has several investment margin facilities with Canadian brokerage companies. The facilities permit draws of a portion of the market value of purchases of qualifying securities, depending upon the type of instrument, with certain market value restrictions. At December 31, 2018 and 2017, Clarke had drawn nil under these facilities and had total cash availability of \$20.0 million (2017 – \$6.6 million) (see note 17 to the consolidated financial statements for the year ended December 31, 2018).

Unrecorded commitments

At December 31, 2018, Clarke continued to be a party to the following unrecorded commitments:

- Operating leases, as discussed under “Contractual Obligations and Capital Resource Requirements” above, in the annual MD&A for the year ended December 31, 2018, and in note 12 to the consolidated financial statements for the year ended December 31, 2018.
- Other commitments, as discussed in note 12 to the consolidated financial statements for the year ended December 31, 2018.

FOURTH QUARTER

A comparison of results for the three months ended December 31, 2018, compared to three months ended December 31, 2017, is as follows:

	Three months ended December 31, 2018	Three months ended December 31, 2017
	\$	\$
Revenue		
Realized and unrealized gains (losses) on investments	(10.9)	1.1
Dividend income	0.9	0.9
Interest income	0.1	0.1
Provision of services	1.4	1.1
Other income (loss)	0.3	(0.1)
	(8.2)	3.1
Expenses		
Cost of services provided	1.1	0.9
General and administrative expenses	0.5	0.9
Pension expense (recovery)	(0.1)	0.2
Share-based payment expense	—	0.4
Depreciation and amortization	0.1	0.1
Income (loss) before income taxes	(9.8)	0.6
Provision for income taxes	—	1.2
Net loss	(9.8)	(0.6)
Comprehensive income (loss)	(12.2)	10.9

Net realized and unrealized losses on investments for the fourth quarter of 2018 were \$10.9 million compared to gains of \$1.1 million for the same period in 2017. Dividend and interest income were consistent year over year. General and administrative expenses during the fourth quarter of 2018 were \$0.4 million lower than expenses during the same period in 2017. The Company had a net loss of \$9.8 million in the fourth quarter of 2018 compared to \$0.6 million in the same period in 2017. This was largely driven by the unrealized losses on investments during the period compared to the same period in the prior year. Comprehensive loss for the fourth quarter was \$12.2 million compared to comprehensive income of \$10.9 million for the same period in 2017.

For the three months ended December 31, 2018, Clarke's basic EPS was negative \$0.79, compared to \$0.04 for the same period in 2017.

Net cash provided by operating activities was \$0.7 million for the fourth quarter of 2018, compared to \$1.4 million provided in the same period in 2017. Cash flow provided in the fourth quarter of 2018 and 2017 was driven mainly by the dividends and interest received during the period as well as the ferry operations.

Net cash used in investment activities was \$5.6 million in the fourth quarter of 2018, compared to \$9.6 million provided in the same period in 2017. Net purchases of securities in the fourth quarter of 2018 totalled \$5.6 million compared to net sales of \$6.6 million in the fourth quarter of 2017. The Company also received a pension plan surplus distribution of \$2.7 million after-tax during the fourth quarter of 2017.

Net cash used in financing activities for the fourth quarter of 2018 was \$2.3 million compared to net cash used of \$0.9 million for the same period in 2017. During the fourth quarter of 2018 the Company made its regular long-term debt repayments and continued to repurchase shares under its NCIB.

SUMMARY OF QUARTERLY RESULTS

Key financial information for the current and preceding seven quarters is as follows:

<i>Three months ended</i>	Mar. 2017	Jun. 2017	Sept. 2017	Dec. 2017	Mar. 2018	Jun. 2018	Sep. 2018	Dec. 2018
	\$	\$	\$	\$	\$	\$	\$	\$
Revenue and other income (loss)	5.6	1.9	2.4	3.1	3.5	2.8	8.8	(8.2)
Net income (loss)	4.2	—	—	(0.6)	2.1	0.9	6.2	(9.8)
Other comprehensive income (loss)	0.8	0.7	(0.6)	11.5	0.2	—	21.2	(2.4)
Comprehensive income (loss)	5.0	0.7	(0.6)	10.9	2.3	0.9	27.4	(12.2)
Basic and diluted EPS (in dollars)	0.28	—	—	(0.04)	0.16	0.07	0.49	(0.79)

As seen in the table above, our results can fluctuate significantly from quarter to quarter, mainly as a result of certain accounting standards the Company follows. Under IFRS, realized and unrealized gains and losses on our publicly-traded securities are recorded in "revenue" on our consolidated statements of earnings. The Company does not believe that quarterly fluctuations in the stock prices of our investee companies necessarily reflect a change in the value of the underlying businesses in which we are invested. The value of the underlying businesses are often more stable than their stock prices reflect. Clarke views its investments on a longer-term basis as opposed to on a quarter-to-quarter basis. These fluctuations, however, often provide us with an opportunity to invest more capital in particular investments that we like or vice-versa.

RELATED PARTY TRANSACTIONS

The Company was party to the following related party transactions during the year ended December 31, 2018:

- The Company was a party to rental agreements and tax services agreements with companies owned or partially owned by the Executive Chairman and his immediate family member. One rental agreement ended during 2018 and another rental agreement began in 2018. Included in 'Expenses' is rental and tax services expenses of \$0.1 million (2017 – \$0.1 million) under this agreements.
- The Company provides administrative and asset management services to two pension plans it sponsors. Included in 'Revenue' is \$0.5 million (2017 – \$0.4 million) for services provided to the pension plans during the year.

- During the prior year, the Company provided consulting and tax services for Holloway and Terravest which are investments in associates of the Company. Included in 'Revenue' is \$0.2 million for the services provided.
- During the prior year, the Company sold marketable securities through the facilities of the Toronto Stock Exchange to the Clarke Inc. Master Trust, which holds the units of the pension plans administered by the Company. The sale was made for investment purposes and the Company received net proceeds of \$5.9 million.

Key management consists of the directors and officers of the Company. The compensation accrued is as follows:

Year ended December 31, 2018	Board of directors	Officers	Total
	\$	\$	\$
Salary and fees	0.1	0.3	0.4
Bonus	—	0.1	0.1
Pension value	1.1	—	1.1
Total	1.2	0.4	1.6

FINANCIAL INSTRUMENTS

In the normal course of operations, the Company uses the following financial and other instruments:

- To generate investment returns, the Company will invest in equity, debt and other securities. These instruments may have interest rate, market, credit and foreign exchange risk associated with them.
- To manage foreign exchange, interest rate and general market risk, the Company may enter into futures and forward exchange contracts. These instruments may have interest, market, credit and foreign exchange risk associated with them. Clarke hedges its foreign currency exposure on U.S. dollar denominated investments. Clarke anticipates continuing this policy for the foreseeable future.

As an investment company, Clarke has a significant number of financial instruments. Notes 1, 5, 8, 11, 17 and 18 to the consolidated financial statements for the year ended December 31, 2018 and the Company's 2018 AIF, provide further information on classifications in the financial statements, and risks, pertaining to the use of financial instruments by the Company.

SIGNIFICANT EQUITY INVESTMENTS

In accordance with National Instrument 51-102 of the Canadian Securities Administrators, the Company has determined that Holloway and Terravest are significant equity investees. Accordingly, we are required to disclose the following summary financial information. The summarized financial information provided is for the most recent annual period and the comparative annual period. For those reporting entities that have not yet released their annual consolidated financial statements for the current year, the prior year financial information is provided.

Holloway

Holloway's core business is hotel ownership. Holloway owns 30 hotels comprising 3,347 rooms. As of December 31, 2018, Clarke owned 46.4% of the outstanding shares of Holloway.

