



What
matters
most

COMPANY PROFILE

We are the largest provider of property and casualty (P&C) insurance in Canada and a leading provider of specialty insurance in North America, with close to \$10 billion in total annual premiums¹. We have over 13,000 full- and part-time employees who serve more than five million personal, business, public sector and institutional clients through offices in Canada and the U.S. In Canada, Intact distributes insurance under the Intact Insurance brand through a wide network of brokers, including its wholly-owned subsidiary BrokerLink, and directly to consumers through belairdirect. In the U.S., OneBeacon Insurance Group, a wholly-owned subsidiary, provides specialty insurance products through independent agencies, brokers, wholesalers and managing general agencies.

Financial highlights

(in millions of Canadian dollars, except as noted)

	2017	2016	2015	2014	2013
Consolidated performance					
Direct premiums written	8,747	8,293	7,922	7,461	7,345
Net earned premiums	8,530	7,946	7,535	7,207	7,014
Underwriting income	486	375	628	519	142
Net investment income	432	414	424	427	406
Net distribution income	132	111	104	75	75
Net operating income	771	660	860	767	500
Non-operating gains (losses)	(31)	(152)	(216)	10	(95)
Net income	792	541	706	782	431
Combined ratio	94.3%	95.3%	91.7%	92.8%	98.0%
Net operating income per share (\$)	5.60	4.88	6.38	5.67	3.62
Earnings per share (\$)	5.75	3.97	5.20	5.79	3.10
Book value per share (\$)	48.00	42.72	39.83	37.75	33.94
Operating return on equity	12.9%	12.0%	16.6%	16.3%	11.2%
Return on equity	12.8%	9.6%	13.4%	16.1%	9.3%
Adjusted return on equity	13.0%	11.0%	14.3%	16.8%	10.3%

See the full story online: intactfc.com/2017annualreport

Please visit our online annual report to view videos, interactive features and additional information on what matters most to us.



¹ DPW (pro-forma) for 2017 comprises the DPW of P&C Canada and the DPW (pro-forma) of P&C U.S., using an exchange rate of 1.30

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Certain statements made in this annual report are forward-looking statements. These statements include, without limitation, statements relating to the company's new products and services, its revenue projections, its use of technology, its funding of projects, its position within the industry and market conditions. All such forward-looking statements are made pursuant to the "safe harbour" provisions of applicable Canadian securities laws.

Forward-looking statements, by their very nature, are subject to inherent risks and uncertainties and are based on several assumptions, both general and specific, which give rise to the possibility that actual results or events could differ materially from our expectations expressed in or implied by such forward-looking statements as a result of various factors, including those discussed in the Company's most recently filed Annual Information Form and annual MD&A. As a result, we cannot guarantee that any forward-looking statement will materialize and we caution you against unduly relying on any of these forward-looking statements. Except as may be required by Canadian securities laws, we do not undertake any obligation to update or revise any forward-looking statements contained in this annual report, whether as a result of new information, future events or otherwise. Please read the cautionary note at the beginning of the annual MD&A.

WHAT MATTERS MOST

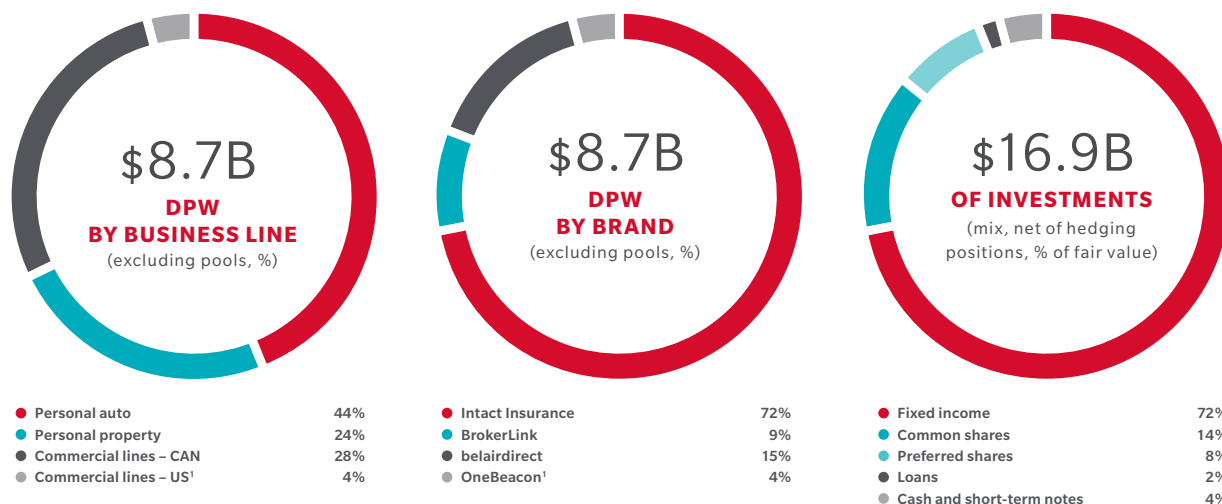
At Intact, our purpose is to help people, businesses and society prosper in good times and be resilient in bad times. **We believe insurance is not about things. Insurance is about people.**



FINANCIAL HIGHLIGHTS

Our superior operating performance and financial strength have translated into 12% compound annual growth in dividends per share, and 13% compound annual total return since our IPO in 2004.

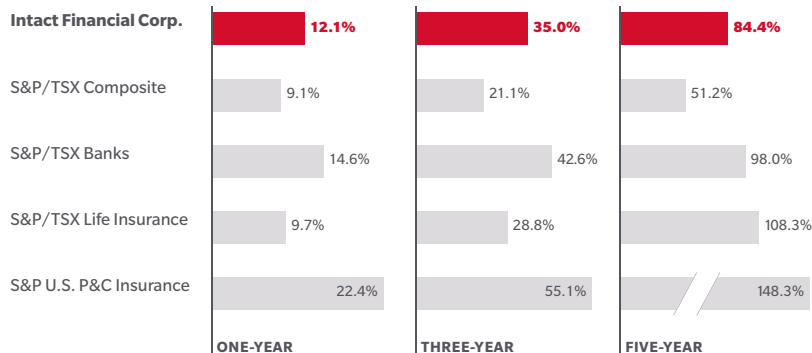
Direct premiums written (DPW) and investment mix



Total shareholder return

On a total shareholder return basis (including dividends), our 13% CAGR over the past five years compares favourably versus our peers.

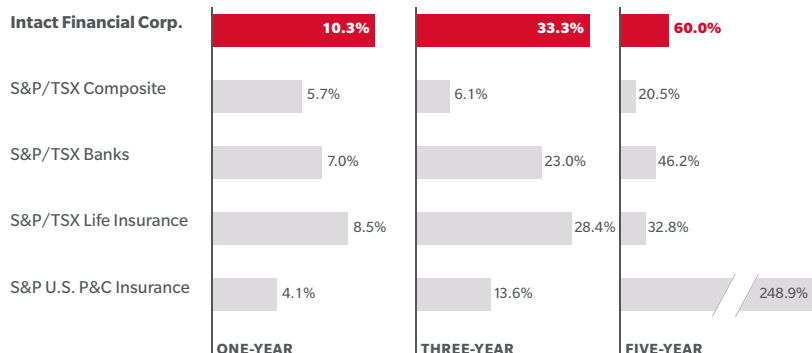
13% CAGR



Dividends per share growth

We are proud of our dividend growth track record, including a five-year CAGR of 10%, which compares favourably versus our peers.

10% CAGR



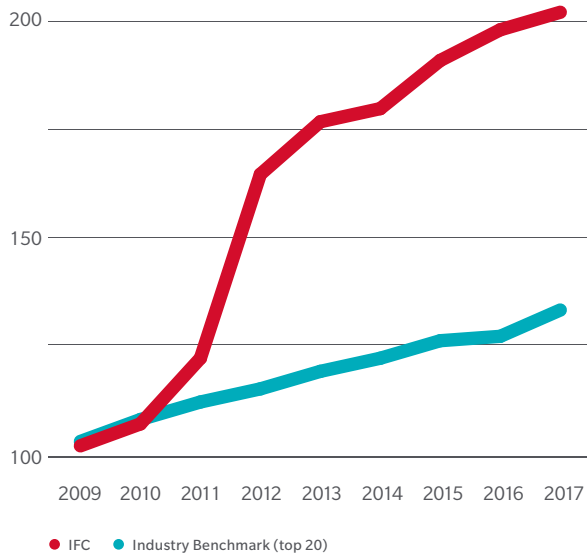
Source: Bloomberg

¹ Includes the DPW of OneBeacon since its acquisition on September 28, 2017

CANADIAN INDUSTRY OUTPERFORMANCE

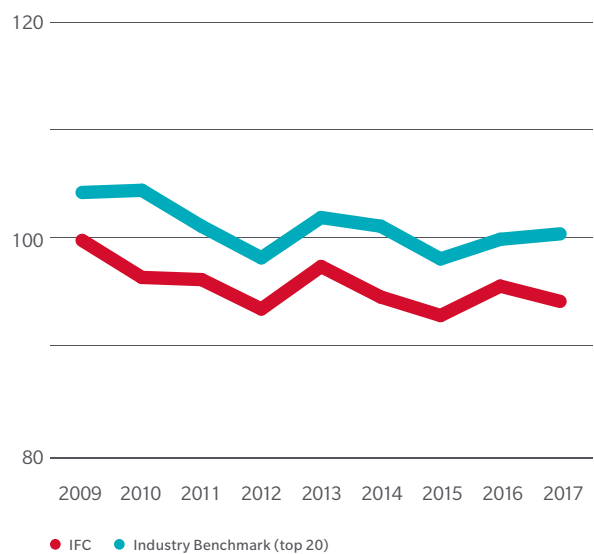
Direct premiums written growth (%) (Base 100 = 2008)

The combination of our organic growth and accretive acquisitions has led to a significant growth outperformance versus the industry.



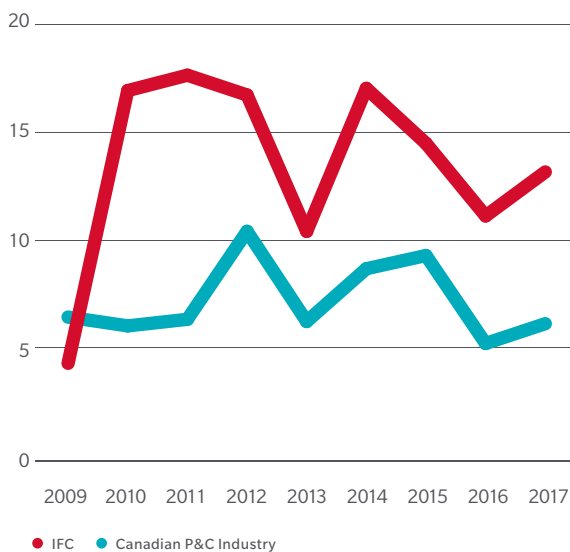
Combined ratio¹ (%)

Our sophisticated pricing, underwriting discipline and in-house claims expertise have enabled us to outperform the industry's combined ratio.



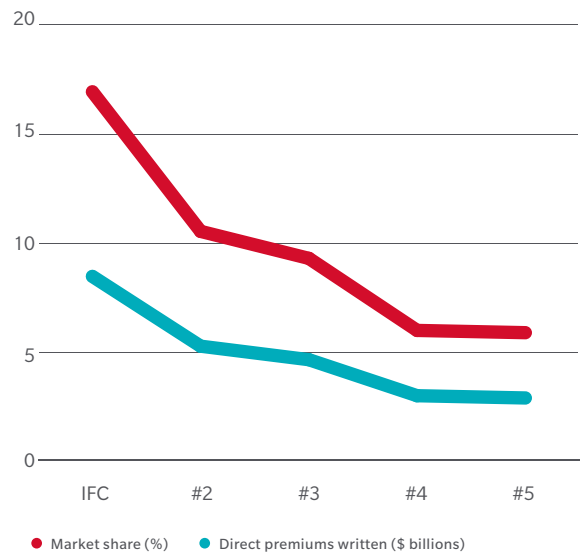
Return on equity² (%)

Our superior underwriting results, investment performance and capital management have led to a better ROE than the industry.



Market share by company

With an estimated market share of 17%, we are approximately 18 times the size of the average company in the industry.



¹ Combined ratio includes the market yield adjustment ("MYA").

² ROEs reflect IFRS beginning in 2010. Since 2011, IFC's ROE is adjusted return on common shareholders' equity ("AROE"), as defined in our glossary.

Industry data: IFC estimate based on MSA Research Inc. data, excluding Lloyd's, ICBC, SGI, SAF, MPI, Genworth, Canada Guarantee and IFC, as at Dec. 31, 2017. The industry benchmark consists of the 20 largest comparable companies in the Canadian P&C industry.



What matters to you matters to us.

We understand if it happens to you, it happens to us. Empathy is everything. That is why one in five Canadians trusts us to protect what matters most to them.



Being customer driven

Canada is one of the top five most connected countries in the world. Today, seven out of 10 Canadians have a smartphone. Software and data are transforming the way we live. We are evolving our products and solutions to continue to meet customers' changing needs.

Every day, we challenge ourselves to be better – design faster, simpler and offer more empathetic customer and broker experiences, go beyond their expectations and always deliver an experience that is second to none.

We appreciate that customers' time is valuable. We are leveraging technology to design relevant products and provide options for customers to connect with us. Our digital innovations save customers and brokers time and make it easy for them. In five easy steps, small business owners in Québec can get a quote for their commercial automobiles with Intact Insurance's first-in-Canada online quick quote tool. With our mobile app, customers can access our self-serve portal Client Centre on the go, anywhere, anytime.



Building the best team

We are building a workplace where employees enjoy coming to work every day.

Our promise to our employees is that we won't compromise on our values of integrity and respect because they matter as much as results. We'll support them in their career and growth, surround them with inspiring teams, and offer them a financial rewards program that recognizes their success.

For example, our mobile-friendly and easy-to-navigate career site is a tool that supports employees in growing their careers, allowing them and potential employees to apply for a position quickly using their [®]LinkedIn profile, join the Intact Talent Community to receive job alerts, and share jobs with their social networks. Our monthly employee webcast provides employees the chance to be surrounded with inspiring leaders and teams, through interaction with our Chief Executive Officer and other senior leaders. Employees can post questions via a crowd sourcing platform and vote on the top questions that are most important to them.



Creating a leading specialty insurer in North America

In 2017, we acquired OneBeacon Insurance Group, expanding our footprint into the U.S. We are accelerating our goal of becoming a world-class property and casualty (P&C) insurer, by combining our leading commercial lines track record, deep data, claims and digital expertise with OneBeacon's outstanding team and specialty lines capabilities. Our goal is to generate \$3 billion in annual direct premiums written for specialty lines in North America by 2020.

We are creating opportunities for growth in Canada and diversifying Intact's business and geographical mix. Brokers have begun using our cross-border services to better serve customers with businesses in Canada and the U.S. Our new Canadian cross-border team has expertise writing U.S. risks and can make decisions locally. We have leveraged OneBeacon's expertise and products and introduced solutions for entertainment and technology customers in Canada, offering them targeted coverage that reflects their specific industries and exposures.



Continuing to excel

We know that having a strong track record is not a guarantee of future success. We are building on our strengths to continue to lead in the future. Our goal is to outperform the P&C insurance industry based on return on equity (ROE) by at least 500 basis points each year and grow net operating income per share (NOIPS) 10% yearly over time.

We were honoured to be ranked second of 242 companies in The Globe and Mail's 2017 Board Games report card. Intact's score improved from 98 to 99 out of 100 points.

Through Intact Ventures Inc., we deepen our learning by partnering with and investing in companies with the potential to redefine the P&C insurance industry with innovative business models and new technology. We recently invested in Hangar and Humatics. Our relationship with Hangar will give us greater insights into using drones for assessing claims. Humatics' data will help us price, segment, underwrite and further elevate the customer experience we are known for as micro location sensors become more prevalent in our society.



Making a social impact

We are making a difference in the communities where we live and work. We are working on all fronts – from research and creating standards, to developing product design and exploiting data to tackle the challenges of climate change. In addition to the previously announced \$4.25 million in funding to establish the Intact Centre on Climate Adaptation (Intact Centre), the Intact Foundation is investing another \$1 million in partnerships to protect Canadians from the increasing impacts of climate change.

Our second area of focus is tackling child poverty, a significant issue in our country. We will be funding over \$1.3 million in 25 communities nationally, activating community poverty reduction strategies through our partner, United Way.

We have evolved our employee programs to provide more choices and make it easy for employees to support their communities. For example, our new Skills for Impact program empowers employees to use their skills and knowledge to help charities during regular work hours.

What matters most



At Intact, we believe insurance is not about things. Insurance is about people. That is why we have made it our purpose to help people, businesses and society prosper in good times and be resilient in bad times. It drives everything we do and gives meaning to our work.

In building a leading North American property and casualty (P&C) insurer, our work starts with the customer. Our teams are working hard to provide customers with an experience that is second to none. One where customers know, what matters to them matters to us. We believe this is the best way to have customers as advocates.

Our people know they make a difference and their work matters. To build on that, we aim to be one of Canada's best employers and a destination for top talent. We are creating an environment that people are proud to be a part of and enjoy coming to work every day.

With satisfied customers and engaged employees, we aim to be one of the most respected companies in Canada. By leading in the marketplace with our values, consistently outperforming the industry in terms of profitability and growing our earnings by more than 10% per year over time, we are well on our way. Our success allows us to give back to communities where we operate and help make a difference to society at large.

Year in review

2017 was a pivotal year for Intact. Our entry into the U.S. specialty lines market was a major step forward. The OneBeacon acquisition combines Intact's leading commercial lines track record and deep data, claims and digital expertise with OneBeacon's high calibre team and specialty lines capabilities.

It also bolsters Intact's Canadian business with new products and cross-border capabilities, and better positions us to compete with international insurers. Beyond strong growth prospects in Canada, this transaction creates a significant new

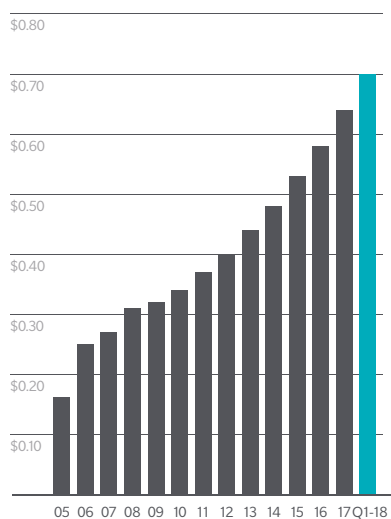
growth pipeline to leverage Intact's consolidation expertise in a fragmented specialty lines market. We are working with our new colleagues in the U.S. and Mike Miller, an exceptional leader, to leverage their expertise and bring the underwriting performance in specialty lines to the low 90s in the next 24 months. We expect the acquisition to contribute to earnings growth within two years.

Our financial performance in 2017 delivered a return on equity (ROE) of 13%. However we are not satisfied with that performance which was tempered by some setbacks in personal automobile. Despite this, we have made excellent progress on many fronts. We have improved customer experience across all our channels, maintained strong employee engagement, opened a massive new pipeline of earnings growth in the U.S. and made meaningful strides in artificial intelligence, technology and claims management.

We delivered a solid combined ratio of 94.3% in 2017, resulting in net operating income of \$771 million while growing our top line by more than 5%. I am pleased with the strong performance and continued momentum in personal property and commercial lines, with combined ratios of 89.1% and 86.5% respectively.

Although our performance in personal auto was challenging and remains unacceptable at a combined ratio of 101.7%, we have made important strides in curbing claims inflation, improving risk selection and increasing rates. With increased cost of repairs in the past year, we are executing on our action plan with discipline and remain committed to bring personal auto's combined ratio back to the mid-90s. We are confident this is a short to mid-term issue and our

Quarterly dividends per share



actions should bring us back to our long-term track record of performance. For seven of the last 10 years, we have operated personal auto in the mid-90s and have averaged a combined ratio in the mid-90s over five and 10 years. We will keep at it until we achieve our goal.

We ended 2017 in a very strong financial position with a total capital margin of over \$1.1 billion and debt-to-total capital at 23%. Our book value per share grew 12% in 2017 to \$48. Coupled with good earnings momentum, we have increased our dividend per share by 9% in 2018, the 13th consecutive annual increase since our IPO. We believe we are well positioned to capture growth opportunities that the market will offer in the coming years.

Being customer driven

Consumers' expectations are changing rapidly. Software and data are transforming the way we interact, gather and share information, and how we live. Ninety per cent of Canadians use the Internet and 50% do so through a mobile device. We have focused on digital transformation for many years. 2017 was no exception.

We'll continue to invest in products, tools and training to make the customer experience simpler, faster and more convenient. Leveraging data, artificial intelligence and technology, our Intact Lab and Data Lab are instrumental in helping us improve and become better at what we do, and enhance the experience we offer customers and brokers.

Our mobile telematics offer is now available across the country. We have transformed how Canadians can buy home insurance online and expanded our services to mobile users. We have also introduced some of these functionalities to commercial lines.

On the distribution front, we are making it easier for customers and brokers to connect with us. Intact Insurance's Buy Online strategy continues to grow and generate new business for brokers.

Within weeks of closing the OneBeacon acquisition, we deployed cross-border capabilities in the U.S. and in Canada. We also introduced a new product suite for technology and entertainment customers in Canada. We are now able to tailor our offer to the specific needs of commercial lines customers.

Committed to outperform

To become one of the most respected companies in Canada, we are committed to outperform our industry every year in terms of profitability. In the last decade, we have outperformed our competitors by 550 basis points (bps) in terms of ROE, above our 500 bps objective. We closed 2017 with an outperformance of 690 bps.

We continue to invest in people, systems and partnerships to expand that advantage. We are deploying new technology platforms in claims, as well as in personal and commercial lines. We are also building on our actuarial and data management capabilities, investing heavily in artificial intelligence and establishing partnerships with leading universities in data science.

We remain focused on integrating the supply chain in claims by insourcing the delivery of customer experience. Our four claims service centres across Canada translate into a better customer experience, greater satisfaction and lower cost.

Our quest for outperformance doesn't stop at the fundamentals of insurance. Our investment management team, considered one of the best in Canada by its peers, manages a wide range of asset classes across North America. Working closely with our insurance, treasury, tax and capital teams, they optimize our asset allocation to match the unique nature of our P&C activities. With \$20 billion of assets under management, they are focused on delivering superior after tax returns. On that front, they have a tremendous track record delivering nearly 160 bps of ROE outperformance since 2010.

In building a leading North American property and casualty (P&C) insurer, our work starts with the customer. Our teams are working hard to provide customers with an experience that is second to none. One where customers know, what matters to them matters to us.



Favourable market conditions ahead

We are entering 2018 in a changing marketplace across our product lines in Canada and the U.S.

2017 was a difficult year for the Canadian industry, with a ROE slightly above 6%, but we are starting to see meaningful corrective actions taking shape and as a result a firmer rate environment.

In personal lines, we expect to see mid-single digit revenue growth in the industry. Claims inflation in personal automobile driven by physical damage and the escalating cost of automobile repairs are putting severe strain on the industry's performance. In home insurance, the industry is still adapting its offer and prices to better reflect the cost of natural disasters.

In Canada, the commercial lines market remains very competitive, but we are starting to see capacity constraints in certain sectors. As a result, pricing continues to firm up. We expect low-to-mid-single digit revenue growth in this segment for the industry.

We are new to the U.S. market but a number of segments in which we operate are showing clear signs of rate momentum. We like the direction it is heading.

We expect the industry's ROE to remain below its long-term performance in 2018 but we are maintaining our 500 bps industry outperformance objective. We are confident that the growth opportunities will be stronger in the coming year. Our people, who have shown great discipline over time, stand ready to take advantage of this environment.

Making a difference

Creating an environment where our people can contribute and make a real difference is important to our success. For the past three years, we have been recognized as one of Canada's Best Employers and a Top 100 Employer. We were also named a Top Employer for Young People for a second time.

We are fortunate to have loyal people and a group of best-in-class leaders that lives our values and leads by example. Today's leaders are strong, engaged and constantly trying to improve every day. Tomorrow's leaders are equally impressive. We have close to five successors ready within three years for the top 120 leaders of the organization. When I see these emerging leaders in action, I am thrilled about our long-term prospect.

We are passionate about helping people. We are empowering Canadians to protect themselves from the impacts of severe weather. The Intact Centre on Climate Adaptation (Intact Centre) is establishing standards and advising governments on building homes to help Canadians adapt to climate change. We are also investing in a number of meaningful employee-focused partnerships including the Roméo Dallaire Child Soldiers Initiative. The work being done by the Intact Senior Fellow LGen Roméo Dallaire and his team is inspiring. They have formed strong partnerships and delivered results. Partnering with the United Nations (UN) and the Government of Canada, they have developed the Vancouver Principles to prioritize the prevention of recruiting and using child soldiers in UN peacekeeping missions.

2018 and beyond

We have started 2018 on a sound strategic footing: a bold customer driven transformation, expanding distribution, massive technology, digital and artificial intelligence deployments coupled with robust measures to improve underwriting fundamentals. Our employees are engaged and excited about building our business and recognize the opportunities. Combined with favourable marketplace conditions, we are in a strong position to expand our leadership and build momentum for years to come. We'll continue to build on our success as a customer driven organization. By leading with our values, improving what we do every day and driving change, we will succeed.

I am very proud to work with such a strong and talented team. I want to thank our 13,000 people for their loyalty, commitment and contributions. Our board of directors, strong and dedicated, has been a key to our success. My team and I are grateful for their contributions.

I am convinced that our engaged employees who are committed to our customer driven mindset will get us to where we want to be – one of Canada's most respected companies.

Thank you for your support.

Charles Brindamour
Chief Executive Officer

Expanding opportunities for growth

Intact's 2017 results were solid. Under the strong leadership of Charles Brindamour and the management team, the Company stayed focused on its strategy and executed its plans with a disciplined approach. Intact's acquisition of OneBeacon Insurance Group and expansion into the U.S. was a milestone in the Company's history and will create new growth opportunities.

The Company has again delivered great value to shareholders and increased its common share dividend for the 13th consecutive year. Through enhanced risk selection, segmentation, leveraging data analytics, machine learning and artificial intelligence, Intact is well poised to continue to outperform. With a comprehensive integration plan for OneBeacon already underway, the Company is on its way to achieve its goal of creating a leading specialty solutions insurer in North America.

The Company has been positioned to succeed in a changing environment. Intact is accelerating its development in digital technology, software engineering and artificial intelligence to design relevant products and provide options for our customers to interact with us.

Succession planning and talent development are important elements that continue to contribute to Intact's success. The Board is confident that the Company's new organizational structure adopted following the OneBeacon transaction will accelerate its customer driven transformation, optimize distribution of services to Canadians across all channels, build on outstanding talent and further enable its North American scope.

Intact's commitment to help people and businesses extends beyond protecting what's important to them. Protecting North Americans from the impacts of extreme weather caused by climate change has increased in urgency in recent years. The frequency of severe weather events in Canada has increased seven times in the past 20 years. Intact's leadership in establishing the Intact Centre on Climate Adaptation at the University of Waterloo to make Canada more resilient to climate change is gaining good momentum. This partnership plays a key role in establishing standards and influencing how homes and communities will be built, and gives homeowners tools to make their homes more flood resilient.

Upholding a high standard of governance, compliance and ethics is integral to delivering on the Company's goal of being one of the most respected companies in Canada. This effort has culminated in Intact attaining top marks for good governance in The Globe and Mail's 2017 Board Games report card. Intact ranked second out of 242 companies. Additionally, Intact was awarded Best Financial Reporting by IR Magazine Awards – Canada.

In 2017, we welcomed Sylvie Paquette to the Board of Directors. Ms. Paquette brings with her vast experience and knowledge of Canada's P&C insurance industry. Her achievements are well recognized. Ms. Paquette was one of Canada's Top 100 Most Powerful Women (2009) and received the "Inspiration – Andrée Corriveau" Award from the Association of Québec Women in Finance (2014). Ms. Paquette's strengths and expertise contribute positively to the Company's strategic objectives and further strengthen the collective expertise of the Board.



To the management team and employees at Intact, on behalf of my colleagues, I thank you for another strong and outstanding year. Your striving for excellence, your dedication to being customer driven and your passion to make a difference continue to differentiate Intact from its competitors in a rapidly changing marketplace. I also want to thank customers, brokers and shareholders for their continued support and trust.

A handwritten signature in black ink, appearing to read 'Claude Dussault', written over a light grey background.

Claude Dussault
Chairman of the Board

MD&A and Financial Statements

Please note that the following MD&A and Financial Statements are provided as distinct sections with individual pagination:

MD&A – pages 1 to 85;

Financial Statements – pages 1 to 69.



Intact Financial Corporation
Management's Discussion and Analysis

For the year ended December 31, 2017

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INTACT FINANCIAL CORPORATION

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

The following MD&A is the responsibility of management and has been reviewed and approved by the Board of Directors (or "Board") for the year ended December 31, 2017. This MD&A is intended to enable the reader to assess our results of operations and financial condition for the three- and twelve-month periods ended December 31, 2017 compared to the corresponding periods in 2016. It should be read in conjunction with our Consolidated financial statements for our fiscal year ended December 31, 2017. This MD&A is dated February 6, 2018.

"Intact", the "Company", "IFC", "we" and "our" are terms used throughout the document to refer to Intact Financial Corporation and its subsidiaries. Further information about Intact Financial Corporation, including the Annual Information Form, may be found online on SEDAR at www.sedar.com.

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Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Non-IFRS financial measures

We use both IFRS and non-IFRS financial measures to assess our performance. Non-IFRS financial measures do not have any standardized meaning prescribed by IFRS and are unlikely to be comparable to any similar measures presented by other companies. *See Section 27 – Non-IFRS financial measures for the definition and reconciliation to the most comparable IFRS measures.* These measures and other insurance-related terms used in this MD&A are defined in the glossary available in the "Investors" section of our web site at www.intactfc.com.

Cautionary note regarding forward-looking statements

Certain of the statements included in this MD&A about the Company's current and future plans, expectations and intentions, results, levels of activity, performance, goals or achievements or any other future events or developments constitute forward-looking statements. The words "may", "will", "would", "should", "could", "expects", "plans", "intends", "trends", "indications", "anticipates", "believes", "estimates", "predicts", "likely", "potential" or the negative or other variations of these words or other similar or comparable words or phrases, are intended to identify forward-looking statements. This MD&A contains forward-looking statements with respect to the acquisition (the "Acquisition") of OneBeacon Insurance Group, Ltd. ("OneBeacon") and the integration and future plans relating to the Acquisition.

Forward-looking statements are based on estimates and assumptions made by management based on management's experience and perception of historical trends, current conditions and expected future developments, as well as other factors that management believes are appropriate in the circumstances. Many factors could cause the Company's actual results, performance or achievements or future events or developments to differ materially from those expressed or implied by the forward-looking statements, including, without limitation, the following factors: the Company's ability to implement its strategy or operate its business as management currently expects; its ability to accurately assess the risks associated with the insurance policies that the Company writes; unfavourable capital market developments or other factors which may affect the Company's investments, floating rate securities and funding obligations under its pension plans; the cyclical nature of the P&C insurance industry; management's ability to accurately predict future claims frequency and severity, including in the Ontario personal auto line of business, as well as the evaluation of losses relating to the Fort McMurray wildfires, catastrophe losses caused by severe weather and other weather-related losses; government regulations designed to protect policyholders and creditors rather than investors; litigation and regulatory actions; periodic negative publicity regarding the insurance industry; intense competition; the Company's reliance on brokers and third parties to sell its products to clients and provide services to the Company; the Company's ability to successfully pursue its acquisition strategy; the Company's ability to execute its business strategy; the Company's ability to achieve synergies arising from successful integration plans relating to acquisitions; economic, financial, business and political conditions, as well as their resulting effect on management's estimates and expectations in relation to accretion, equity IRR, net operating income per share, MCT, combined and debt-to-total capital ratio and the other metrics used in relation to the Acquisition; the terms and conditions of the Acquisition; the Company's participation in the Facility Association (a mandatory pooling arrangement among all industry participants) and similar mandated risk-sharing pools; terrorist attacks and ensuing events; the occurrence and frequency of catastrophe events, including a major earthquake; the Company's ability to maintain its financial strength and issuer credit ratings; the Company's access to debt and equity financing; the Company's ability to compete for large commercial business; the Company's ability to alleviate risk through reinsurance; the Company's ability to successfully manage credit risk (including credit risk related to the financial health of reinsurers); the Company's ability to contain fraud and/or abuse; the Company's reliance on information technology and telecommunications systems and potential failure of or disruption to those systems, including evolving cyber-attack risk; the impact of developments in technology on the Company's products and distribution; the Company's dependence on and ability to retain key employees; changes in laws or regulations; the exercise of the over-allotment option in connection with the Offering; general economic, financial and political conditions; the Company's dependence on the results of operations of its subsidiaries and the ability of the Company's subsidiaries to pay dividends; the volatility of the stock market and other factors affecting the trading prices of the Company's securities; the Company's ability to hedge exposures to fluctuations in foreign exchange rates; future sales of a substantial number of its common shares; changes in applicable tax laws, tax treaties or tax regulations or the interpretation or enforcement thereof.

All of the forward-looking statements included in this MD&A are qualified by these cautionary statements and those made in the section entitled Risk management (Sections 19-24) hereafter. These factors are not intended to represent a complete list of the factors that could affect the Company. These factors should, however, be considered carefully. Although the forward-looking statements are based upon what management believes to be reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward-looking statements. When relying on forward-looking statements to make decisions, investors should ensure the preceding information is carefully considered. Undue reliance should not be placed on forward-looking statements made herein. The Company and management have no intention and undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Glossary of abbreviations

Description		Description	
AEPS	Adjusted EPS	Moody’s	Moody’s Investor Service Inc.
AFS	Available for sale	MYA	Market yield adjustment
AMF	Autorité des marchés financiers	NAIC	National Association of Insurance Commissioners
AOCI	Accumulated OCI	NCIB	Normal course issuer bid
AROE	Adjusted ROE	NEP	Net earned premiums
BVPS	Book value per share	NOI	Net operating income
CAD	Canadian Dollar	NOIPS	NOI per share
CAGR	Compound annual growth rate	OCI	Other comprehensive income
CAN	Canada	OROE	Operating ROE
CAT	Catastrophe	OSFI	Office of the Superintendent of Financial Institutions
DBRS	Dominion Bond Rating Services	P&C	Property & Casualty
DPW	Direct premiums written	PTOI	Pre-tax operating income
EPS	Earnings per share to common shareholders	PYD	Prior year claims development
Fitch	Fitch Ratings Inc.	RBC	Risk-based capital
FVTPL	Fair value through profit and loss	ROE	Return on equity
IFRS	International Financial Reporting Standards	S&P	Standard & Poor’s
KPI	Key performance indicator	U.S.	United States
MCT	Minimum capital test	USD	U.S. Dollar
MD&A	Management’s Discussion and Analysis		

Important notes

- Unless otherwise noted, DPW refer to DPW normalized for the effect of multi-year policies, excluding industry pools, fronting and exited lines (referred to as “DPW” in this MD&A). *See Table 37 for details on exited lines and Table 39 for the reconciliation to DPW, as reported under IFRS.* All underwriting results and related ratios exclude the MYA and the results of our U.S. Commercial exited lines, unless otherwise noted. The expense and general expense ratios are presented herein net of other underwriting revenues.
- DPW (pro forma) for 2017 are comprised of the DPW of P&C Canada and the DPW (pro forma) of P&C U.S.
- Catastrophe claims are any one claim, or group of claims, equal to or greater than \$7.5 million for P&C Canada (US\$5 million for P&C U.S.) related to a single event (referred to as the “CAT threshold”). A non-catastrophe weather event is a group of claims, which is considered significant but that is smaller than the CAT threshold, related to a single weather event. A large loss is defined as a single claim larger than \$0.25 million for P&C Canada (US\$0.25 million for P&C U.S.) but smaller than the CAT threshold.
- Regulatory Capital Ratios refer to MCT (as defined by OSFI and the AMF in Canada) and RBC (as defined by the NAIC in the U.S.). All references to “total capital margin” in this MD&A include the aggregate of capital in excess of company action levels in regulated entities (170% MCT, 200% RBC) plus available cash in unregulated entities (*see Section 18.2 - Capital position for details*).
- Unless otherwise noted, market share and market related data for P&C Canada are based on the latest available data (Q3-2017) from MSA Research Inc. (“MSA”) and excludes Lloyd’s Underwriters Canada, Insurance Corporation of British Columbia, Saskatchewan Government Insurance, Saskatchewan Auto Fund, Genworth Financial Mortgage Insurance Company Canada and Canada Guaranty Mortgage Insurance Company. MSA data excludes certain Québec regulated entities. Market share and market positioning reflect the impact of announced or completed acquisitions and are therefore presented on a *pro forma* basis.
- Unless otherwise noted, market share and market related data for P&C U.S. are based on the latest available data from SNL Insurance.
- Certain totals, subtotals and percentages may not agree due to rounding. Not meaningful (nm) is used to indicate that the current and prior year figures are not comparable, not meaningful, or if the percentage change exceeds 1,000%.