Selected Financial Information (audited)	Year ended	Year ended
	December 31, 2017	December 31, 2016
	\$	\$
Total assets	322.4	351.4
Total liabilities	(216.6)	(246.4)
Shareholders' equity	105.8	105.0
Total revenue	105.7	106.5
Net income (loss)	6.5	(1.3)

Terravest

Terravest is engaged in (i) the manufacturing of residential and commercial tanks and pressure vessels, (ii) the manufacturing of storage and transportation equipment, (iii) the manufacturing of wellhead processing equipment for the oil and natural gas industry, and (iv) well servicing for the oil and natural gas industry. As of December 31, 2018, Clarke owned 31.6% of the outstanding shares of Terravest.

Selected Financial Information (audited)	Year ended	Year ended
	September 30, 2018	September 30, 2017
	\$	\$
Total assets	244.2	207.4
Total liabilities	(155.5)	120.8
Shareholders' equity	88.7	86.6
Total revenue	269.9	192.5
Net income	17.2	9.0

DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The implementation of Canadian Securities Administrators National Instrument 52-109 - Certification of Disclosure in Issuers' Annual and Interim Filings represents a continuous improvement process, which has prompted the Company to formalize existing processes and control measures and to introduce new ones. The objective of this instrument is to improve the quality, reliability, and transparency of information that is filed or submitted under securities regulation.

In accordance with this instrument, the Company has filed certificates signed by the President & Chief Executive Officer and the Chief Financial Officer that, among other things, report on the design and effectiveness of disclosure controls and procedures and the design and effectiveness of internal controls over financial reporting.

Management has designed disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to the President & Chief Executive Officer and the Chief Financial Officer, particularly during the period in which annual filings are being prepared. These two certifying officers evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2018, and based on their evaluation, concluded that these controls and procedures were adequate and effective.

Management has also designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. The President & Chief Executive Officer and the Chief Financial Officer have supervised Company's management in the evaluation of the design and effectiveness of the Company's internal controls over financial reporting as of the end of the period covered by the annual filings and believe the design and effectiveness to be adequate to provide such reasonable assurance using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework (2013).

Finally, there have been no changes in the Company's disclosure controls and procedures or internal controls over financial reporting during the year ended December 31, 2018 that have materially affected, or are reasonably likely to materially affect, the effectiveness of the internal controls over financial reporting.

ENVIRONMENTAL MATTERS

The Company's businesses are exposed to the following environmental risks in conducting regular operations: (i) contamination of owned or leased property; and (ii) contamination of the environment relating to spills or leaks originating from the Company's ferry.

The Company's businesses regularly review their operations and facilities to identify any potential environmental contamination or liability. Limited internal reviews, which may include third party environmental assessments, have been conducted at all the Company's wholly-owned real estate within the past five years. These limited reviews identified no material remediation issues and potential risks and there have been no material events arising subsequently that would indicate additional obligations.

The Company believes it and its businesses comply in all material respects with all relevant environmental laws and regulations. The Company is not aware of any material uninsured pending or proceeding actions against it or any of its businesses relating to environmental issues.

CAUTIONARY STATEMENT REGARDING USE OF NON-IFRS ACCOUNTING MEASURES

This MD&A makes reference to the Company's book value per share as a measure of the performance of the Company as a whole. Book value per share is measured by dividing shareholders' equity at the date of the statement of financial position by the number of Common Shares outstanding at that date. Clarke's method of determining this amount may differ from other companies' methods and, accordingly, this amount may not be comparable to measures used by other companies. This amount is not a performance measure as defined under IFRS and should not be considered either in isolation of, or as a substitute for, net earnings prepared in accordance with IFRS.

FORWARD-LOOKING STATEMENTS

This MD&A may contain or refer to certain forward-looking statements relating, but not limited, to the Company's expectations, intentions, plans and beliefs with respect to the Company. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "expects", "does not expect", "is expected", "budgets", "estimates", "forecasts", "intends", "anticipates" or "does not anticipate", "believes", or equivalents or variations of such words and phrases, or state that certain actions, events or results, "may", "could", "would", "should", "might" or "will" be taken, occur or be achieved. Forward-looking statements include, without limitation, those with respect to the future or expected performance of the Company's investee companies, the future price and value of securities held by the Company, changes in these securities holdings, the future price of oil and value of securities held in the Company's energy basket, changes to the Company's hedging practices, currency fluctuations and requirements for additional capital. Forward-looking statements rely on certain underlying assumptions that, if not realized, can result in such forward-looking statements not being achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors that could cause the actual results of the Company to be materially different from the historical results or from any future results expressed or implied by such forward-looking statements. Such risks and uncertainties include, among others, the Company's investment strategy, legal and regulatory risks, general market risk, potential lack of diversification in the Company's investments, interest rates, foreign currency fluctuations, the sale of Company investments, the fact that dividends from investee companies are not guaranteed, reliance on key executives, commodity market risk, risks associated with investment in derivative instruments and other factors. With respect to the Company's investment in a ferry operation, such risks and uncertainties include, among others, weather conditions, safety, claims and insurance, labour relations, and other factors.

Although the Company has attempted to identify important factors that could cause actions, events or results not to be as estimated or intended, there can be no assurance that forward-looking statements will prove to be accurate as actual results and future events could differ materially from those anticipated in such statements. Other than as required by applicable Canadian securities laws, the Company does not update or revise any such forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events. Accordingly, readers should not place undue reliance on forward-looking statements.

SIGNIFICANT ACCOUNTING POLICIES, JUDGMENTS AND ESTIMATES

Please refer to notes 1, 2 and 4 of our consolidated financial statements for the year ended December 31, 2018 for a detailed discussion regarding our significant accounting policies and application of significant accounting judgments, estimates and assumptions. Such changes are reflected in the assumptions when they occur.

Marketable securities

The Company has interests in several publicly-traded marketable security investments. The Company does not own greater than fifty percent of the outstanding shares of these investments nor does it hold options or have other contractual arrangements that would lead to increased ownership. De facto control exists in circumstances when an entity owns less than 50% of the voting shares in another entity, but has control for reasons other than potential voting rights, contract or other statutory means. The Company does not consider de facto control to be present in any of the marketable security investments and does not consolidate these investments.

Venture capital organization

The Company has elected to use the exemption in IAS 28 for venture capital organizations. The Company considered the characteristics of a venture capital organization in deciding to use the exemption. The Company holds its investments in the short to medium-term; the points of exit are actively monitored; and the investments are managed without distinguishing between investments that qualify as associates and those that do not. As such, the Company has concluded that it meets the definition of a venture capital organization and qualifies for the exemption.

Pension benefits and asset ceiling

The cost of defined benefit pension plans and the present value of the pension obligation are determined using actuarial valuations. An actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of the discount rate, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and its long term nature, a defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date. In determining the appropriate discount rate, management considers the interest rates of corporate bonds in the respective currency with at least AA rating, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation. The underlying bonds are further reviewed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, on the basis that they do not represent high quality bonds. The mortality rate is based on publicly available mortality tables. Future salary increases and pension increases are based on expected future inflation rates. Further details about the assumptions used are disclosed in note 6 of the consolidated financial statements for the year ended December 31, 2018. Management is also required to make certain assumptions regarding the quantification of the asset ceiling, which impacts the accrued pension benefit recorded on the consolidated statement of financial position.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to taxable income and expense already recorded. The Company establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences of interpretation may arise on a wide variety of issues depending on the conditions prevailing in the respective company's domicile. As the Company assesses the probability for litigation and subsequent cash outflow with respect to taxes as remote, no contingent liability has been recognized.

STANDARDS ISSUED BUT NOT YET EFFECTIVE

The standard issued but not yet effective up to the date of issuance of the Company's consolidated financial statements is listed below. This is a standard and interpretation issued, which the Company reasonably expects to be applicable at a future date. The Company intends to adopt this standard when it becomes effective.

IFRS 16 Leases

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Applying that model, a lessee is required to recognize: 1) assets and liabilities for all leases with a term of more than twelve months, unless the underlying asset is of low value and 2) depreciation of lease assets separately from interest on lease liabilities on the statements of earnings. The standard is effective for annual periods beginning on or after January 1, 2019. The Company has assessed this new standard and has concluded that there will be no leases with a term of more than twelve months on the effective date. Therefore, there will be no impact to the consolidated financial statements when adopted. The Company will continue to monitor all leases to ensure proper recognition for those that meet the criteria in future periods.

Clarke Inc.

December 31, 2018 and 2017



Independent auditor's report

To the Shareholders of Clarke Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Clarke Inc. and its subsidiaries (together, the Company) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at December 31, 2018 and 2017;
- the consolidated statements of earnings for the years then ended;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of cash flows for the years then ended;
- the consolidated statements of shareholders' equity for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis (MD&A).

PricewaterhouseCoopers LLP
Cogswell Tower, 2000 Barrington Street, Suite 1101, Halifax, Nova Scotia, Canada B3J 3K1
T: +1 902 491 7400, F: +1 902 422 1166

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from



error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Maxime Lessard.

(Signed) "PricewaterhouseCoopers LLP"

Chartered Professional Accountants, Licensed Public Accountants

Halifax, Nova Scotia
February 13, 2019

Clarke Inc.**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION***(in thousands of Canadian dollars)*

As at December 31

2018
\$2017
\$

	2018	2017
	\$	\$
ASSETS		
Current		
Cash and cash equivalents	7,002	20,773
Marketable securities <i>(note 5)</i>	120,174	119,419
Receivables	750	670
Income taxes receivable	55	5,710
Prepaid expenses	104	99
Total current assets	128,085	146,671
Accrued pension benefit asset <i>(note 6)</i>	34,666	10,270
Fixed assets and investment properties <i>(note 7)</i>	944	444
Long-term investments <i>(note 8)</i>	—	1,843
Deferred income tax assets <i>(note 9)</i>	381	1,420
Total assets	164,076	160,648
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	723	1,440
Income taxes payable	22	127
Current portion of long-term debt <i>(note 11)</i>	1,000	645
Total current liabilities	1,745	2,212
Long-term debt <i>(note 11)</i>	2,444	430
Deferred income tax liabilities <i>(note 9)</i>	9,894	1,618
Total liabilities	14,083	4,260
Commitments <i>(note 12)</i>		
Shareholders' equity		
Share capital <i>(note 10)</i>	39,826	47,330
Retained earnings	70,994	89,010
Accumulated other comprehensive income	37,628	18,503
Share-based payments <i>(note 13)</i>	1,545	1,545
Total shareholders' equity	149,993	156,388
Total liabilities and shareholders' equity	164,076	160,648

See accompanying notes to the consolidated financial statements

On behalf of the Board:

/s/ George Armoyan
*Director**/s/ Blair Cook*
Director

Clarke Inc.**CONSOLIDATED STATEMENTS OF EARNINGS***(in thousands of Canadian dollars, except per share amounts)*

Years ended December 31	2018	2017
	\$	\$
Revenue		
Unrealized gains (losses) on investments	(9,210)	30,380
Realized gains (losses) on investments	4,057	(27,182)
Dividend income	3,735	3,573
Interest income	173	774
Provision of services	7,395	6,749
Other income (loss) (note 14)	768	(1,075)
	6,918	13,219
Expenses		
Cost of services provided	4,228	3,923
General and administrative expenses	1,814	2,529
Pension expense	468	400
Share-based payment expense (note 13)	—	298
Depreciation (note 7)	331	232
Interest expense	129	52
	6,970	7,434
Income (loss) before income taxes	(52)	5,785
Provision for income taxes (note 9)	512	2,279
Net income (loss)	(564)	3,506
Basic earnings (loss) per share:		
<i>(in dollars) (note 10)</i>	(0.04)	0.24
Diluted earnings (loss) per share:		
<i>(in dollars) (note 10)</i>	(0.04)	0.24

See accompanying notes to the consolidated financial statements

Clarke Inc.**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME***(in thousands of Canadian dollars)*

Years ended December 31

2018

2017

\$**\$**

Net income (loss)**(564)**3,506

Other comprehensive income**Items that will not be reclassified to profit or loss**Remeasurement gains and effect of changes to asset ceiling on defined benefit pension plans, net
of income tax expense of \$7,609 (2017 – \$1,319) *(note 6)***19,125**12,361

Other comprehensive income**19,125**12,361

Comprehensive income**18,561**15,867

See accompanying notes to the consolidated financial statements

Clarke Inc.**CONSOLIDATED STATEMENTS OF CASH FLOWS***(in thousands of Canadian dollars)*

Years ended December 31	2018	2017
	\$	\$
OPERATING ACTIVITIES		
Net income (loss)	(564)	3,506
Adjustments for items not involving cash <i>(note 15)</i>	6,877	(3,529)
	6,313	(23)
Net change in non-cash working capital balances <i>(note 15)</i>	5,644	4,800
Net cash provided by operating activities	11,957	4,777
INVESTING ACTIVITIES		
Proceeds on disposition of marketable securities	4,139	17,828
Purchase of marketable securities	(9,446)	(230)
Proceeds on disposition of fixed assets	1	2
Purchase of fixed assets <i>(note 7)</i>	(832)	(190)
Distribution of pension plan surplus, net of tax <i>(note 6)</i>	1,216	23,411
Proceeds on disposition of long-term investments <i>(note 8)</i>	1,717	—
Return of capital (net of purchases) of long-term investments	64	1,125
Net cash provided by (used in) investing activities	(3,141)	41,946
FINANCING ACTIVITIES		
Repurchase of shares for cancellation <i>(note 10)</i>	(24,956)	(2,738)
Proceeds from long-term debt <i>(note 11)</i>	3,069	—
Repayment of long-term debt <i>(note 11)</i>	(700)	(644)
Dividends paid <i>(note 10)</i>	—	(29,338)
Net cash used in financing activities	(22,587)	(32,720)
Net change in cash during the year	(13,771)	14,003
Cash and cash equivalents, beginning of year	20,773	6,770
Cash and cash equivalents, end of year	7,002	20,773

See accompanying notes to the consolidated financial statements

Clarke Inc.**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY***(in thousands of Canadian dollars)*

Years ended December 31	2018	2017
	\$	\$
Share capital		
Common shares:		
Balance at beginning of year	47,330	48,121
Common shares repurchased for cancellation <i>(note 10)</i>	(7,504)	(791)
Balance at end of year	39,826	47,330
Retained earnings		
Balance at beginning of year	89,010	116,789
Net income (loss)	(564)	3,506
Dividends declared <i>(note 10)</i>	—	(29,338)
Purchase price in excess of the book value of common shares repurchased for cancellation <i>(note 10)</i>	(17,452)	(1,947)
Balance at end of year	70,994	89,010
Accumulated other comprehensive income		
Balance at beginning of year	18,503	6,142
Other comprehensive income	19,125	12,361
Balance at end of year	37,628	18,503
Share-based payments		
Balance at beginning of year	1,545	1,247
Share-based payment expense <i>(note 13)</i>	—	298
Balance at end of year	1,545	1,545
Total shareholders' equity	149,993	156,388

See accompanying notes to the consolidated financial statements

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of operations

Clarke Inc. (the “Company”) was incorporated on December 9, 1997 pursuant to the Canada Business Corporations Act. The head office of the Company is located at 145 Hobsons Lake Drive, Halifax, Nova Scotia. The Company is an investment holding company with investments in a diversified group of businesses, operating primarily in Canada. The Company continuously evaluates the acquisition, retention and disposition of its investments. Changes in the mix of investments should be expected. These consolidated financial statements were approved by the Board of Directors on February 13, 2019.

Basis of presentation and statement of compliance

These consolidated financial statements of the Company and its subsidiaries were prepared in accordance with International Financial Reporting Standards (“IFRS”). These consolidated financial statements were prepared on a going concern basis under the historical cost convention, as modified by the revaluation of any financial instruments recorded at fair value.