OVERVIEW

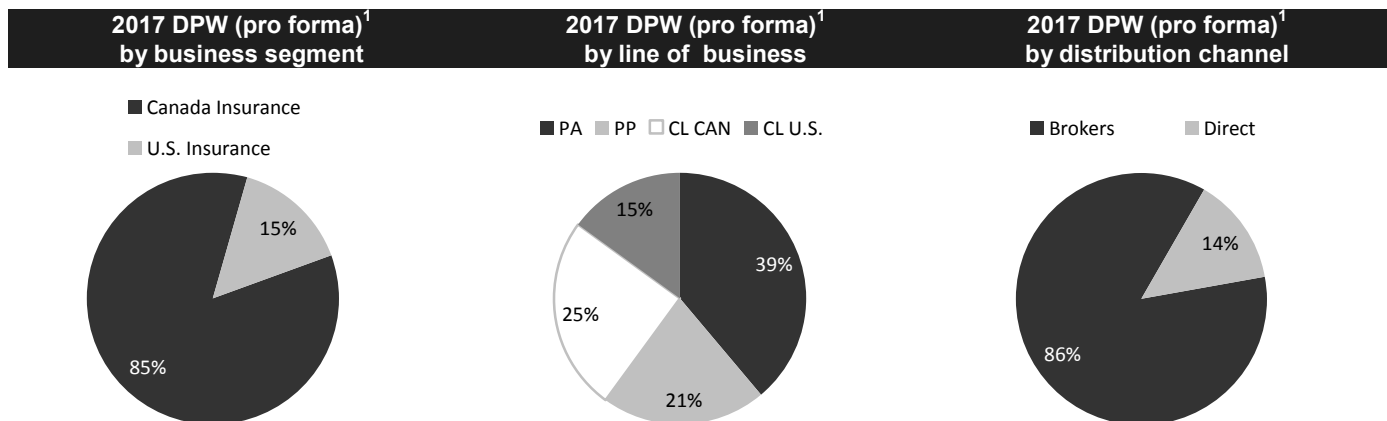
Section 1 – About Intact Financial Corporation

1.1 Building a world-class P&C insurer

- Largest provider of P&C insurance in Canada and a leading provider of specialty insurance in North America, with close to \$10 billion in annual DPW¹.
- Over 13,000 full- and part-time employees who serve more than five million personal, business, public sector and institutional customers through offices in Canada and the U.S.
- In Canada, we distribute insurance under the Intact Insurance brand through a wide network of brokers, including our wholly-owned subsidiary BrokerLink, and directly to consumers through belairdirect. In the U.S., OneBeacon, a wholly-owned subsidiary, provides specialty insurance products through independent agencies, brokers, wholesalers and managing general agencies.
- We are a proven industry consolidator with a track record of 16 successful P&C acquisitions since 1988.

1.2 What we offer

With our comprehensive range of auto, home and business insurance products, we offer customers protection tailored to meet their unique needs. Across Intact, we may have different responsibilities but we share the same goal: We are here to help people, businesses and society prosper in good times and be resilient in bad times. Making a difference is important to us; it is our purpose.



¹ DPW (pro forma) for 2017 are comprised of the DPW of P&C Canada and the DPW (pro forma) of P&C U.S., using an exchange rate of 1.30.
PA: Personal auto; PP: Personal property; CL: Commercial lines

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

1.3 Our business segments

Following the acquisition of OneBeacon on September 28, 2017, we now report our financial results under the following business segments. The composition of our segments is aligned with our management structure and internal financial reporting based on geography and the nature of our activities.

Intact Financial Corporation	
Canada Insurance (CAN)	<p>Comprised of the underwriting (P&C Canada) and distribution activities in Canada</p> <ul style="list-style-type: none"> • Underwriting of automobile, home and business insurance contracts to individual and businesses in Canada. Underwriting results in Canada are reported under three lines of business: <ul style="list-style-type: none"> • Personal auto • Personal property • Commercial, which include Commercial auto and Commercial P&C • Distribution operations, including the operating results of our wholly-owned broker, BrokerLink, as well as our share of results of broker affiliates.
U.S. Insurance (U.S.)	<p>Comprised of the underwriting activities in the U.S. (P&C U.S.)</p> <ul style="list-style-type: none"> • Underwriting of specialty contracts to small and midsize businesses in the U.S., which are reported under: <ul style="list-style-type: none"> • Commercial lines, which include the underwriting results of OneBeacon since September 28, 2017 (see Sections 5 and 10.2).
Corporate and Other (Corporate)	<p>Comprised of the following activities, which are managed at the Corporate level:</p> <ul style="list-style-type: none"> • Investment management • Treasury and capital management • Other corporate activities <p>Operating results include net investment income, finance costs, as well as other income and expenses (including corporate expenses and ancillary income).</p>



We measure our consolidated performance mainly based on NOIPS and business segment performance based on pre-tax operating income (PTOI). Comparative information has been reclassified accordingly.

Table 1 – Operating performance¹

December 31,	CAN	U.S.	Corporate	2017 Total	CAN	U.S.	Corporate	2016 Total
DPW	8,440	307	-	8,747	8,293	-	-	8,293
Operating income								
Underwriting income	478	8	-	486	375	-	-	375
Net investment income	-	-	432	432	-	-	414	414
Finance costs	-	-	(82)	(82)	-	-	(72)	(72)
Net distribution income	132	-	-	132	111	-	-	111
Other income (expense)	-	-	5	5	-	-	10	10
PTOI	610	8	355	973	486	-	352	838
NOI				771				660
NOIPS (in dollars)				5.60				4.88

¹ Refer to Section 27 – Non-IFRS financial measures.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

1.4 What we are aiming to achieve

	Our objectives for 2017	Selected 2017 achievements
<p>Our customers are our advocates</p>	<ul style="list-style-type: none"> • Progress on goal of two million advocates by 2020 	<ul style="list-style-type: none"> • 1.1 million advocates, up 11% from last year. • Maintained #1 and #2 brand consideration nationally for Intact Insurance and belairdirect. • Launched Client Centre, which gives personal lines customers digital access to their policy documents, billing statements and real-time claims status updates. • Launched Canada's first commercial online auto quick quote tool. • Launched a mobile telematics app, allowing good drivers to save on car insurance without having to install any hardware in their vehicles. • Launched our fourth Service Centre in Canada with Intact Service Centre in Montreal, a one-stop shop for customers with auto insurance claims.
<p>Our employees are engaged</p>	<ul style="list-style-type: none"> • Be one of Canada’s best employers 	<ul style="list-style-type: none"> • Recognized as an Aon Best Employer – Canada 2018, Platinum level, for a 3rd year in a row.
<p>Our company is one of the most respected</p>	<ul style="list-style-type: none"> • Exceed Canadian industry ROE by 500 bps • Grow NOIPS 10% yearly over time 	<ul style="list-style-type: none"> • Outperformed the P&C insurance industry’s ROE by 590 bps in the first nine months of 2017. • NOIPS in 2017 was up 15% over 2016 on improved underwriting results and strong distribution performance. • Acquisition of OneBeacon in 2017 is expected to add mid-single digit accretion to NOIPS by the end of 2019.

1.5 Consistent outperformance driven by unique advantages

10-year outperformance vs the industry¹



1. All market share and outperformance data as at December 31, 2016. See Section 11.3 for more information on industry outperformance.

Unique advantages



See Section 11 for discussion on our unique strategic advantages.

Management’s Discussion and Analysis for the year ended December 31, 2017

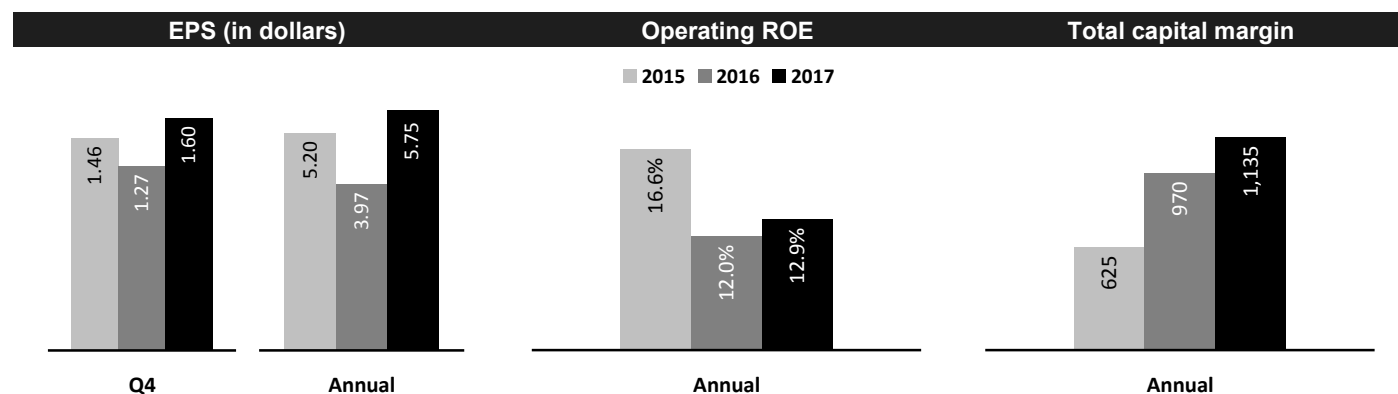
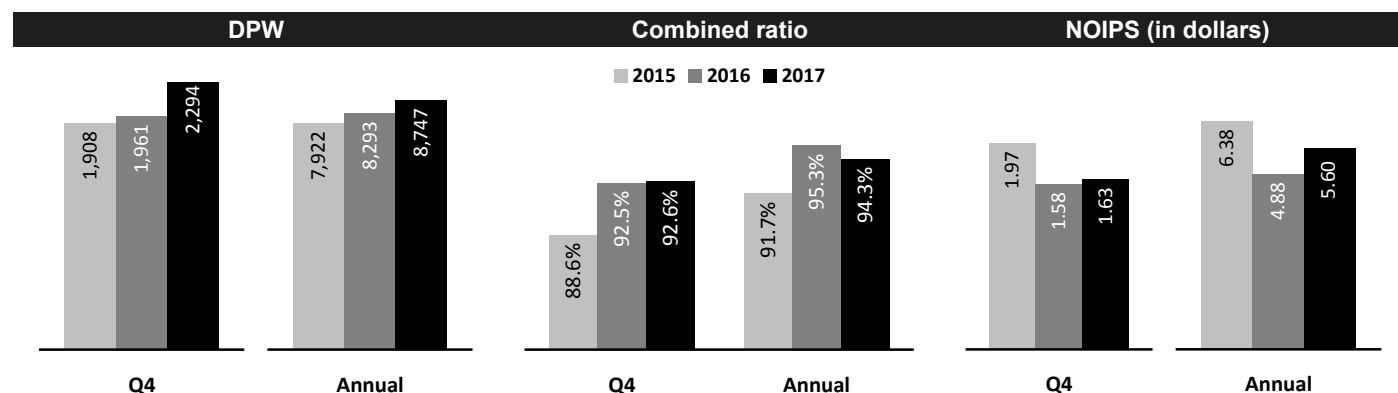
(in millions of Canadian dollars, except as otherwise noted)

Section 2 – Our 2017 performance at a glance

2017 Highlights

DPW growth	NOIPS growth	OROE	Total capital margin	BVPS
+5%	+15%	12.9%	\$1.1 billion	+12%

- Net operating income per share up 3% to \$1.63 in Q4-2017 and up 15% to \$5.60 in the full year
- DPW grew 17% in the quarter, bolstered by OneBeacon
- Combined ratio of 92.6% in the quarter reflected strong performance in Canadian property and commercial operations, and the inclusion of OneBeacon
- Earnings per share up 45% to \$5.75 in 2017, driving book value per share growth of 12%
- Operating ROE of 13%, with over \$1.1 billion in total capital margin
- Quarterly dividend increased 9% to \$0.70 per share



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 3 – Consolidated performance

On September 28, 2017, we completed the acquisition of OneBeacon. Its results of operations and balance sheet are included in our consolidated results and financial position from that date.

Table 2 – Consolidated performance¹

	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW	2,294	1,961	17%	8,747	8,293	5%
NEP	2,400	2,043	17%	8,530	7,946	7%
Operating income						
Underwriting income	178	153	25	486	375	111
Net investment income	121	104	17	432	414	18
Net distribution income	28	24	4	132	111	21
Finance costs	(25)	(18)	(7)	(82)	(72)	(10)
Other income (expense)	2	13	(11)	5	10	(5)
PTOI	304	276	10%	973	838	16%
NOI	236	212	11%	771	660	17%
Non-operating gains (losses)	(58)	(52)	(6)	(31)	(152)	121
Effective income tax rate	5.9%	23.7%	(17.8) pts	15.9%	21.1%	(5.2) pts
Net income	232	171	36%	792	541	46%
Underwriting ratios						
Claims ratio	63.5%	62.9%	0.6 pts	65.4%	64.9%	0.5 pts
Expense ratio	29.1%	29.6%	(0.5) pts	28.9%	30.4%	(1.5) pts
Combined ratio	92.6%	92.5%	0.1 pts	94.3%	95.3%	(1.0) pts
Per share measures, basic and diluted (in dollars)						
NOIPS	1.63	1.58	3%	5.60	4.88	15%
EPS	1.60	1.27	26%	5.75	3.97	45%
AEPS	1.55	1.56	(1)%	5.82	4.53	28%
BVPS	48.00	42.72	12%			
Return on equity for the last 12 months						
OROE	12.9%	12.0%	0.9 pts			
ROE	12.8%	9.6%	3.2 pts			
AROE	13.0%	11.0%	2.0 pts			
Total capital margin	1,135	970	165			
Debt-to-total capital ratio	23.1%	18.6%	4.5 pts			

¹ Refer to Section 27 – Non-IFRS financial measures.

Table 3 – Performance by business segment¹

	Section	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW growth							
Canada Insurance	4.4	1,987	1,961	1%	8,440	8,293	2%
U.S. Insurance	5.3	307	-	nm	307	-	nm
		2,294	1,961	17%	8,747	8,293	5%
Combined ratio							
Canada Insurance	4.4	91.9%	92.5%	(0.6) pts	94.2%	95.3%	(1.1) pts
U.S. Insurance	5.3	97.4%	-	nm	97.4%	-	nm
		92.6%	92.5%	0.1 pts	94.3%	95.3%	(1.0) pts
PTOI							
Canada Insurance	4.4	198	177	12%	610	486	26%
U.S. Insurance	5.3	8	-	nm	8	-	nm
Corporate and Other	6.4	98	99	(1)%	355	352	1%
		304	276	10%	973	838	16%

¹ Refer to Section 27 – Non-IFRS financial measures.

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

	Q4-2017 vs Q4-2016	2017 vs 2016
DPW growth	<ul style="list-style-type: none"> • Our premium base has grown 17% in the quarter and 5% in the full year, mainly from our U.S. acquisition of OneBeacon, which closed on September 28, 2017. • Premium growth in Canada of 1% in the quarter and 2% in the full year was tempered by the impact of robust profitability actions, including rate increases in all lines of business. 	
Underwriting income	<ul style="list-style-type: none"> • Combined ratio in Canada was solid at 91.9%, reflecting strong underlying performance in personal property and commercial lines, rigorous expense management and challenging results in personal auto where profitability actions continue. • Combined ratio in the U.S. (OneBeacon) was 97.4%. In Q4-2017, we exited underperforming lines and began realizing synergies. We are executing on our profitability action plan and are on track to bring the U.S. combined ratio to a low 90s level within 24 to 36 months of closing. 	<ul style="list-style-type: none"> • Combined ratio in Canada improved slightly to 94.2% on lower CAT losses and rigorous expense management.
Net investment income	<ul style="list-style-type: none"> • Net investment income was up \$17 million in the quarter and \$18 million in the full year mainly due to the acquisition of OneBeacon. Excluding the impact of OneBeacon, net investment income was flat compared to 2016 as the low yield environment continued to impact our investment income in 2017. 	
Net distribution income	<ul style="list-style-type: none"> • Strong performance, up 17% in the quarter and 19% in the full year, driven by continued growth and improved profitability of our broker network. 	
PTOI	<ul style="list-style-type: none"> • PTOI of \$304 million was up 10% on improved performance in Canada and the addition of OneBeacon. 	<ul style="list-style-type: none"> • PTOI of \$973 million was up 16%, on improved performance in Canada.
NOIPS	<ul style="list-style-type: none"> • NOI of \$236 million was up 11% on higher results in Canada and the addition of OneBeacon. This translated to a NOIPS of \$1.63 compared to \$1.58 in Q4-2016. 	<ul style="list-style-type: none"> • NOI of \$771 million was up 17% (15% on a per share basis), on lower CAT losses, strong distribution income and rigorous expense management.
OROE	<ul style="list-style-type: none"> • OROE of 13%, reflecting higher earnings and the issuance of common shares in connection with the acquisition of OneBeacon. 	
Effective income tax rate	<ul style="list-style-type: none"> • Effective income tax rate of 5.9% in the quarter and 15.9% in the full year reflected a one-time income tax recovery of \$27 million following the enactment of the U.S. Corporate Tax reform in December 2017. • Excluding this one-time impact, the effective income tax rate was 17.0% in Q4-2017 and 18.8% in 2017. The decrease versus last year was mainly driven by higher non-taxable gains in 2017. 	
Net income	<ul style="list-style-type: none"> • Net income of \$232 million was up 36% on improved operating performance in Canada, the addition of OneBeacon and a one-time positive impact from the U.S. Corporate Tax reform, partly offset by integration costs in connection with the acquisition of OneBeacon. 	<ul style="list-style-type: none"> • Net income of \$792 million was up 46% on improved operating performance in Canada, strong gains, as well as a one-time positive impact from the U.S. Corporate Tax reform.
Financial condition	<ul style="list-style-type: none"> • BVPS increased 12% from a year ago to \$48.00. • Our debt-to-total capital ratio as at December 31, 2017 went down since the closing of OneBeacon, but remained higher than December 31, 2016 driven by the acquisition of OneBeacon. • We ended the year in a strong capital position, with over \$1.1 billion of total capital margin as at December 31, 2017. 	

SEGMENT PERFORMANCE

Section 4 – Canada Insurance

4.1 Canada’s largest home, auto and business insurer

- Largest P&C insurer in Canada, with over \$8 billion in annual DPW and an approximate market share of 17%.
- We distribute insurance in Canada under the Intact Insurance brand through a wide network of brokers, including our wholly-owned subsidiary BrokerLink, and directly to consumers through belairdirect.
- Largest private sector provider of P&C insurance in B.C., Alberta, Ontario, Québec, Nova Scotia and Newfoundland & Labrador.

4.2 We offer a comprehensive range of insurance products

Personal auto

- We offer various levels of coverage to our customers for their vehicles including accident benefits, third party property and physical damage. Our coverage is also available for motor homes, recreational vehicles, motorcycles, snowmobiles, and all terrain vehicles. While the rate approval process and timing varies by province, insurers must file for rate adjustments in Ontario and Alberta before they can be effected.

Personal property

- Our customers can get protection for their homes and contents from risks such as fire, theft, vandalism, water damage and other damages, as well as personal liability coverage. Property coverage is also available for tenants, condominium owners, non-owner occupied residences and seasonal residences.

Commercial lines (including specialty lines)

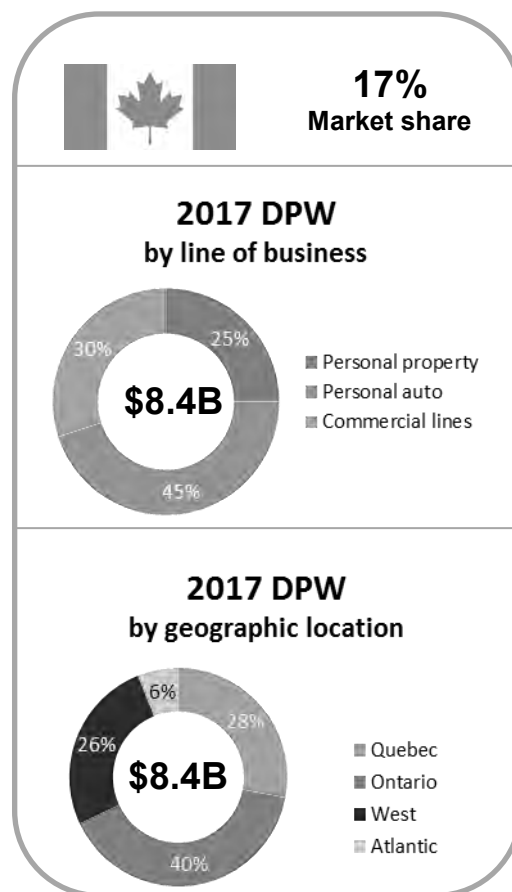
- We provide a broad range of coverages tailored to the needs of a diversified group of small and medium sized businesses including commercial landlords, manufacturers, contractors, wholesalers, retailers, transportation businesses, agriculture businesses and service providers.
- Commercial property coverages protect the physical assets of the business and include business interruption insurance. Liability coverages include commercial general liability, product liability, professional liability as well as cyber endorsement.
- Commercial vehicle coverages provide protection for commercial auto, fleets, garage operations, light trucks, public vehicles and the transportation needs of the sharing economy.

4.3 Operating performance

Strong performance on lower CAT losses, continued growth of our broker network and rigorous expense management.

Table 4 – Operating performance

	Section	Q4-2017	Q4-2016	Change	2017	2016	Change
Canada Insurance							
	P&C Canada	170	153	11%	478	375	27%
	Distribution	28	24	17%	132	111	19%
PTOI		198	177	12%	610	486	26%



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

4.4 P&C Canada

Table 5 – Underwriting results for P&C Canada¹

	Section	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW		1,987	1,961	1%	8,440	8,293	2%
Personal auto	4.5	824	829	(1)%	3,818	3,792	1%
Personal property	4.6	505	486	4%	2,135	2,030	5%
Commercial lines	4.7	658	646	2%	2,487	2,471	1%
NEP		2,074	2,043	2%	8,204	7,946	3%
Current year claims (excluding CAT claims)		1,372	1,313	59	5,321	5,165	156
Current year CAT claims		31	34	(3)	313	385	(72)
Unfavourable (favourable) PYD		(77)	(62)	(15)	(253)	(389)	136
Total net claims		1,326	1,285	41	5,381	5,161	220
Underwriting expenses		578	605	(27)	2,345	2,410	(65)
Underwriting income		170	153	17	478	375	103
Underwriting ratios							
Underlying current year loss ratio		66.2%	64.2%	2.0 pts	64.9%	64.8%	0.1 pts
CAT loss ratio (including reinst. premiums)		1.5%	1.8%	(0.3) pts	3.8%	5.0%	(1.2) pts
Unfavourable (favourable) PYD ratio		(3.7)%	(3.1)%	(0.6) pts	(3.1)%	(4.9)%	1.8 pts
Claims ratio		64.0%	62.9%	1.1 pts	65.6%	64.9%	0.7 pts
Commissions		14.5%	15.6%	(1.1) pts	15.2%	16.3%	(1.1) pts
General expenses		9.7%	10.3%	(0.6) pts	9.7%	10.5%	(0.8) pts
Premium taxes		3.7%	3.7%	- pts	3.7%	3.6%	0.1 pts
Expense ratio		27.9%	29.6%	(1.7) pts	28.6%	30.4%	(1.8) pts
Combined ratio		91.9%	92.5%	(0.6) pts	94.2%	95.3%	(1.1) pts
Personal auto	4.5	101.2%	100.9%	0.3 pts	101.7%	99.9%	1.8 pts
Personal property	4.6	79.7%	75.6%	4.1 pts	89.1%	90.9%	(1.8) pts
Commercial lines	4.7	87.4%	93.2%	(5.8) pts	86.5%	91.5%	(5.0) pts

¹ Refer to Section 27 – Non-IFRS financial measures.

Q4-2017 vs Q4-2016	2017 vs 2016
<ul style="list-style-type: none"> • DPW growth of 1% in the quarter and 2% in the full year reflected solid growth in personal property and specialty lines, tempered by the impact of robust profitability actions, including rate increases in all lines of business. • Underlying current year loss ratio of 66.2% reflected a strong underlying performance in personal property and commercial lines, and challenging results in personal auto where improvement initiatives continue. • CAT losses of \$31 million were in line with last year, while slightly above expectations. • Favourable PYD ratio of 3.7% reflected positive prior year development in all lines of business. • Expense ratio improved in all lines of business from lower variable costs and rigorous expense management. • Combined ratio in Canada was solid at 91.9%, reflecting strong underlying performance in personal property and commercial lines, lower expenses and challenging results in personal auto where profitability actions continue. 	<ul style="list-style-type: none"> • Underlying current year loss ratio remained strong at 64.9% and reflected the benefits of our profitability initiatives, and challenging results in personal auto despite our actions. • CAT losses of \$313 million were above expectations, while lower than last year, which included the impact of the Fort McMurray wildfires and severe weather in Q3-2016. • Favourable PYD ratio declined to 3.1%, in line with long-term averages. • Combined ratio improved to 94.2%, reflecting lower CAT losses and expense management.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

4.5 Personal auto

Table 6 – Underwriting results for personal auto

	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW	824	829	(1)%	3,818	3,792	1%
Written insured risks (in thousands)	917	928	(1)%	4,319	4,358	(1)%
NEP	952	942	1%	3,782	3,704	2%
Underwriting income (loss)	(11)	(9)	nm	(64)	5	nm
Underlying current year loss ratio	81.4%	78.5%	2.9 pts	77.7%	76.5%	1.2 pts
CAT loss ratio (including reinst. premiums)	0.2%	0.4%	(0.2) pts	0.7%	2.0%	(1.3) pts
Unfavourable (favourable) PYD ratio	(2.8)%	(1.4)%	(1.4) pts	0.3%	(3.1)%	3.4 pts
Claims ratio	78.8%	77.5%	1.3 pts	78.7%	75.4%	3.3 pts
Expense ratio	22.4%	23.4%	(1.0) pts	23.0%	24.5%	(1.5) pts
Combined ratio	101.2%	100.9%	0.3 pts	101.7%	99.9%	1.8 pts

Q4-2017 vs Q4-2016

2017 vs 2016

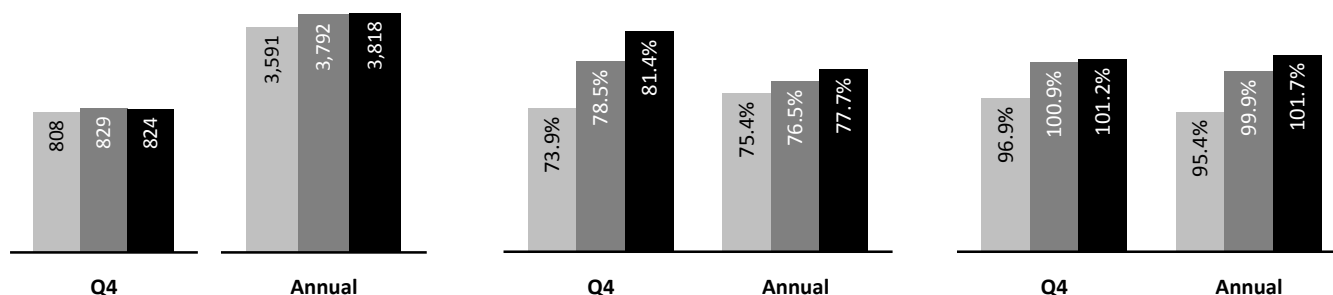
- **DPW growth was negative 1% in the quarter and positive 1% in the full year**, reflecting rate increases taken across the country ahead of our competitors and the impact of segmentation initiatives.
- **Underlying current year loss ratio of 81.4%** was elevated due to physical damage costs and weather-related claims.
- **Favourable PYD ratio of 2.8%** improved compared to recent quarters and was more in line with historical averages.
- **The combined ratio of 101.2% remained higher than expected** due to increasing physical damage costs and weather-related claims. While our actions to date have tempered increasing claims costs, further pricing, claims and segmentation actions are being implemented to address physical damage cost trends. With strengthened claims liabilities and additional profitability actions involving rate, underwriting and claims, we are committed to bring the combined ratio of this line back to the mid 90’s.
- **Underlying current year loss ratio of 77.7%** remained elevated, driven by higher than expected physical damage costs.
- **CAT loss ratio of 0.7%** was lower than last year from severe summer storms across Canada in 2016.
- **PYD ratio deteriorated from last year’s favourable 3.1%** on adverse development on large losses and the impact from the actuarial review performed in Q3-2017.
- **Combined ratio deteriorated to 101.7%** mainly on unfavourable PYD.

DPW

Underlying current year loss ratio

Combined ratio

■ 2015 ■ 2016 ■ 2017



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

4.6 Personal property

Table 7 – Underwriting results for personal property

	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW	505	486	4%	2,135	2,030	5%
Written insured risks (in thousands)	562	562	-%	2,413	2,393	1%
NEP	522	494	6%	2,040	1,880	9%
Underwriting income	106	120	(12)%	222	170	31%
Underlying current year loss ratio	49.3%	39.9%	9.4 pts	49.6%	48.9%	0.7 pts
CAT loss ratio (including reinst. premiums)	1.9%	2.6%	(0.7) pts	10.2%	11.6%	(1.4) pts
Unfavourable (favourable) PYD ratio	(3.2)%	(2.8)%	(0.4) pts	(3.0)%	(4.7)%	1.7 pts
Claims ratio	48.0%	39.7%	8.3 pts	56.8%	55.8%	1.0 pts
Expense ratio	31.7%	35.9%	(4.2) pts	32.3%	35.1%	(2.8) pts
Combined ratio	79.7%	75.6%	4.1 pts	89.1%	90.9%	(1.8) pts

Q4-2017 vs Q4-2016

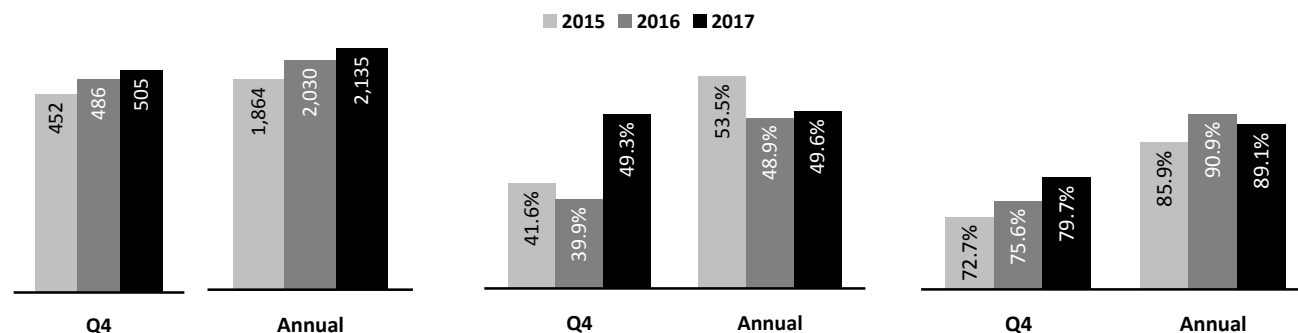
2017 vs 2016

- **DPW growth of 4% in the quarter and 5% in the full year**, driven by rate increases and growth initiatives in favourable market conditions.
- **Strong underlying current year loss ratio of 49.3%** deteriorated from last year's outstanding performance on higher level of weather-related claims.
- **CAT loss ratio of 1.9%** included losses from wind and rain storms.
- **Favourable PYD ratio remained healthy at 3.2%.**
- **Combined ratio of 79.7%** reflected the effectiveness of our profitability actions and expense management.
- **Very strong underlying current year loss ratio of 49.6%** was driven by the effectiveness of our profitability actions.
- **CAT losses** were above expectations, driven by severe wind and water events in Central Canada.
- **Favourable PYD ratio of 3.0%**, remained healthy, though lower than last year.
- **Combined ratio of 89.1%** reflected a strong performance in an elevated CAT environment, meeting our target to operate at 95% or better even with adverse weather.

DPW

Underlying current year loss ratio

Combined ratio



Management’s Discussion and Analysis for the year ended December 31, 2017

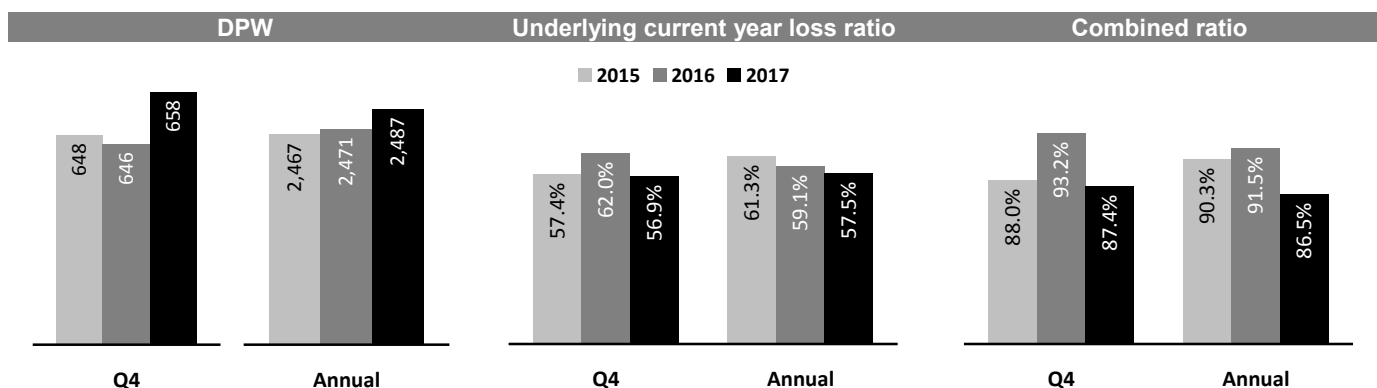
(in millions of Canadian dollars, except as otherwise noted)

4.7 Commercial lines

Table 8 – Underwriting results for Commercial lines Canada, including Commercial P&C and Commercial auto

	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW	658	646	2%	2,487	2,471	1%
Commercial P&C	463	466	(1)%	1,733	1,768	(2)%
Commercial auto	195	180	8%	754	703	7%
NEP	600	607	(1)%	2,382	2,362	1%
Underwriting income (loss)	75	42	79%	320	200	60%
Underlying current year loss ratio	56.9%	62.0%	(5.1) pts	57.5%	59.1%	(1.6) pts
CAT loss ratio (including reinst. premiums)	2.9%	2.9%	- pts	3.1%	4.6%	(1.5) pts
Unfavourable (favourable) PYD ratio	(5.6)%	(5.8)%	0.2 pts	(8.4)%	(7.9)%	(0.5) pts
Claims ratio	54.2%	59.1%	(4.9) pts	52.2%	55.8%	(3.6) pts
Expense ratio	33.2%	34.1%	(0.9) pts	34.3%	35.7%	(1.4) pts
Combined ratio	87.4%	93.2%	(5.8) pts	86.5%	91.5%	(5.0) pts

- | Q4-2017 vs Q4-2016 | 2017 vs 2016 |
|---|---|
| <ul style="list-style-type: none"> DPW growth of 2% in the quarter reflected improving growth momentum in commercial lines. Strong growth in specialty lines was tempered by our ongoing pricing and segmentation actions in commercial P&C deployed in competitive markets. Profitability measures in commercial auto, including segmented rate increases, continued to be deployed in favourable market conditions. Very strong underlying current year loss ratio improved to 56.9% in the quarter and 57.5% in the full year driven by the effectiveness of our profitability actions and lower large losses. CAT loss ratio remained above expectations in the quarter and the full year. Favourable PYD ratio of 5.6% included unfavourable development on some large losses. | <ul style="list-style-type: none"> Favourable PYD ratio of 8.4% was higher than expected, mainly due to the impact of the Q3-2017 net reserve change. Refer to Section 15.2 – Q3-2017 net reserve change. Combined ratio of 87.4% in the quarter and 86.5% in the full year reflected a very strong underlying performance, exceeding our target of a low 90s combined ratio. |



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

4.8 Distribution

Net distribution income represents the operating results from our wholly owned broker, BrokerLink, as well as our share of results from broker affiliates.