The preparation of financial statements in accordance with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgement in applying the Company’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 3.

Principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. The significant subsidiaries of the Company are CKI Holdings Partnership, Quinpool Holdings Partnership, 8590435 Canada Inc. and La Traverse Rivière-du-Loup – St-Siméon Limitée. All intercompany transactions have been eliminated on consolidation. All subsidiaries have the same reporting year end as the Company, and all follow the same accounting policies.

Cash and cash equivalents

Cash and cash equivalents include deposits in banks, certificates of deposit and short-term investments with original maturities of three months or less.

Marketable securities, investments in associates and long-term investments

The Company has elected to use the exemption in *IAS 28 – Investments in associates* (“IAS 28”) for venture capital companies. Under this exemption, the Company may designate all investments managed in the same way at fair value through profit or loss. The Company has designated all publicly-traded securities at fair value through profit or loss, regardless of whether or not significant influence exists. In these cases, all realized and unrealized gains and losses are recorded in the consolidated statements of earnings.

Transaction costs

Transaction costs related to investments are expensed as incurred. Transaction costs for all other financial instruments are capitalized and for instruments with maturity dates are then amortized over the expected life of the instrument using the effective interest method.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Revenue recognition

Distributions from investments that are treated as a return of capital for income tax purposes reduce the average cost of the underlying investment. Dividend income is recorded on the ex-dividend date. Interest income is recorded using the effective interest rate method ("EIR") for all financial instruments measured at amortized cost.

Services revenue from the Company's ferry business is recognized upon provision of those services and customer acceptance of those services, as there are no further performance obligations to be satisfied at that point.

Foreign currency translation

The Company's consolidated financial statements are presented in Canadian dollars, which is also the functional currency of the parent company.

Transactions in foreign currencies are initially recorded at their respective functional currency rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date. There were no non-monetary assets or liabilities denominated in foreign currencies as at December 31, 2018. All foreign exchange gains and losses are recorded in other income as incurred.

Taxes

Current income tax

Current income tax assets and liabilities for the periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute these amounts are those that are enacted or substantively enacted, at the reporting date in the countries where the Company operates and generates taxable income.

Current income tax relating to items recognized directly in shareholders' equity is recognized in shareholders' equity and not in the consolidated statements of earnings. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred income tax

Deferred income tax is provided using the liability method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax liabilities are recognized for all taxable temporary differences, except in respect of taxable temporary differences associated with investments in subsidiaries where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized, except:

- Where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

- In respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred income tax asset to be recovered. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the reporting date.

Deferred income tax relating to items recognized outside profit or loss is recognized outside profit or loss. Deferred income tax items are recognized in correlation to the underlying transaction either in accumulated other comprehensive income or directly in shareholders' equity.

Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current income tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Sales tax

Revenues, expenses and assets are recognized net of the amount of sales tax, except:

- Where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable.
- Receivables and payables are stated with the amount of sales tax included. The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the consolidated statements of financial position.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at the inception date, whether fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset, even if that right is not explicitly specified in an arrangement.

Operating lease payments are recognized as an expense in the consolidated statements of earnings on a straight-line basis over the lease term.

Fixed assets and investment properties

Fixed assets and investment properties are stated at cost, net of accumulated depreciation and/or accumulated impairment losses, if any. Such cost includes the cost of replacing part of the fixed asset. When significant parts of a fixed asset are required to be replaced at intervals, the Company recognizes such parts as individual assets with specific useful lives and depreciation, respectively. All other repair and maintenance costs are recognized in the consolidated statements of earnings as incurred. Depreciation is calculated over the estimated useful lives of the assets as follows:

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Fixed assets and investment properties	Years	Method
Computer hardware	2 to 5, 30%	Straight-line/declining balance
Furniture and equipment	8, 20%	Straight-line/declining balance
Ferry and vessel dry dock costs	3 to 5	Straight-line

A fixed asset and any significant part of a fixed asset initially recognized is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statements of earnings when the asset is derecognized. The assets' residual values, useful lives and methods of depreciation are reviewed at each financial year end and adjusted prospectively, if appropriate.

Financial instruments — initial recognition and subsequent measurement

i) Financial assets

Initial recognition and measurement

Financial assets within the scope of IFRS 9 are classified as financial assets at amortized cost; fair value through profit or loss; or fair value through other comprehensive income, as appropriate. The Company determines the classification of its financial assets at initial recognition, based on trade date. All financial assets are recognized initially at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Company's financial assets include cash and cash equivalents, marketable securities, receivables and long-term investments.

Subsequent measurement

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are carried in the consolidated statements of financial position at fair value with changes in fair value recognized in the consolidated statements of earnings.

Impairment of financial assets

The Company assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtor is experiencing significant financial difficulty and where observable data indicate that there is a measurable decrease in the estimated future cash flows.

Financial assets carried at amortized cost

For financial assets carried at amortized cost, the Company applies the simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. Trade receivables are written off when there is no reasonable expectation of recovery.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the consolidated statements of earnings. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in the consolidated statements of earnings. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Company. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to interest expense in the consolidated statements of earnings.

ii) Financial liabilities

Initial recognition and measurement

Financial liabilities within the scope of IFRS 9 are classified as financial liabilities at fair value through profit or loss, or at amortized cost. The Company determines the classification of its financial liabilities at initial recognition. All financial liabilities are recognized initially at fair value and in the case of other financial liabilities, plus directly attributable transaction costs. The Company's financial liabilities include accounts payable and accrued liabilities, and long-term debt.

Subsequent measurement

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortized cost using the EIR method. Gains and losses are recognized in the consolidated statements of earnings when the liabilities are derecognized as well as through the EIR method amortization process. The EIR amortization is included in interest expense in the consolidated statements of earnings.

Derecognition and modification

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the consolidated statements of earnings.

iii) Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statements of financial position if there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

iv) Fair value of financial instruments

The fair value of financial instruments that are traded in active markets at each reporting date is determined by reference to quoted market last bid price, without any deduction for transaction costs. For financial instruments not traded in an active market, the fair value is determined using appropriate valuation techniques. Such techniques may include using recent arm's length market transactions; reference to the current fair value of another instrument that is substantially the same; a discounted cash flow analysis or other valuation models. An analysis of fair values of financial instruments and further details as to how they are measured are provided in note 18.

Operating segments

The Company has one reporting segment, the Investment segment, which includes investments in a diversified group of businesses, operating primarily in Canada.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statements of earnings net of any reimbursement.

Per share information

Basic earnings per share is calculated based on net income using the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated based on the weighted average number of common shares that would have been outstanding during the year, including adjustments for stock options outstanding using the treasury stock method. Under the treasury stock method: (i) the exercise of options is assumed to be at the beginning of the year, or at the time of issuance, if later; (ii) the proceeds from the exercise of options are assumed to be used to repurchase common shares at the average market price during the year, and (iii) the incremental number of shares are included in the denominator of the diluted earnings per share calculation. Exercise of these options is not assumed to occur for the purposes of computing diluted earnings per share if the effect would be anti-dilutive.

Impairment of non-financial assets

The Company assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset's recoverable amount. The recoverable amount is the higher of an asset's or cash-generating unit's ("CGU") fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks of the asset. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly-traded subsidiaries or other available fair value indicators. Impairment losses are recognized in the consolidated statements of earnings.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimates the asset's or CGU's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such a reversal is recognized in the consolidated statements of earnings.