In Table 9 below, we have also presented distribution EBITA (earnings before interest, taxes, amortization and integration costs).

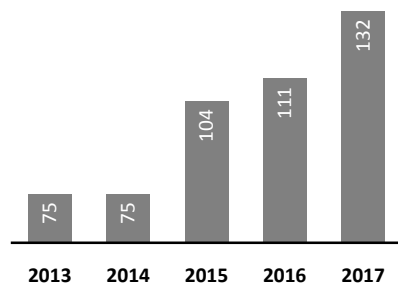
Table 9 – Reconciliation of net distribution income to distribution EBITA

	Q4-2017	Q4-2016	Change	2017	2016	Change
Net distribution income, as currently reported	28	24	17%	132	111	19%
Adjustments to EBITA basis						
Add: interest expense	3	3	-	9	13	(31)%
Add: income taxes	3	2	50%	17	10	70%
Distribution EBITA	34	29	17%	158	134	18%

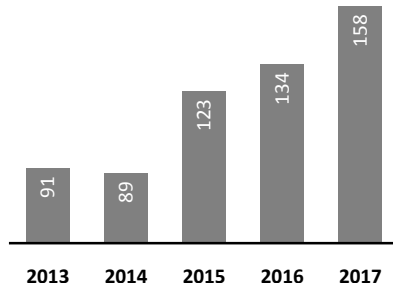
2017 vs 2016

- **Strong performance** driven by the expansion and improved profitability of our broker network. In 2017, our brokers generated an operating margin close to 30%. We expect net distribution income to continue to grow in the future.
- In addition, our broker loans generated \$17 million of interest income, which is included in Net investment income.

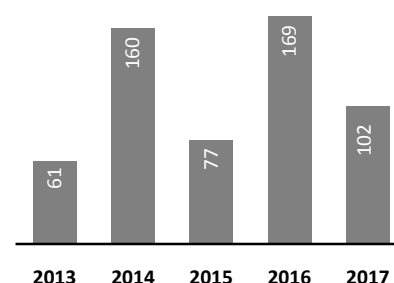
Net distribution income



Distribution EBITA



Net distribution investments



Since 2013, net distribution income and distribution EBITA have grown at a CAGR of 15% from continued growth and improved profitability.

Continued growth in our network, thanks to close to \$570 million of net distribution investments made in the last 5 years.

Refer to Section 11.1 – Canadian distribution strategy for more details.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 5 – U.S. Insurance

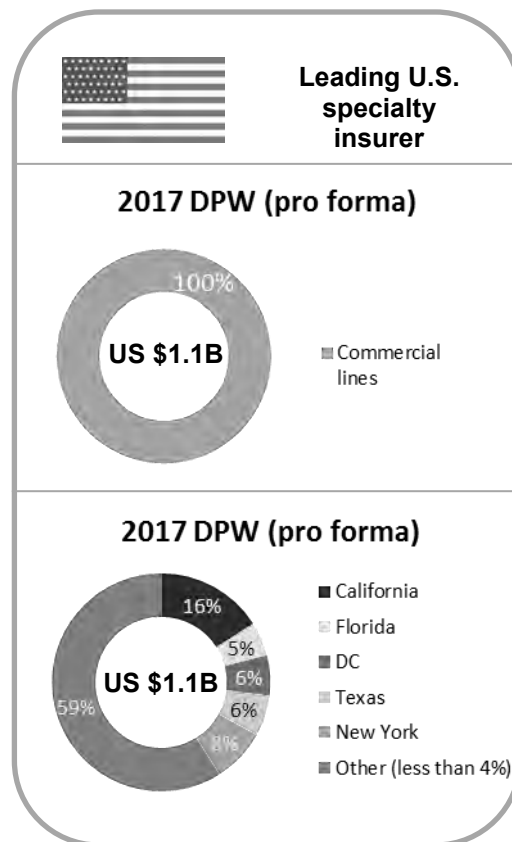
On September 28, 2017, we completed our US\$1.7 billion (\$2.3 billion) acquisition of OneBeacon.

5.1 OneBeacon, a pure-play specialty lines insurer

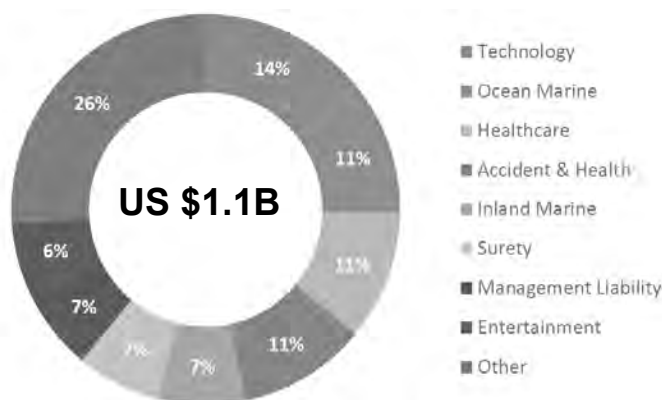
- Leading U.S. specialty insurer focused on small to mid-sized businesses, with over US\$1 billion in annual DPW.
- Distributes insurance products and services in the U.S. under the OneBeacon brand through independent agencies, regional and national brokers, wholesalers and managing general agencies.
- OneBeacon operates through five underwriting companies: Atlantic Specialty Insurance Company, Homeland Insurance Company of Delaware, Homeland Insurance Company of New York, OBI America Insurance Company and OBI National Insurance Company.

5.2 What we offer

- Specialty products that solve the unique needs of particular customers or industry groups including accident and health, technology, ocean and inland marine, public entities, and entertainment.
- Additionally provide distinct products and tailored coverages to a broad customer base across the U.S. such as healthcare, tuition reimbursement, surety, management liability, financial services, specialty property, environmental and financial institutions.
- Each OneBeacon business is managed by an experienced team of specialty insurance professionals focused on a specific customer group or industry segment. Competitive factors for most of our insurance products are price, product terms and conditions, agency and broker relationships, claims service, company scale and financial stability.



Pro forma DPW by business unit



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

5.3 P&C U.S.

Results reflect the first full quarter within IFC following the close of the OneBeacon acquisition in Q3-2017. All figures in the table below are shown in CAD, using an average exchange rate of 1.2709.

The underwriting results for P&C U.S. excluded the results of exited lines (mainly Programs, and Architects & Engineers) in Q4-2017, which are reported in Non-operating results (*see Section 26 – Non-operating results*).

At the date of acquisition of OneBeacon, we purchased an adverse development coverage (“ADC”) on claims liabilities for 2016 and prior accident years to mitigate the risk of adverse development on the acquired book of claims liabilities (*see Section 15.2 – Reinsurance*).

Table 10 – Underwriting results for P&C U.S.¹

	Q4-2017	Q4-2016	Change	2017	2016	Change
DPW	307	-	nm	307	-	nm
NEP	326	-	nm	326	-	nm
Current year claims	183	-	nm	183	-	nm
Unfavourable (favourable) PYD	15	-	nm	15	-	nm
Net claims incurred	198	-	nm	198	-	nm
Underwriting expenses	120	-	nm	120	-	nm
Underwriting income	8	-	nm	8	-	nm
Underwriting ratios						
Underlying current year loss ratio	55.9%	-	nm	55.9%	-	nm
Unfavourable (favourable) PYD ratio	4.6%	-	nm	4.6%	-	nm
Claims ratio	60.5%	-	nm	60.5%	-	nm
Commissions	16.8%	-	nm	16.8%	-	nm
General expenses	18.2%	-	nm	18.2%	-	nm
Premium taxes	1.9%	-	nm	1.9%	-	nm
Expense ratio	36.9%	-	nm	36.9%	-	nm
Combined ratio	97.4%	-	nm	97.4%	-	nm

¹ Excluding the results of exited lines (*see Section 27 – Non-IFRS financial measures*).

Commercial lines

- **Premiums of \$307 million**, supported by profitability actions, including underwriting and rate actions in selected lines. Actions are well underway to grow the business through existing broker relationships and new growth pipelines.
- On a pro forma basis, Q4-2017 premiums represented a growth of 1.9% compared to Q4-2016.
- **Underlying current year loss ratio was healthy at 55.9%**.
- **Unfavourable PYD ratio of 4.6%** included our net share of prior year losses and the impact of discounting on the amount recoverable from the ADC.
- **Expense ratio of 36.9%** reflected expense management initiatives and lower variable compensation. As at December 31, 2017, we estimate our synergy run-rate at close to \$9 million in annual savings.
- **Combined ratio was 97.4% from continuing operations**. We are executing on our profitability action plan and are on track to bring the U.S. combined ratio to a low 90s level within 24 to 36 months of closing.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 6 – Corporate and Other

Comprised of the following activities, which are managed at the Corporate level:

- Investing related to P&C insurance
- Treasury and capital management
- Other corporate activities

Results include net investment income, financing costs, corporate expenses, as well as other income and expenses, as shown in Table 11 below.

6.1 \$17 billion of high-quality investments strategically managed

Following the acquisition of OneBeacon, our investments totalled \$16.9 billion as at December 31, 2017, up \$2.5 billion from December 31, 2016. Our approach to investment management continues to reflect our objective of maximizing after-tax returns and outperforming our peers’ investment returns over the long-term, while ensuring policyholder protection and maintaining strong regulatory capital levels.

We continue to manage our investment portfolio to achieve these objectives via appropriate asset allocation and active management investment strategies, while minimizing the potential for large investment losses with diversification and limits on our investment exposures. Such limits are specified in our investment policies and are designed to be consistent with our overall risk tolerance. Management monitors and ensures compliance with our investment policies.

6.2 Maximizing long-term shareholder value by optimizing capital

Our objectives when managing capital consist of:

- maintaining strong regulatory capital levels, while ensuring policyholders are well protected; and
- maximizing long-term shareholder value by optimizing capital used to operate and grow the Company.

6.3 Treasury management: evolving in an international context

We have a centralized best-in-class treasury management approach that ensures access to funds in multiple currencies and control of global market variable fluctuations on shareholders’ equity.

6.4 Performance

Table 11 – Operating performance¹

	Section	Q4-2017	Q4-2016	Change	2017	2016	Change
Operating performance							
Net investment income	6.5	121	104	17	432	414	18
Finance costs		(25)	(18)	(7)	(82)	(72)	(10)
Other revenues (expenses)		2	13	(11)	5	10	(5)
PTOI		98	99	(1)	355	352	3
Selected non-operating gains (losses) ¹							
Currency and other net gains (losses)	6.6	18	(6)	24	105	(1)	106
Net investment gains (losses)	6.7	(24)	(91)	67	(36)	(71)	35
Net gains (losses)		(6)	(97)	91	69	(72)	141

¹ Refer to Section 26 – Non-operating results for more details.



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

6.5 Net investment income

Table 12 – Net investment income

	Q4-2017	Q4-2016	Change	2017	2016	Change
Interest income	81	66	15	275	265	10
Dividend income	50	47	3	194	184	10
Investment income, before expenses	131	113	18	469	449	20
Expenses	(10)	(9)	(1)	(37)	(35)	(2)
Net investment income	121	104	17	432	414	18
Average net investments¹	16,644	13,819	20%	14,663	13,396	9%
Market-based yield²	3.11%	3.27%	(16) bps	3.20%	3.36%	(16) bps

¹ Defined as the mid-month average fair value of net equity and fixed-income securities held during the reporting period.

² Refer to Section 27 – Non-IFRS financial measures.

2017 vs 2016

- **Net investment income** increased due to the acquisition of OneBeacon on September 28, 2017. Excluding the impact of OneBeacon, net investment income was flat compared to 2016.
- **Average net investments** increased, mainly reflecting the acquisition of OneBeacon.
- **The lower market-based yield** reflected the addition of the OneBeacon portfolio (recorded at fair value at closing), as well as the increase in equity markets throughout the year (see Section 6.8 – Capital markets).

6.6 Currency and other net gains (losses)

Currency and other net gains (losses) are reported in Non-operating results and included the following items.

Table 13 – Currency and other net gains (losses)

	Q4-2017	Q4-2016	Change	2017	2016	Change
Foreign currency	1	-	1	65	-	65
Distribution transactions and other ¹	17	(6)	23	40	(1)	41
Currency and other net gains (losses)	18	(6)	24	105	(1)	106

¹ Including net gains on investments in associates and joint ventures related to a change of control.

Q4-2017 vs Q4-2016

2017 vs 2016

- **Net gains of \$18 million in Q4-2017** were driven by a realized gain on the sale of a small non-core subsidiary.
- **Net gains of \$105 million in 2017** were mainly driven by:
 - pre-acquisition gains on book value hedges related to OneBeacon. Prior to closing, these derivatives, which lower our book value exposure to the USD, were marked-to-market through P&L (see Section 17.4 – Currency management);
 - net gains on distribution transactions; and
 - a realized gain on the sale of a small non-core subsidiary.

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

6.7 Net investment gains (losses)

Net investment gains (losses) are reported in Non-operating results and included the following items.

Table 14 – Net investment gains (losses)

	Q4-2017	Q4-2016	Change	2017	2016	Change
Fixed-income strategies¹						
Realized and unrealized gains (losses) on FVTPL bonds	(20)	(118)	98	(127)	(103)	(24)
Other gains (losses)	(3)	(2)	(1)	5	(1)	6
	(23)	(120)	97	(122)	(104)	(18)
Equity strategies						
Realized and unrealized gains (losses): ²						
equity securities, net of derivatives	25	37	(12)	123	66	57
embedded derivatives	(15)	(8)	(7)	(50)	(13)	(37)
Net foreign currency gains on investments	1	4	(3)	33	21	12
Impairment losses on common shares	(12)	(4)	(8)	(20)	(41)	21
	(1)	29	(30)	86	33	53
Net investment gains (losses)	(24)	(91)	67	(36)	(71)	35
FVTPL bonds	(20)	(118)	98	(127)	(103)	(24)
Other strategies	(4)	27	(31)	91	32	59
	(24)	(91)	67	(36)	(71)	35

¹ Our U.S. fixed-income portfolio held in our Canadian P&C entities is hedged using foreign-currency forward contracts, resulting in minimal currency gains or losses.

² Excluding foreign currency impact on equity securities, which are reported in Net foreign currency gains on investments.

We own perpetual preferred shares with embedded call option derivatives which give the issuer the right to redeem the shares at a particular price. These embedded derivatives are marked-to-market through net income, while changes in value of our AFS preferred shares flow through OCI. When preferred share prices increase, the value of these written options also increases, generating a mark-to-market loss. Conversely, when preferred prices decline, the value of these derivatives also falls, resulting in a mark-to-market gain.

Q4-2017 vs Q4-2016	2017 vs 2016
<p>Unrealized losses on our FVTPL bonds in 2017 and 2016 were driven by rising interest rates. Losses on our FVTPL bonds were partially offset by gains arising from the changes in the discount rate for our claims liabilities (referred to as MYA).</p> <p>Other net investment losses of \$4 million in Q4-2017 reflected:</p> <ul style="list-style-type: none"> mark-to-market losses on our embedded derivatives related to preferred shares, and impairment losses, mostly offset by: gains on our common share strategies, reflecting the continued strength in common share markets (see Section 6.8 – Capital markets). <p>Other net investment gains of \$27 million in Q4-2016 were driven by realized gains on our equity strategies, reflecting the significant appreciation in equity markets.</p>	<p>Other net investment gains of \$91 million in 2017 were driven by:</p> <ul style="list-style-type: none"> gains on our equity strategies, reflecting the appreciation in equity markets, mitigated by: mark-to-market losses on our embedded derivatives related to the rise in value of preferred shares. <p>Other net investment gains of \$32 million in 2016 were driven by:</p> <ul style="list-style-type: none"> realized gains on our equity securities and currency gains arising on the sale of U.S. equities, partly offset by: impairment losses of \$41 million, principally on energy stocks.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

6.8 Capital markets

While the correlation between the performance of capital markets and the performance of our investment portfolio is not perfect, the following market indicators may be useful in understanding the overall performance of our investments.

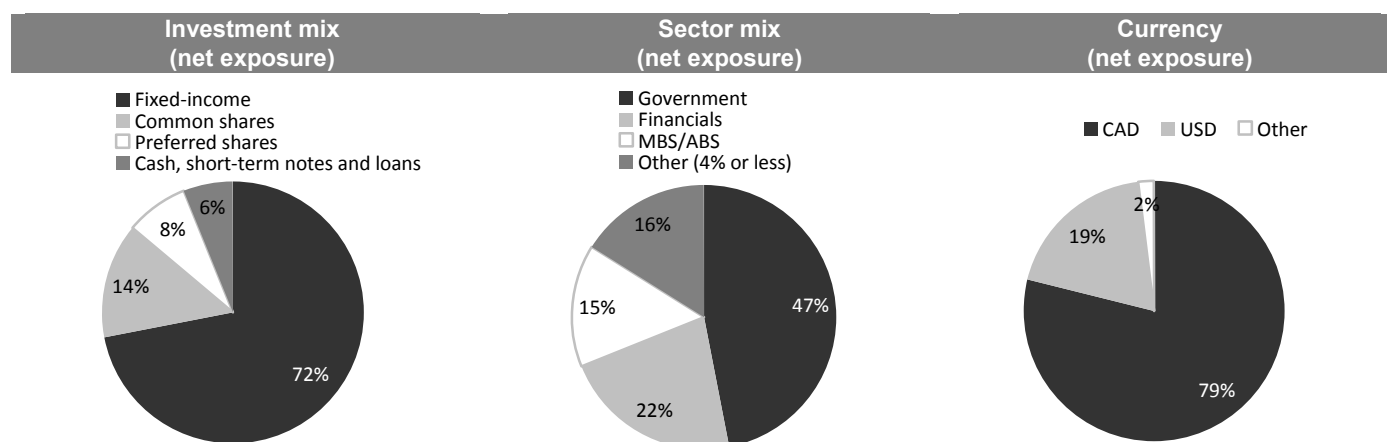
Table 15 – Selected market indicators

Selected market indicators	Q4-2017	Q4-2016	2017	2016
S&P/TSX Composite	4%	4%	6%	18%
S&P/TSX Financials	5%	11%	9%	19%
S&P/TSX Preferred Share Index	1%	4%	8%	1%
5Y Canada Sovereign Index (estimated variance in bps)	13 bps	44 bps	78 bps	37 bps
5Y AA Corporate spread (estimated variance in bps)	(5) bps	(3) bps	(21) bps	(27) bps
DJ Dividend 100 Composite (U.S.)	9%	5%	17%	9%
5Y U.S. Sovereign Index (estimated variance in bps)	27 bps	78 bps	28 bps	17 bps
Strengthening (weakening) of CAD vs USD	(1)%	(2)%	6%	3%

Comments on capital markets performance

- North American equity markets rose significantly throughout 2017. The **S&P/TSX Composite Index** increased by 4% in Q4-2017 (6% in 2017), while our benchmark **DJ Dividend 100 Composite (U.S.) Index** increased 9% in Q4-2017 (17% in 2017). This resulted in an increase in the fair value of our common share portfolios and gains on our AFS equity strategies. Our total comprehensive return on common equities was strong in 2017.
- **The S&P/TSX Preferred Share Index** increased by 1% in Q4-2017 (8% in the full year) buoyed up by strong equity markets and the positive impact of higher interest rates on the prices of rate-reset preferred shares, leading to an increase in the fair value of our AFS preferred shares (and a loss on the related embedded derivatives).
- **Five-year Canadian Sovereign yields** increased by approximately 13 bps in Q4-2017 (78 bps in 2017), leading to lower bond valuations and mark-to-market losses during the quarter.

Our net exposure, after reflecting the impact of hedging strategies related to investments and OneBeacon, is outlined below as at December 31, 2017.



ENVIRONMENT & OUTLOOK

Section 7 – Insurance industry at a glance

7.1 P&C insurance in Canada

<p>Large and highly fragmented</p>	<ul style="list-style-type: none"> • A \$48 billion market representing approximately 3% of gross domestic product (GDP), according to MSA data for 2016. • The top five insurers represent 49% of the market, and the top 20 have a combined market share of 85%. Intact is the largest player with approximately 17% market share. • There has been consolidation in recent years and we expect more to come.
<p>Evolving and growing over time</p>	<ul style="list-style-type: none"> • Over the last 30 years, the industry has grown at a 5.1% CAGR and delivered a ROE of approximately 10%. • Brokers distribute approximately 60% of insurance policies, while direct writers distribute 40%. • Emerging technologies and innovations are beginning to transform the insurance landscape as they enable new ways to measure, control and price risk, engage with customers, reduce cost, improve efficiency, and expand insurability. This will likely fuel further innovation, transformation and consolidation within the industry.
<p>Regulated</p>	<ul style="list-style-type: none"> • Insurance companies are licensed under insurance legislation in each of the provinces and territories in which they conduct business. • Home and commercial insurance rates are unregulated, while personal auto rates are regulated in most provinces. • Capital for federal insurance companies is regulated by OSFI and by provincial authorities in the case of provincial insurance companies (<i>see Section 18 – Capital management</i>)

7.2 U.S. specialty insurance

<p>Highly fragmented with no clear leader</p>	<ul style="list-style-type: none"> • U.S. commercial P&C insurance is a \$288 billion market, with specialty insurance accounting for more than 40% in 2016. • U.S. commercial specialty industry is a fragmented industry. The top 10 players represent just over 40% of the market, with the largest player capturing roughly 7% in 2016. Outside of the top six players, no single insurer contributes more than 3% of the total estimated market. The majority of the top 25 players have a market share between 1% and 2.5%.
<p>Niche market with lucrative potential</p>	<ul style="list-style-type: none"> • The specialty insurance market offers niche and unique products and services that are not written by most P&C insurance companies. These products generally require specialized underwriting knowledge compared with more traditional insurance products. • The combined ratio (and in turn the ROE) of many specialty products have outperformed those typically offered in the standard market due to more pricing and policy form flexibility. • This unique risk and specialty focus can also come with above-average earnings volatility.
<p>Evolving and growing over time</p>	<ul style="list-style-type: none"> • Over the last 20 years, the specialty insurance market has grown at a 4.1% CAGR. • Market has experienced elevated merger and acquisition activity in recent years and this trend is likely to continue. • The agency channel (independent agencies, brokers, wholesalers and managing general agencies) is the primary distribution channel for specialty insurance products. • Trends in litigation, regulation, economic maturity, social and workforce issues, and technology will continue to support growth and drive product innovation.

Section 8 – Operating environment

8.1 Auto insurance in Canada

In April 2017, the Ontario Government released a report on auto insurance by David Marshall, Ontario’s advisor on auto insurance. His report contained 35 recommendations to get customers back on track faster and reach maximum medical recovery, all while moving to a care, not cash, environment.

In August 2017, the Government of Ontario launched public consultations on the Marshall Report on Auto Insurance. Intact took part in public roundtables and also submitted a formal written submission.

On December 5, 2017, the Government of Ontario released their **Fair Auto Insurance Plan (“FAIP”)** based on recommendations made by David Marshall and feedback from public consultations. Implementation dates for the measures remain to be determined, but are expected to be staggered throughout 2018. Key initiatives include:

Standard Treatment Plans	<ul style="list-style-type: none"> • Making sure people with the most common collision injuries receive timely, appropriate and effective treatment by developing and implementing standard treatment plans that focus on recovery, monitoring health outcomes and increasing awareness of the best treatment practices. • This is expected to reduce costs in the system by changing the emphasis from cash payouts to ensuring appropriate care for victims.
Independent Examination Centres	<ul style="list-style-type: none"> • Creating independent examination centres to provide assessments of more serious auto collision injuries, to help resolve and reduce diagnosis disputes, and to reduce system costs and inefficiencies stemming from disputes. This will include developing standards for assessors and ensuring that the opinions of neutral assessments are respected.
Serious Fraud Office	<ul style="list-style-type: none"> • Establishing an integrated and dedicated office that will combat systemic fraud in Ontario and support activities to address auto insurance fraud

The FAIP represents an opportunity to re-design the entire Ontario auto insurance product, which could lead to more sustainable consumer costs. We believe that these initiatives, if implemented, should benefit both consumers and the industry over time.

8.2 U.S. Corporate Tax reform

Following enactment of the U.S. Tax Cuts and Jobs Act (“U.S. Corporate Tax reform”) we recorded a net non-operating income tax recovery of \$27 million in Q4-2017, primarily associated with the remeasurement of deferred tax liabilities related to the acquisition of OneBeacon. This accounting adjustment has no impact on our underlying performance, measured using operating and adjusted financial measures (see **Section 27 – Non-IFRS financial measures**).

Overall the tax reform provisions are expected to have a negligible impact on NOIPS and EPS in 2018 and beyond.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

8.3 Weather conditions at a glance



CANADA

2017	2016
<ul style="list-style-type: none"> From a Q4 perspective, in Eastern Canada, precipitations were below average overall. However, single important snowfall events caused disruption in transportation and lead to water damages. The end of the year was also impacted by lower than average temperatures. In Western Canada, early winter conditions combined with strong winds caused property damages. 	<ul style="list-style-type: none"> Q4-2016 was impacted by the remnants of Hurricane Matthew in the Maritimes. In addition, an early start to winter brought difficult road conditions which caused an elevated claims count in most regions.
<ul style="list-style-type: none"> From an annual perspective, the first half of the year was marked by higher than normal precipitation combined with late season snow melt leading to the overflowing of rivers in several regions. During summer, drier and warmer temperatures in Western Canada led to the wildfire in Southern British Columbia. Conversely, Québec and Ontario received higher than normal precipitation and several thunderstorms causing, flooding in many areas. 	<ul style="list-style-type: none"> Our 2016 financial results were impacted, with CAT losses exceeding our expectations and historical averages (<i>see Section 8.4 - CAT losses</i>) as severe weather and natural disasters including the Fort McMurray wildfires, severe hail and thunderstorms, as well as Hurricane Matthew, caused record-breaking industry losses.



U.S.

Q4-2017

<ul style="list-style-type: none"> In October 2017, wildfires started to burn in California causing damage to many properties and spreading rapidly every day. As numerous fires continued to spread, a second wave of wildfires commenced in December thereby strengthening the severity of California’s weather conditions in Q4-2017. The fires have forced many people to be evacuated from their homes and neighbourhoods and have continued to burn in the early weeks of 2018. We reported no CAT losses in Q4-2017. Given the nature of our operations in the U.S., we are less impacted by CAT losses from wildfires and severe weather conditions.
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See Section 12 – Social responsibility for details on climate change adaptation.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

8.4 CAT losses

CAT losses can be caused by a variety of events, including weather (such as wildfires, hailstorms and floodings) and non-weather events (such as industrial fires, surety and liability claims). The incidence and severity of CAT losses, while inherently unpredictable, can have a significant impact on our underwriting performance by quarter and by line of business. We generally seek to manage our exposure to CAT losses through individual risk selection and the purchase of CAT reinsurance (see Section 15.2 – Reinsurance hereafter for more details).

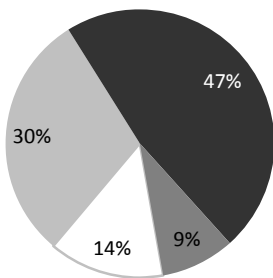
Table 16 – Net current year CAT losses

	2017	2016	2015	2014	2013	5-year average P&C Canada	
						In \$	% NEP
Net CAT losses	313	385	116	243	486	309	4.1%
By line of business							
Personal auto	27	73	37	41	44	44	0.6%
Personal property	210	210	42	140	271	175	2.3%
Commercial lines - Canada	76	102	37	62	171	90	1.2%
Commercial lines - U.S.	-	n/a	n/a	n/a	n/a	-	-
By quarter							
Q1	88	21	11	75	18	43	0.6%
Q2	105	164	22	33	143	94	1.2%
Q3	89	166	81	125	270	146	1.9%
Q4	31	34	2	10	55	26	0.4%

During the 2013-17 period, average net CAT losses of \$309 million included net losses from some of the costliest insured natural disasters in Canadian history: the Fort MacMurray wildfires in 2016, as well as the Alberta and Toronto floods in 2013. During the 2008-17 period, net CAT losses were closer to \$230 million on average.

Net CAT losses
5-year average
(by quarter)

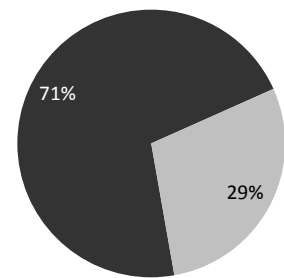
Q1 Q2 Q3 Q4



Historically, the third quarter has experienced roughly **half** of the CAT losses for the year

Net CAT losses
5-year average
(by line of business)

Personal lines Commercial lines



Historically, roughly **three-quarters** of CAT losses impacted the personal lines of business.

Given claim cost inflation trends and the acquisition of OneBeacon, we have raised our current CAT expectations (net of reinsurance) from \$250 million to **\$275 million per year**.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 9 – Outlook

	P&C insurance industry 12-month outlook	Our response
Personal auto	<ul style="list-style-type: none"> Industry profitability remains challenged with average loss ratios in the mid-to-upper 70s for the first nine months of the year. Claims inflation remains a headwind which is leading to rate increases in all markets. Continued increases in the volume ceded to risk sharing pools and non-standard auto markets together with the rate action we see across the country support our view of a firming market. We expect growth at a mid single-digit level for the industry. 	<ul style="list-style-type: none"> Our actions continue on pricing, underwriting and claims to tackle trends, which should lead to meaningful profitability improvements in the coming year, with some near term pressure on growth. Our brand investments and further digital enhancements in this line of business will continue to help selectively grow our market position. We have been investing in telematics, big data, and artificial intelligence to maintain our advantage in data and segmentation.
Personal property	<ul style="list-style-type: none"> As companies are adjusting to changing weather patterns, we expect the current firm market conditions to continue. As a result, we expect growth at a mid single-digit level. 	<ul style="list-style-type: none"> We expect to continue to capitalize on market conditions with rate increases to ensure our results are sustainable even in severe weather conditions.
Commercial lines Canada	<ul style="list-style-type: none"> These lines of business remain competitive, mainly in the larger risks. We expect growth at a low-to-mid single-digit rate. 	<ul style="list-style-type: none"> We continue to develop innovative products to address customer needs (e.g. cyber risk coverage and sharing economy). At the same time, our focus on training and service excellence remains. Following the acquisition of OneBeacon we have strengthened our capabilities in specialty lines. We are now leveraging OneBeacon’s tailored specialty products and services in Canada with the launch of products for technology and entertainment sectors. Growth initiatives are underway with underwriting desks now serving our cross-border customers.
Overall P&C Canada	<ul style="list-style-type: none"> Given the growth trends through 2017, we expect growth at a mid single-digit rate in 2018. Overall, we expect the Canadian industry’s ROE to improve but remain below its long-term average of 10% over the next 12 months. 	<ul style="list-style-type: none"> We continue to invest in brand, digital strategies, customer experience and distribution networks to meet our objectives. We expect that with our pricing and underwriting discipline, and our claims management capabilities, we will continue to outperform the industry.
Distribution	<ul style="list-style-type: none"> The Canadian P&C broker industry remains fragmented with continuing opportunities for consolidation. 	<ul style="list-style-type: none"> We will continue to support our brokers as they expand and grow their businesses, while also actively participating in broker consolidation via BrokerLink.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

	P&C insurance industry 12-month outlook	Our response
U.S. Commercial lines	<ul style="list-style-type: none"> The U.S. Commercial specialty industry is highly fragmented with the top 10 players capturing just over 40% of the market share in 2016. While the pricing environment is competitive, there are early signs of upward trends in certain specialty lines with low single-digit growth expected in 2018. 	<ul style="list-style-type: none"> Our objective is to grow the U.S. specialty business and operate at a combined ratio in the low 90s within 24-36 months. Actions have begun on our performance improvement plan; we have exited underperforming lines, launched risk selection and claims initiatives and are moving fast to realize synergies.
Investments	<ul style="list-style-type: none"> While there is upward momentum on interest rates, investment yields remain low by historical standards. 	<ul style="list-style-type: none"> The addition of the OneBeacon investment portfolio will generate growth in our Net investment income over the next 12 months. Our investment management team continues to optimize the mix of our consolidated investment portfolio, taking into account factors such as risk, return, capital, regulation and the recent tax legislation changes in the United States.
Financial strength	<ul style="list-style-type: none"> Global capital requirements are continuing to influence the asset allocation decisions of many companies. 	<ul style="list-style-type: none"> We expect to continue to maintain our strong financial position, allowing IFC to capture growth opportunities as they arise and withstand any headwinds from volatile markets or natural disasters.

STRATEGY

Section 10 – Strategy update

10.1 What we are aiming to achieve

The pace of change in our industry, and indeed around the world, continues to accelerate. Consumer and customer needs and expectations are also changing. They expect fast, simple, effortless and empathetic experiences. We have been building our company to be customer driven and will continue to enhance our efforts to be easy to do business with and go beyond expectations to deliver second to none experiences as well as provide best-in-class service to our brokers.

We have a company of talented and diverse employees who are very committed to our customer driven value. We are committed to ensuring they have the tools and training to do their best work.

We will continue to earn the right to be one of the most respected companies, a company where we are true to our values, where our people are engaged because they know their work matters, and where our customers are our advocates because they know what matters to them, matters to us.

Objectives by 2020

Our customers are our advocates

- 3 out of 4 customers are our advocates
- 3 out of 4 customers actively engage with us digitally

Our strategy

- Be easy to deal with and go beyond expectations to deliver a customer experience that is second to none.
- Be the recognized leader in small and mid-sized businesses and specialty lines through service, expertise and product.
- Build core brands to become trusted, household names.
- Leverage best-in-class digital distribution and service platforms for customers and brokers.
- Contribute to the resiliency and prosperity of communities by leading in climate adaptation initiatives.

Our employees are engaged

- Be a best employer
- Be a destination for top talent and experts

Our strategy

- Build the best team to succeed now and in the future.
- Create a workplace where we are engaged and can contribute our best every day by delivering on our promise.
- Live our values and leadership success factors.



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Our specialty solutions business is a leader in North America

- Achieve combined ratio in the low 90s
- Generate \$3 billion in annual DPW

Our strategy

- Deliver targeted synergies in back office and claims.
- Introduce new products to Canada and export Canadian lines to U.S.
- Grow cross-border business.
- Retain key talent and management.

See Section 10.2 below for additional details on our transition plan.

Our company is one of the most respected

- Exceed industry ROE by 5 points in Canada and the U.S.
- Grow NOIPS 10% yearly over time

Our strategy

- Deepen our strengths in pricing, risk selection, claims and investments.
- Simplify processes to become the most efficient operator.
- Lead in data, artificial intelligence (AI), and behavioural analytics.
- Leverage our size in claims through efficiencies in the supply chain.
- Manage capital opportunistically.
- Consolidate Canadian industry in manufacturing and distribution.

10.2 Creating a leading provider of specialty insurance in North America

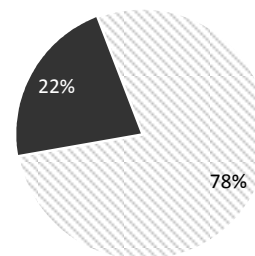
On September 28, 2017, we completed our US\$1.7 billion (\$2.3 billion) acquisition of OneBeacon. OneBeacon is a specialty P&C insurance provider that offers a wide range of insurance products in the U.S. primarily through independent agencies, regional and national brokers, wholesalers and managing general agencies.

- With the acquisition of OneBeacon, we have created a leading provider of specialty insurance in North America, with over \$2 billion in combined annual premiums. It combines Intact's leading commercial lines track record and deep data, claims and digital expertise with OneBeacon's high calibre team and specialty lines capabilities.
- The acquisition bolsters our Canadian business with new products and cross-border capabilities, and better positions us to compete with international insurers.
- Furthermore, it provides an additional growth pipeline in the U.S. and enables IFC to leverage our consolidation expertise in a fragmented specialty lines market.

¹ DPW (pro forma) for 2017 are comprised of the DPW of P&C Canada and the DPW (pro forma) of P&C U.S.

2017 DPW (pro forma)¹

■ Specialty lines ▨ Other P&C lines



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Value creation

- With the addition of the OneBeacon team we have created a leading North American specialty lines insurer focused on small to medium sized enterprises.
- We expect the acquisition to deliver mid-single digit accretion to NOIPS by the end of 2019.