Pensions and other post-employment benefits

The Company has two defined benefit pension plans covering full-time employees who commenced employment before September 2003. One plan is federally regulated by OSFI and the second plan is provincially regulated by Retraite Quebec. For other employees, the Company has a RRSP and defined contribution matching pension plan. The cost of providing benefits under the defined benefit plans is determined separately for each plan using the projected unit credit method. Remeasurement gains and losses and the effect of the limit on the asset ceiling of the defined benefit plans are included in other comprehensive income. The past service costs, current service costs, net interest on surplus and non-investment management fees are recognized as an expense in the consolidated statements of earnings. The defined benefit asset comprises the fair value of plan assets less the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds, as explained in note 3). Plan assets are not available to the creditors of the Company, nor can they be paid directly to the Company. Fair value is based on market price information and in the case of quoted securities it is the published bid price. The value of any defined benefit asset recognized is restricted to the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

2. ADOPTION OF NEW STANDARDS

The following standards became applicable January 1, 2018 and the Company changed its accounting policies as a result of adopting the standards. No retrospective adjustments were necessary as a result of the new standards.

IFRS 9 *Financial Instruments*

IFRS 9 replaced *IAS 39 Financial instruments: recognition and measurement*. The standard is effective for annual periods beginning on or after January 1, 2018. IFRS 9 includes requirements for recognition and measurement, impairment, derecognition and general hedge accounting. The Company has assessed this new standard and there has been no impact to the consolidated financial statements from this adoption.

Financial assets within the scope of IFRS 9 are classified in the following measurement categories: amortized cost, fair value through profit or loss, or fair value through other comprehensive income. Financial liabilities are classified in the following measurement categories: fair value through profit or loss, or amortized cost.

The following table summarizes the changes in the classification of the Company's financial instruments upon adoption of IFRS 9. The adoption of the new classification did not result in any changes in the measurement or carrying amount of the financial instruments.

Clarke Inc.

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(in thousands of Canadian dollars, except per share amounts)

2. ADOPTION OF NEW STANDARDS (CONT'D)

Financial instruments	Classification under IAS 39	Classification under IFRS 9
Cash and cash equivalents	Loans and receivables	Amortized cost
Receivables	Loans and receivables	Amortized cost
Marketable securities	Fair value through profit or loss	Fair value through profit or loss
Long-term investments	Fair value through profit or loss	Fair value through profit or loss
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Long-term debt	Other liabilities	Amortized cost

For trade receivables, the Company applies the simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. Trade receivables are written off when there is no reasonable expectation of recovery.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 replaced the previous guidance on revenue recognition and provides a framework for the recognition, measurement and disclosure of revenue contracts with customers. The standard is effective for annual periods beginning on or after January 1, 2018, and is applied retrospectively. The standard applies only to the Company's 'Provision of services' revenue classification on the consolidated statements of earnings. The Company had no contracts with customers entered into but not yet completed at January 1, 2017 or December 31, 2017. There has been no impact to the consolidated financial statements from this adoption and no changes in the revenue recognition policy described in note 1.

3. STANDARDS ISSUED BUT NOT YET EFFECTIVE

The standard issued but not yet effective up to the date of issuance of the Company's consolidated financial statements is listed below. This is a standard and interpretation issued, which the Company reasonably expects to be applicable at a future date. The Company intends to adopt this standard when it becomes effective.

IFRS 16 Leases

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Applying that model, a lessee is required to recognize: 1) assets and liabilities for all leases with a term of more than twelve months, unless the underlying asset is of low value and 2) depreciation of lease assets separately from interest on lease liabilities on the statements of earnings. The standard is effective for annual periods beginning on or after January 1, 2019. The Company has assessed this new standard and has concluded that there will be no leases with a term of more than twelve months on the effective date. Therefore, there will be no impact to the consolidated financial statements when adopted. The Company will continue to monitor all leases to ensure proper recognition for those that meet the criteria in future periods.

4. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the Company's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these judgements, estimates and assumptions could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

4. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (CONT'D)

Judgements

In the process of applying the Company's accounting policies, management has made the following judgements, which have the most significant effect on the amounts recognized in the consolidated financial statements:

Marketable securities

The Company has interests in several publicly-traded marketable security investments. The Company does not own greater than fifty percent of the outstanding shares of these investments nor does it hold options or have other contractual arrangements that would lead to increased ownership. De facto control exists in circumstances when an entity owns less than 50% of the voting shares in another entity, but has control for reasons other than potential voting rights, contract or other statutory means. The Company does not consider de facto control to be present in any of the marketable security investments and does not consolidate these investments.

Venture capital organization

The Company has elected to use the exemption in IAS 28 for venture capital organizations. The Company considered the characteristics of a venture capital organization in deciding to use the exemption. The Company holds its investments in the short to medium-term; the points of exit are actively monitored; and the investments are managed without distinguishing between investments that qualify as associates and those that do not. As such, the Company has concluded that it meets the definition of a venture capital organization and qualifies for the exemption.

Estimates and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Company based its estimates and assumptions on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments however, may change due to market changes or circumstances arising beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

Pension benefits and asset ceiling

The cost of defined benefit pension plans and the present value of the pension obligation are determined using actuarial valuations. An actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of the discount rate, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and its long term nature, a defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date. In determining the appropriate discount rate, management considers the interest rates of corporate bonds in the respective currency with at least AA rating, with extrapolated maturities corresponding to the expected duration of the defined benefit obligation. The underlying bonds are further reviewed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, on the basis that they do not represent high quality bonds. The mortality rate is based on publicly available mortality tables. Future salary increases and pension increases are based on expected future inflation rates. Further details about the assumptions used are disclosed in note 6. Management is also required to make certain assumptions regarding the quantification of the asset ceiling, which impacts the accrued pension benefit recorded on the consolidated statement of financial position.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

4. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (CONT'D)

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to taxable income and expense already recorded. The Company establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences of interpretation may arise on a wide variety of issues depending on the conditions prevailing in the respective company's domicile. As the Company assesses the probability for litigation and subsequent cash outflow with respect to taxes as remote, no contingent liability has been recognized.

5. MARKETABLE SECURITIES

The Company's marketable securities include publicly traded equities measured at fair value through profit or loss. Included in the Company's marketable securities balance is Holloway Lodging Corporation ("Holloway") and TerraVest Industries Inc. ("Terravest") which are investments in associates designated at fair value through profit or loss (note 19). Both investments are Canadian publicly traded companies.

6. EMPLOYEE FUTURE BENEFITS

The Company has two defined benefit pension plans providing pensions for staff who commenced employment prior to September 1, 2003. For all other staff, the Company provides RRSP and defined contribution matching pension plans.

The Company measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 for each year. The most recent actuarial valuation of one defined benefit pension plan for funding purposes was as of December 31, 2017 and for the second defined benefit pension plan was as of December 31, 2015.

The Company amended the surplus policy of one of its pension plans during the year. As a result, there is no longer a cumulative asset ceiling impact, and the Company has recognized its entire surplus on the consolidated statements of financial position. The effect of the change is included in other comprehensive income for the year.

The Company received a pre-tax distribution in 2018 from one of its pension plans in the amount of \$1,870 (2017 – \$3,858) in accordance with the surplus withdrawal rules of the Quebec Supplemental Pension Plans Act.

During the prior year, the Company received approval from the Nova Scotia Pension Regulation Division to terminate and wind-up the Clarke Group Pension Plan, which was a third plan administered by the Company. Following a settlement of that plan's liabilities, the Company received a pre-tax distribution of surplus in the amount of \$29,586.

Total cash payments

Total cash payments for employee future benefits for the year ended December 31, 2018, consisting of cash contributed by the Company to its RRSP and defined contribution matching pension plans were \$100 (2017 – \$96).