Profitable growth

- Actions are in progress to grow the many profitable OneBeacon specialty lines by harnessing existing broker relationships and the momentum created by the stability of our ownership.
- Additional growth pipelines have been opened with commercial lines underwriting desks on each side of the border to support customers with businesses in both countries.
- In Q4-2017, we started offering OneBeacon's tailored specialty products and services in Canada, beginning with the launch of tailored products for technology and entertainment risks.

Profitability improvement

- The profitability action plan for OneBeacon is on track to achieve a low-90s combined ratio within 24-36 months of closing and mid-single digit accretion to NOIPS by the end of 2019.

The profitability action plan is composed of:

- **Underwriting:** We have exited Programs and Architects & Engineers lines of business and are leveraging Intact's analytics and segmentation expertise to take underwriting actions in select other lines. Results of exited lines are reported in Non-operating results (Underwriting results of exited lines) (*see Section 26 – Non-operating results for details*).
- **Claims:** We are increasing internalization of claims handling and implementing further indemnity control procedures.
- **Expense synergies:** We expect US\$25 million in expense synergies over three years. These comprise internalizing investment management, combining reinsurance programs, de-listing and eliminating U.S. public company reporting, as well as shared services and technology savings. On a run-rate basis, we have realized approximately one-third of these expense synergies at the end of 2017.

Risk management

- At the date of acquisition of OneBeacon, we purchased an adverse development coverage (ADC) on claims liabilities for 2016 and prior accident years to mitigate the risk of adverse development on the acquired book of claims liabilities. The cost of this coverage was recorded as a non-operating expense. *Refer to Section 15.2 – Reinsurance for more details.*
- The acquisition also brings important diversification benefits to all our operations, including earnings stability and reduced tail risk.



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

10.3 Other developments at a glance

Innovation

In line with our strategy to deliver a customer experience that is second to none and build a best in class digital distribution and service platform:

- in December, Intact Insurance launched **Canada’s first commercial auto quick quote tool**. The online tool is currently available in Québec and will be rolled out across Canada over the next year;
- in August, Belairdirect launched a **mobile app** which gives customers digital access to proof of insurance, insurance documents, belairdirect roadside assistance (Québec only) and billing information;
- in April, we launched our Intact **Service Centre in Montreal**, our fourth Service Centre in Canada, a one-stop shop for customers with auto insurance claims;
- Intact Insurance in Québec launched **Client Centre**, which gives personal lines customers digital access to their policy documents, billing statements and real-time claims status updates; and
- we improved our **telematics offering** for Intact Insurance customers in Alberta, Québec and parts of Ontario by launching a mobile app, allowing good drivers to save on car insurance without having to install any hardware in their vehicles.

In line with our long-term strategy to invest and partner with emerging and innovative businesses (*Section 11.2 – Innovation*):

- we invested in **Hangar Technology Inc.**, the world’s first drone logistics platform, helping firms increase efficiency, showcase content and integrate more actionable insights into their workflows. Hangar’s clients use its premium aerial data software products (drones), all without having to handle any of the logistics of owning, acquiring, flying or editing the data from them.
- we invested in **Humatics Corporation (“Humatics”)**. Humatics is reinventing the relationships between people, robots, and infrastructure in the connected world. Humatics’ breakthrough technologies for ultra-low-cost millimeter scale positioning create a new category “microlocation”; enabling a world of precise, collaborative relationships between people, places and things.
- we announced a \$2.5 million commitment to the **Vector Institute**, a new independent artificial intelligence research facility.

Acquisitions and financing activities

- On September 28, 2017, we completed our US\$1.7 billion (\$2.3 billion) acquisition of OneBeacon. *Please refer to Section 10.2 – Creating a leading provider of specialty insurance in North America and Section 17 – Treasury management.*
- During 2017, **BrokerLink** acquired brokers in the Greater Toronto, Ottawa and Southern areas of Ontario, Edmonton, Calgary, Alberta, and in Newfoundland & Labrador. This increased its presence in personal, commercial, and farm insurance.

Awards and recognition

We were recognized:

- as an **Aon Best Employer – Canada 2018, Platinum level**, recognizing IFC for its strong level of employee engagement, leadership, performance culture and employment brand;
- by **The Globe and Mail’s Report on Business Board Games** corporate governance index in 2017, placing **second** among 242 companies and trusts in the S&P/TSX Composite Index; and
- as an **Iconic Canadian Brand** by Interbrand Canada Inc. (“Interbrand”) for Canada150, recognizing the 150 companies, organizations and institutions that are authentically Canadian. Interbrand considered 10 factors that constitute a strong brand, and focused on clarity, authenticity and engagement as the most differentiating factors.

We were honoured by **La Gouvernance au Féminin**, a Québec-based not-for-profit organization that supports women in their leadership development, career enhancement and access to board seats, with the Certification of Parity for our actions towards the advancement of women in business. Intact was also one of the three companies that achieved platinum level certification in recognition of our commitment to advancing the cause of women.

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(in millions of Canadian dollars, except as otherwise noted)

Section 11 – Unique advantages

We have several unique advantages which have enabled us to sustainably outperform other P&C insurers in Canada. These advantages are described in the table below.

Leading North American P&C Operator	
 <p>Seamless distribution strategy</p>	<ul style="list-style-type: none"> • Our multi-channel distribution strategy includes the most recognized broker and direct-to-consumer brands. This strategy maximizes growth in the market and enables us to appeal to different customer preferences while being more responsive to consumer trends and needs. • We have more than 2,000 relationships across Canada and the U.S. for customers that prefer the highly-personalized and community-based service that an insurance broker provides. • We provide our brokers with a variety of digital distribution service platforms, alongside sales training and financing to enable them to continue to grow and develop their businesses.
 <p>Digital first experiences</p>	<ul style="list-style-type: none"> • Our industry leading mobile and digital experiences separate us from our peers. Our ability to design, deliver and iterate on new experiences for brokers and customers makes us a preferred company to deal with. Speed, simplicity and transparency are core tenets of our focus.
 <p>Engaged & talented teams</p>	<ul style="list-style-type: none"> • Our people are the cornerstone to the execution of our strategy. We benefit from attracting, retaining and engaging some of the best talent both within and outside our industry. How we organize and behave provides a sustainable and replicable approach to continuous operational improvement.
 <p>Scaled & diversified core operations</p>	<ul style="list-style-type: none"> • Our large database of customer and claims information enables us to identify trends in claims and more accurately model the risk of each policy. • We can negotiate preferred terms with suppliers, including service and quality guarantees for repairs and workmanship, and lower material costs. • Our business is well diversified across geographic regions and business lines which provides significant financial flexibility.
 <p>Sophisticated data & analytics capabilities</p>	<ul style="list-style-type: none"> • Our superior data expertise and proprietary segmentation and machine learning models are used to price and manage risk which allows us to identify certain segments of the market that are more profitable than others and in turn establish a model that will both attract and maintain clients with profitable profiles.
 <p>Deep claims expertise & network</p>	<ul style="list-style-type: none"> • Substantially all of our claims are handled in house with our preferred network, which translates into a data advantage helping claims settle faster and at a lower cost, with a more consistent service experience for the customer.
 <p>Proven consolidator & integrator</p>	<ul style="list-style-type: none"> • We are a proven industry consolidator with 16 successful acquisitions since 1988. • Our primary strategy is to pursue consolidation in the Canadian market and expansion in foreign markets where we can deploy our expertise in pricing, risk selection, claims, distribution and digital expertise. With these acquisitions, we look to expand our product offering and improve customer experience. • Our outperformance is driven by three key factors: thorough due diligence to assess all the risks and opportunities; swift and effective integration with seamless impact to our customers; and financial benefit from significant synergies due to our scale.
 <p>Tailored investment management</p>	<ul style="list-style-type: none"> • In-house investment management provides greater flexibility in support of our insurance operations at competitive costs. In establishing our asset allocation, we consider a variety of factors including prospective risk and return of various asset classes, the duration of claim obligations, the risk of underwriting activities and the capital supporting our business. • Our primary investment objective is to maximize after-tax total return via appropriate asset allocation and active management of investment strategies.

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(in millions of Canadian dollars, except as otherwise noted)

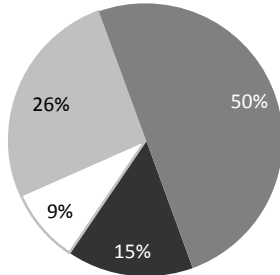
11.1 Canadian distribution strategy

Our multi-channel distribution strategy includes broker and direct-to-consumer brands.

<p>We offer our customers a multitude of options to contact us: online, on the phone or in person.</p>	<p>With our strong brands, our customers have coverage options: via our broker network with Intact Insurance, or with us directly via belairdirect.</p>	<p>We have a large network of brokerages, including our wholly-owned subsidiary, BrokerLink, which operates in Ontario, Alberta and Atlantic Canada.</p>	<p>We’re joining our expertise with other strong brands (National Bank of Canada and Sun Life Financial) to connect with new customers.</p>
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DPW by distribution channel

- Belairdirect (direct)
- BrokerLink
- Intact insurance- Affiliated brokers ¹
- Intact Insurance- Other brokers



¹Affiliated brokers are those in which we provide equity or debt financing.

Our broker channel

- Our scale and financial strength make us a strong supporter of our broker partners in terms of brand, technology, products and expertise, business opportunities, as well as financial solutions.
- To further develop broker relationships, we continue to invest in our broker network with equity and debt financing. Through these relationships, we are able to foster growth in their organizations, participate in the consolidation of the broker network, and enhance our product distribution.

Our direct channel

- Our direct-to-consumer strategy is to be the digital leader with a national cost-efficient platform which provides a simplified customer experience that is second to none.
- We continue to seek opportunities to double our direct-to-consumer business in the mid-term by expanding our reach and find innovative solutions to make it easy for our customers to protect the things they care about.

11.2 Innovation

Shaping our future in the age of big data

Artificial Intelligence (AI) and machine learning have transformational potential for the insurance industry, the economy and consumers. Our strategic partnerships with academia (such as Montreal’s IVADO, Laval University and the Vector Institute) and the recent creation of the Data Lab position us to harness the potential of these emerging technologies now and into the future. While data has always been integral to assessing risk and determining pricing, these technologies can expand our data advantage to innovate and improve product offerings so we can better serve customers. We are also using them to help increase our understanding of risk (including climate risk), and help reduce and prevent risk for customers.

Intact ventures continues to help us accelerate

Launched in 2016, Intact Ventures Inc. (Intact Ventures), is focused on investing and/or partnering with companies that are redefining the P&C insurance landscape with innovative business models and new technology. Building relationships with ground-breaking companies will enable us to accelerate our learning, design smarter products and leverage unique technology.

In return, we will support the growth of these companies by providing them with access to our expertise and talent. We want to ensure that we continue to be a leader in a fast paced industry to serve the best interests of our customers, as well as our portfolio of companies and partners.

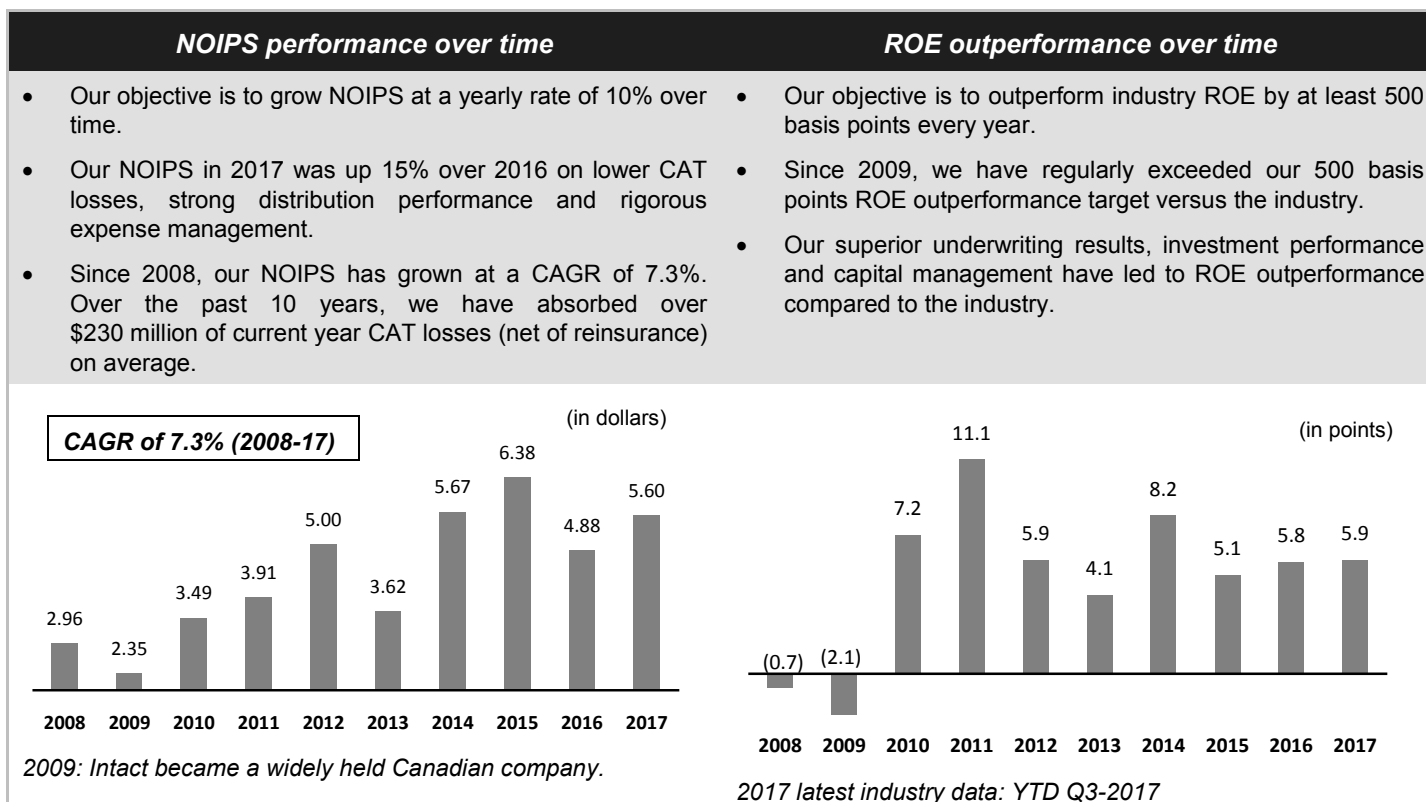
Our goal is to connect with companies that are defining:

- the future of transportation;
- how we leverage big data;
- how people interact with their homes, cars and their surroundings;
- collaborative consumption within the sharing economy; and
- insurance technology, digital tools and alternative distribution models.

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11.3 Delivering on our key financial objectives



IFC’s industry outperformance over time

Industry data below represents an IFC estimate based on MSA. Industry benchmark consists of the 20 largest comparable companies in the P&C industry based on industry data. *Please refer to Important notes on page 3 of this MD&A for further details.*

Table 17 – Canadian P&C Industry – IFC outperformance (underperformance)

	YTD Q3-2017	Full year 2016	Full year 2015	Full year 2014	Full year 2013
ROE (annualized)¹					
P&C Industry	5.9 pts	5.8 pts	5.1 pts	8.2 pts	4.1 pts
DPW growth (including industry pools)					
Industry benchmark	(2.3) pts	2.4 pts	3.4 pts	(1.5) pts	3.7 pts
Combined ratio (including MYA)					
Industry benchmark	6.0 pts	4.7 pts	5.2 pts	6.5 pts	4.5 pts

AMF (Québec) chartered insurance companies are not required to report on Q1 and Q3 results. As such, we have included estimates for non-reporters in our industry benchmark group, based on publicly available information. Actual results may vary.

¹ IFC’s ROE corresponds to the AROE.

- Our ROE outperformance of 5.9 points versus the P&C insurance industry is above our objective of 5 points.
- Our growth underperformance against our industry benchmark was 2.3 points, reflecting robust profitability actions, including rate increases taken across the country ahead of competitors.
- Our combined ratio outperformance against our industry benchmark was 6.0 points, mainly attributable to the effectiveness of our profitability actions.

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(in millions of Canadian dollars, except as otherwise noted)

11.4 Delivering value to our shareholders

2018: our 13th consecutive annual dividend increase	Book value per share increase over time
<ul style="list-style-type: none"> We strive to maintain our dividend track record through sustainable annual dividend increases. We have increased our common share dividends each year since going public, with a 10% increase in 2017. Our decision to increase common share dividends by 9% to \$0.70 in 2018 reflects the strength of our financial position and confidence in our ongoing operating earnings and capital generation. 	<ul style="list-style-type: none"> Our operating performance and financial strength have translated into close to \$1.6 billion in capital returned to common shareholders through dividends and share repurchases over the past five years. Our BVPS was up 12% to \$48.00 in 2017, driven by EPS increase of 45%. We remained committed to our financial objectives in terms of ROE and NOIPS to enhance value to shareholders.

(in dollars)

Year	'05	'06	'07	'08	'09	'10	'11	'12	'13	'14	'15	'16	'17	'18
Dividend	0.16	0.25	0.27	0.31	0.32	0.34	0.37	0.40	0.44	0.48	0.53	0.58	0.64	0.70

(in dollars)

Year	'08	'09	'10	'11	'12	'13	'14	'15	'16	'17
BVPS	21.96	24.88	26.47	29.73	33.03	33.94	37.75	39.83	42.72	48.00

2004: Initial public offering on TSX (ING Group retained 70%).

BVPS

Table 18 – Evolution of BVPS (in dollars)

As at December 31,	Q4-2017	2017	2016	2015
BVPS, beginning of period	46.56	42.72	39.83	37.75
EPS	1.60	5.75	3.97	5.20
Dividends on common shares	(0.64)	(2.56)	(2.32)	(2.12)
Impact of market movements on AFS securities ¹	0.65	0.22	1.62	(1.26)
Net actuarial gains (losses) on employee future benefits ¹	(0.20)	(0.49)	(0.20)	0.27
NCIB and other	0.03	(0.23)	(0.18)	(0.01)
Impact from issuance of common shares	-	2.59	-	-
BVPS, end of period	48.00	48.00	42.72	39.83
Period-over-period increase	3%	12%	7%	6%

¹ Reported in AOCI.

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Section 12 – Social responsibility

We strive to create an environment where our employees live our values every day. Our values are organized according to five core themes, one being **Social responsibility**.



We respect the environment and its finite resources. We believe in making the communities where we live and work safer, healthier and happier. We encourage the involvement and citizenship of all our employees. Our commitment to social responsibility also serves as the mandate of the Intact Foundation, which principally donates to organizations that are committed to climate change adaptation and breaking the cycle of poverty for children in Canada.

Some of our 2017 programs and initiatives are outlined below.

12.1 Climate change adaptation

✓ *Intact Centre on Climate Adaptation*

The frequency and intensity of natural disasters has increased in recent years. At IFC, we remain committed to helping people protect themselves from extreme weather caused by climate change. Our investment in the Intact Centre on Climate Adaptation™ (“Intact Centre”) continues to foster innovative solutions to help reduce the physical, financial and social impacts of extreme weather on Canadian communities.

We have committed \$4.25 million over five years to establish the Intact Centre at the University of Waterloo, IFC’s most significant investment in addressing the impacts of climate change. Established in 2015, the Intact Centre is an applied research and climate resilience incubator with a national focus working with homeowners, communities, governments, and businesses to identify and reduce the impacts of extreme weather and climate change.

The Intact Centre has worked to establish a leading position on the climate change adaptation file in Canada.

2017 milestones include:

- Releasing two significant applied research reports to the Canadian public.
 - ***When big storms hit – the role of wetlands to limit urban and rural flood damage***: Developed in partnership with the Federal Ministry of Natural Resources and Forestry and charitable organization Ducks Unlimited, this research demonstrates that wetlands can reduce flood damages by up to 40%.
 - ***Preventing disaster before it strikes – developing a Canadian standard for new flood-resilient residential communities***: Developed in partnership with The Standards Council of Canada, this report identifies 20 best practices for designing new communities in Canada that are more flood-resilient. The development of a national standard for new flood-resilient residential communities is being developed based on this research.
- Members of the Intact Centre team either chair or are members of seven different domestic and international standards-setting committees to advance climate change adaptation. Most notably, Intact Centre head Dr. Blair Feltmate was appointed chair of the Government of Canada expert panel on climate change adaptation and resilience. The expert panel advises the Government of Canada on progress measurement on national climate adaptation and resilience initiatives, including supporting climate-smart infrastructure and updating building codes.
- In August 2017, the Intact Centre launched the pilot Home Flood Protection Program (“HFPP”) in the Greater Toronto Area in Ontario. The HFPP is an on-site flood-risk evaluation service for homeowners. A trained assessor and the homeowner review 50 points of potential water entry into the home.

Read more on the following websites:

<http://www.intactcentreclimateadaptation.ca/programs/>

<http://www.intactcentreclimateadaptation.ca/about/climate-change-adaptation-project-canada/>

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✓ *Managing the impacts of climate change*

Climate change in Canada has resulted in a higher frequency of severe weather events and unpredictable weather patterns. In particular, our property insurance business has been impacted and increased in the cost of claims associated with severe storms: water damage alone accounts for 40% of total claims. As a result, we have launched several initiatives in home insurance to adapt the nature of the product offered and its pricing. We are also reinforcing our claims capabilities, increasing our education awareness efforts towards distribution partners and customers and offering prevention discounts.

There are five areas where managing the impacts of climate change is integrated into IFC's business:

- **Underwriting:** determine the risk drivers related to our new climate realities.
- **Pricing:** reflects the scope of risks related to climate change impacts.
- **Claims Management:** ensure claims can be managed efficiently and effectively across Canada. For example, IFC has designated teams in place across the country that deal efficiently with catastrophic events and ensure service reliability for customers.
- **Reinsurance:** we re-insure certain risks to limit our losses in the event of catastrophic events or other significant losses. *See Section 15.2 – Reinsurance for more details.*
- **Outreach & Education:** we believe it is essential that Canadians adapt to climate change. As a result, we have launched many home insurance initiatives to help customers understand how to adapt. We continue to work with partners, such as the Intact Centre and the Insurance Bureau of Canada, to promote climate change adaptation initiatives to governments, including the development of tools for communities to assess the vulnerabilities of their infrastructure to climate change and prioritize investments in their modernization. By intensifying our education efforts and creating greater awareness of the risks our country faces and the preventative measures that we can adopt, we help Canadians adapt to severe weather caused by climate change.

Climate change risk management is part of the mandate of the risk management committee, which includes:

- reviewing the reports of the Chief Risk Officer on risk management, reinsurance programs, implementation plans, actuary and progress reports;
- the risk matrix identifying the top 10 enterprise risks (including the occurrence and severity of natural disasters that may be affected by climate change) and the emerging risks;
- reviewing catastrophe programs, exposure management tests and action plans;
- reviewing and approving the reinsurance risk management policy; and
- remaining informed of climate change adaptation and risk mitigation measures for the Canadian marketplace.

✓ *Intact Foundation climate change grants*

In 2017, the Intact Foundation introduced a new granting program, focused on funding climate change adaptation projects in communities across Canada in three arenas: developing community action plans, implementing resiliency projects, and finding new innovations to advance climate change resilience in Canada. Eight projects were selected for funding, receiving a collective \$1 million investment in climate change adaptation across the country. Selected partners include the University of Alberta, Ducks Unlimited, and Bluenose Coastal Action Committee.

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12.2 Social responsibility

✓ *Making our communities safer, healthier, and happier*

- IFC and the Intact Foundation contributed over \$3.7 million to charitable initiatives across Canada.
- Employees across Canada have donated over 6,500 hours through team volunteering initiatives and personal volunteer hours throughout the year.
- The Intact Foundation introduced a new "skills for impact" program, matching employee professional skills to help with projects of Intact Foundation charitable partners in 2017.
- Intact employees generously donated over \$1.3 million towards United Way/Centraide organizations nationally, supporting initiatives which help children living in poverty in our communities across the country.

✓ *Supporting women in their leadership development*

We were honoured by La Gouvernance au Féminin, a Québec-based not-for-profit organization that supports women in their leadership development, career enhancement and access to board seats, with the Certification of Parity for our actions towards the advancement of women in business. Intact was also one of the three companies that achieved platinum level certification in recognition of our commitment to advancing the cause of women.



12.3 Good governance

✓ *Intact receives top marks for good governance in Canada*

Along with being a best employer and having customers as advocates, we also strive to be recognized as one of the most respected companies in Canada. In the Globe and Mail's 2017 Board Games, we continue to advance this objective with top marks for corporate governance. Board Games looks at over 50 different corporate governance practices in four broad subcategories related to board composition, compensation, shareholder rights and disclosure. Out of 242 companies, Intact ranked second. We improved from the previous year and ranked among top Canadian companies in the annual Board Games results. This goes a long way in validating that Intact is consistently striving for excellence, one of our core values. The Board Games report measures the quality of governance practices of all S&P/TSX composite index companies.

Well-governed companies usually outperform other companies, and are able to attract investors whose support can help finance further growth.

More ESG information can be found in our 2017 Social Impact Report.

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(in millions of Canadian dollars, except as otherwise noted)

FINANCIAL CONDITION

Section 13 – Financial position

2017 Highlights

Investment portfolio	BVPS for the last 12 months	Debt-to-total capital ratio	Total capital margin ¹
\$16.9 billion	+12%	23.1%	\$1.1 billion

13.1 Balance sheets

On September 28, 2017 we acquired all of the outstanding shares of OneBeacon for US\$1.7 billion (\$2.3 billion). The amounts recognized for the assets acquired and liabilities assumed at the acquisition date are presented below in Canadian dollars.

Table 19 – Balance sheets

As at	Section	OneBeacon Sept. 28, 2017 (closing date)	Total IFC Dec. 31, 2017	Total IFC Dec. 31, 2016
Assets				
Investments	14	3,383	16,853	14,386
Premium receivables		343	3,351	3,057
Reinsurance assets	15	358	822	482
Deferred acquisition costs		108	881	747
Other assets		366	1,618	1,489
Intangible assets and goodwill		1,560	4,403	2,705
Total assets		6,118	27,928	22,866
Liabilities				
Claims liabilities	15	2,038	10,475	8,536
Unearned premiums		813	5,365	4,573
Financial liabilities related to investments		18	246	529
Other liabilities		557	2,138	1,747
Debt outstanding	17	364	2,241	1,393
Total liabilities		3,790	20,465	16,778
Shareholders' equity				
Common shares	17		2,816	2,082
Preferred shares			783	489
Contributed surplus			128	129
Retained earnings			3,520	3,197
AOCI			216	191
Shareholders' equity			7,463	6,088
Book value per share (in dollars)	11.4		48.00	42.72

¹ Aggregate of capital in excess of CALs in regulated entities plus available cash in unregulated entities (see Section 18.2 – Capital position).

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Section 14 – Investments

Our investment portfolio is mainly comprised of Canadian and U.S. securities. Our invested assets increased to \$16.9 billion as at December 31, 2017 largely due to the OneBeacon acquisition.

- Our Canadian investment portfolio comprises principally Canadian securities and includes a mix of cash and short-term notes, fixed-income securities, preferred shares, common shares and loans.
- Our U.S. investment portfolio is comprised of fixed-income securities (mainly asset-backed securities and corporate bonds) and U.S. common shares.

Table 20 – Investments by asset class

As at December 31,	2017	2016
Cash, cash equivalents and short-term notes	380	273
Fixed-income securities	11,012	8,696
Preferred shares	1,409	1,377
Common shares	3,659	3,635
Loans	393	405
	16,853	14,386

The following tables show the economic exposure of our investment portfolio after reflecting the impact of hedging strategies related to investments.

Net exposure by asset class

As part of our investment strategies, from time to time we take long/short equity positions in order to maximize the value added from active equity portfolio management, or to mitigate overall common share market volatility. We also use strategies where market risk from long common share positions is reduced through the use of swap agreements or other hedging instruments.

On a consolidated basis, the acquisition of OneBeacon does not significantly change our net investment mix by asset class, although OneBeacon's product mix within asset classes, especially fixed-income, differed from Intact's (Canada) as at December 31, 2017. The OneBeacon portfolio is mainly comprised of fixed-income securities (including highly rated asset- and mortgage-backed securities and BBB Corporate bonds) and U.S. equities.

Table 21 – Investment mix by asset class (net exposure)

As at December 31,	2017	2016
Cash, cash equivalents, and short-term notes	4%	3%
Fixed-income	72%	70%
Preferred shares	8%	10%
Common equities	14%	14%
	98%	97%
Loans	2%	3%
	100%	100%

Net currency exposure

Table 22 – Investment portfolio – currency (net exposure)

As at December 31,	2017	2016
CAD	79%	95%
USD	19%	5%
Other	2%	-%
	100%	100%

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Our U.S. fixed-income portfolio held in our Canadian P&C entities (\$1,284 million) is hedged using foreign-currency forward contracts, resulting in minimal currency gains or losses on this portfolio.

Net sectoral exposure

Table 23 – Sector mix by asset class, excluding cash, short-term notes and loans (net exposure)

As at December 31,	Fixed-income securities	Preferred shares	Common shares	Total 2017	Total 2016
Government	47%	-	-	33%	41%
Financials	22%	77%	29%	33%	36%
ABS and MBS	15%	-	-	11%	1%
Energy	1%	12%	15%	4%	5%
Industrials	3%	-	11%	4%	3%
Consumer staples	3%	-	8%	3%	3%
Telecommunication	1%	-	6%	1%	1%
Utilities	1%	11%	7%	3%	2%
Consumer discretionary	2%	-	8%	3%	2%
Materials	1%	-	6%	1%	1%
Information technology	2%	-	6%	2%	3%
Health care	2%	-	4%	2%	2%
	100%	100%	100%	100%	100%

Our fixed-income portfolio remains concentrated in the government and financial sectors providing liquidity and stability to our balance sheet.

Our fixed-income portfolio has more structured debt securities, following the OneBeacon acquisition. As at December 31, 2017, these securities comprised \$987 million of asset-backed securities ("ABS") and \$715 million of mortgage-backed securities ("MBS"). Residential MBS ("RMBS") and Commercial MBS ("CMBS") make up respectively 53% and 47% of our MBS portfolio. Approximately 95% of these securities are rated A or better.

We continue to have no exposure to leveraged securities.

High-quality investment portfolio

Fixed income

Our fixed-income portfolio includes high quality government and corporate bonds. Approximately 90% of our fixed-income portfolio was rated 'A-' or better as at December 31, 2017 (98% as at December 31, 2016).

On a consolidated basis, the weighted-average rating of our fixed-income portfolio was 'AA', ('AA+' at December 31, 2016). The decrease in the rating of the fixed-income securities reflected the impact of the OneBeacon investment portfolio. The average duration of our fixed-income portfolio was 3.53 years (4.02 years as at December 31, 2016), reflecting the acquisition of OneBeacon.

Table 24 – Credit quality of fixed-income securities¹

As at December 31,	2017	2016
Fixed-income securities		
AAA	41%	46%
AA	28%	36%
A	21%	16%
BBB	8%	2%
BB and not rated	2%	-
	100%	100%

¹ Source: S&P, DBRS and Moody's.

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Preferred shares

Table 25 – Credit quality of preferred shares¹

As at December 31,	2017	2016
P1	-	-
P2	79%	79%
P3	21%	21%
	100%	100%

¹ Source: S&P, DBRS and Moody's.

Our preferred share portfolio is made up of high-quality Canadian issuers. The weighted-average rating of our preferred share portfolio was 'P2' as at December 31, 2017 and 2016.

Net pre-tax unrealized gain (loss) on AFS securities

In determining the fair value of investments, we rely on quoted market prices. In cases where an active market does not exist, the estimated fair values are based on recent transactions or current market prices for similar securities.

Table 26 – Net pre-tax unrealized gain (loss) on AFS securities

As at	December 31, 2017	Sept. 30, 2017	June 30, 2017	March 31, 2017	December 31, 2016
Fixed-income securities	22	25	69	93	83
Preferred shares	79	40	33	26	(67)
Common shares	212	124	114	194	253
Net pre-tax unrealized gain position	313	189	216	313	269

Dec. 31, 2017 vs Sept. 30, 2017	Dec. 31, 2017 vs 2016
<p>Our pre-tax unrealized gain position increased by \$124 million due to:</p> <ul style="list-style-type: none"> mark-to-market gains on common shares and preferred shares, reflecting strong North American equity markets. <i>See Section 6.8 – Capital markets for more details.</i> 	<p>Our pre-tax unrealized gain position rose by \$44 million due to:</p> <ul style="list-style-type: none"> an increase in preferred share prices, reflecting strong equity markets and the impact of higher interest rates on the price of rate-reset preferred shares; lower bond prices, reflecting higher interest rates; and realized gains on our AFS common share portfolio. Realized and unrealized gains (total comprehensive return) on AFS equities in 2017 reflected strong equity markets.

Gains and losses in the common share portfolio are generally realized on an ongoing basis under normal capital market conditions.

Impairment recognition on AFS common shares

Table 27 – Aging of unrealized losses on AFS common shares

As at	Dec 31, 2017	Sept 30, 2017	June 30, 2017	March 31, 2017	Dec 31, 2016
Less than 25% below book value	34	48	41	23	14
More than 25% below book value for less than 6 consecutive months	4	2	27	6	2
More than 25% below book value for 6 consecutive months or more, but less than 9 consecutive months	13	24	7	4	4
Unrealized losses on AFS common shares	51	74	75	33	20

Impairment losses on AFS common shares amounted to \$20 million in 2017, compared to \$41 million in 2016. Assuming no change in equity markets from December 31, 2017, impairment losses of \$17 million would be recognized in 2018. Since common shares are measured at fair value on the Company's balance sheet, impairment losses would have no impact on our BVPS. *Refer to Note 2 – Summary of significant accounting policies of the accompanying Consolidated financial statements for additional details on our accounting policy regarding the impairment of financial assets.*

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Section 15 – Claims liabilities and reinsurance

15.1 Claims liabilities

Assumptions

Claims liabilities increased to \$10.5 billion as at December 31, 2017, mainly due to the impact of the acquisition of OneBeacon.

The main assumption underlying the claims liability estimates is that our future claims development will follow a similar pattern to past claims development experience. Claims liability estimates are also based on various quantitative and qualitative factors, including:

- average claims cost, including claim handling costs (severity);
- average number of claims by accident year (frequency);
- trends in claims severity and frequency;
- payment patterns;
- other factors such as inflation, expected or in-force government pricing and coverage reforms, and level of insurance fraud;
- discount rate; and
- risk margin.

The total claims reserve is made up of two main elements:

- 1) reported claims case reserves, and
- 2) incurred but not reported ("IBNR") reserves.

IBNR reserves supplement the case reserves by taking into account:

- possible claims that have been incurred but not yet reported to us by policyholders;
- expected over/under estimation in case reserves based on historical patterns; and
- other claims adjustment expenses or subrogation amounts not included in the initial case reserve.

Case reserves and IBNR should be sufficient to cover all expected claims liabilities for events that have already occurred, whether reported or not, taking into account the time value of money, using a rate that reflects the estimated market yield of the underlying assets backing these claims liabilities. IBNR and risk margin are reviewed and adjusted at least quarterly.

The discount is applied to the total claims reserve and adjusted on a regular basis for changes in market yields. If market yields rise, the discount would increase and reduce total claims liabilities and, therefore, positively impact underwriting income in that period, all else being equal. If market yields decline, it would have the opposite effect.

See Section 26 – Non-operating results for more details on the impact of MYA on underwriting.

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Q3-2017 net reserve change

As a result of the acquisition of OneBeacon on September 28, 2017, we harmonized our accounting and actuarial practices as required under IFRS. With operations in Canada and the U.S., we reviewed our approach to determine the risk margin at the consolidated level to align the methodology applied to both countries using results from our economic capital model. The model reflects the benefit of risk diversification between lines of business and geographies. Diversification reduces the uncertainty associated with the unfavourable development of claims liabilities for both our Canadian and U.S. operations. This refinement in estimate recognized in Q3-2017 resulted in a decrease in net claims of \$196 million for our Canadian operations. *See Note 3 and Note 10 to the accompanying Consolidated Financial Statements for details.*

During Q3-2017, following an extensive file-by-file and actuarial reviews at the portfolio level, we took a more cautious reserve position reflecting uncertainty, mainly in personal auto, leading to an increase in claims liabilities.