Clarke Inc.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2018 and 2017

*(in thousands of Canadian dollars, except per share amounts)***6. EMPLOYEE FUTURE BENEFITS (CONT'D)****Defined benefit plan assets**

	2018	2017
	\$	\$
Fair value of plan assets		
Balance, beginning of year	83,831	111,426
Interest income	2,738	3,725
Employee contributions	2	2
Benefits paid	(2,876)	(3,227)
Non-investment management fees	(344)	(477)
Remeasurement gains	1,007	5,826
Surplus distribution	(1,870)	(33,444)
Balance, end of year	82,488	83,831

Defined benefit plan obligations

	2018	2017
	\$	\$
Accrued benefit obligation		
Balance, beginning of year	51,656	49,943
Current service cost	637	608
Interest cost	1,729	1,861
Employee contributions	2	2
Benefits paid	(2,876)	(3,227)
Remeasurement losses (gains)	(3,326)	2,469
Balance, end of year	47,822	51,656

Reconciliations of the funded status of the benefit plans to the amounts recorded on the consolidated statements of financial position are:

	2018	2017
	\$	\$
Fair value of plan assets	82,488	83,831
Accrued benefit obligation	(47,822)	(51,656)
Funded status of plans – surplus	34,666	32,175
Cumulative impact of asset ceiling	—	(21,905)
Accrued pension benefit asset, net of impact of asset ceiling	34,666	10,270

Elements of the defined benefit expense recognized in the consolidated statements of earnings are as follows:

For the years ended December 31	2018	2017
	\$	\$
Current service cost	637	608
Net interest on surplus	(513)	(685)
Provision for non-investment management fees	344	477
Defined benefit expense recognized	468	400

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

6. EMPLOYEE FUTURE BENEFITS (CONT'D)

Elements of the defined benefit recovery recognized in other comprehensive income are as follows:

For the years ended December 31	2018	2017
	\$	\$
Net remeasurement gains	4,333	3,357
Change in amount of asset ceiling	22,401	10,323
Deferred income tax expense	(7,609)	(1,319)
Defined benefit recovery recognized	19,125	12,361

Significant assumptions

	2018	2017
	%	%
Accrued benefit obligation:		
Discount rate	3.90	3.40
Rate of compensation increase*	2.50 – 4.00	2.50 – 4.00
Benefit costs for the year:		
Discount rate	3.40	3.80
Rate of compensation increase *	2.50 – 4.00	2.50 – 4.00

* The rate of compensation increase is only applicable to the two remaining active members of the Pension Plan.

7. FIXED ASSETS AND INVESTMENT PROPERTIES

	Furniture, equipment and computer hardware	Ferry and vessel dry dock costs	Investment properties – land	Total
	\$	\$	\$	\$
Cost				
January 1, 2017	391	3,660	167	4,218
Additions	16	174	—	190
Disposals	(261)	—	—	(261)
December 31, 2017	146	3,834	167	4,147
Additions	5	827	—	832
Disposals	(1)	—	—	(1)
December 31, 2018	150	4,661	167	4,978
Accumulated depreciation and impairment				
January 1, 2017	369	3,363	—	3,732
Depreciation	14	218	—	232
Disposals	(261)	—	—	(261)
December 31, 2017	122	3,581	—	3,703
Depreciation	14	317	—	331
December 31, 2018	136	3,898	—	4,034
Carrying value – 2017	24	253	167	444
Carrying value – 2018	14	763	167	944

Clarke Inc.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2018 and 2017

*(in thousands of Canadian dollars, except per share amounts)***7. FIXED ASSETS AND INVESTMENT PROPERTIES (CONT'D)**

During the year ended December 31, 2018, the Company incurred costs of \$827 to complete a dry dock for a vessel owned by a subsidiary. The Company capitalizes dry dock costs and amortizes them on a straight-line basis over the period until the next scheduled dry dock which is expected to be in the first quarter of 2021.

The Company's investment properties represent land previously used in operations that are now held for future resale. Depreciation for the year ended December 31, 2018 was \$331 (2017 – \$232). At December 31, 2018, there were no assets under finance leases.

8. LONG-TERM INVESTMENTS

During the year, the Company exited an investment in a private equity fund for proceeds of \$1,717. The net loss on sale for the year was \$57.

9. INCOME TAXES

The provision for income taxes for the years ended December 31 consists of:

	2018	2017
	\$	\$
Consolidated statements of earnings		
Current income tax		
Current income tax charge	(1,523)	4,501
Adjustments in respect of current income tax of previous year	329	—
Deferred income tax		
Relating to origination and reversal of temporary differences	800	(1,641)
Relating to the change in recoverable amount of a deferred income tax asset	906	(581)
Provision for income taxes	512	2,279

The provision for income taxes varies from the expected provision at statutory rates for the following reasons:

	2018	2017
	\$	\$
Provision for (recovery of) income taxes at statutory rate of 28.56% (2017 – 28.80%)	(15)	1,666
Increase (decrease) from statutory rate:		
Effect of difference in statutory rates of subsidiaries	(17)	(39)
Non-taxable component of realized and unrealized investment losses (gains)	541	(353)
Non-taxable dividend income	(968)	(1,032)
Non-deductible expenses	2	87
Change in recoverable amount of deferred income tax asset	906	(581)
Amounts related to gains in defined benefit pension plans	—	2,626
Other	63	(95)
Provision for income taxes at effective rate	512	2,279

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

9. INCOME TAXES (CONT'D)

The significant components of the Company's deferred income tax assets and liabilities are as follows:

Year ended December 31, 2018	Deferred income tax asset (liability) beginning of year	Recognized directly in shareholders' equity	Recognized directly in earnings	Deferred income tax asset (liability) end of year
	\$	\$	\$	\$
Intangible assets	(260)	—	200	(60)
Marketable securities	1,949	—	(1,936)	13
Fixed assets	682	—	(294)	388
Long-term investments	(34)	—	44	10
Employee future benefits	(2,958)	(7,609)	667	(9,900)
Loss carry forwards	423	—	(387)	36
	(198)	(7,609)	(1,706)	(9,513)
Deferred income tax assets	1,420	—	(1,039)	381
Deferred income tax liabilities	(1,618)	(7,609)	(667)	(9,894)
	(198)	(7,609)	(1,706)	(9,513)

Year ended December 31, 2017	Deferred income tax asset (liability) beginning of year	Recognized directly in shareholders' equity	Recognized directly in earnings	Deferred income tax asset (liability) end of year
	\$	\$	\$	\$
Intangible assets	(195)	—	(65)	(260)
Marketable securities	19	—	1,930	1,949
Fixed assets	765	—	(83)	682
Long-term investments	(59)	—	25	(34)
Employee future benefits	(8,995)	(1,319)	7,356	(2,958)
Loss carry forwards	7,364	—	(6,941)	423
	(1,101)	(1,319)	2,222	(198)
Deferred income tax assets	1,069	—	351	1,420
Deferred income tax liabilities	(2,170)	(1,319)	1,871	(1,618)
	(1,101)	(1,319)	2,222	(198)

The ultimate realization of deferred income tax assets is dependent upon taxable profits during the periods in which those temporary differences become deductible. In concluding that it is probable that the recorded deferred income tax assets will be realized, management has relied upon existing taxable temporary differences as support for the recorded amounts.

At December 31, 2018, there was no deferred income tax liability recognized for taxable temporary differences related to undistributed profits of certain of the Company's subsidiaries as the Company is able to control and determine, whether to, and the method for distributing those profits and has determined that those taxable temporary differences will not reverse in the foreseeable future. The taxable temporary differences associated with investments in subsidiaries for which a deferred income tax liability has not been recognized aggregate to \$163,316 (2017 – \$159,813).

As at December 31, 2018, the Company had non-capital losses carried forward for tax purposes of \$121 (2017 – nil) and capital losses carried forward for tax purposes of nil (2017 – \$2,939).