Overall, the above-mentioned reserve changes (referred to as “**Q3-2017 net reserve change**”) had a favourable impact of 0.7 points on the combined ratio for YTD Q3-2017. The net estimated impact on the combined ratio by line of business was as follows:

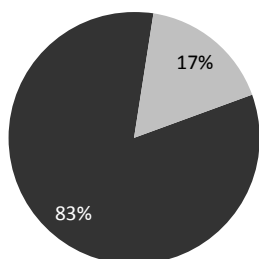
Table 28 – Net estimated impact by line of business

	YTD Q3-2017
P&C Canada	
Personal auto	0.8 pts
Personal property	(0.7) pts
Commercial lines	(2.8) pts
Total unfavourable (favourable) impact	(0.7) pts

OneBeacon claims liabilities have been recorded at fair value at closing and reflected the impact of the conversion to IFRS, including discounting and risk margin. Risks associated with these claims liabilities have been mitigated by the purchase of an adverse development coverage (ADC) from a major reinsurer. The determination of the risk margin also takes into account the reduced volatility resulting from this coverage (*see Section 15.4 – Reinsurance*).

Net claims liabilities by business segment

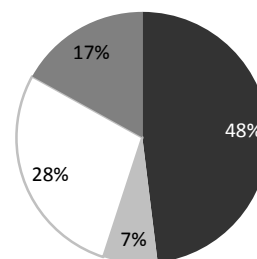
■ P&C Canada ■ P&C U.S.



Diversification reduces the uncertainty associated with the unfavourable development of claims liabilities for both our Canadian and U.S. operations.

Net claims liabilities by line of business

■ PA ■ PP □ CL CAN ■ CL U.S.



PA: Personal auto; PP: Personal property; CL: Commercial lines

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Prior year developments

PYD can fluctuate from quarter to quarter and year to year and, therefore, should be evaluated over longer periods of time.

In the past five years, favourable PYD as a percentage of opening reserves ranged between 3% to 6% per year for our Canadian operations, higher than our long-term historical averages.

We expect the average favourable PYD as a percentage of opening reserves to be in the 2%-4% range over the long term. Higher interest rates will trend PYD around the lower end of this range, with an offset in the CAY loss ratio.

Annualized rate of favourable PYD – P&C Canada
(as a % of opening reserves)

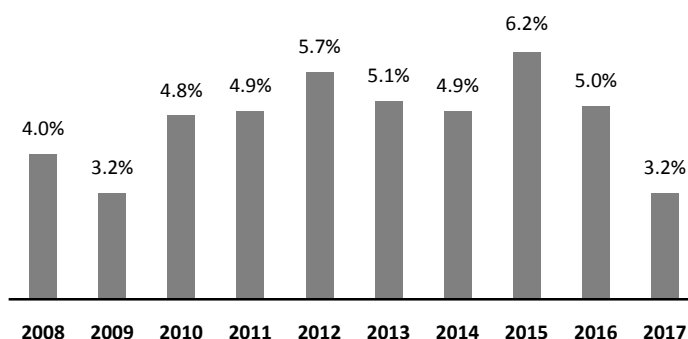


Table 29 – Unfavourable (favourable) PYD

	2017	2016	2015	2014	2013	5-year average P&C Canada	
						In \$	% NEP
PYD	(238)	(389)	(477)	(364)	(374)		
P&C Canada	(253)	(389)	(477)	(364)	(374)	(371)	(4.9)%
By line of business							
Personal auto	10	(115)	(212)	(141)	(188)	(129)	(1.7)%
Personal property	(62)	(88)	(70)	(71)	(65)	(71)	(0.9)%
Commercial lines – Canada	(201)	(186)	(195)	(152)	(121)	(171)	(2.3)%
Commercial lines – U.S.	15	n/a	n/a	n/a	n/a	n/a	n/a
By quarter							
Q1	(82)	(163)	(189)	(141)	(110)	(137)	(1.8)%
Q2	(41)	(93)	(106)	(65)	(95)	(80)	(1.1)%
Q3	(53)	(71)	(107)	(80)	(103)	(83)	(1.1)%
Q4	(62)	(62)	(75)	(78)	(66)	(71)	(0.9)%

Table 30 – PYD by line of business

	Q4-2017	Q4-2016	Change	2017	2016	Change
By line of business						
Personal auto	(27)	(13)	(14)	10	(115)	125
Personal property	(17)	(13)	(4)	(62)	(88)	26
Commercial lines – Canada	(33)	(36)	3	(201)	(186)	(15)
Commercial lines – U.S.	15	-	15	15	-	15
Total unfavourable (favourable) development	(62)	(62)	-	(238)	(389)	151
Unfavourable (favourable) annualized rate of PYD¹						
P&C Canada	(3.8)%	(3.2)%	(0.6) pts	(3.2)%	(5.0)%	1.8 pts
P&C U.S.	3.0%	-	nm	3.0%	-	nm
Consolidated	(2.5)%	(3.2)%	0.7 pts	(1.9)%	(5.0)%	3.1 pts

¹ As a % of opening reserves for P&C Canada and as at the closing date for P&C U.S. (OneBeacon).

Q4-2017 vs Q4-2016

2017 vs 2016

- Favourable PYD of \$62 million reflected positive development in all lines of business in Canada and unfavourable development in the U.S.
- Unfavourable PYD in the U.S. included our share of prior year losses and the impact of discounting on the amount recoverable from the ADC.
- Favourable PYD of \$238 million was below last year, mainly on unfavourable development in personal auto.

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15.2 Reinsurance

In the ordinary course of business, we reinsure certain risks with other reinsurers to limit our maximum loss in the event of catastrophic events or other significant losses. Our objectives related to ceded reinsurance are capital protection, reduction in the volatility of results, increase in underwriting capacity and access to the expertise of reinsurers. The placement of ceded reinsurance is done almost exclusively on an excess-of-loss basis (per event or per risk). Ceded reinsurance complies with regulatory guidelines. Furthermore, the reinsurance treaties call for timely reimbursement of ceded losses.

Because of the importance of the catastrophe program in place, a certain level of concentration exists with high-quality reinsurers, but diversification of reinsurers remains a key element and is analyzed and implemented to avoid excessive concentration in a specific reinsurance group. A single catastrophe event such as an earthquake could financially weaken a reinsurer, so distribution of risk is an important reinsurance strategy for us.

Annually, we review and adjust our reinsurance coverage as well as our net retention of risks in order to reflect our current exposures and our capital base. For multi-risk events and catastrophes, the coverage limits are well in excess of the regulatory requirements with respect to the earthquake risk as per our conservative approach.

Canadian operations

Table 31 – Reinsurance net retention and coverage limits by nature of risk

As at December 31	2017	2016
Single risk events		
Retentions:		
on property policies	7.5	7.5
on liability policies	3 - 10	3 - 10
Multi-risk events and catastrophes		
Retention	100	100
Coverage limits	3,600	3,575

For certain special classes of business or types of risks, the retention for single risk events may be lower through specific treaties or the use of facultative reinsurance. For multi-risk events and catastrophes, we retain participations averaging 5.1% as at December 31, 2017 (December 31, 2016 – 5.3%) on reinsurance layers between the retention and coverage limit. The coverage limit prudently exceeds our risk assessment of an earthquake in Western Canada at a 1-in-500 year return period.

In line with industry practice, our reinsurance recoverables with licensed Canadian reinsurers (\$227 million as at December 31, 2017, \$388 million as at December 31, 2016) are generally unsecured as Canadian regulations require these reinsurers to maintain minimum asset and capital balances in Canada to meet their Canadian obligations, and claims liabilities take priority over the reinsurer’s subordinated creditors. We have collateral in place to support amounts receivable and recoverable from unregistered reinsurers.

U.S. operations

As at December 31, 2017, our newly acquired U.S. operations are covered by its own reinsurance program for single risk events but also for multi-risk events and catastrophes. Under the property catastrophe reinsurance program, the first US\$20 million of losses resulting from any single catastrophe are retained, with the coverage limit for the next US\$110 million of losses being entirely reinsured. In addition to the corporate catastrophe reinsurance protection, we also have dedicated reinsurance protection for certain lines of business. Among these, the retention for single risk events is US\$3 million on property policies and main liability policies.

In connection with the acquisition of OneBeacon, we entered into a reinsurance contract pursuant to which a major reinsurer will assume 80% of negative reserve development with respect to OneBeacon's claims liabilities for accident years 2016 and prior. The purchase of this adverse development coverage (“ADC”) has reduced the potential volatility in our prior years claims liabilities and resulted in a release of risk margin in 2017. The maximum amount recoverable under the ADC is US\$200 million and is subject to some exclusions and limitations.

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(in millions of Canadian dollars, except as otherwise noted)

Section 16 – Employee future benefit programs

We sponsor a number of funded and unfunded defined benefit pension plans in Canada that provide benefits to members in the form of a guaranteed level of pension payable for life based on final average earnings and contingent upon certain age and service requirements. We provide active employees in Canada a choice between a defined benefit and a defined contribution pension plan. We offer employees in the U.S. a 401(k) plan.

Benefit obligations arising from our defined benefit plans are dependent on assumptions, such as the discount rate, life expectancy of pensioners, inflation and rate of compensation increase.

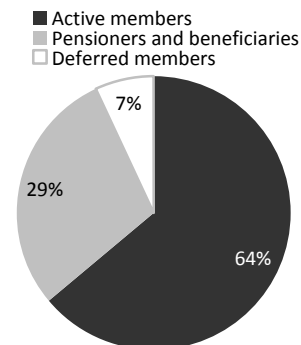
Because of the long-term nature of our pension obligations, movements in discount rates and investment returns could bring volatility in our balance sheet. In the past few years, we have taken a multi-faceted approach to ensure the sustainability of our pension plans and gradually reduced the risk and volatility that stems from our pension liabilities and assets, including:

- increasing the target allocation of fixed-income securities to reduce our exposure to market volatility;
- improving our pension asset-liability matching to reduce our interest-rate exposure;
- adding inflation sensitive assets;
- making voluntary contributions to improve the funding status of our pension plans; and
- amending pension plan benefits and conditions.

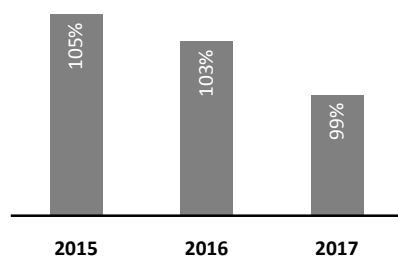
We regularly monitor the risks inherent in our defined benefit pension plans on an asset-liability basis. We continue to evaluate various alternatives to better manage the risk related to these plans.

Refer to Note 26 – Employee future benefits of the accompanying Consolidated financial statements for details on actuarial gains and losses recognized in OCI, assumptions used and sensitivity analysis, as well as risk management and investment strategy.

Defined benefit obligation
(as at the date of the latest actuarial valuation)

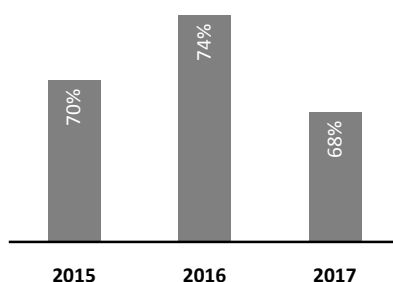


Funding ratio



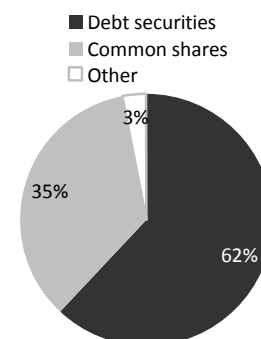
Our pension plans remained well funded as at December 31, 2017. The lower funding ratio was driven by a decrease in discount rates.

Interest rate hedge ratio



Hedge ratio down to 68%, driven by the increase in long-term interest rates.

2017 pension plan asset mix



Pension plan asset mix is essentially unchanged from 2016.

Funding ratio: Plan assets as a percentage of funded plans’ obligations.

Interest rate hedge ratio: The duration of the pension asset portfolio divided by the duration of the registered pension plans’ obligation. Our objective is to remain in a modest range around our pension fund investment policy target of 70%, assuming the funding ratio is 100%.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 17 – Treasury management

17.1 Financing structure

2017 Financing structure

Debt-to-total capital ratio	Weighted-average debt maturity	Weighted-average debt coupon	Weighted-average preferred share coupon
23.1%	12 years	3.39% (after tax)	4.07% (after tax)

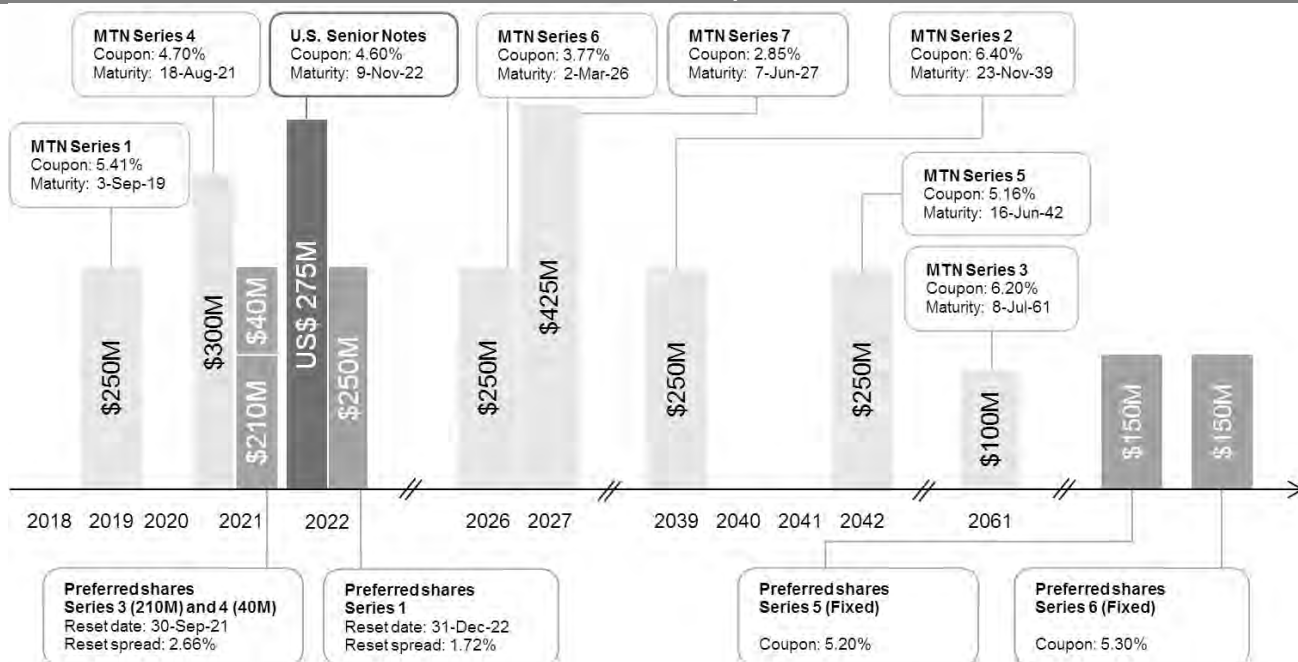
Evolving in an international context, we ensure that we are able to access funds in multiple currencies. With respect to financing, we believe that our optimal financing structure is one where the debt-to-total capital ratio is generally at or below 20%, all currency combined. The debt-to-total capital ratio may on occasion exceed 20% with a firm plan to revert back to 20% within a short period of time. Our debt-to-total capital ratio increased to 24.7% following the acquisition of OneBeacon at the end of September 2017, and decreased to 23.1% as at December 31, 2017 (18.6% as at December 31, 2016). Our debt-to-total capital ratio is expected to return to 20% within 24 months following the closing of the acquisition.

We have a diversified maturity profile with reasonable levels of debt and preferred shares, which improves our overall cost of capital:

- We currently have seven series of medium-term notes outstanding with maturities ranging between 2 and 44 years.
- The notes carry a weighted average coupon of 4.61% (3.39% after tax).
- All debt tranches are prudent in size with no large peaks, reducing financing risk.
- Preferred shares provide flexibility in our capital structure at a reasonable cost.
- Debt and preferred shares represent about 30% of our total capital structure.

Our notes and preferred shares are presented in the table below.

Finance structure – Notes and preferred shares



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(in millions of Canadian dollars, except as otherwise noted)

Credit facility

At closing of the acquisition, to maintain financial flexibility, we increased the size of our credit facility from \$300 million to \$750 million. We also extended the access to our unsecured revolving term credit facility to OneBeacon and cancelled the credit facility they had in place. Our five-year credit facility matures on August 28, 2022 and may be drawn as follows:

<u>Type:</u>	<u>At a rate of:</u>
Prime loans	Prime rate plus a margin
Base rate (Canada) advances	Base rate plus a margin
Bankers’ acceptances	Bankers’ acceptance rate plus a margin
Libor advances	Libor rate plus a margin

The outstanding balance under our credit facility amounted to \$60 million as at December 31, 2017 at an interest rate of 2.62% (nil as at December 31, 2016).

As part of the covenants under the credit facility, we are required to maintain certain financial ratios, which were fully met as at December 31, 2017 and 2016.

Base shelf prospectus

On November 15, 2017, we filed a final short form base shelf prospectus with the securities regulatory authorities in each of the provinces and territories of Canada that will allow us to offer up to \$7.0 billion in any combination of debt, preferred shares or common share securities, subscription receipts, warrants, share purchase contracts and units over the following 25 months. We also filed a supplement to our base shelf prospectus to establish a medium-term note program that would allow us to issue up to \$1.7 billion in unsecured medium-term notes. As at December 31, 2017, the amounts available under the respective prospectuses were \$7.0 billion and \$1.7 billion, respectively.

Preferred shares rate reset

On December 1, 2017, we announced that we did not intend to exercise our right to redeem our Non-cumulative Rate Reset Class A Series 1 Preferred Shares (“Series 1 Preferred Shares”) on December 31, 2017. On December 18, 2017, we also announced that, after having taken into account all elections received before the conversion deadline with respect to the Series 1 Preferred Shares tendered for conversion on December 31, 2017 into non-cumulative Floating rate Class A Series 2 Preferred Shares (“Series 2 Preferred Shares”), the holders of Series 1 Preferred Shares were not entitled to convert their shares as the amount of shares elected for conversion did not meet the minimum threshold requirement. Subject to certain conditions on December 31, 2022 and on December 31 every five years thereafter, the holders of Series 1 Preferred Shares will have the right to convert their shares into Series 2 Preferred Shares. In addition, we have the option to redeem the Series 1 and Series 2 Preferred Shares on the same dates.

17.2 Ratings

Independent third party rating agencies assess our insurance subsidiaries’ ability to meet their ongoing policyholder obligations (“financial strength rating”) and our ability to honour our financial obligations (“senior unsecured debt rating”). Ratings are an important factor in establishing our competitive position in the insurance market, mainly in commercial insurance, and accessing capital markets at competitive pricing levels.

Shortly after the closing of the OneBeacon acquisition, Moody’s and Fitch upgraded the financial strength rating and the senior unsecured debt rating of OneBeacon and OneBeacon’s U.S. regulated entities (consolidated under Atlantic Specialty Insurance Company) respectively. A.M. Best upgraded the senior unsecured debt rating of OneBeacon and reaffirmed the financial strength rating its of U.S. regulated entities. Ratings of IFC and its principal Canadian P&C insurance subsidiaries were reaffirmed by A.M. Best, DBRS, Moody’s and Fitch in the context of the acquisition of OneBeacon.

Table 32 – Ratings

	A. M. Best	DBRS	Moody’s	Fitch
Financial strength ratings				
IFC’s principal Canadian P&C insurance subsidiaries	A+	AA(low)	A1	AA-
OneBeacon U.S. regulated entities	A		A2	AA-
Senior unsecured debt ratings				
IFC	a-	A	Baa1	A-
OneBeacon	bbb+		Baa2	A-

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

17.3 OneBeacon acquisition financing

The acquisition of OneBeacon closed on September 28, 2017 and was financed using a combination of:

- common equity financing (\$754 million);
- medium-term notes (\$425 million);
- preferred shares (\$300 million); and
- credit facility and excess capital.

Refer to Note 18 – Debt outstanding and Note 19 – Common shares and Preferred shares to the accompanying Consolidated financial statements for more details.

17.4 Currency management

We manage our cash flow and book value exposure to U.S. dollar currency volatility.

OneBeacon purchase price hedge

As at May 2, 2017 (date of the announcement), we hedged the purchase price exposure to fluctuations of the CAD/USD exchange rate by entering into currency derivatives to effectively lock the CAD equivalent purchase price at \$2.3 billion. These derivatives qualified as cash flow hedges and were marked-to-market through OCI until closing. At closing, currency losses accumulated in AOCI amounting to \$200 million were included in the purchase price of OneBeacon.

Book value exposure

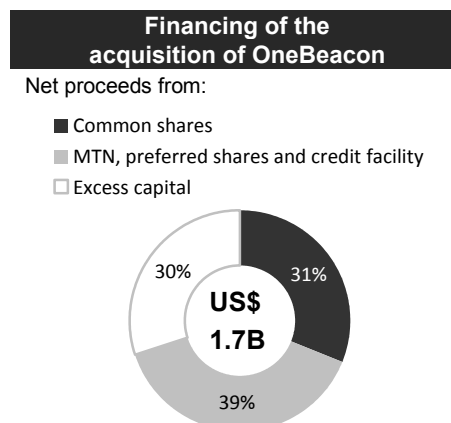
Our objective is to benefit from currency diversification, while managing the impact of USD volatility on our book value. Foreign currency derivative contracts, such as currency swaps and forwards, are used as risk management tools.

- On May 2, 2017, we entered into foreign currency forward contracts for a notional amount of US\$600 million to reduce the book value exposure of our USD denominated assets relative to the CAD, including OneBeacon. These derivatives represented economic hedges and were marked-to-market through net income up to closing of the OneBeacon acquisition.
- At closing, we designated these forward contracts as a net investment hedge of our foreign operation, OneBeacon. On December 20, 2017, we terminated half of the US\$600 million hedging relationship so that US\$300 million foreign currency forward contracts would be marked-to-market through net income partially offsetting the currency impact of USD denominated investments also going through net income. This left US\$300 million contracts as net investment hedge of our foreign operations as at December 31, 2017.
- Since closing, gains or losses on this hedge, together with foreign exchange translation gains or losses on the net investment in OneBeacon are recognized in OCI.

Our net currency exposure to the USD (net of derivatives) was US\$1,452 million as at December 31, 2017 (US\$415 million as at December 31, 2016). *Refer to Note 9.1 b) – Exposure to currency risk of the accompanying Consolidated financial statements for more details.*

Cash flow exposure

USD inflows from OneBeacon will be used to pay U.S. dollar denominated claims and expenses in connection with our Canadian operations. Any remaining exposure is managed using foreign currency derivative contracts such as currency swaps and forwards.



Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

17.5 Understanding our cash flows

Cash inflows from operating activities mainly consist of insurance premiums and investment income. Cash inflows in excess of required outflows are deployed in our investment portfolio to generate additional investment income in the future.

Table 33 – Cash flows

	Q4-2017	Q4-2016	Change	2017	2016	Change
Cash flows from operating activities	23	153	(130)	781	925	(144)
Cash flows deployed on:						
Business combinations	-	(19)	19	(2,139)	(19)	(2,120)
Equity investments in brokerages and other, net	(25)	(38)	13	(108)	(275)	167
Purchases of intangibles and P&E, net	(24)	(30)	6	(98)	(120)	22
Dividends	(99)	(80)	(19)	(378)	(324)	(54)
Share-based payments in shares	(4)	-	(4)	(37)	(19)	(18)
NCIB (see Section 29.3)	-	(7)	7	(7)	(44)	37
Cash flows generated from: (see Section 17.3)						
Issuance of common shares	-	-	-	731	-	731
Issuance of medium-term notes	-	-	-	422	248	174
Issuance of Class A Preferred shares	-	-	-	292	-	292
Amount drawn (repaid) under our credit facility	(150)	-	(150)	60	-	60
Cash flow available for investment activities¹	(279)	(21)	(258)	(481)	372	(853)
Excess capital deployed on OneBeacon acquisition	-	-	-	660	-	660
Other net investment sales (purchases)	(76)	52	(128)	(184)	(345)	161
Net increase (decrease) in cash and cash equivalents	(355)	31	(386)	(5)	27	(32)

¹ A non-IFRS financial measure which includes net cash flows from cash and cash equivalents and the investment portfolio.

Liquidity generated by the issuance of common shares, medium-term notes, Class A Preferred shares, drawdown on our credit facility, together with a portion of the net investment sales, was used to finance the OneBeacon acquisition.

17.6 Contractual obligations

The table below presents the expected timing of contractual liquidity requirements as at December 31, 2017.

Table 34 – Contractual obligations

	Total	Payments due by period			
		Less than 1 year	1 - 3 years	3 - 5 years	Thereafter
Principal repayment on notes outstanding	2,181	-	250	664	1,267
Interest payments on notes outstanding	1,283	101	185	153	844
Claims liabilities ¹	10,410	4,139	2,857	1,606	1,808
Operating leases on premises and equipment	810	168	245	167	230
Pension obligations ²	48	8	16	7	17
Total contractual obligations	14,732	4,416	3,553	2,597	4,166

¹ Represents the undiscounted value and includes incurred but not reported reserves.

² These amounts represent the annual mandatory funding required by regulators, based on the latest actuarial valuations and expected benefit payments for unfunded plans.

We consider that we have sufficient capital resources, cash flows from operating activities and borrowing capacity to support our current and anticipated activities, scheduled principal and interest payments on our outstanding debt, the payment of dividends and other expected financial requirements in the near term.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 18 – Capital management

2017 Highlights

Total capital margin	MCT (Canada)	RBC (U.S.)
Over \$1.1 billion	205%	459%

18.1 Capital management objectives

Our objectives when managing capital consist of:

- maintaining strong regulatory capital levels (see Regulatory capital section below), while ensuring policyholders are well protected; and
- maximizing long-term shareholder value by optimizing capital used to operate and grow the Company.

We seek to maintain adequate capital levels to ensure that the probability of breaching the regulatory minimum requirements is very low. Such levels may vary over time depending on our evaluation of risks and their potential impact on capital. We also keep higher levels of excess capital when we foresee growth or actionable opportunities in the near term. Furthermore, we intend to return excess capital to shareholders through annual dividend increases and, when excess capital levels permit, through share buybacks.

Refer to Section 29 – Shareholder information for more details.

Regulatory capital

The amount of capital deployed in any particular company or country depends upon local regulatory requirements, as well as the Company’s internal assessment of capital requirements in the context of its risk profiles, requirements and strategic plans. The Company’s practice is to maintain the capitalization of its regulated operating subsidiaries at a level that will exceed the relevant minimum regulatory capital requirements in the jurisdictions in which they operate (referred to as regulator supervisory minimum levels).

Canada	<ul style="list-style-type: none"> • Our federally chartered Canadian P&C insurance subsidiaries are subject to the regulatory capital requirements defined by OSFI and the Insurance Companies Act, while our Québec provincially chartered subsidiaries are subject to the requirements of the AMF and the Act respecting insurance. • Federal and Québec regulated P&C insurers are required, at a minimum, to maintain a MCT ratio of 100%. • OSFI and the AMF have also established a regulator supervisory target capital ratio of 150%, which provides a cushion above the minimum requirement.
U.S.	<ul style="list-style-type: none"> • Our U.S. insurance operations are subject to regulation and supervision in each of the states where they are domiciled and licensed to conduct business. • State insurance departments have established the insurer solvency laws and regulatory infrastructure to maintain accredited status with the National Association of Insurance Commissioners ("NAIC"). • A key solvency-driven NAIC accreditation requirement is a state's adoption of RBC requirements. • Dividends from our major U.S. insurance subsidiary are subject to the New York Regulator’s prior approval for a two year period ending September 30, 2019.

Regulatory capital guidelines change from time to time and may impact our capital levels. We carefully monitor all changes, actual or proposed.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

18.2 Capital position

All our regulated P&C insurance subsidiaries were well capitalized on an individual basis with capital levels well in excess of regulator supervisory minimum levels, as well as Company action levels (CALs). CALs represent the thresholds below which regulator notification is required together with a company action plan to restore capital levels.

Table 35 – Estimated aggregated capital position

	December 31, 2017			September 30, 2017			December 31, 2016	
	Canada (MCT)	U.S. (RBC)	IFC capital margin	Canada (MCT)	U.S. (RBC)	IFC capital margin	Canada (MCT)	IFC capital margin
Regulatory capital ratios (RCRs)	205%	459%	-	201%	413%	-	218%	-
Industry-wide supervisory minimum levels	150%	150%	-	150%	150%	-	150%	-
CALs	170%	200%	-	170%	200%	-	170%	-
Capital above CALs (capital margin)	618	438	1,056	558	315	873	947	947
Other regulated/unregulated entities ¹			79			282		23
Total capital margin			1,135			1,155		970

¹ Other regulated entities include Split Rock Insurance, Ltd. (Bermuda) and IB Reinsurance Inc. (Barbados).

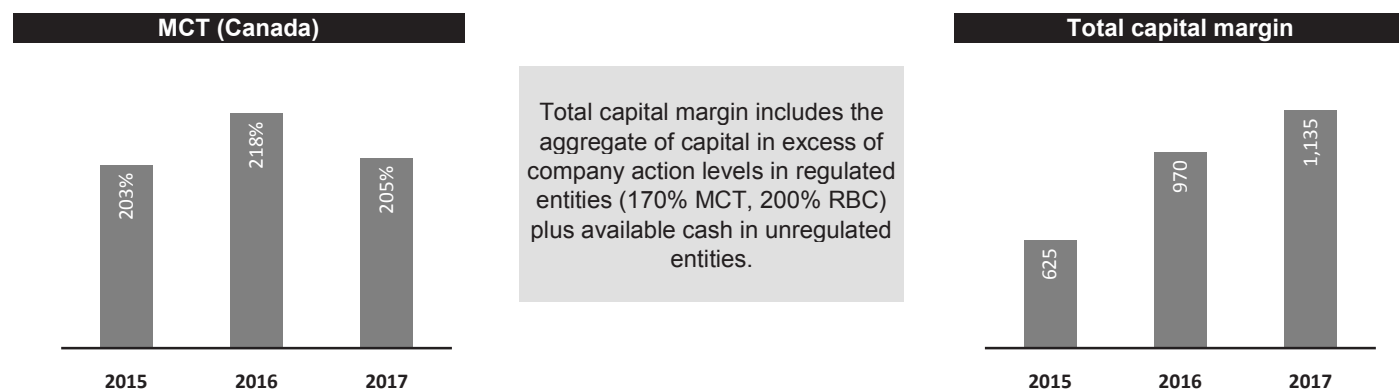
U.S. capital levels comprise the RBC levels of OneBeacon’s U.S. regulated entities, consolidated in Atlantic Specialty Insurance Company (ASIC). As at December 31, 2017, ASIC’s risk based capital (RBC) level stood at 459% up 46 points from September 30, 2017, as capital was reallocated to ASIC from our U.S. operations.

In Canada, our estimated aggregate MCT level was strong at 205% as at December 31, 2017, up 4 points from September 30, 2017 and down 13 points from December 31, 2016.

- Improvement in Q4-2017 was driven by strong operating results and the benefit of the phase-in.
- Decline from December 31, 2016 reflected the use of \$660 million of capital to finance the acquisition of OneBeacon.

IFC’s total capital margin stood at \$1,135 million as at December 31, 2017. This represents the aggregate of capital in excess of CALs in regulated entities plus available cash in unregulated entities.

For details on our Own Risk and Solvency Assessment, please refer to Section 22.8 - Own Risk and Solvency Assessment.



RISK MANAGEMENT

Section 19 – Overview

We have a comprehensive risk management framework and internal control procedures designed to manage and monitor various risks in order to protect our business, clients, employees, shareholders, and other stakeholders. Our risk management programs aim at mitigating risks that could materially impair our financial position, accepting risks that contribute to sustainable earnings and growth and disclosing these risks in a full and complete manner.

Effective risk management rests on identifying, understanding and communicating all material risks we are exposed to in the course of our operations. In order to make sound business decisions, both strategically and operationally, management must have continual direct access to the most timely and accurate information possible. Either directly or through its committees, the Board of Directors ensures that our management has put appropriate risk management programs in place. The Board of Directors, directly and in particular through its Risk Management Committee oversees our risk management programs, procedures and controls and, in this regard, receives periodic reports from, among others, the Risk Management Department through the Chief Risk Officer, internal auditors and the independent auditors. A summary of our key risks and the processes for managing and mitigating them is outlined below.

The risks described below and all other information contained in our public documents, including our Consolidated financial statements, should be considered carefully. The risks and uncertainties described below are those we currently believe to be material but they are not the only risks and uncertainties we face. If any of these risks, or any other risks and uncertainties that we have not yet identified, or that we currently consider to be not material, actually occur or become material risks, our business prospects, financial condition, results of operations and cash flows could be materially adversely affected.

While we employ a broad and diversified set of risk mitigation and risk transfer techniques, those techniques and the judgments that accompany their application cannot anticipate every economic and financial outcome in all market environments or the specifics and timing of such outcomes.

Section 20 – Risk management structure



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

The Board of Directors is responsible for the oversight of risk management to ensure that risks are properly measured, monitored and reported. In this regard, the Board is supported by its Risk Management Committee that covers enterprise wide risks. In addition, we have an internal Enterprise Risk Committee composed of senior executives.

The Board and Committee structures are reviewed periodically to be aligned with best practices, applicable laws and regulatory guidelines on corporate governance. The following structure is in place and remains largely unchanged from 2016.

Board of Directors	Main responsibility is to oversee our management of business and affairs, including our pension funds. In this regard, the Board establishes policies, reporting mechanisms and procedures in view of safeguarding our assets and ensuring our long-term viability, profitability and development.
Risk Management Committee	Assists the Board of Directors with its oversight role with respect to our management in order to build a sustainable competitive advantage, by fully integrating the Enterprise Risk Management policy into all of our business activities, strategic planning and our subsidiaries and operations, including our pension funds.
Compliance Review and Corporate Governance (CRCG) Committee	Ensures a high standard of governance, compliance and ethics in our company, including our pension funds and that we meet our legal requirements and engage in best practices as determined by the Board of Directors. In this regard, the CRCG Committee oversees our governance framework and that of our pension funds, our compliance framework, our compliance programs which includes related party transactions (“RPT”), our market conduct programs and policies, as well as the implementation of corporate compliance initiatives.
Human Resources and Compensation Committee	Assists the Board of Directors in fulfilling its governance supervisory responsibilities for strategic oversight of our human capital, including organization effectiveness, succession planning and compensation and the alignment of compensation with our philosophy and programs consistent with our overall business objectives.
Audit Committee	Assists the Board of Directors with its oversight of the integrity of our financial statements and financial information, the accounting and financial reporting process, the qualifications, performance and independence of the external auditors, the performance of the internal audit function and the quality and integrity of internal controls.
Enterprise Risk Committee	This committee is composed of senior officers and is chaired by the Chief Risk Officer designated by the Board of Directors. It meets regularly and oversees our risk management priorities, assesses the effectiveness of risk management programs, policies and actions of each key function of our business and reports on a quarterly basis to the Risk Management Committee. The Enterprise Risk Committee evaluates our overall risk profile, aiming for a balance between risk, return, and capital, and approves risk policies. The Enterprise Risk Committee is mandated to: (i) identify risks that could materially affect our business; (ii) measure risks both in terms of the impact on financial resources and reputation; (iii) monitor risks; and (iv) manage risk in accordance with the risk appetite statement determined by the Board of Directors. Periodically, this committee may establish sub-committees to review specific subjects in greater detail and report back on its findings and recommendations. This allows the Enterprise Risk Committee to access the expertise throughout our company and to operate more efficiently in addressing key risks.
Other committees	We have other committees responsible for managing, monitoring and reviewing specific aspects of risk related to our operations, investments, profitability, insurance operations, security and business continuity. Further details follow on how these committees operate, ensure compliance with laws and regulations and report to the Enterprise Risk Committee.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 21 – Corporate governance and compliance program

We believe that sound corporate governance and compliance monitoring related to legal and regulatory requirements are paramount for maintaining the confidence of different stakeholders including our investors. Legal and regulatory compliance risk arises from non-compliance with the laws, regulations or guidelines applicable to us as well as the risk of loss resulting from non-fulfilment of a contract. We are subject to strict regulatory requirements and detailed monitoring of our operations in all states, provinces and territories where we conduct business, either directly or through our subsidiaries. Our corporate governance and compliance program is built on the following foundations:

21.1 Corporate governance and compliance program

Corporate governance ensuring compliance with laws and regulatory requirements			
Sound corporate governance standards	Effective disclosure controls and processes	Sound corporate compliance structures and processes	Specialized resources independent from operations
<p>The Board of Directors and its committees are structured in accordance with sound corporate governance standards.</p> <p>Directors are presented with relevant information in all areas of our operations to enable them to effectively oversee our management, business objectives and risks. The Board of Directors and the Audit Committee periodically receive reports on all important litigation, whether in the ordinary course of business where such litigation may have a material adverse effect, or outside the ordinary course of business.</p>	<p>Disclosure controls and processes have been put in place so that relevant information is obtained and communicated to senior management and the Board of Directors to ensure that we meet our disclosure obligations, while protecting the confidentiality of information.</p> <p>A decision-making process through the Disclosure Committee is also in place to facilitate timely and accurate public disclosure.</p>	<p>Effective corporate governance depends on sound corporate compliance structures and processes.</p> <p>We have established an enterprise-wide Compliance Policy and framework including procedures and policies necessary to ensure adherence to laws, regulations and related obligations. Compliance activities include identification, mitigation and monitoring of compliance/reputation risks, as well as communication, education, and activities to promote a culture of compliance and ethical business conduct.</p>	<p>To manage the risks associated with compliance, regulatory, legal and litigation issues, we have specialized resources reporting to the SVP, Corporate and Legal services that remain independent of operations.</p> <p>The SVP, Corporate and Legal services reports to the Board of Directors and its committees on such matters, including with respect to privacy and Ombudsman complaints.</p> <p>We also use third party legal experts and take provisions when deemed necessary or appropriate.</p>

While senior management has ultimate responsibility for compliance, it is a responsibility that each individual employee shares. This is clearly set out in our core Business Values and Code of Conduct and employees sign a confirmation that they have reviewed and complied with them annually.