Clarke Inc.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2018 and 2017

*(in thousands of Canadian dollars, except per share amounts)***9. INCOME TAXES (CONT'D)**

Certain deferred income tax assets have not been recognized. They are as follows:

	2018	2017
	\$	\$
Marketable securities	1,445	790
Capital loss carry forwards	135	135
Total	1,580	925

10. SHARE CAPITAL AND EARNINGS PER SHARE

As at and for the year ended December 31	2018		2017	
	# of shares	\$	# of shares	\$
Authorized				
Unlimited number of common shares – no par value				
Unlimited number of First Preferred shares				
Unlimited number of Second Preferred shares				
Issued				
Outstanding common shares, beginning of year	14,600,967	47,330	14,844,867	48,121
Common shares repurchased for cancellation	(2,315,079)	(7,504)	(243,900)	(791)
Outstanding common shares, end of year	12,285,888	39,826	14,600,967	47,330

Earnings per share

The following table reconciles the basic and diluted per share computations from continuing operations:

	2018			2017		
	Loss \$	Weighted average shares (in thousands) #	Per share amount \$	Earnings \$	Weighted average shares (in thousands) #	Per share amount \$
Basic earnings (loss) per share	(564)	12,630	(0.04)	3,506	14,755	0.24
Common shares issued on assumed exercising of stock options		65		—	61	
Diluted earnings (loss) per share	(564)	12,695	(0.04)	3,506	14,816	0.24

All potentially dilutive securities issued relate to stock options for the years ended December 31, 2018 and 2017. The stock options were dilutive for the years ended December 31, 2018 and 2017.

Substantial issuer bid (“SIB”)

During the year, the Company purchased for cancellation 1,851,579 common shares under a SIB at a cost of \$19,442. The purchase price in excess of the historical book value of the shares in the amount of \$13,440 has been charged to retained earnings and \$6,002 has been charged to share capital.

Clarke Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018 and 2017

(in thousands of Canadian dollars, except per share amounts)

10. SHARE CAPITAL AND EARNINGS PER SHARE (CONT'D)

Normal course issuer bid ("NCIB")

In the year ended December 31, 2018, the Company purchased for cancellation 463,500 (2017 – 243,900) common shares under a NCIB at a cost of \$5,514 (2017 – \$2,738). The purchase price in excess of the historical book value of the shares in the amount of \$4,012 (2017 – \$1,947) has been charged to retained earnings and \$1,502 (2017 – \$791) has been charged to share capital.

11. LONG-TERM DEBT

	2018	2017
	\$	\$
Term loan, original amount of \$4,800, payable in monthly principal instalments of \$72 excluding February through April, due September 2019, bearing interest at financial institution's floating base rate minus 1.50% (3.80% as at December 31, 2017).	—	1,075
Term loan, original amount of \$4,000, payable in monthly principal instalments of \$111 excluding February through April, due July 2022, bearing interest at financial institution's floating base rate minus 1.00% (5.05% as at December 31, 2018), secured by fixed charge against ferry, <i>MV Trans-Saint-Laurent</i> , machinery, tools, vehicles, and intellectual property, with a carrying value of \$773.	3,444	—
Less: current portion of long-term debt	(1,000)	(645)
	2,444	430

During the year, the Company refinanced the term loan in one of its subsidiaries and received additional proceeds of \$3,069 for a total new loan obligation of \$4,000. The existing debt was replaced by another from the same lender on substantially different terms, and treated as a derecognition of the original liability and the recognition of a new liability.

The aggregate maturities of long-term debt for each of the next four twelve month periods are as follows: 2019 – \$1,000; 2020 – \$1,000; 2021 – \$1,000; and 2022 – \$444.

12. COMMITMENTS

The Company has lease commitments related to properties in 2019 for \$97. The Company provides indemnification agreements to certain employees acting on behalf of the Company including while serving on various boards of directors of the Company's investments.

13. SHARE-BASED PAYMENTS

The Company has reserved 7.50% of its issued and outstanding common shares under a stock option plan for directors, officers and certain employees. As at December 31, 2018, there were 250,000 options outstanding and exercisable. The grant date was August 18, 2014 with an original exercise price of \$12.19 per share. The current exercise price is \$8.19 per share as a result of two modifications in 2017. The options are fully vested and expire on August 7, 2021. There were no options exercised, cancelled or forfeited during the year ended December 31, 2018. The share-based payment expense included in the consolidated statements of earnings for the year ended December 31, 2018 was nil (2017 – \$298).

Clarke Inc.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2018 and 2017

*(in thousands of Canadian dollars, except per share amounts)***13. SHARE-BASED PAYMENTS (CONT'D)**

The following table shows the assumptions used to determine the original share-based payments expense and the prior year modifications, using the Black-Scholes option pricing model:

	Original issuance	First Modification	Second Modification
Fair value per option granted	\$3.40	\$2.70	\$3.48
Assumptions:			
Risk-free interest rate	1.68%	1.34%	1.70%
Expected dividend yield	3.65%	—	—
Expected volatility	46.78%	29.13%	28.52%
Expected time until exercise	7.0 years	4.5 years	4.0 years
Expected forfeiture rate	9.50%	9.50%	9.50%

14. OTHER INCOME (LOSS)

Other income (loss) is comprised of the following:

	2018	2017
	\$	\$
Foreign exchange gains (losses)	768	(1,077)
Gains on disposition of fixed assets	—	2
Other income (loss)	768	(1,075)

The foreign exchange gains and losses for the years ended December 31, 2018 and 2017 are primarily the result of unrealized foreign exchange gains and losses on foreign investments.

15. SUPPLEMENTAL CASH FLOW INFORMATION

	2018	2017
	\$	\$
Income taxes paid	832	50
Interest received	178	980
Interest paid	114	52
	2018	2017
Adjustments for items not involving cash	\$	\$
Realized/unrealized gains on investments	5,153	(3,198)
Deferred income tax recovery (<i>note 9</i>)	1,706	(2,222)
Unrealized foreign exchange losses (gains)	(781)	963
Pension expense (<i>note 6</i>)	468	400
Depreciation (<i>note 7</i>)	331	232
Share-based payment expense (<i>note 13</i>)	—	298
Gains on disposition of fixed assets (<i>note 14</i>)	—	(2)
	6,877	(3,529)

Clarke Inc.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2018 and 2017

*(in thousands of Canadian dollars, except per share amounts)***15. SUPPLEMENTAL CASH FLOW INFORMATION (CONT'D)**

	2018	2017
	\$	\$
Net changes in non-cash working capital balances		
Receivables	(80)	338
Income taxes receivable	6,309	3,321
Prepaid expenses	(5)	(8)
Accounts payable and accrued liabilities	(475)	(135)
Income taxes payable	(105)	1,284
	5,644	4,800

All dividends received, interest and taxes are classified as cash flows from operating activities.

16. RELATED PARTY DISCLOSURES

The Company had the following related party transactions in the normal course of operations and measured at fair value:

- (i) The Company was a party to rental agreements and tax services agreements with companies owned or partially owned by the Executive Chairman and his immediate family member. One rental agreement ended during 2018 and another rental agreement began in 2018. Included in 'Expenses' is rental and tax services expenses of \$99 (2017 – \$107) under the agreements.
- (ii) The Company provides administrative and asset management services to two pension plans it sponsors. Included in 'Revenue' is \$470 (2017 – \$404) for services provided to the pension plans during the year.
- (iii) During the prior year, the Company provided consulting and tax services for Holloway and Terravest which are investments in associates of the Company. Included in 'Revenue' is \$160 for the services provided in 2017.
- (iv) During the prior year, the Company sold marketable securities through the facilities of the Toronto Stock Exchange to the Master Trust. The sale was made for investment purposes and the Company received net proceeds of \$5,894.

Key management consists of the directors and officers of the Company. The compensation accrued is as follows:

Year ended December 31, 2018	Board of directors	Officers	Total
	\$	\$	\$
Salary and fees	80	339	419
Bonus	—	75	75
Pension value	1,137	7	1,144
Total	1,217	421	1,638

17. CAPITAL DISCLOSURES

The Company's capital consists of shareholders' equity and long-term debt. To maintain or adjust its capital structure, the Company may, from time to time, issue new shares, issue new debt, repurchase existing debt or shares and/or adjust the amount of dividends paid to shareholders. There were no significant changes in the Company's capital management approach from the prior year.