Section 22 – Enterprise Risk Management

22.1 Mandate

The Enterprise Risk Management strategy is designed to provide an overview of our risks and ensure that appropriate actions are taken to protect our clients, employees, shareholders and other stakeholders.

We have an integrated risk-based approach to significantly increase the effectiveness of the program, ensuring that delegated authorities actions are consistent with the overall strategy and risk appetite. Overall, the risk profile and communication must be transparent with the objective of minimizing surprises to internal and external stakeholders on risk management.

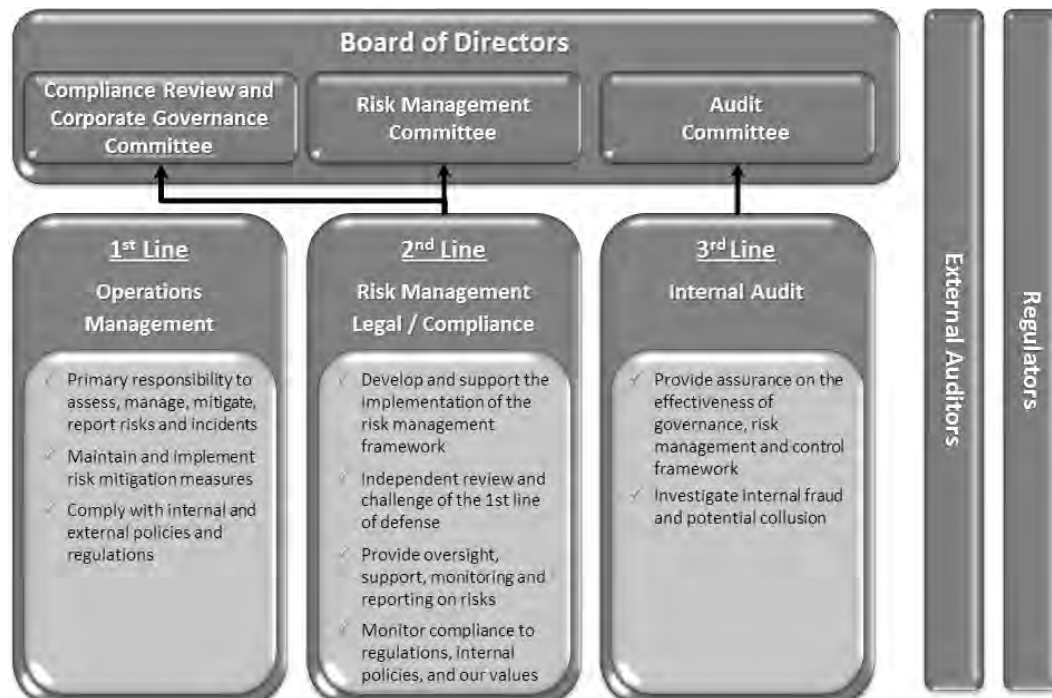
Our risks are separated into four main categories: Strategic Risk, Insurance Risk, Financial Risk and Operational Risk.

22.2 Objectives

- overseeing and objectively challenging the execution of risk management activities;
- identifying, as completely as possible, the most important risks and issues that may affect us;
- monitoring identified risks, major incidents and control weaknesses and reviewing adopted strategies;
- allocating risk ownership and responsibilities;
- gathering early warning information;
- escalating risk management issues and vetoing high risk business activities;
- enforcing compliance with the risk policies;
- disclosing key risks completely and transparently; and
- supporting management in raising risk awareness and insight.

22.3 A shared responsibility

Managing risk is a shared responsibility at Intact. The three lines of defence model is employed to clearly identify the roles and responsibilities of those involved in the risk management process.



Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

22.4 Risk Appetite

How do we manage corporate risk?

From a risk management perspective, our objective is to protect the sustainability of our activities, while delivering on our promises to our stakeholders. To do so, we strive to maintain our financial strength, even in unpredictable environments or under extreme stress. We take a prudent approach to managing risk, and the following principles help us establish the nature and scope of risks we are willing to assume:

- we focus on our core competencies;
- we keep our overall risk profile in check;
- we protect ourselves against extreme events;
- we promote a strong risk management culture; and
- we maintain our ability to access capital markets at reasonable costs.

Please consult our website for a more detailed discussion of our Risk Appetite under the Corporate Governance section.

22.5 Main risk factors and mitigating actions

Our practice is to regularly identify our top risks, assess the likelihood of occurrence and evaluate the potential impacts should they materialize both in terms of financial resources and reputation. We also consider potential emerging risks that are newly developing or changing risks which are inherently more difficult to quantify.

We then determine mitigation plans and assign accountability for each risk if deemed appropriate given our overall assessment, our risk appetite, and our business objectives.



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(in millions of Canadian dollars, except as otherwise noted)

22.6 Top and emerging risks that may affect future results

Each year the Enterprise Risk Management Committee identifies the top risks that the Company faces. The following section presents the top and emerging risks identified with the most severe potential impact. In assessing the potential impact for each of the top risks, the presence and effectiveness of risk mitigation activities are taken into consideration. Our main risk factors together with our practices used to mitigate these risks are explained below.

TOP AND EMERGING RISKS

Major earthquake in Canada.....	60
Catastrophe events risk	61
Increased competition and disruption.....	62
Turbulence in financial markets	63
Reserve and pricing inadequacy.....	64
Governmental and/or regulatory intervention	65
Failure of an acquisition.....	67
Failure of a major technology initiative	67
Information technology and cyber security risk.....	68
Inability to contain fraud and/or abuse	69
Customer satisfaction risk.....	69
The emergence of autonomous vehicles and crash avoidance technology	70
The legalization of cannabis (marijuana).....	70

Major earthquake in Canada		Insurance risk
<i>Risk we are facing</i>		
The occurrence of a major earthquake in Canada may produce significant damage in large, heavily populated areas.		
<i>Potential impact</i>	<i>How we manage this risk</i>	
<p>The occurrence of a major earthquake in Canada could have a significant impact on our profitability and financial condition and that of the entire P&C insurance industry in Canada. Depending on the magnitude of the earthquake, its epicentre, and on the extent of the damages, the losses could be substantial even after significant reinsurance recoveries. There could also be significant additional costs to find the required reinsurance capacity upon further renewals. In addition, we could be subject to increased assessments from the P&C Insurance Compensation Corporation (PACICC) leading to further costs if other insurers are unable to meet their contractual obligations with their clients. Based on our assessment, our exposure to a major earthquake in Western Canada has increased slightly in 2017 versus the prior year taking into consideration potential exposure in the Pacific Northwest of the United States related to our U.S. specialty insurance operations.</p>	<p>Our risk management strategy consists of regular monitoring of insured value accumulation and concentration of risks. We use earthquake models to help assess our possible losses at various return periods and use reinsurance to transfer a material amount of risk. Consequently, the diversification of risk among an appropriate number of reinsurers is vital for us. <i>See Section 15.4 – Reinsurance for more details on our reinsurance program.</i></p> <p>In 2017, we completed a comprehensive review of the models we use to evaluate our earthquake exposure. We concluded that the models we use to help us assess our risk are sound. Given the nature of earthquake risk, different models provide different assessments of the same exposure. We continue to maintain a prudent amount of reinsurance that exceeds our risk assessment of an earthquake in Western Canada, including the U.S. Pacific Northwest, at a 1-in-500 year return period.</p>	

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Catastrophe events risk **Insurance risk**

Risk we are facing

Climate change is a challenge faced by the entire P&C insurance industry. In particular, our property insurance business has been affected due to changing climate patterns and an increase in the number and cost of claims associated with severe storms and other natural disasters. Water damages now make up more than half of our home insurance claims.

Catastrophe events include natural disasters and unnatural events.

- There are a wide variety of natural disasters including but not limited to hurricanes, wind storms, hailstorms, rainstorms, ice storms, floods, severe winter weather and forest fires.
- Unnatural catastrophe events including but not limited to hostilities, terrorist acts, riots, explosions, crashes and derailments, and wide scale cyber-attacks.

Despite the use of sophisticated models, the incidence and severity of catastrophe events are inherently unpredictable. The extent of losses from a catastrophe event is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophe events are restricted to small geographic areas; however, hurricanes and other storms may produce significant damage in large, heavily populated areas. Catastrophe events can cause losses in a variety of P&C insurance lines.

Potential impact

Claims resulting from natural or unnatural catastrophe events could cause substantial volatility in our financial results and could materially reduce our profitability or harm our financial condition.

Over the last few years, we have witnessed a continued increase in the number and severity of weather events. Changing weather patterns may have an impact on the likelihood and severity of natural catastrophes, such as wildfires in the West and heavy precipitation in the East. The trend in climate change continues to pose a meaningful risk to our ability to meet our business objectives.

We began offering cyber risk insurance to our commercial customers in 2015 and have expanded our offerings in this space over time. The acquisition of OneBeacon expands further our exposure to this risk. We may be adversely affected by a large scale cyber-attack that simultaneously compromises the systems of many of our insureds.

In addition, we have exposure to terrorism risk in the U.S. through our U.S. specialty business. Terrorism can take many forms and both our property and workers’ compensation policies may be affected by an event.

How we manage this risk

To address this issue, we have ongoing initiatives including pricing and product changes to reflect new climate realities, regular reviews of claims processes and a greater focus on consumer loss prevention. Many initiatives have been implemented over the last several years including the expanded use of deductibles and sub-limits, and the introduction of depreciation schedules in personal property insurance across Canada. These initiatives should help mitigate, to some extent, P&C insurance losses resulting from water damage and harsh weather. In 2017, we improved segmentation in our property insurance business with additional focus on wildfire risk.

The Intact Centre on Climate Adaptation at the University of Waterloo is focused on key areas that will reduce climate change and extreme weather risk for home owners, governments and businesses. This is one of several initiatives to promote awareness on the potential impact of climate change to provide practical solutions for society as a whole to implement.

In addition, our reinsurance program offers protection against multi-risk events and catastrophes. *See Section 15.2 – Reinsurance for more details on our reinsurance program.*

To help mitigate the risks associated with our cyber risk insurance product, we focus on small to medium size companies with relatively modest policy limits. In addition, we purchase reinsurance specifically to transfer some of the risk in the event a large scale cyber-attack triggers a high volume of claims.

In addition to private reinsurance, we also participate in the U.S. federal government terrorism insurance backstop (TRIPRA) that mitigates our exposure under certain circumstances as outlined in federal legislation.

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Increased competition and disruption

Strategic risk

Risk we are facing

The P&C insurance industry is highly competitive and we believe that it will remain so for the foreseeable future.

We believe that competition in our business lines is based on price, service, commission structure, product features, financial strength and scale, ability to pay claims, ratings, reputation and name or brand recognition. We compete with a large number of domestic and foreign insurers as well as with several Canadian banks that are selling insurance products. These firms may use business models different than ours and sell products through various distribution channels, including aggregators, brokers and agents who sell products exclusively for one insurer and directly to the consumer. We compete not only for business and individual customers, employers and other group customers but also for brokers and other distributors of investment and insurance products.

We distribute our products primarily through a network of brokers and a great part of our success depends on the capacity of this network to be competitive against other distributors, including direct insurers and web aggregators, as well as our ability to maintain our business relationships with them. These brokers sell our competitors’ insurance products and may stop selling our insurance products altogether. Strong competition exists among insurers for brokers with demonstrated ability to sell insurance products.

Potential impact

Intense competition for our insurance products could harm our ability to maintain or increase our profitability, premium levels and written insured risk volume.

The entrance of a new player in the market or a shift in methods to purchase insurance could challenge our distribution model. The use of information technology in the distribution and pricing of insurance products (e.g. telematics, the use of Big Data, etc.) has increased over the last several years and this trend is expected to continue in the near future. Artificial intelligence is another area that is gaining much attention and could have a material impact on the insurance industry. Competitors may use these technologies more effectively than us or there may be negative reputational consequences arising from our initiatives.

Demutualization and further consolidation in the Canadian P&C industry remains likely which may result in an erosion of our competitive advantage.

The rise of the sharing economy may have a material impact on overall premium volumes in the P&C insurance industry, particularly if there are fewer automobiles in circulation.

The evolution of customer preferences for different distribution channels or alternate business models (e.g. peer-to-peer insurance) could lead to a material decline in our market share. Premium volume and profitability could be materially adversely affected if there is a material decrease in the number of brokers that choose to sell our insurance products. In addition, our strategy of distributing through the direct channel may adversely impact our relationship with brokers who distribute our products.

How we manage this risk

Our multi-channel distribution strategy including the broker channel, direct-to-consumer brands and web platforms, enhances our ability to adapt to evolving conditions in the insurance market. We have established close relationships with our independent distributors by providing them with advanced technology, as well as training to help strengthen their market position. We closely monitor pricing gaps between our various channels and manage the different channels under different brand names including BrokerLink, our wholly-owned broker network.

We also have a number of initiatives that we are pursuing to help mitigate the risk of competition and disruption including:

- Investing significantly in promoting our brands with an increasing focus on using web and mobile technology to reach consumers;
- Promoting our own usage-based insurance (UBI) product to better meet customer needs;
- Increased digitalization of the customer experience;
- Opening innovative service centres in major Canadian cities to provide an unmatched customer experience; and
- Creating Intact Ventures (*see Section 11.2*) to be at the forefront of technological change as it applies to the P&C insurance industry.

We also constantly seek to develop innovative and competitive products. We launched the Intact Lab, our centre for digital excellence, in 2015 to accelerate innovation and explore advanced technology solutions.

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Turbulence in financial markets **Financial risk**

Risk we are facing

Movements in interest rates, credit spreads, foreign exchange rates, inflation rates, and equity prices cause changes in realized and unrealized gains and losses. Generally, our interest and dividend income will be reduced during sustained periods of lower interest rates. During periods of rising interest rates, the fair value of our existing fixed-income securities will generally decrease and our realized gains on fixed-income securities will likely be reduced or result in realized losses. Changes in credit spreads would have similar impacts as those described above for changes in interest rates. Interest rates continued to be persistently low. In this context, purchases of fixed-income securities will likely be at lower yields than several years ago putting downward pressure on investment income. The significant and prolonged decline in oil prices may have an impact on the value of some of our securities or on the level of investment income we are able to generate given that our investment portfolio contains a significant amount of securities issued by companies in the energy sector. In both 2016 and 2017, our preferred share portfolio experienced significant fluctuations in market value as a result of changes in interest rates and credit spreads.

Potential impact

Changes in the market variables mentioned above could adversely affect our investment income and/or the market value of our securities.

In addition to the risk related to investments discussed previously, an economic downturn and/or increase in the inflation rate have a significant impact on the funded status of our defined benefit pension plans. Consequently, this could impact our financial condition.

General economic conditions, political conditions and many other factors can also adversely affect the equity markets and, consequently, the fair value of the equity securities we own and ultimately affect the timing and level of realized gains or losses.

Our preferred share portfolio depreciate in value as a result of negative developments in interest rate and/or credit markets.

Our fixed income portfolio may experience defaults resulting in impairments and lower income prospectively.

How we manage this risk

While our strategy is long-term in nature, it is regularly reviewed to adapt to the investment environment when necessary, especially in times of turbulence and increased volatility. We closely monitor concentration across and within asset classes and ensure that exposures remain within the risk tolerance stated in our investment policy.

Periodically, we employ several risk mitigation measures such as changes to our strategic asset mix, hedging of interest rate, foreign exchange, or equity risk and increased holdings in cash. These actions serve to reduce exposures in the investment portfolio and decrease the sensitivity of our regulatory capital ratios to financial market volatility.

Regular stress testing of our investment risk exposures assists management in assessing the overall level of financial risk and helps to ensure that exposures remain within established risk tolerances.

The Company’s exposure to financial risk arising from its financial instruments together with the Company’s risk management policies and practices used to mitigate it are explained in our Consolidated financial statements. Consult the following sections for more information.

Reference to our Consolidated financial statements

Market risk
Notes 9.1 and 9.2

Credit risk
Note 9.4

Basis risk
Note 9.3

Liquidity risk
Note 9.5

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Reserve and pricing inadequacy

Insurance risk

Risk we are facing

Our success depends upon our ability to accurately assess the risks associated with the insurance policies that we write. We establish reserves to cover our estimated liability for the payment of all losses and loss adjustment expenses (“LAE”) incurred with respect to premiums collected or due on the insurance policies that we write. Reserves do not represent an exact calculation of a liability. Rather, reserves are our estimates of what we expect to be the ultimate cost of resolution and administration of claims. These estimates are based upon various factors, including:

- actuarial projections of the cost of settlement and administration of claims reflecting facts and circumstances then known;
- estimates of trends in claims severity and frequency;
- judicial theories of liability;
- variables in claims handling procedures;
- economic factors (such as inflation);
- judicial and legislative trends, and actions such as class action lawsuits and judicial interpretation of coverage or policy exclusions; and
- the level of insurance fraud.

Product design and pricing risk is the risk that the established price is or becomes insufficient to ensure an adequate return for shareholders as compared to our profitability objectives. This risk may be due to an inadequate assessment of market needs, new business context, a poor estimate of the future experience of several factors, as well as the introduction of new products that could adversely impact the future behaviour of policyholders.

Potential impact

Most or all of these factors are not directly quantifiable, particularly on a prospective basis, and the effects of these and unforeseen factors could negatively impact our ability to accurately assess the risks of the policies that we write. In addition, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer and additional lags between the time of reporting and final settlement of claims.

The following factors may have a substantial impact on our future actual losses and LAE experience:

- amounts of claims payments;
- expenses that we incur in resolving claims;
- legislative and judicial developments; and
- changes in economic variables such as interest rates and/or inflation.

To the extent that actual losses and LAE exceed our expectations and the reserves reflected in our Consolidated financial statements, we will be required to reflect those changes by increasing our reserves. In addition, government regulators could require that we increase our reserves if they determine that our reserves were understated in the past. When we increase reserves, our income before income taxes for the period will decrease by a corresponding amount. In addition, increasing or strengthening reserves causes a reduction in our P&C insurance subsidiaries’ capital and could cause a downgrading of the financial strength ratings of our P&C insurance subsidiaries. Any such downgrade could, in turn, adversely affect our ability to sell insurance policies. *See Section 15.3 – PYD for more details on the claims reserve and prior year claims development.*

Inadequate pricing may lead to material declines in underwriting income and/or deficient reserves.

How we manage this risk

Establishing an appropriate level of reserves is an inherently uncertain process. We continually refine our reserve estimates in an ongoing process as claims are reported and settled.

Our reserve review committee scrutinizes reserves by business segment, and analyzes trends and variations in losses to ensure that we maintain a sufficient level of claims reserve.

Our profitability committees review the results of each business line and determine if appropriate action is required in terms of product design or pricing to remediate poor underwriting performance.

We have adopted policies which specify our retention limits and risk tolerance and our application depends on training and the discipline of our underwriting teams. Once the retention limits have been reached, we use reinsurance to cover the excess risk. Moreover, our profitability and ability to grow may also be adversely affected by our mandatory participation in the Facility Association and assumed risk-sharing pools in several automobile insurance markets including Ontario, Québec, Alberta, and the Maritimes.

In addition, on an annual basis, our external auditor provides an independent review of our reserves in the context of the audit of the Consolidated financial statements. This review includes establishing their own view of a reasonable range for the estimate.

Following the acquisition of OneBeacon, we purchased reinsurance to protect against adverse development for OneBeacon’s reserves from 2016 and prior years. This risk mitigation strategy offers partial protection in case of a deterioration in our U.S. dollar claims reserves.

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Governmental and/or regulatory intervention

Strategic Risk

Risk we are facing

Our insurance subsidiaries are subject to regulation and supervision by insurance regulatory authorities of the jurisdictions in which they are incorporated and licensed to conduct business.

These laws and regulations:

- delegate regulatory, supervisory and administrative powers to federal, provincial and territorial insurance commissioners and agencies;
- are generally designed to protect policyholders and creditors, and are related to matters including:
 - requirements on privacy and the protection of personal information;
 - personal auto insurance rate setting;
 - risk-based capital and solvency standards;
 - restrictions on types of investments;
 - maintenance of adequate reserves for unearned premiums and unpaid claims;
 - examination of insurance companies by regulatory authorities, including periodic financial and market conduct examinations;
 - licensing of insurers, agents and brokers;
 - limitations on upstream dividends from operating companies; and
 - transactions with affiliates;
- typically require us to periodically file financial statements and annual reports, prepared on a statutory accounting basis, and other information with insurance regulatory authorities, including information concerning our capital structure, ownership and financial condition including, on an annual basis, the aggregate amount of contingent commissions paid and general business operations.

Regulatory authorities closely monitor the solvency of insurance companies by requiring them to comply with strict solvency standards based on the risk assumed by each company with respect to asset composition, liability composition, and the matching between these two components. We are required to submit regular reports to the regulatory authorities regarding our solvency, and publish our solvency ratio every quarter. Solvency requirements are amended from time to time.

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Governmental and/or regulatory intervention (cont’d)	Strategic risk
<p>Potential impact</p> <p>We believe that our insurance subsidiaries are in material compliance with all applicable regulatory requirements. However, it is not possible to predict the future impact of changing federal, provincial and territorial regulations on our operations. Laws and regulations enacted in the future may be more restrictive than current laws. Overall, our business is heavily regulated and changes in regulation may reduce our profitability and limit our growth prospects.</p> <p>We could be subject to regulatory actions, sanctions and fines if a regulatory authority believed we had failed to comply with any applicable law or regulation. Any such failure to comply with applicable laws could result in the imposition of significant restrictions on our ability to do business or significant penalties, which could adversely affect our reputation, results of operations and financial condition. In addition, any changes in laws and regulations could materially adversely affect our business, results of operations and financial condition.</p> <p>We may be subject to governmental or administrative investigations and proceedings in the context of our highly regulated sectors of activity. We cannot predict the outcome of these investigations, proceedings and reviews, and cannot be sure that such investigations, proceedings or reviews or related litigation or changes in operating policies and practices would not materially adversely affect our results of operations and financial condition. In addition, if we were to experience difficulties with our relationship with a regulatory body in a given jurisdiction, it could have a material adverse effect on our ability to do business in that jurisdiction and the price of our common shares.</p> <p>In addition, our written premiums and profitability can be significantly affected by many factors, including:</p> <ul style="list-style-type: none"> • developing trends in tort and class action litigation; • changes in other laws or regulations, including the adoption of consumer initiatives regarding rates charged for automobile or other insurance coverage or claims handling procedures; • forced reductions in premiums or additional costs imposed by governments that limit our ability to properly price our insurance products; • modification of tax laws or a change in interpretation to existing tax laws, either retroactively or prospectively; and • nationalization of one or more of our business lines. <p>Furthermore, a significant increase in solvency requirements would increase the possibility of regulatory intervention and may reduce our ability to generate attractive returns for shareholders. This may also negatively impact our ability to execute our growth strategy and attain our financial objectives.</p>	<p>How we manage this risk</p> <p>We are supported by an in-house team of lawyers and staff, and by outside counsel when deemed necessary or appropriate, in handling general regulation and litigation issues and are an active member of the major industry associations.</p> <p>Our government relations team ensures contact with the governments of the various jurisdictions in which we operate, and can be proactive in situations that could affect our business.</p> <p>We regularly monitor trends and make adjustments to our strategy and products, when deemed appropriate, to ensure the sustainability of insurance products and to avoid the potential for additional regulation that may negatively impact our reputation, profitability, and financial condition.</p> <p>To reduce the risk of breaching the regulatory capital requirements, we have established an internal target capital ratio in excess of the supervisory target of 150% in our principal Canadian insurance subsidiaries and above 200% for our U.S. insurance subsidiaries. We operate above our internal target under normal circumstances to reduce the likelihood of regulatory intervention. Our Enterprise Risk Committee regularly review risks related to solvency and conducts stress testing to identify vulnerabilities and possibly areas for remediation. Our capital management policy contains guidelines to help ensure that we maintain adequate capital to withstand adverse event scenarios and has documented procedures to take corrective actions should any unanticipated conditions arise.</p> <p>In addition, we conducted a full internal solvency assessment as described hereafter in <i>Section 22.8 – Own Risk and Solvency Assessment (ORSA)</i>.</p>

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Failure of an acquisition	Strategic risk
<p>Risk we are facing</p> <p>Our primary strategy is to pursue consolidation in the Canadian market and expansion in foreign markets where we can deploy our expertise in pricing, underwriting, claims management and multi-channel management.</p> <p>On September 28, 2017, we completed the US\$1.7 billion (\$2.3 billion) acquisition of OneBeacon, a specialty P&C insurance provider that offers a wide range of specialty insurance products in the United States. Failure on our part to manage this U.S. acquisition could have a material adverse effect on our business, results of operations and financial condition. In addition to specific country risks, we cannot be sure that we will be able to identify appropriate profitability targets or successfully integrate this acquired business into our operations.</p>	
<p>Potential impact</p> <p>With respect to the acquisition of OneBeacon, we are faced with a number of integration risks including but not limited to:</p> <ul style="list-style-type: none"> – the inability to derive the expected returns from the acquisition, which would lead to a lower future return on equity for shareholders; – the inability to realize growth and profitability action plans, such as cross-border opportunities and underwriting profitability targets. Under certain adverse circumstances, this may lead to a write down of goodwill; – challenges in harmonizing processes; and – a departure of key employees during the integration phase. <p>In addition to the potential financial impact, our reputation may be adversely affected if such an event were to occur. Consequently, it may impact the cost or availability of capital for future acquisitions.</p>	<p>How we manage this risk</p> <p>We are a proven industry consolidator with 16 successful P&C acquisitions since 1988. We have a dedicated corporate development team that follows a rigorous selection process. Our approach to conducting due diligence to assess all the risks and opportunities is well developed and is consistently executed. We also assign dedicated and experienced task forces to ensure a swift and effective integration with seamless impact to our customers. There is also strong oversight by the Board of Directors regarding acquisitions.</p>

Failure of a major technology initiative	Operational risk
<p>Risk we are facing</p> <p>To maintain our performance levels, we are required to regularly modernize our systems. Often significant time and investment is required for accomplishing these projects. Any unplanned delays, unforeseen costs, or unsuccessful execution of such projects could lead to a significant decline in service levels, impact employee morale negatively and reduce our competitiveness. There is no assurance that we will succeed in meeting our objectives for these projects.</p>	
<p>Potential impact</p> <p>Our technology strategy may take too long to execute or may not be adequate to maintain a competitive advantage. The complexity and interdependence of our infrastructure and applications may lead to higher costs and more errors. Implementation of new technology may introduce more complexity in the interim prior to simplification after decommissioning older systems.</p> <p>We could decide to abandon one or more of our technology initiatives resulting in a material write down.</p>	<p>How we manage this risk</p> <p>Senior management provides careful oversight and ensures that proper funding and resources are allocated to our key projects. Risk assessments are conducted to identify potential areas for remediation or the necessity for additional controls. A dedicated committee was created to ensure proper focus is devoted to major technology projects.</p>

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Information technology and cyber security risk	Operational risk
<p>Risk we are facing</p>	
<p>Information technology and cyber security risks continue to be key risks for many industries in Canada and around the globe. Criminal organizations, hackers, and other external actors have become more active and better equipped to attack even robust systems and networks. Our dependency on technology, network, telephony and critical applications makes our ability to operate and our profitability vulnerable to business interruptions, service disruptions, theft of intellectual property and confidential information, litigation and reputational damage.</p> <p>The volume and sophistication of cyber-attacks continue to increase. These attacks may include targeted attacks on systems and applications, introduction of malicious software, denial of service attacks, and phishing attacks which could result in the fraudulent use or theft of data, and may involve attempts to fraudulently induce employees, customers or third party service providers to disclose sensitive information in order to gain access to the Company’s data. Distributed Denial of Service (DDos) and Ransomware attacks continue to increase in frequency and severity. These activities are designed to disrupt the operations of an organization and/or to benefit the attacker financially.</p> <p>We may be unable to prevent cyber-attacks that result in system disruption or a breach of confidential information, whether personal or corporate in nature. Third party service providers and other suppliers may also be the subject of successful cyber-attacks leading to a material impact on our systems or the theft of confidential information.</p>	
<p>Potential impact</p> <p>Despite our commitment to information and cyber security, we may not be able to fully mitigate all risks associated with the increased sophistication and volume in the threat landscape. As such, we may be the subject to a cyber-attack resulting in system unavailability, data corruption or deletion, or the disclosure of confidential or personal information. Massive denial of service attacks and system intrusion attempts could compromise our ability to operate or we may be unable to safeguard personal and confidential information from public disclosure. Other potential consequences include our inability to provide customers with real-time access to information on their insurance policies, provide quotes for new insurance products or enable customers to report claims electronically.</p> <p>These events and attacks may lead to wide ranging consequences including:</p> <ul style="list-style-type: none"> • financial loss, which also includes lost productivity, remediation costs, and costs associated with potential legal action; • regulatory action, which may include regulatory fines and/or increased scrutiny by government; and • reputational damage such as lost consumer confidence and lower customer retention. 	<p>How we manage this risk</p> <p>To ensure the security and resilience of our systems, the safeguard of our confidential information and the integrity of our information and databases, dedicated teams plan, test and execute our continuity and security plans. This includes threat and vulnerability assessments and the implementation of appropriate mitigation actions. Our security teams constantly monitor our systems and are ready to intervene if an incident occurs. To ensure the expected levels of service are delivered by our critical third-party service providers, service level agreements are signed and added to relevant contracts.</p> <p>We continuously upgrade our applications to better protect our systems and information. We regularly monitor external trends in cyber security to ensure we are able to rapidly mitigate known vulnerabilities.</p> <p>We benchmark our information security practices to assess areas of our cyber security program that require additional effort and to learn from industry leading practices.</p> <p>Our Information Technology Security Committee oversees information security initiatives and ensures effective collaboration across teams. As part of our overall security program, we provide employee information security awareness and training to enhance our ability to resist cyber-attacks. In addition, our Enterprise Risk Committee oversees the establishment of our cyber security strategy and monitors the progress of our mitigation action plans.</p>

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Inability to contain fraud and/or abuse

Operational risk

Risk we are facing

As a property and casualty insurer, we may be subject to internal or external fraud. Our insureds may exaggerate claims for personal gain. Despite our efforts to control fraud and abuse, our staff, systems, and processes may be unable to accurately detect and prevent internal or external fraud.

Potential impact

Fraud may result in unanticipated losses and a negative impact on our reputation. Our written premiums and profitability can be significantly affected by regulatory regimes which limit our ability to detect and defend against fraudulent claims and fraud rings.

How we manage this risk

We have strong internal controls in place to prevent and detect potential internal fraud. Internal and external audits are performed to verify that the controls are followed.

Fraud detection software is used by our claims teams to detect potential external fraud and flag cases for further investigation.

Government authorities also have an incentive to help reduce fraud in the system and maintain affordable insurance for consumers. Ontario Bill 15 - *Fighting Fraud and Reducing Automobile Insurance Rates Act* is one example of government action that aims to reduce auto insurance fraud.

Customer satisfaction risk

Strategic risk

Risk we are facing

Our insurance products and services are ultimately distributed to individual consumers and businesses. From time to time, unsatisfied customers, consumer advocacy groups or the media may generate negative publicity related to our claims handling or underwriting practices. Untimely or poor handling of such negative publicity may increase the impact of a situation and materially affect our reputation and growth prospects.

In addition, a lack of appropriate focus on customers’ needs and wants may threaten our ability to meet customer expectations, resulting in poor customer retention.

Potential impact

Negative publicity resulting from unsatisfied customers may result in increased regulation and legislative scrutiny of practices in the P&C insurance industry as well as increased litigation. Such events may further increase our costs of doing business and adversely affect our profitability by impeding our ability to market our products and services, requiring us to change our products or services or increasing the regulatory burdens under which we operate. The periodic negative publicity of insurance and related businesses may negatively impact our financial results and financial condition.

Social media could amplify the impact of a reputational issue. It could result in further damage to our reputation and impair our future growth prospects.

How we manage this risk

To mitigate these risks, we have established escalation procedures to help ensure that our customers have multiple channels to express any dissatisfaction. This includes a Customer Experience Team and an Ombudsman’s Office which both offer the opportunity for customer dissatisfaction to be resolved. In addition, management proactively identifies potential issues and performs an additional review to help ensure that our customers are treated fairly.

The wording of our insurance policies is reviewed periodically by management to detect and remediate potential issues before they arise.

New products and significant changes in existing products undergo a rigorous product development life-cycle including an independent review by the risk management function prior to launch. Potential reputational issues can be identified in the early stages of product development and, if required, changes are implemented prior to launch.

The Enterprise Risk Committee regularly monitors our operations to identify situations that can negatively affect customer satisfaction.

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The emergence of autonomous vehicles and crash avoidance technology **Emerging risk**

Risk we are facing

Commercialisation of fully- or semi-autonomous vehicles could profoundly change the transportation and auto insurance industries. The speed at which autonomous vehicles are adopted will depend on a number of factors including, but not limited to, the success of the new technology, the legal and regulatory environment, and customer preferences. These vehicles may have a dramatically different risk profile than current modes of transportation.

Potential impact

If the potential of autonomous vehicles and crash avoidance technology is realized, a number of changes may occur including a significant reduction in accident frequency and the emergence of new ways to provide automobile insurance coverage. This could cause a material decline in our written premiums.

How we manage this risk

We recognize the potential impact of this emerging technology and have been closely monitoring developments on this topic for some time. We devote part of our research agenda to include items such as the future of mobility insurance and autonomous vehicles. We believe it is crucial to understand this emerging technology and the possible implications to be able to adjust our corporate strategy accordingly.

The legalization of cannabis (marijuana) **Emerging risk**

Risk we are facing

Under proposed legislation by Canada’s federal government, marijuana would become legal under certain circumstances in July 2018. In addition, several states in the U.S. such as California have also proposed the legalization of marijuana. Cannabis for medical use is already permitted in many states and the trend to allow its use for recreational purpose may accelerate in the coming years.

Potential impact

Marijuana legalization could have an impact our results in various ways, including:

- higher frequency and severity of auto insured losses as a result of impaired driving; and
- an increase in claims related to liability insurance or workers compensation.

This could cause a decline in our underwriting income.

How we manage this risk

In 2017, we have taken actions to better understand how this risk may impact our business. Consequently, we have conducted a stress test inspired by other jurisdictions (e.g. Colorado) that have legalized marijuana for recreational purposes.

Our personal lines and commercial lines teams have reviewed our product wordings and underwriting guidelines to ensure we have a clear risk appetite around exposures related to marijuana producers and distributors. We will continue to monitor this risk and make adjustments to product pricing or features as more information becomes available.

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22.7 Other risk factors that may affect future results***Legal risk***

In addition to the occasional employment-related litigation, we are a defendant in a number of claims relating to our insurance and other related business operations. We may from time to time be subject to a variety of legal actions relating to our current and past business operations. Plaintiffs may also continue to bring new types of legal claims against us. Current and future court decisions and legislative activity may increase our exposure to these types of claims. Multiparty or class action claims may present additional exposure to substantial economic, non-economic or punitive damage awards. The loss of even one of these claims, if it resulted in a significant damage award or a judicial ruling that was otherwise detrimental, could have a material adverse effect on our results of operations and financial condition. Unfavourable claim rulings may render fair settlements more difficult to reach. We cannot determine with any certainty what new theories of recovery may evolve or what their impact may be on our businesses.

Reinsurance risk

We use reinsurance to help manage our exposure to insurance risk, including major catastrophe events. The availability and cost of reinsurance is subject to prevailing market conditions, both in terms of price and available capacity, which can affect our premium volume, profitability and regulatory capital position. Both worldwide and Canadian catastrophe losses have an impact on the reinsurance market in Canada. In recent years, the availability of alternative capital in the reinsurance market has helped maintain the supply of capital and added downward pressure on rates. However, reinsurance companies may exclude some coverage from the policies that we purchase from them or may alter the terms of such policies from time to time. These gaps in reinsurance protection expose us to greater risks and greater potential losses and could adversely affect our ability to write future business. We may not be able to successfully mitigate risks through reinsurance arrangements, which could cause us to reduce our premiums written in certain lines or could result in losses. In addition, the cost of reinsurance could increase significantly year over year, impacting our profitability if we are unable to pass on these costs to consumers. Furthermore, a significant decline in the availability of reinsurance could impact our premium volume, our profitability and our regulatory capital position.

People risk

Our success has been, and will continue to be, dependent on our ability to retain the services of key employees and to attract additional qualified personnel in the future. In addition, a significant decline in employee morale could materially affect our operations including an increase in the risk of human error or deliberate acts that harm the company. The loss of the services of any of our key employees, or the inability to identify, hire and retain other highly qualified personnel in the future, could adversely affect the quality and profitability of our business operations.

We have developed a focused recruiting strategy to aggressively market careers and opportunities at Intact. The strategy includes an updated web site, focused external recruiting, campaigns, rebranding, and targeted advertising. It also includes partnering with four universities on graduate recruiting as well as commercial and personal lines trainee program recruiting. Talent identification and development programs have been implemented to retain and grow existing talent. We also have a comprehensive succession planning program at various levels within the organization to ensure we are prepared for unplanned departures and retirements. Furthermore, our employee engagement surveys continue to reveal a high level of engagement among employees. IFC was recognized by multiple organizations as one of Canada's best employers. We believe that a high level of employee engagement helps mitigate some of the operational risks associated with people. However, there is no assurance that the Company will be successful in retaining and motivating our key talent across the organization.

Business interruption risk

We may experience an abrupt interruption of activities caused by unforeseeable and/or catastrophe events, an example of which being a global pandemic (e.g. the Ebola virus) or a large scale cyber-attack. Our service levels may decline materially resulting in negative financial and reputational consequences. Losses can relate to property, financial assets, trading positions and also to key personnel. If our business continuity plans cannot be put into action or do not take such events into account, losses may increase further.

We continuously monitor world events, such as the Ebola virus outbreak in 2014, to enable us to pro-actively adapt our response plan. In order to maintain the integrity and continuity of our operations in the event of a crisis, we have developed personalized alert and mobilization procedures as well as communication protocols. For example, emergency action plans, business continuity plans, business recovery plans, major health crisis plans, building evacuation plans and crisis communication plans have all been defined and are tested on an ongoing basis. This process is supported by a crisis management structure adapted to our organization and to the type of events we may have to manage.

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Credit downgrade risk

Independent third party rating agencies assess our ability to honour our financial obligations (the "senior unsecured debt rating") and our insurance subsidiaries' ability to meet their ongoing policyholder obligations (the "financial strength rating"). See *Section 17.2 – Ratings for more details*.

The rating agencies periodically evaluate us to confirm that we continue to meet the criteria of the ratings previously assigned to us. We may not be in a position to maintain either the issuer credit ratings or the financial strength ratings we have received from the rating agencies. An issuer credit rating downgrade could result in materially higher borrowing costs. A financial strength rating downgrade could result in a reduction in the number of insurance contracts we write and in a significant loss of business; as such business could move to other competitors with higher ratings, thus causing premiums and earnings to decrease.

This is more applicable to our commercial insurance where clients place a higher emphasis on such ratings. Credit downgrades may affect our ability to raise capital or may result in an increase in the cost of raising capital with negative implications for shareholders and other stakeholders.

Limit on dividend and capital distribution risk

As a holding company, IFC is a legal entity and is separate and distinct from its operating subsidiaries, most of which are regulated insurance companies. While no regulatory approval is required for dividend payments from the regulated insurance companies, notice to OSFI is required together with pro forma capital calculations showing internal target capital levels are maintained both before and after such dividends are paid out. In addition, for competitive reasons, our insurance subsidiaries maintain financial strength ratings which require us to maintain minimum capital levels in our insurance subsidiaries. These regulations and ratings targets limit the ability of our insurance subsidiaries to pay unlimited dividends or invest all of their capital in other ways. In certain stress scenarios limitations on our subsidiaries' ability to pay dividends to IFC could have a material adverse effect on our ability to pay shareholder dividends and may result in a material decline in the price of securities we have issued.

Deferred tax assets

We have a deferred tax asset related to net operating loss carryforwards and tax credit carryforwards as at December 31, 2017, that are subject to carryforward limitations in the U.S. Utilization of these assets and other assets included in our net deferred tax asset is dependent on generating sufficient future taxable income of the appropriate type (i.e. ordinary income or capital gains) in the appropriate jurisdiction. If it is determined that it is more likely that sufficient future taxable income will not be generated, we would be required to increase the valuation allowance (an offset to our deferred tax asset) in future periods, which could have an adverse effect on our results of operations.

Distribution risk

Distribution risk is the risk related to the distribution of our P&C insurance products. It includes the inherent risk of dealing with independent distributors, the risk related to new market entrants and the risk associated with our multiple distribution channel strategy. We may also face the risk that one of our channels or business models would not be sustainable in a specific market or context. From time to time we issue loans or take equity participation in certain brokers and consequently, we expose ourselves to other risks including financial risk and regulatory risk. For various reasons, the broker channel has been in a consolidation mode for the last few years and we believe that this situation will continue. The acquisition of brokers by others or even by other insurers may impact our relationship with some of them and harm our ability to grow our business. In order to maintain strong relationships with brokers, each relationship is managed by officers in each of the main regions in which we operate. To mitigate the financial risk arising from loans to brokers we generally receive guarantees and use standard agreements which contain general security and oversight clauses. The Board of Directors participates in this oversight process by reviewing these activities periodically.

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22.8 Own Risk and Solvency Assessment

Since 2014, we have conducted our Own Risk and Solvency Assessments ("ORSA") at least annually. ORSA encompasses processes to identify, assess, monitor, and manage the risks we take in conducting our business. ORSA also covers the determination of our capital needs and solvency position. ORSA is an integral part of the implementation of our Enterprise Risk Management strategy. This exercise was conducted over and above the Dynamic Capital Adequacy Testing (DCAT) performed annually by the Appointed Actuary (*refer to Note 20 – Capital management to the accompanying Consolidated financial statements for details*).

Our ORSA revealed that the financial resources of our insurance subsidiaries are sufficient to meet policyholder obligations after adverse situations at a confidence level of 99% conditional tail expectation (CTE) over a one-year time horizon. We considered all our material risk exposures in making this determination. We concluded that our overall risk is well balanced primarily between insurance risk and financial risk, while operational risk contributes a modest additional amount. Diversification and other adjustments modestly reduce our overall risk assessment.

We also compared our assessment of our own capital requirements with that of regulatory bodies on the same basis. Our overall assessment continues to be materially lower than current regulatory requirements given the same confidence level and time horizon. Our 2017 assessment of capital required decreased slightly compared to that of 2016. Our capital sufficiency remains very strong when comparing both available financial resources and tangible equity to our assessment of capital required.

The revisions to the MCT Guidelines in 2015 and again in 2016 have resulted in lower capital requirements for IFC and continue to converge directionally with our assessment for the main categories of risk. We believe the convergence of the regulatory view of risk with our own risk assessment is a positive development for IFC and the Canadian P&C industry.

Section 23 – Off-balance sheet arrangements

23.1 Securities lending

We participate in a securities lending program to generate fee income. This program is managed by our custodian, a major Canadian financial institution, whereby we lend securities we own to other financial institutions to allow them to meet their delivery commitments. We loaned securities, which are reported as investments in the accompanying Consolidated financial statements, with a fair value of \$1,087 million as at December 31, 2017 (\$720 million as at December 31, 2016).

Collateral is provided by the counterparty and is held in trust by the custodian for our benefit until the underlying security has been returned to us. The collateral cannot be sold or re-pledged externally by us, unless the counterparty defaults on its financial obligations. Additional collateral is obtained or refunded on a daily basis as the market value of the underlying loaned securities fluctuates. The collateral consists of government securities with an estimated fair value of 105% of the fair value of the loaned securities and amounts to \$1,144 million as at December 31, 2017 (\$758 million as at December 31, 2016).

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Section 24 – Sensitivity analyses

Sensitivity analyses are one risk management technique that assists management in ensuring that risks assumed remain within our risk tolerance level. Sensitivity analyses involve varying a single factor to assess the impact that this would have on our results and financial condition. No management action is considered.

Actual results can differ materially from these estimates for a variety of reasons and therefore, these sensitivities should be considered as directional estimates.

Table 36 - Sensitivity analysis (after tax)

For the years ended December 31,	2017			2016		
	Net income	OCI	BVPS	Net income	OCI	BVPS
Equity price risk						
Common share prices (10% decrease) ¹	(1)	(201)	(1.45)	9	(193)	(1.40)
Preferred share prices (5% decrease) ²	13	(62)	(0.35)	8	(57)	(0.37)
Interest rate risk (100 basis point increase)	9	(64)	(0.40)	4	(75)	(0.54)
Currency risk (strengthening of the CAD by 10% vs all currencies)³						
USD investments supporting P&C Canada	6	(1)	0.04	2	(47)	(0.34)
International equities supporting P&C Canada	-	(19)	(0.14)	-	-	-
Consolidated net assets of a U.S. subsidiary	-	(176)	(1.26)	-	-	-

¹ Net of any equity hedges, including the impact of any impairment.

² Including the impact on related embedded derivatives.

³ After giving effect to forward-exchange contracts.

The above analyses were prepared using the following assumptions:

- shifts in the yield curve are parallel;
- interest rates, equity prices and foreign currency move independently;
- credit, liquidity and basis risks have not been considered;
- impact on our pension plans has been considered; and
- risk reduction measures perform as expected, with no material basis risk and no counterparty defaults.

AFS debt or equity securities in an unrealized loss position, as reflected in AOCI may be realized through sale in the future.

A decline in the price of AFS perpetual preferred shares is recorded in OCI and would normally lead to a lower valuation for associated embedded derivative liabilities which are recorded as gains in Net income. Conversely, an increase in the price of these preferred shares is also recorded in OCI and would normally lead to a higher valuation for associated embedded derivative liabilities which are recorded as losses in Net income.

ADDITIONAL INFORMATION

Section 25 – Financial KPIs and definitions

25.1 Our financial KPIs

Our most relevant key performance indicators are outlined in the table below. DPW, Underlying current year loss ratio, NOI, NOIPS, OROE, ROE, AROE and AEPS are considered non-IFRS financial measures. See Section 27 – Non-IFRS financial measures for the reconciliation to the most comparable IFRS measures.

		2017	2016	2015	2014	2013
Growth	DPW growth	5.5%	4.7%	6.2%	1.6%	7.2%
Underwriting performance	Underlying current year loss ratio	64.5%	64.8%	66.1%	64.3%	64.9%
	Claims ratio	65.4%	64.9%	61.3%	62.6%	66.9%
	Expense ratio	28.9%	30.4%	30.4%	30.2%	31.1%
	Combined ratio	94.3%	95.3%	91.7%	92.8%	98.0%
Consolidated performance	Net underwriting income	486	375	628	519	142
	Net investment income	432	414	424	427	406
	Net distribution income	132	111	104	75	75
	NOI	771	660	860	767	500
	NOIPS (in dollars)	5.60	4.88	6.38	5.67	3.62
	OROE	12.9%	12.0%	16.6%	16.3%	11.2%
	ROE	12.8%	9.6%	13.4%	16.1%	9.3%
	AROE	13.0%	11.0%	14.3%	16.8%	10.3%
	EPS (in dollars)	5.75	3.97	5.20	5.79	3.10
	AEPS (in dollars)	5.82	4.53	5.54	6.01	3.44
Financial strength	BVPS (in dollars)	48.00	42.72	39.83	37.75	33.94
	MCT (Canada)	205%	218%	203%	209%	203%
	RBC (U.S.)	459%	n/a	n/a	n/a	n/a
	Total capital margin	1,135	970	625	681	550
	Debt-to-total capital ratio	23.1%	18.6%	16.6%	17.3%	18.7%

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25.2 Definitions of our financial KPIs

Our most relevant key performance indicators are defined below. Underlying current year loss ratio, NOI, NOIPS, ROE, OROE, AROE and AEPS are considered non-IFRS financial measures. *See Section 27 - Non-IFRS financial measures for the reconciliation to the most comparable IFRS measures.*

- **AEPS** and **AROE** are **adjusted measures**, meaning that they exclude the after-tax impact of acquisition-related items, such as amortization of intangible assets recognized in business combinations, as well as integration and restructuring costs.
- **NOI**, **NOIPS** and **OROE** are **operating measures**, meaning that they exclude non-operating items detailed in *Section 26 – Non-operating results.*
- **EPS** and **ROE** are **IFRS measures**, meaning that their definition is determined in accordance with IFRS.

Incentive compensation is based on the comparison of results for DPW growth, combined ratio, NOIPS and AROE as defined above, against those of our Canadian P&C insurance industry benchmark. *See Section 11.3 –Delivering on our key financial objectives for more details on our performance versus the industry.*

Growth	DPW growth for a specific period	$\frac{\text{DPW for a specified period} - \text{DPW for the previous year}}{\text{DPW for the previous year}}$	Written insured risks growth for a specific period	$\frac{\text{\# of vehicles and premises in personal insurance} - \text{Total \# for the previous year}}{\text{Total \# for the previous year}}$
	Underwriting results	Underlying current year loss ratio for a specific period	$\frac{\text{Current year claims ratio excluding CAT losses and PYD}}{\text{NEP before the impact of reinstatement premiums}}$	Expense ratio for a specific period
	Claims ratio for a specific period	$\frac{\text{Claims incurred (net of reinsurance)}}{\text{NEP}}$	Combined ratio for a specific period	$\text{Claims ratio} + \text{Expense ratio}$
<p>A combined ratio under 100% indicates a profitable underwriting result. A combined ratio over 100% indicates an unprofitable underwriting result.</p>				

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Consolidated performance	Net distribution income for a specific period	Operating income excluding interest and taxes from our wholly-owned broker (BrokerLink) + Operating income including interest and taxes from our broker associates	Distribution EBITA for a specific period	Operating income excluding interest and taxes from our wholly-owned broker (BrokerLink) and our broker associates
	Net investment income for a specific period	As detailed in Table 12 – Net investment income	ROE for a 12-month period	$\frac{\text{Net income attributable to common shareholders}^1}{\text{Average common shareholders' equity}^2}$
	NOI for a specific period	As detailed in Table 2 – Consolidated performance	AROE for a 12-month period	$\frac{\text{Adjusted net income attributable to common shareholders}}{\text{Average common shareholders' equity}^2}$
	NOIPS for a specific period	$\frac{\text{NOI attributable to common shareholders}}{\text{WANSO}^3}$	EPS for a specific period	As reported in the accompanying Consolidated statements of income
	OROE for a 12-month period	$\frac{\text{NOI attributable to common shareholders}}{\text{Average common shareholders' equity}^2 \text{ (excluding AOCI)}}$	AEPS for a specific period	$\frac{\text{Adjusted net income attributable to common shareholders}}{\text{WANSO}^3}$

Financial strength	BVPS as at the end of a specific period	$\frac{\text{Common shareholders' equity}^4}{\text{Number of common shares outstanding at the same date}}$	Total capital margin as at the end of a specific period	Aggregate of capital in excess of company action levels in regulated entities (170% MCT, 200% RBC) plus available cash in unregulated entities.
	Regulatory capital ratio as at the end of a specific period	Minimum capital test (as defined by OSFI and the AMF in Canada) and Risk-based capital (as defined by the NAIC in the U.S.)	Debt-to-total capital ratio as at the end of a specific period	$\frac{\text{Total debt outstanding}}{\text{Sum of the total shareholders' equity}^4 \text{ and total debt outstanding as at the same date}}$

¹ Net income is determined in accordance with IFRS.

² The average shareholders' equity is the mean of shareholders' equity at the beginning and the end of the period, adjusted for significant capital transactions, if appropriate. Shareholder's equity is determined in accordance with IFRS.

³ Weighted-average number of common shares outstanding during the same period.

⁴ Shareholder's equity is determined in accordance with IFRS.

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Section 26 – Non-operating results

Non-operating results, a non-IFRS financial measure, include elements that are not representative of our operating performance because they relate to special items, bear significant volatility from one period to another, or because they are not part of our normal activities. As a result, these elements are excluded from the calculation of NOI and related non-IFRS financial measures.

Table 37 – Non-operating results

	Q4-2017	Q4-2016	Change	2017	2016	Change
Net investment gains (losses)	(24)	(91)	67	(36)	(71)	35
Currency and other gains (losses) ¹	18	(6)	24	105	(1)	106
Total investment, currency and other gains (losses)	(6)	(97)	91	69	(72)	141
Positive (negative) impact of MYA on underwriting	11	87	(76)	92	34	58
Difference between expected return and discount rate on pension assets	(12)	(6)	(6)	(45)	(26)	(19)
Integration and restructuring costs ²	(12)	(19)	7	(57)	(23)	(34)
Amortization of intangible assets recognized in business combinations	(25)	(12)	(13)	(62)	(53)	(9)
Underwriting results of exited lines	(10)	-	(10)	(10)	-	(10)
Other	(4)	(5)	1	(18)	(12)	(6)
Non-operating gains (losses)	(58)	(52)	(6)	(31)	(152)	121
Income tax expense on the above items	27	11	16	25	33	(8)
U.S. Corporate Tax reform	27	-	27	27	-	27
After-tax non-operating gains (losses)	(4)	(41)	37	21	(119)	140

¹ Including a currency derivative gain related to book value hedge of OneBeacon of \$65 million in 2017.

² Including \$10 million in Q4-2017 and \$40 million in 2017 in connection with the acquisition of OneBeacon.

- Investment gains and losses as well as the effect of MYA on underwriting arise mostly from changes in market conditions, which can be volatile to earnings.
- Claims liabilities are discounted at the estimated market yield of the assets backing these liabilities. The impact of changes in the discount rate used to discount claims liabilities based on the change in the market-based yield of the underlying assets is referred to as MYA.
- Integration and restructuring costs include items such as retention bonuses, the initial net impact of a reinsurance coverage which provides protection against certain negative reserve developments, pre-acquisition finance costs and acquisition-related expenses.
- The difference between the expected return and discount rate on pension assets is treated as non-operating results, as we believe the gap in these measures is not reflective of our internal investment management expertise and management of our pension asset portfolio.
- Underwriting results of exited lines included the results of the U.S. Commercial's business units Programs, and Architects and Engineers.

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Section 27 – Non-IFRS financial measures

Non-IFRS financial measures do not have standardized meanings prescribed by IFRS and may not be comparable to similar measures used by other companies in our industry. These non-IFRS financial measures are used by management and financial analysts to assess our performance. Further, they provide users with an enhanced understanding of our results and related trends and increase transparency and clarity into the core results of the business.

NOI, NOIPS and OROE

- Exclude non-operating results (see Section 26 for details)

Table 38 – Reconciliation of NOI, NOIPS and OROE to net income

	Q4-2017	Q4-2016	2017	2016
Net income	232	171	792	541
Add (less) income tax expense (recovery)	14	53	150	145
Add non-operating losses	58	52	31	152
Pre-tax operating income	304	276	973	838
Tax impact	(68)	(64)	(202)	(178)
NOI	236	212	771	660
Less preferred share dividends	(10)	(4)	(27)	(20)
NOI to common shareholders	226	208	744	640
Divided by weighted-average number of common shares (in millions)	139.2	131.1	133.1	131.2
NOIPS, basic and diluted (in dollars)	1.63	1.58	5.60	4.88
NOI to common shareholders – last 12 months			744	640
Average common shareholders' equity, excluding AOCI			5,758	5,332
OROE for the last 12 months			12.9%	12.0%

All underwriting results and related ratios excluded the MYA and results of our U.S. Commercial exited lines, unless otherwise noted.

DPW

- Represents the total amount of premiums for new and renewal policies billed (written) during the reporting period, normalized for the effect of multi-year policies, excluding industry pools, fronting and exited lines.
- This measure matches DPW to the year in which coverage is provided, whereas under IFRS, the full value of multi-year policies is recognized in the year the policy is written.

Table 39 – Reconciliation of DPW and DPW growth to DPW, as reported under IFRS

	Q4-2017	Q4-2016	2017	2016
DPW, as reported under IFRS	2,301	1,937	8,748	8,197
Less impact of industry pools and fronting	(2)	10	(2)	32
Less results of exited lines	(18)	-	(18)	-
Add share of the results of jointly held insurance operations	-	7	-	47
DPW (full term)	2,281	1,954	8,728	8,276
Add impact of the normalization for multi-year policies	13	7	19	17
DPW	2,294	1,961	8,747	8,293
DPW growth	17%	3%	5%	5%

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Underlying current year loss ratio

- Represents our current year claims ratio excluding catastrophe losses, reinstatement premiums, and PYD.
- Catastrophe events are not predictable, and as such, excluding them provides clearer insight into our analysis of current year performance.

Table 40 – Reconciliation of NEP before reinstatement premiums to NEP and of current year claims to net claims incurred, as reported under IFRS

	Q4-2017	Q4-2016	2017	2016
NEP, as reported under IFRS	2,428	2,035	8,558	7,902
Add share of the results of jointly held insurance operations	-	8	-	44
Less NEP of exited lines	(28)	-	(28)	-
NEP	2,400	2,043	8,530	7,946
Add (deduct) reinstatement premiums ceded (recovered)	(2)	2	(2)	29
NEP, before reinstatement premiums	2,398	2,045	8,528	7,975
Net claims incurred, as reported under IFRS	1,552	1,196	5,538	5,108
Less positive (negative) impact of MYA on underwriting results	11	87	92	34
Less difference between expected return and discount rate on pension assets allocated to net claims incurred	(6)	(3)	(18)	(10)
Add share of the results of jointly held insurance operations	-	5	-	29
Less net claims of exited lines	(33)	-	(33)	-
Total net claims	1,524	1,285	5,579	5,161
Less current year CAT claims	(31)	(34)	(313)	(385)
Add favourable (unfavourable) PYD	62	62	238	389
Current year claims	1,555	1,313	5,504	5,165
NEP, before reinstatement premiums	2,398	2,045	8,528	7,975
Underlying current year loss ratio	64.8%	64.2%	64.5%	64.8%

Underwriting expenses

Table 41 – Reconciliation of underwriting expenses to underwriting expenses, as reported under IFRS

	Q4-2017	Q4-2016	2017	2016
Underwriting expenses, as reported under IFRS	735	635	2,605	2,533
Less difference between expected return and discount rate on pension assets	(6)	(4)	(27)	(16)
Less other underwriting revenues	(26)	(30)	(108)	(123)
Less underwriting expenses of exited lines	(5)	-	(5)	-
Add profit (loss) from jointly held insurance operations	-	4	-	16
Underwriting expenses	698	605	2,465	2,410

ROE

- Excludes the dividends declared on preferred shares.

Table 42 – Reconciliation of ROE to net income

	Q4-2017	Q4-2016	2017	2016
Net income	232	171	792	541
Less preferred share dividends	(10)	(4)	(27)	(20)
Net income attributable to common shareholders	222	167	765	521
Net income attributable to common shareholders – last 12 months			765	521
Average common shareholders' equity			5,961	5,417
ROE for the last 12 months			12.8%	9.6%

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AEPS and AROE

- Exclude the after-tax impact of amortization of intangible assets recognized in business combinations, as well as integration and restructuring costs.
- We believe that these items are not appropriate in assessing our underlying performance.

Table 43 – Reconciliation of AEPS and AROE to net income

	Q4-2017	Q4-2016	2017	2016
Net income	232	171	792	541
Adjustments, net of tax				
Remove currency derivative gain related to the acquisition of OneBeacon	(7)	-	(62)	-
Remove positive impact from U.S. Corporate Tax reform	(27)	-	(27)	-
Add amortization of intangibles recognized in business combinations	20	23	50	56
Add integration and restructuring costs	7	14	49	17
Adjusted net income	225	208	802	614
Less preferred share dividends	(10)	(4)	(27)	(20)
Adjusted net income attributable to common shareholders	215	204	775	594
Divided by weighted-average number of common shares (in millions)	139.2	131.1	133.1	131.2
AEPS, basic and diluted (in dollars)	1.55	1.56	5.82	4.53
Adjusted net income attributable to common shareholders - LTM			775	594
Average common shareholders' equity			5,961	5,417
AROE for the last 12 months			13.0%	11.0%

Cash flow available for investment activities

- Includes net cash flows from cash and cash equivalents and the investment portfolio.
- See Section 17.5 – *Understanding our cash flows* for a reconciliation of this non-IFRS financial measure.

Market-based yield

- Represents the annualized total pre-tax investment income (before expenses), divided by the mid-month average fair value of net equity and fixed-income securities held during the reporting period (average net investments).
- This calculation provides users with a consistent measure of our relative investment performance.

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Section 28 – Accounting and disclosure matters

Reference to our Consolidated financial statements

Significant accounting judgments, estimates and assumptions	Change in accounting policy	Related-party transactions	Standards issued but not yet effective
<i>Note 3</i>	<i>None</i>	<i>Note 29</i>	<i>Note 32</i>

28.1 New accounting standards effective January 1, 2017

There were no new accounting standards, which have a significant impact on our Consolidated financial statements, effective January 1, 2017. Please refer to Note 2 – *Summary of significant accounting policies* in the Consolidated financial statements.

28.2 Significant accounting judgments, estimates and assumptions

The preparation of financial statements in conformity with IFRS requires management to use judgments, estimates and assumptions that can have a significant impact on reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as at the balance sheet date, as well as reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from these estimates.

The key estimates and assumptions that have a risk of causing a material adjustment to the carrying value of certain assets and liabilities within the next financial year are as follows:

Reference to our Consolidated financial statements

Description	Note	Description	Note
Business combinations	<i>Note 4.3</i>	Impairment of financial assets	<i>Note 22.2</i>
Valuation of claims liabilities	<i>Note 10.3</i>	Measurement of income taxes	<i>Note 23.3</i>
Impairment of goodwill and intangible assets	<i>Note 14.2</i>	Valuation of DB obligation	<i>Note 26.6</i>

28.3 Related-party transactions

We enter into transactions with associates and joint ventures in the normal course of business. Most of these related-party transactions are with entities associated with our distribution channel. These transactions mostly comprise of commissions for insurance policies, as well as interest and principal payments on loans. These transactions are measured at the amount of the consideration paid or received, as established and agreed by the related parties. Management believes that such exchange amounts approximate fair value.

We also enter into transactions with key management personnel and post-employment plans. Our key management personnel comprise all members of the Board of Directors and certain members of the Executive Committee. Key management personnel can purchase our insurance products offered in the normal course of business. The terms and conditions of such transactions are essentially the same as those available to our clients and employees. Transactions with post-employment plans comprise the contributions paid to these plans.

Management’s Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

28.4 Financial instruments

An important portion of our Consolidated balance sheets is composed of financial instruments. *For additional information, please refer our Consolidated financial statements.*

Reference to our Consolidated financial statements

Significant accounting policies	Derivative financial instruments	Fair value measurement
<i>Note 2</i>	<i>Note 7</i>	<i>Note 8</i>

28.5 Disclosure controls and procedures

We are committed to providing timely, accurate and balanced disclosure of all material information about the Company and to providing fair and equal access to such information. Management is responsible for establishing and maintaining our disclosure controls and procedures to ensure that information used internally and disclosed externally is complete and reliable. Due to the inherent limitations in all control systems, an evaluation of controls can provide only reasonable, not absolute assurance, that all control issues and instances of fraud or error, if any, within the Company have been detected. We continue to evolve and enhance our system of controls and procedures.

Management, at the direction and under the supervision of the Chief Executive Officer and the Chief Financial Officer of the Company, has evaluated the effectiveness of our disclosure controls and procedures. The evaluation was conducted in accordance with the requirements of National Instrument 52-109 – *Certification of Disclosure in Issuer’s Annual and Interim Filings* (“NI 52-109”) of the Canadian Securities Administrators. This evaluation confirmed, subject to the inherent limitations noted above, the effectiveness of the design and operation of disclosure controls and procedures as at December 31, 2017. Management can therefore provide reasonable assurance that material information relating to the Company and its subsidiaries is reported to it on a timely basis so that it may provide investors with complete and reliable information.

28.6 Internal controls over financial reporting

Management has designed and is responsible for maintaining adequate internal control over financial reporting (“ICFR”) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

Management has limited the scope of design of its disclosure controls and procedures and its ICFR to exclude the controls, policies and procedures of OneBeacon, which was acquired by IFC on September 28, 2017. OneBeacon’s total assets and total liabilities represented approximately 21% and 18% of total consolidated assets and total consolidated liabilities, respectively, as at December 31, 2017. The impact of the acquisition on the total consolidated net income for the year ended December 31, 2017 amounted to a net loss of \$2 million. Management is committed to removing this limitation within the timeframe permitted by regulation.

Management has evaluated the design and operating effectiveness of its ICFR as defined in NI 52-109, excluding OneBeacon’s ICFR as explained above. The evaluation was based on the criteria established in the “Internal Control-Integrated Framework” issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). This evaluation was performed by the Chief Executive Officer and the Chief Financial Officer of the Company with the assistance of other Company Management and staff to the extent deemed necessary. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the ICFR were appropriately designed and operating effectively, as at December 31, 2017.

In spite of its evaluation, Management does recognize that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance and not absolute assurance of achieving the desired control objectives.

No significant changes were made to our ongoing ICFR during 2017 that have materially affected, or are reasonably likely to materially affect, the Company’s ICFR.

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 29 – Shareholder information**29.1 Authorized share capital**

Our authorized share capital consists of an unlimited number of common shares and Class A shares.

29.2 Outstanding share data

Table 44 – Outstanding share data (number of shares)

As at February 2, 2018	
Common shares	139,188,634
Class A	
Series 1 preferred shares	10,000,000
Series 3 preferred shares	8,405,004
Series 4 preferred shares	1,594,996
Series 5 preferred shares ¹	6,000,000
Series 6 preferred shares ²	6,000,000

¹ Series 5 preferred shares were issued on May 24, 2017.² Series 6 preferred shares were issued on August 18, 2017.

Refer to our Annual Information Form for more detailed information on the rights of shareholders and to Note 19 – Common shares and preferred shares to the accompanying Consolidated financial statements for additional information.

29.3 Dividends declared on common shares and preferred shares

Table 45 – Dividends declared per share

	Q1-2018	Q4-2017	FY 2017
Common shares	0.70	0.64	2.56
Class A			
Series 1 preferred shares	0.21225	0.2625	1.0500
Series 3 preferred shares	0.20825	0.20825	0.83305
Series 4 preferred shares	0.217725	0.2143725	0.8067975
Series 5 preferred shares	0.325	0.325	0.7845
Series 6 preferred shares	0.33125	0.49007	0.49007

Please also see Section 11.4 – Delivering value to our shareholders.

29.4 NCIB

On February 13, 2017, we renewed our NCIB program which permits us to purchase for cancellation during the next 12 months up to 6,551,741 common shares, representing approximately 5% of our issued and outstanding common shares as at February 1, 2017.

- From January 1 to February 10, 2017, 20,400 common shares had been repurchased for cancellation under the 2016 NCIB program at an average price of \$93.70 for total consideration of \$1.9 million.
- From February 13 to September 30, 2017, 51,100 common shares had been repurchased for cancellation under the 2017 NCIB program at an average price of \$94.19 per share for a total consideration of \$4.8 million.

Following the announcement of the acquisition of OneBeacon on May 2, 2017, we suspended our purchases under the NCIB to maintain excess capital prior to the closing date of the transaction. We used excess capital for deleveraging, in line with our conservative transaction financing plan. This 2017 NCIB program will expire on February 12, 2018.

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

Section 30 – Selected annual and quarterly information

30.1 Selected annual information

Table 46 – Selected annual information

	2017	2016	2015
Total revenues ¹	9,157	8,538	8,070
Underwriting income ²	486	375	628
Net income	792	541	706
EPS, basic and diluted (in dollars)	5.75	3.97	5.20
Cash dividends declared per share (in dollars)			
Common shares	2.56	2.32	2.12
Class A			
Series 1 Preferred Shares	1.05	1.05	1.05
Series 3 Preferred Shares	0.83	1.00	1.05
Series 4 Preferred Shares	0.81	0.20	n/a
Series 5 Preferred Shares	0.78	n/a	n/a
Series 6 Preferred Shares	0.49	n/a	n/a

¹ Total revenues exclude other underwriting revenues and NEP of exited lines. Refer to Note 27 – Segment information to the accompanying Consolidated financial statements for details.

² Refer to Section 27 – Non-IFRS financial measures.

Table 47 – Selected annual information

As at December 31,	2017	2016	2015
Investments	16,853	14,386	13,504
Total assets	27,928	22,866	21,315
Debt outstanding	2,241	1,393	1,143
Shareholders' equity	7,463	6,088	5,724

30.2 Selected quarterly information

Table 48 – Selected quarterly information¹

	2017				2016			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
DPW	2,294	2,209	2,500	1,744	1,961	2,193	2,458	1,681
Total revenues ²	2,576	2,231	2,204	2,146	2,188	2,187	2,090	2,073
NEP	2,400	2,082	2,051	1,997	2,043	2,036	1,937	1,930
Current year CAT losses	31	89	105	88	34	166	164	21
Favourable PYD	(62)	(53)	(41)	(82)	(62)	(71)	(93)	(163)
Underwriting income	178	170	103	35	153	61	16	145
Combined ratio	92.6%	91.8%	95.0%	98.2%	92.5%	97.0%	99.2%	92.5%
Net investment income	121	101	105	105	104	102	104	104
Net distribution income	28	30	50	24	24	30	43	14
NOI	236	219	193	123	212	137	114	197
Net income	232	171	243	146	171	125	93	152
Per share measures, basic and diluted (in dollars)								
NOIPS	1.63	1.61	1.44	0.90	1.58	1.01	0.83	1.46
EPS	1.60	1.25	1.82	1.08	1.27	0.91	0.67	1.11

¹ Refer to Section 27 – Non-IFRS financial measures.

² Total revenues exclude other underwriting revenues and NEP of exited lines.

See also the discussion on seasonality of the business hereafter.

Management's Discussion and Analysis for the year ended December 31, 2017

(in millions of Canadian dollars, except as otherwise noted)

30.3 Seasonality of the P&C Canadian insurance business

The P&C Canadian insurance business is seasonal in nature. While NEP are generally stable from quarter to quarter, underwriting results are driven by weather conditions which may vary significantly between quarters. The underlying seasonality in our combined ratio is best illustrated by excluding the impact of CAT losses (*see Table 50*).

For instance, in 2017 our first and second quarters saw a higher combined ratio including CAT losses than the third and fourth quarters, meaning that underwriting results were relatively less profitable in Q1-2017 and Q2-2017. When CAT losses are excluded, the first and fourth quarters of 2017 saw a slightly higher combined ratio than the other quarters in 2017, meaning that the underwriting results were relatively less profitable in Q1-2017 and Q4-2017 than the rest of the year.