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17. CAPITAL DISCLOSURES (CONT'D)

The Company has a demand revolving loan of \$20,000 secured by marketable securities. The interest rate for the demand revolving loan was 4.70% at December 31, 2018 (2017 – 3.95%). The Company had drawn nil on the demand revolving loan at December 31, 2018 and 2017. The short-term loan facility is subject to restrictive covenants and security arrangements. The restrictive covenants are governed by a minimum current ratio (1.20:1.00) and maximum adjusted tangible net worth ratio (1.25:1.00). For the year ended December 31, 2018, all of the restrictive covenants were met for the Company's primary short-term facilities. The Company has unrestricted access to its credit facilities subject to pledging sufficient securities as collateral. Due to an internal reorganization of these securities that ended subsequent to December 31, 2017, the Company's access to the facility at December 31, 2017 was nil. The reorganization was completed during the first quarter of 2018, and the Company regained access to the \$20,000 limit. Any decline in the fair value of securities within the portfolio may limit the Company's access to the full amount of the short-term facilities.

The Company also maintains several investment accounts with various brokers. Under one broker arrangement, the Company has access to an investment margin account for purposes of financing eligible marketable securities. Any Canadian dollar financing used under this arrangement bears interest at the prime rate of a Canadian chartered bank and is collateralized by the marketable securities purchased. The interest rate was equal to 3.95% at December 31, 2018 (2017 – 3.20%). Any US dollar financing used under this arrangement bears interest at the US base rate less 1.00% and is collateralized by the marketable securities purchased. The interest rate was equal to 5.50% at December 31, 2018 (2017 – 4.50%). The Company had drawn nil on the Canadian dollar and US dollar facilities, respectively, at December 31, 2018 and 2017.

18. FINANCIAL INSTRUMENTS

The Company's financial instruments at December 31, 2018 and 2017 included cash and cash equivalents, marketable securities, receivables, long-term investments, accounts payable and accrued liabilities and long-term debt.

The Company's financial instruments are classified as follows:

Loans and receivables	Fair value through profit or loss	Other liabilities
Cash and cash equivalents	Marketable securities	Accounts payable and accrued liabilities
Receivables	Long-term investments	Long-term debt

The carrying value of cash and cash equivalents, receivables and accounts payable and accrued liabilities approximates their fair value due to the short-term maturity of these instruments. The difference between the carrying values and the fair values of the Company's long-term debt is not material given that the instrument is subject to a floating rate of interest that adjusts with changes to the bank rates

Marketable securities are recorded at fair value based on quoted market prices at December 31, 2018 and 2017. Securities designated as "fair value through profit or loss" are included in the consolidated statements of financial position at fair value, with any movement being recorded as an unrealized gain or loss on investments in the consolidated statements of earnings. The carrying value of long-term investments, for which there is no quoted market value and which are not publicly traded on a recognized securities exchange, are determined using the net asset value per unit as provided by the individual funds.

The Company uses the following hierarchy in attempting to maximize the use of observable inputs and minimize the use of unobservable inputs, primarily using market prices in active markets:

Level 1 – Quoted prices in active markets for identical assets or liabilities. An active market for an asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing on an ongoing basis.

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*(in thousands of Canadian dollars, except per share amounts)***18. FINANCIAL INSTRUMENTS (CONT'D)**

Level 2 – Observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable that can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following details the fair value hierarchy classification for financial instruments carried at fair value on the consolidated statements of financial position:

Fair Value at December 31, 2018				
Description	Total	Level 1 Quoted prices in active markets for identical assets	Level 2 Significant other observable inputs	Level 3 Significant unobservable inputs
Marketable securities	120,174	120,174	—	—

Fair Value at December 31, 2017				
Description	Total	Level 1 Quoted prices in active markets for identical assets	Level 2 Significant other observable inputs	Level 3 Significant unobservable inputs
Marketable securities	119,419	119,419	—	—
Long-term investments	1,843	—	1,843	—
	121,262	119,419	1,843	—

Risks associated with financial assets and liabilities

The Company is exposed to various financial risks arising from its financial assets and liabilities. These include market risk relating to equity prices, interest rates and foreign exchange rates, liquidity risk and credit risk. To manage these risks, the Company performs detailed risk assessment procedures at the individual investment level, under the framework of a global risk management philosophy.

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. For the Company, market risk is comprised of equity price risk, interest rate risk and foreign exchange risk.

Equity price risk

Equity price risk refers to the risk that the fair value of marketable securities and long-term investments will vary as a result of changes in market prices of the investments. The carrying values of investments subject to equity price risk are, in almost all instances, based on quoted market prices as of the consolidated statements of financial position dates. Market prices are subject to fluctuation and, consequently, the amount realized in the subsequent sale of an investment may significantly differ from the reported market value. Fluctuations in the market price of a security may have no relation to the intrinsic value of the security. Furthermore, amounts realized in the sale of a particular security may be affected by the quantity of the security being sold.

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*(in thousands of Canadian dollars, except per share amounts)***18. FINANCIAL INSTRUMENTS (CONT'D)**

The table below shows the impact to the Company on consolidated net income of a 10% increase or decrease in market prices on securities carried at market value in the consolidated statements of financial position of the Company. The selected change does not reflect what could be considered the best or worst case scenarios.

Fair value	Price change	Estimated fair value after price change	After-tax impact on net income
\$	%	\$	\$
120,174	10% increase	132,191	10,301
120,174	10% decrease	108,157	(10,301)

The Company manages its equity price risk by purchasing and holding securities of companies that it believes trade at a discount to their intrinsic values.

Interest rate risk

Interest rate risk refers to the risk that interest expense on floating rate debt will vary as a result of changes in underlying interest rates. At December 31, 2018, the after-tax net income effect of a 1% change in interest rates would have been \$25 on floating rate debt of \$3,444.

Foreign exchange risk

Foreign exchange risk refers to the risk that values of financial assets and liabilities denominated in foreign currencies in the consolidated statements of financial position of the Company will vary as a result of changes in underlying foreign exchange rates.

The Company has investments throughout North America, and as such is exposed to movements in the US/Canadian exchange rate. At December 31, 2018, the effect of a 20% change in the US/Canadian exchange rate on after-tax consolidated net income would have been \$831 based on a US net asset balance of US\$4,264.

The Company manages its exposure to foreign exchange risk by entering into foreign exchange contracts. At December 31, 2018 and 2017, the Company did not have any forward contracts outstanding to sell US dollars.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting its financial obligations. The Company believes it has access to sufficient capital through cash on hand, operating cash flows and existing borrowing facilities to meet these obligations. At December 31, 2018, the Company had cash of \$7,002 and available unused facilities totalling \$20,000. The following table shows the timing of expected payments of current liabilities and long-term debt:

	Due within 1 year	1 to 3 years	3 to 5 years	After 5 years
	\$	\$	\$	\$
Accounts payable and accrued liabilities	723	—	—	—
Long-term debt	1,000	2,000	444	—
	1,723	2,000	444	—

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18. FINANCIAL INSTRUMENTS (CONT'D)

Credit risk

Credit risk refers to the risk that a counterparty will fail to fulfill its obligations under a contract and, as a result, will cause the Company to suffer a loss. This risk is mitigated through credit policies that limit transactions according to counterparties' credit quality. The Company assesses the credit quality of all counterparties, taking into account their financial position, past experience and other factors. The Company believes there are no significant concentrations of credit risk due to the low level of trade receivables, cash balances and available facilities. The maximum exposure to credit risk associated with financial assets is the total carrying value of those receivables. There were no expected credit loss allowances as at December 31, 2018 and no receivables were written off during the year.

19. SUBSEQUENT EVENTS

On January 24, 2019, Holloway completed a SIB by repurchasing 1,553,755 of its common shares. As a result, the Company acquired control of Holloway and owned approximately 51% of the common shares on that date. The Company will begin consolidating Holloway's results beginning in the first quarter of 2019.

CLARKE

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