Table 49 – Seasonal indicator, including CAT losses

	2017	2016	2015	2014	2013	2012	2011	2010	Eight-year average
Q1	1.04	0.97	1.02	1.05	0.97	0.99	1.00	0.98	1.00
Q2	1.01	1.04	1.00	1.00	1.00	0.99	1.03	0.98	1.01
Q3	0.97	1.02	1.02	1.00	1.05	1.03	0.99	1.01	1.01
Q4	0.98	0.97	0.96	0.95	0.98	0.99	0.98	1.03	0.98

Table 50 – Seasonal indicator, excluding CAT losses

	2017	2016	2015	2014	2013	2012	2011	2010	Eight-year average
Q1	1.03	1.01	1.03	1.04	1.04	1.02	1.04	1.00	1.03
Q2	0.99	0.99	1.01	1.02	0.97	0.98	0.96	0.99	0.99
Q3	0.97	0.99	0.98	0.96	0.97	0.97	0.99	0.98	0.98
Q4	1.01	1.01	0.98	0.98	1.02	1.03	1.01	1.03	1.01

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Intact Financial Corporation

Consolidated financial statements

For the year ended December 31, 2017

Management's responsibility for financial reporting

Management is responsible for the preparation and presentation of the Consolidated financial statements of Intact Financial Corporation and its subsidiaries, collectively known as "the Company". This responsibility includes selecting appropriate accounting policies and making estimates and informed judgments based on the anticipated impact of current transactions, events and trends, consistent with International Financial Reporting Standards.

In meeting its responsibility for the reliability of consolidated financial statements, the Company maintains and relies on a comprehensive system of internal control comprising organizational procedural controls and internal accounting controls. The Company's system of internal control includes the communication of policies and of the Company's Code of Conduct, comprehensive business planning, proper segregation of duties, delegation of authority for transactions and personal accountability, selection and training of personnel, safeguarding of assets and maintenance of records. The Company's internal auditors review and evaluate the system of internal control.

The Company's Board of Directors, acting through the Audit Committee, which is composed entirely of Directors, who are neither officers nor employees of the Company, oversees management's responsibility for the design and operation of effective financial reporting and internal control systems, as well as the preparation and presentation of financial information.

The Audit Committee conducts such review and inquiry of management and the internal and external auditors as it deems necessary to establish that the Company employs an appropriate system of internal control, adheres to legislative and regulatory requirements and applies the Company's Code of Conduct. The internal and external auditors, as well as the Actuary, have full and unrestricted access to the Audit Committee, with and without the presence of management.

Pursuant to the Insurance Companies Act of Canada or to the Insurance Act (Québec) ("the Acts"), the Group Chief Actuary, who is a member of management, is appointed by the Board of Directors. The Group Chief Actuary is responsible for discharging the various actuarial responsibilities required by the Acts and conducts a valuation of policy liabilities, in accordance with generally accepted actuarial standards, reporting his results to management and the Audit Committee.

The Company's external auditors, Ernst & Young LLP, are appointed by the shareholders to conduct an independent audit of the Consolidated financial statements of the Company and meet separately with both management and the Audit Committee to discuss the results of their audit, financial reporting and related matters. The Independent Auditors' Report to shareholders appears on the following page.

February 6, 2018



Charles Brindamour
Chief Executive Officer



Louis Marcotte
Senior Vice President and
Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of
Intact Financial Corporation

We have audited the accompanying consolidated financial statements of Intact Financial Corporation, which comprise the consolidated balance sheets as at December 31, 2017 and 2016, and the consolidated statements of comprehensive income, changes in shareholders' equity and cash flows for the years ended December 31, 2017 and 2016, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Intact Financial Corporation as at December 31, 2017 and 2016, and its financial performance and its cash flows for the years ended December 31, 2017 and 2016 in accordance with International Financial Reporting Standards.

Ernst & Young LLP¹

Montréal, Canada
February 6, 2018

¹ CPA auditor, CA, public accountancy permit no A114960



INTACT FINANCIAL CORPORATION

Consolidated financial statements For the year ended December 31, 2017

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INTACT FINANCIAL CORPORATION

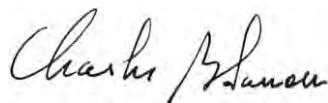
Consolidated balance sheets

(in millions of Canadian dollars, except as otherwise noted)

As at December 31,	Note	2017	2016
Assets			
Investments	5		
Cash and cash equivalents		\$ 163	\$ 168
Debt securities		11,229	8,801
Preferred shares		1,409	1,377
Common shares		3,659	3,635
Loans		393	405
Investments		16,853	14,386
Premium receivables		3,351	3,057
Reinsurance assets	13	822	482
Income taxes receivable		24	116
Deferred tax assets	23	112	142
Deferred acquisition costs		881	747
Other assets	17	782	549
Investments in associates and joint ventures	15	550	543
Property and equipment	16	150	139
Intangible assets	14	2,161	1,302
Goodwill	14	2,242	1,403
Total assets		\$ 27,928	\$ 22,866
Liabilities			
Claims liabilities	10	\$ 10,475	\$ 8,536
Unearned premiums	11	5,365	4,573
Financial liabilities related to investments	6	246	529
Income taxes payable		262	10
Deferred tax liabilities	23	257	404
Other liabilities	17	1,619	1,333
Debt outstanding	18	2,241	1,393
Total liabilities		20,465	16,778
Shareholders' equity			
Common shares	19	2,816	2,082
Preferred shares	19	783	489
Contributed surplus		128	129
Retained earnings		3,520	3,197
Accumulated other comprehensive income			
Available-for-sale securities		224	195
Translation of foreign operations, net of hedges		(2)	-
Other		(6)	(4)
		7,463	6,088
Total liabilities and shareholders' equity		\$ 27,928	\$ 22,866

See accompanying notes to the Consolidated financial statements.

On behalf of the Board:



Charles Brindamour
Director



Eileen Mercier
Director

INTACT FINANCIAL CORPORATION

Consolidated statements of income

(in millions of Canadian dollars, except as otherwise noted)

For the years ended December 31,	Note	2017	2016
Direct premiums written		\$ 8,748	\$ 8,197
Premiums ceded		(221)	(212)
Net premiums written		8,527	7,985
Changes in unearned premiums		31	(83)
Net earned premiums		8,558	7,902
Other underwriting revenues		108	122
Investment income	21		
Interest income		275	265
Dividend income		194	184
Other revenues		158	143
Total revenues		9,293	8,616
Net claims incurred	10	(5,538)	(5,108)
Underwriting expenses		(2,605)	(2,533)
Investment expenses		(37)	(35)
Net gains (losses)	22	69	(70)
Share of profit from investments in associates and joint ventures	15	16	16
Finance costs		(82)	(72)
Integration and restructuring costs		(57)	(22)
Other expenses		(117)	(106)
Income before income taxes		942	686
Income tax expense	23	(150)	(145)
Net income attributable to shareholders		\$ 792	\$ 541
Weighted-average number of common shares outstanding (in millions)	24	133.1	131.2
Earnings per common share, basic and diluted (in dollars)	24	\$ 5.75	\$ 3.97
Dividends paid per common share (in dollars)	19	\$ 2.56	\$ 2.32

See accompanying notes to the Consolidated financial statements.

INTACT FINANCIAL CORPORATION

Consolidated statements of comprehensive income

(in millions of Canadian dollars, except as otherwise noted)

For the years ended December 31,	Note	2017	2016
Net income attributable to shareholders		\$ 792	\$ 541
Other comprehensive income (loss)			
Available-for-sale securities:			
net changes in unrealized gains (losses)		295	378
income tax benefit (expense)		(81)	(94)
reclassification of net losses (gains)		(251)	(105)
income tax benefit (expense)		66	29
		29	208
Cash flow hedges:			
net changes in unrealized gains (losses)		(200)	-
reclassification of net losses (gains)		200	-
		-	-
Foreign exchange gains (losses) on:			
translation of foreign operations, net of tax		7	-
net investment hedges		(12)	-
income tax benefit (expense)		3	-
		(2)	-
Other		(2)	4
Items that may be reclassified subsequently to net income		25	212
Net actuarial gains (losses) on employee future benefits	26	(89)	(35)
income tax benefit (expense)		24	9
Items that will not be reclassified subsequently to net income		(65)	(26)
Other comprehensive income (loss)		(40)	186
Total comprehensive income attributable to shareholders		\$ 752	\$ 727

See accompanying notes to the Consolidated financial statements.

INTACT FINANCIAL CORPORATION

Consolidated statements of changes in shareholders' equity

(in millions of Canadian dollars, except as otherwise noted)

	Note	Common shares	Preferred shares	Contributed surplus	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance as at January 1, 2017		\$ 2,082	\$ 489	\$ 129	\$ 3,197	\$ 191	\$ 6,088
Net income attributable to shareholders		-	-	-	792	-	792
Other comprehensive income (loss)		-	-	-	(65)	25	(40)
Total comprehensive income (loss)		-	-	-	727	25	752
Common shares issued	19	735	-	-	-	-	735
Preferred shares issued	19	-	294	-	-	-	294
Common shares repurchased for cancellation	19	(1)	-	-	(6)	-	(7)
Dividends declared on:							
common shares	19	-	-	-	(351)	-	(351)
preferred shares	19	-	-	-	(27)	-	(27)
Share-based payments	25	-	-	(1)	(6)	-	(7)
Acquisition of non-controlling interests		-	-	-	(14)	-	(14)
Balance as at December 31, 2017		\$ 2,816	\$ 783	\$ 128	\$ 3,520	\$ 216	\$ 7,463
Balance as at January 1, 2016		\$ 2,090	\$ 489	\$ 119	\$ 3,047	\$ (21)	\$ 5,724
Net income attributable to shareholders		-	-	-	541	-	541
Other comprehensive income (loss)		-	-	-	(26)	212	186
Total comprehensive income (loss)		-	-	-	515	212	727
Common shares repurchased for cancellation	19	(8)	-	-	(36)	-	(44)
Dividends declared on:							
common shares	19	-	-	-	(304)	-	(304)
preferred shares	19	-	-	-	(20)	-	(20)
Share-based payments	25	-	-	10	(5)	-	5
Balance as at December 31, 2016		\$ 2,082	\$ 489	\$ 129	\$ 3,197	\$ 191	\$ 6,088

See accompanying notes to the Consolidated financial statements

INTACT FINANCIAL CORPORATION

Consolidated statements of cash flows

(in millions of Canadian dollars, except as otherwise noted)

For the years ended December 31,	Note	2017	2016
Operating activities			
Income before income taxes		\$ 942	\$ 686
Income taxes received (paid), net		32	(158)
Contributions to the defined benefit pension plans	26	(60)	(61)
Share-based payments		(2)	(3)
Net losses (gains)	22	(69)	70
Adjustments for non-cash items	28	225	208
Changes in other operating assets and liabilities	28	(201)	(31)
Changes in net claims liabilities	10	(86)	214
Net cash flows provided by operating activities		781	925
Investing activities			
Business combinations, net of cash acquired	4	(2,139)	(19)
Proceeds from sale of investments		11,058	8,152
Purchases of investments		(10,582)	(8,497)
Purchases of brokerages and other equity investments, net		(108)	(275)
Purchases of intangibles and property and equipment, net		(98)	(120)
Net cash flows used in investing activities		(1,869)	(759)
Financing activities			
Proceeds from issuance of debt	18	422	248
Amount drawn under a credit facility	18	60	-
Proceeds from issuance of common shares	19	731	-
Proceeds from issuance of preferred shares	19	292	-
Common shares repurchased for cancellation	19	(7)	(44)
Common shares repurchased for share-based payments	25	(37)	(19)
Dividends paid on common shares	19	(351)	(304)
Dividends paid on preferred shares	19	(27)	(20)
Net cash flows provided by (used in) financing activities		1,083	(139)
Net increase (decrease) in cash and cash equivalents		(5)	27
Cash and cash equivalents, beginning of year		168	141
Cash and cash equivalents, end of year		\$ 163	\$ 168
Composition of cash and cash equivalents			
Cash		114	167
Cash equivalents		49	1
Cash and cash equivalents, end of year		163	168
Other relevant cash flow disclosures – operating activities			
Interest paid		84	68
Interest received		277	269
Dividends received		207	204

See accompanying notes to the Consolidated financial statements.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 1 – Status of the Company

Intact Financial Corporation (the “Company”), incorporated under the Canada Business Corporations Act, is domiciled in Canada and its shares are publicly traded on the Toronto Stock Exchange (TSX: IFC). The Company has investments in wholly-owned subsidiaries which operate principally in the property and casualty (“P&C”) insurance market. The Company, through its operating subsidiaries, principally underwrites automobile, home, as well as commercial P&C contracts to individuals and businesses. On September 28, 2017, the Company acquired all of the issued and outstanding shares of OneBeacon Insurance Group, Ltd. (“OneBeacon”), a leading U.S. specialty insurer. Further details of the acquisition are provided in *Note 4 – Business combinations*.

These Consolidated financial statements include the accounts of the Company and its subsidiaries. The Company’s significant operating subsidiaries are presented in *Note 27 – Segment information*.

The registered office of the Company is 700 University Avenue, Toronto, Canada.

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Glossary of abbreviations

ABS	Asset-backed securities	IFRS	International Financial Reporting Standards
AFS	Available for sale	JV	Joint ventures
AMF	Autorité des marchés financiers	LAE	Loss adjustment expenses
AOCI	Accumulated other comprehensive income	LTIP	Long-term incentive plan
CAD	Canadian Dollar	MBS	Mortgage-backed securities
CALs	Company action levels	MCT	Minimum capital test
CGU	Cash generating unit	MYA	Market-yield adjustment
DB	Defined benefits	NCI	Non-controlling interest
DPW	Direct premiums written	NEP	Net earned premiums
DSU	Deferred share unit	OCI	Other comprehensive income
EPS	Earnings per share to common shareholders	OSFI	Office of the Superintendent of Financial Institutions
ESPP	Employee share purchase plan	PSU	Performance stock units
FA	Facility Association	RBC	Risk-based capital
FVTPL	Fair value through profit and loss	RSP	Risk sharing pools
IASB	International Accounting Standards Board	RSU	Restricted stock units
IBNR	Insurance claims incurred but not reported by policyholders	USD	U.S. Dollar

2.1 Basis of presentation

These Consolidated financial statements are prepared in accordance with IFRS, as issued by the IASB. These Consolidated financial statements and the accompanying notes were authorized for issue in accordance with a resolution of the Board of Directors on February 6, 2018.

The key accounting policies applied in the preparation of these Consolidated financial statements are described below. These policies have been applied consistently to all periods presented. Certain comparative figures have been reclassified to conform to the presentation adopted in the current year.

2.2 Basis of consolidation

These Consolidated financial statements include the accounts of the Company and its subsidiaries. Table 2.1 presents the basis of consolidation.

In some cases, voting rights in themselves are not sufficient to assess power or significant influence over the relevant activities of the investee or the sharing of control in a joint arrangement. In such cases, judgment is applied through the analysis of management agreements, the effectiveness of voting rights, the significance of the benefits to which the Company is exposed and the degree to which the Company can use its power to affect its returns from investees.

Acquisitions or disposals of equity interests in a subsidiary that do not result in the Company obtaining or losing control are treated as equity transactions and reported as acquisitions or disposals of NCI in the Consolidated statements of changes in shareholders' equity.

All balances, transactions, income and expenses and profits and losses resulting from intercompany transactions and dividends are eliminated on consolidation.

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Table 2.1 – Basis of consolidation

Investment category	Shareholding	Accounting policies
Subsidiaries		
Entities over which the Company:	Generally more than 50% of voting rights	All subsidiaries are fully consolidated from the date control is transferred to the Company.
1. has the power over the relevant activities of the investee;		
2. is exposed, or has rights to variable returns from its involvement with the investee; and		They are deconsolidated from the date control ceases and any gain or loss is recognized in Net gains (losses).
3. has the ability to affect those returns through its power over the investee.		
Associates		
Entities over which the Company:	Generally between 20% to 50% of voting rights	Equity method
1. has the power to participate in the decisions over the relevant activities of the investee, but		<i>Note 2.8 for details</i>
2. does not have control.		
Joint ventures		
Joint arrangements whereby the parties have:	Generally an equal percentage of voting rights from each party to the joint arrangement	Equity method
1. joint control of the arrangements, requiring unanimous consent of the parties sharing control for strategic and operating decision making; and		<i>Note 2.8 for details</i>
2. rights to the net assets of the arrangements.		

2.3 Insurance contracts

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk is transferred when the Company agrees to compensate a policyholder on the occurrence of an adverse specified uncertain future event. As a general guideline, the Company determines whether it has significant insurance risks, by comparing the benefits that could become payable under various possible scenarios relative to the premium received from the policyholder for insuring the risk.

a) Revenue recognition and premium receivables

Premiums written are reported net of cancellations, promotional returns and sales taxes. Premiums written are recognized on the date coverage begins. Premiums written are deferred as Unearned premiums and recognized as NEP (net of reinsurance), on a pro rata basis over the terms of the underlying policies, usually 12 months.

Premium receivables consist of the premiums due for the remaining months of the contracts.

Other underwriting revenues include:

- fees collected from policyholders in connection with the costs incurred for the Company's yearly billing plans, which are recognized over the terms of the underlying policies; and
- fees received for the administration of a portion of the FA policies.

Other revenues include commission revenues received from external insurance providers by consolidated brokers recognized on an accrual basis.

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b) Claims liabilities

Claims liabilities are established to reflect the estimate of the full amount of all liabilities associated with the insurance contracts earned at the balance sheet date, including IBNR, that have occurred on or before the balance sheet date. They also include a provision for adjustment expenses representing the estimated ultimate expected costs of investigating, resolving and processing these claims (usually referred to as loss adjustment expenses or LAE).

Claims liabilities are first determined on a case-by-case basis as insurance claims are reported. They are reassessed as additional information becomes known. Claims liabilities are estimated by the appointed actuaries using generally accepted actuarial standard techniques and are based on assumptions that represent best estimates of possible outcomes, such as historical loss development factors and payment patterns, claims frequency and severity, inflation, reinsurance recoveries, expenses, changes in the legal environment, changes in the regulatory environment and other matters, taking into consideration the circumstances of the Company and the nature of the insurance policies.

The ultimate amount of these liabilities will vary from the best estimate made for a variety of reasons, including additional information with respect to the facts and circumstances of the insurance claims incurred. To recognize the uncertainty in establishing this best estimate, to allow for possible deterioration in experience and to provide greater comfort that the actuarial liabilities are sufficient to pay future benefits, actuaries are required to include margins in some assumptions.

Claims liabilities are discounted to take into account the time value of money, using a rate that reflects the estimated market yield of the underlying assets backing these claims liabilities at the reporting date. Anticipated payment patterns are revised from time to time to reflect the most recent trends and claims environment. This ensures getting the most accurate and representative market yield-based discount rate.

Claims liabilities are considered to be settled when the contract expires, is discharged or cancelled.

c) Reinsurance assets

The Company reports third party reinsurance balances on the Consolidated balance sheets on a gross basis to indicate the extent of credit risk related to third party reinsurance. The estimates for the reinsurers' share of claims liabilities are presented as an asset and are determined on a basis consistent with the related claims liabilities. Reinsurance assets are reviewed for impairment at each reporting date or more frequently when an indication of impairment arises during the reporting period.

d) Deferred acquisition costs

Policy acquisition costs incurred in acquiring insurance premiums include commissions and premium taxes directly related to the writing or renewal of insurance policies. These acquisition costs are deferred and amortized on the same basis as the unearned premiums and are reported in Underwriting expenses. Deferred acquisition costs are written off when the corresponding contracts are settled or cancelled.

e) Liability adequacy test

At the end of each reporting period, a liability adequacy test is performed to validate the adequacy of unearned premiums and deferred acquisition costs. A premium deficiency would exist if unearned premiums were deemed insufficient to cover the estimated future costs associated with the unexpired portion of written insurance policies. A premium deficiency would be recognized immediately as a reduction of deferred acquisition costs to the extent that unearned premiums plus anticipated investment income are not considered adequate to cover for all deferred acquisition costs and related insurance claims and expenses. If the premium deficiency is greater than the unamortized deferred acquisition costs, a liability is accrued for the excess deficiency.

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2.4 Financial instruments

a) Classification and measurement of financial assets and financial liabilities

Table 2.2 – Classification of the Company's most significant financial assets and financial liabilities

Classification	Financial instruments	Description	Initial and subsequent measurement
AFS	Debt securities	Investments intended to be held for an indefinite period of time and which may be sold in response to liquidity needs or changes in market conditions.	Initially measured at fair value using transaction prices at the trade date. Subsequently measured at fair value using bid prices at end of period, with changes in fair value reported in OCI (when unrealized) or in Net gains (losses) when realized or impaired.
	Common shares and preferred shares	Investments neither classified nor designated as FVTPL.	
	Other instruments	Guaranteed loan as well as investments in mutual and private funds.	
Classified as FVTPL	Common shares	Investments purchased with the intention of generating profits in the near term.	Initially measured at fair value using bid prices (for financial assets) or ask prices (for financial liabilities) at the trade date.
	Derivative financial instruments	Derivatives used for economic hedging purposes and for the purpose of modifying the risk profile of the Company's investment portfolio as long as the resulting exposures are within the investment policy guidelines.	Subsequently measured at fair value using bid prices (for financial assets) or ask prices (for financial liabilities) at end of period, with changes in fair value reported in Net gains (losses).
	Embedded derivatives	Derivatives related to the Company's perpetual preferred shares. Treated as separate derivative financial instruments when their economic characteristics and risks are not clearly and closely related to those of the host instrument.	The effective portion of cash flow hedges, as well as net investment hedges in a foreign operation is recorded in foreign exchange gains (losses) OCI.
	Long/short positions	Market neutral investment strategy, where the Company actively manages both the long and short positions, while mitigating overall equity market volatility.	
Designated as FVTPL on initial recognition	Debt securities backing its claims liabilities and some common shares	A portion of the Company's investments backing its claims liabilities has been voluntarily designated as FVTPL to reduce the volatility caused by fluctuations in fair values of underlying claims liabilities due to changes in discount rates. To comply with regulatory guidelines, the Company ensures that the weighted-dollar duration of debt securities designated as FVTPL is approximately equal to the weighted-dollar duration of claims liabilities.	
Cash and cash equivalents, loans and receivables	Cash and cash equivalents	Highly liquid investments that are readily convertible into a known amount of cash are subject to an insignificant risk of changes in value and have an original maturity of three months or less.	Initially measured at fair value at the issuance date. Subsequently measured at amortized cost using the effective interest method, with changes in fair value reported in Net gains (losses) when realized or impaired.
	Loans and receivables	Financial assets with fixed or determinable payments not quoted in an active market.	

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Classification	Financial instruments	Description	Initial and subsequent measurement
Other financial liabilities	Debt outstanding	The Company's Senior and medium-term notes. Amount drawn under a credit facility.	Initially measured at fair value at the issuance date, at the date of acquisition of OneBeacon for the U.S. Senior notes or when credit facility is used. Subsequently measured at amortized cost using the effective interest method, with changes in fair value reported in Net gains (losses) when the liability is extinguished.

b) Fair value measurement

The fair value of financial instruments on initial recognition is normally the transaction price, being the fair value of the consideration given or received. Subsequent to initial recognition, the fair value of financial instruments is determined based on available information and categorized according to a three-level fair value hierarchy.

In 2017, the Company refined its three-level fair value methodology to categorize all Government and Corporate bonds as Level 2, except for Canadian Federal, Canadian Agency housing trust and U.S. Treasuries, which are categorized as Level 1. December 31, 2016 figures have been revised accordingly and resulted in a reclassification of \$2,447 million of fixed-income securities from Level 1 to Level 2.

Table 2.3 – Three-level fair value hierarchy

Levels	Description	Type of financial instruments normally classified as such
Level 1	Quoted prices in active markets for identical assets or liabilities	<ul style="list-style-type: none"> U.S. Treasuries, Canadian Federal and Canadian Agency housing trust debt securities Common shares and preferred shares Investments in mutual funds Exchange-traded derivatives
Level 2	Valuation techniques for which all inputs that have a significant effect on the fair value are observable (either directly or indirectly)	<ul style="list-style-type: none"> All Government and Corporate debt securities, except for U.S. Treasuries, Canadian Federal and Canadian Agency housing trust Unsecured medium-term notes and 2012 U.S. Senior Notes ABS and MBS Over-the-counter derivatives
Level 3	Valuation techniques for which inputs that have a significant effect on the fair value are not based on observable market data	<ul style="list-style-type: none"> Loans¹ Perpetual preferred shares gross up and related embedded derivatives Hedge and private funds Guaranteed loan

¹ Measured at amortized cost with fair value disclosed.

Level 1

A financial instrument is regarded as quoted in an active market if quoted prices for that financial instrument are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Level 2

Where the fair values of financial assets and financial liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of discounted cash flow models and/or mathematical models.

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For discounted cash flow models, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics.

- Estimated future cash flows are influenced by factors such as economic conditions (including country specific risks), concentrations in specific industries, types of instruments, currencies, market liquidity and financial condition of counterparties.
- Discount rates are influenced by risk free interest rates and credit risk.

The inputs to these models are derived from observable market data where possible. Inputs used in valuations include:

- prevailing market rates for bonds with similar characteristics and risk profiles;
- closing prices of the most recent trade date subject to liquidity adjustments; or
- average brokers' quotes when trades are too sparse to constitute an active market.

Level 3

In limited circumstances, the Company uses input parameters that are not based on observable market data. Non-market observable inputs use fair values determined in whole or in part using a valuation technique or model based on assumptions that are neither supported by prices from observable current market transactions for the same instrument nor based on available market data. In these cases, judgment is required to establish fair values. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

- **Loans** – The fair value of loans is determined using a valuation technique based on the income approach. Future inflows of principal and interest are discounted using a pre-tax risk-free rate from the Government of Canada bonds curve plus a risk premium that is based on the credit risk to which the Company would be exposed from the borrowers. The Company ensures that the discount rate is consistent with borrowing rates on similar loans issued by financial institutions. The Company receives guarantees for loans.
- **Perpetual preferred shares gross up and related embedded derivatives** – The fair value of the Company's perpetual preferred shares with call options (which give the issuer the right to redeem the shares at a particular price) has to be measured separately from preferred shares and accounted for as an embedded derivative. To determine the fair value of embedded derivatives, the Company uses a valuation technique based on the implied volatility of underlying preferred shares. The implied volatility is an unobservable parameter that is calculated using an internally developed valuation model, which can be significantly affected by market conditions. Judgment is also required to determine the time period over which the volatility is measured.
- **Hedge funds and private funds** – Hedge funds and private funds are measured at fair value of which the net assets value ("NAV"), is generally the practical expedient and are no longer classified within the fair value hierarchy. The Company employs a number of procedures to assess the reasonableness of the NAV reported by the fund, including obtaining and reviewing periodic and audited financial statements and discussing each fund's pricing with the fund manager throughout the year. In the event, the Company believes that its estimate of the NAV differs from that reported by the fund due to the illiquidity or other factors, the Company will adjust the fund's reported NAV to more appropriately represent the fair value of our interest in the investment.
- **Guaranteed loan** – The fair value of the guaranteed loan is based on a discounted expected cash flow model using information as of the measurement date. The estimated fair value is sensitive to changes in public debt credit spreads, as well as changes in estimates with respect to other variables including a discount to reflect the lack of liquidity due to its private nature, the credit quality, as well as the timing, amount and likelihood of interest and principal payments on the loan which are subject to regulatory approval.

c) Derivative financial instruments and hedging

The Company enters into a variety of derivative financial instruments to manage its exposure arising from financial assets and financial liabilities. Derivative financial instruments are financial contracts whose value is derived from an underlying interest rate, foreign exchange rate, equity or commodity instrument or index. The Company uses derivatives for economic hedging purposes and for the purpose of modifying the risk profile of the Company's investment portfolio as long as the resulting exposures are within the investment policy guidelines. In certain circumstances, these hedges also meet the requirements for hedge accounting. Risk management strategies eligible for hedge accounting have been designated as cash flow hedges or net investment hedges in a foreign operation.

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Derivatives are initially measured at fair value at the trade date and subsequently re-measured at fair value at the end of each reporting date. Derivative financial instruments with a positive fair value are recorded as assets while derivative financial instruments with a negative fair value are recorded as liabilities. Changes in fair value are recorded in Net gains (losses) unless the derivative financial instruments are part of a qualified hedging relationship, as described below.

- **Cash flow hedges**

The Company has used foreign currency derivatives to hedge the OneBeacon purchase price exposure to fluctuations in the CAD/USD exchange rate. The effective portion of the change in the fair value of the hedging derivative, net of taxes, was recognized in OCI. The Company has elected to reclassify net losses accumulated in OCI at the time of closing to the acquisition cost of its investment in OneBeacon.

- **Net investment hedges in a foreign operation (Book value hedge)**

The Company uses foreign currency derivatives to manage its book value exposure to the USD relative to the CAD of its foreign operation, OneBeacon. The effective portion of gains or losses on hedging derivatives, together with foreign exchange translation gains or losses on the net investment in OneBeacon, is recorded in Foreign exchange gains (losses) in OCI.

Where the Company has elected to apply hedge accounting, a hedging relationship is designated and documented at inception. Hedge effectiveness is evaluated at inception and throughout the term of the hedge and hedge accounting is only applied when the Company expects that the hedging relationship will be highly effective in achieving offsetting changes in fair value or changes in cash flows attributable to the risk being hedged.

Hedge accounting is discontinued prospectively when it is determined that the hedging instrument is no longer effective as a hedge, the hedging instrument is terminated or sold, or upon the sale or early termination of the hedged item.

Derivatives that do not qualify for hedge accounting

Certain derivative instruments, while providing effective economic hedges, are not designated as hedges for accounting purposes. Changes in the fair value of such derivatives are recognized in Net gains (losses). *See Note 7 – Derivative financial instruments for details.*

d) Recognition of financial assets and financial liabilities

Financial assets are no longer recorded when the rights to receive cash flows from the instruments have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership. Financial liabilities are no longer recorded when they have expired or have been cancelled.

Securities lending - Financial assets lent by the Company in the course of securities lending operations remain on the balance sheet because the Company has not substantially transferred the risks and rewards related to the lent assets.

Structured settlements - The Company enters into annuity agreements with various Canadian life insurance companies to provide for fixed and recurring payments to claimants.

- When the annuity agreements are non-commutable, non-assignable and non-transferable, the Company is released by the claimant for the settlement of the claim amount. As a result, the liability to its claimants is substantially discharged and the Company removes that liability from its Consolidated balance sheet. However, the Company remains exposed to the credit risk that life insurers may fail to fulfill their obligations.
- When the annuity agreements are commutable, assignable or transferable, the Company keeps the liability and the corresponding asset on its financial statements.

e) Offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is reported on the Consolidated balance sheets only when there is:

- a legally enforceable right to offset the recognized amounts; and
- an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

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f) Revenue and expense recognition

Net investment income

- Interest income from debt securities and loans is recognized on an accrual basis.
- Premiums and discounts on debt securities classified as AFS, as well as premiums earned or discounts incurred for loans and AFS securities are amortized using the effective interest method.
- Dividends are recognized when the shareholders' right to receive payment is established, which is the ex-dividend date.

Net gains (losses)

- Gains and losses on the sale of AFS debt and equity securities are generally calculated on a first in, first out basis, except for certain equity strategies.
- Transaction costs associated with the acquisition of financial instruments classified or designated as FVTPL are expensed as incurred; otherwise, transaction costs are capitalized on initial recognition and amortized using the effective interest method.
- Transaction costs incurred at the time of disposition of a financial instrument are expensed as incurred.
- If a business combination is achieved in stages, any previously held equity interest is re-measured as at its acquisition date fair value and any resulting gain or loss is recognized in income.

g) Impairment of financial assets other than those classified or designated as FVTPL

The Company determines, at each balance sheet date, whether there is objective evidence that a financial asset or a group of financial assets, other than those classified or designated as FVTPL, are impaired. Those financial assets are impaired according to either a debt, equity, or loans and receivables impairment model. The appropriate impairment model is determined based on the characteristics of each instrument, the capacity of the issuer to pay dividends or interest and the Company's intention to either hold the shares for the long term or sell them. Objective evidence of impairment includes:

Debt impairment model

- One or more loss events (a payment default for example) that occurred after initial recognition and that has an impact on the estimated future cash flows of the financial asset.
- Increased probability that the future cash flows will not be recovered based on counterparty credit rating considerations.

Equity impairment model

- A significant, a prolonged, or a significant and prolonged decline in the fair value of an investment below cost.
- Information about significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which an issuer operates, indicating that the cost of an equity instrument may not be recovered.

Table 2.4 – Objective evidence of impairment for equity impairment model

Unrealized loss position	Common shares
Significant	Unrealized loss of 50% or more
Prolonged	Unrealized loss for 15 consecutive months or more
Significant and prolonged	Unrealized loss for 9 consecutive months or more and unrealized loss of 25%

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Loans and receivables impairment model

A payment default or when there are objective indications that the counterparty will not honour its obligations.

The following table summarizes the measurement and recognition of impairment losses.

Table 2.5 – Impairment models

	Debt	Equity	Loans and receivables
Application	<ul style="list-style-type: none"> Debt securities Preferred shares redeemable at the option of the holder Perpetual preferred shares purchased with the intent of holding for the long-term¹ 	<ul style="list-style-type: none"> Common shares Perpetual preferred shares not impaired using the debt impairment model¹ 	<ul style="list-style-type: none"> Loans and receivables: <ul style="list-style-type: none"> Significant (tested individually) Otherwise (grouped by similar characteristics for testing)
Loss measurement	Difference between amortized cost and current fair value less any unrealized loss on that security previously recognized	Difference between acquisition cost and current fair value less any impairment loss on that security previously recognized	Difference between amortized cost and the present value of the estimated future cash flows
Reported loss	Impairment loss removed from OCI and recognized in Net gains (losses)		Impairment loss recognized in Net gains (losses)
Subsequent fair value increases	Recognized in Net gains (losses) when there is observable positive development on the original impairment loss event. Otherwise, recognized in OCI	Recognized directly in OCI Impairment losses are not reversed	Provision can be reversed when the event that gave rise to its initial recognition subsequently disappears Recognized in Net gains (losses) when there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized

¹ Since the business model of the Company is to purchase preferred shares for the purpose of earning dividend income, with the intent of holding them for the long-term, virtually all preferred shares are assessed for impairment using a debt impairment model.

2.5 Business combinations

Business combinations are accounted for using the acquisition method. The purchase consideration is measured at fair value at acquisition date. At that date, the identifiable assets acquired and liabilities assumed are estimated at their fair value. Acquisition-related costs are expensed as incurred. When the Company acquires a business, it assesses financial assets acquired and financial liabilities assumed for appropriate classification and designation in accordance with the contractual term, economic circumstances and relevant conditions at the acquisition date.

If a business combination is achieved in stages, any previously held equity interest is re-measured as at its acquisition date fair value and any resulting gain or loss is recognized in Net gains (losses).

2.6 Goodwill and intangible assets

a) Goodwill

Goodwill is initially measured at cost, being the excess of the fair value of the consideration transferred over the Company's share in the net identifiable assets acquired and liabilities assumed in a business combination. After initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is allocated to CGUs, or groups of CGUs, that are expected to benefit from the business combination in which they arose. Impairment testing is performed at least annually, on June 30, or more frequently if there are objective indicators of impairment, by comparing the recoverable amount of a CGU with its carrying amount. Impairment testing is undertaken at the lowest level at which goodwill is monitored for internal management purposes.

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Upon disposal of a portion of a CGU, the carrying amount of goodwill related to the portion of the CGU sold is included in the determination of gains and losses on disposal. The carrying amount is determined based on the relative fair value of the disposed portion to the total CGU.

b) Intangible assets

The Company's intangible assets consist of distribution networks, trade names, customer relationships and internally developed software.

- Distribution networks represent the contractual agreements between the Company and unconsolidated brokers for the distribution of its insurance products.
- Customer relationships represent the relationships that exist with the policyholders, either directly (as a direct insurer) or indirectly (through consolidated brokers).

Intangible assets are initially measured at cost, except for intangible assets acquired in a business combination which are recorded at fair value as at the date of acquisition.

The useful lives of intangible assets are assessed to be either finite or indefinite. For each distribution network acquired, that assessment depends on the nature of the distribution network. When the related cash flows are expected to continue indefinitely, intangible assets are assessed as having an indefinite useful life.

Intangible assets with finite lives are amortized over their useful lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Intangible assets with indefinite lives, as well as those intangible assets that are under development, are not subject to amortization, but are tested for impairment on an annual basis.

The amortization method and terms of intangible assets assessed as having finite useful lives are shown below.

Table 2.6 – Amortization methods and terms of intangible assets – finite useful life

Intangible assets	Method	Term
Distribution networks	Straight-line	20 to 25 years
Customer relationships	Straight-line	10 years
Internally developed software	Straight-line	3 to 10 years

Amortization of intangible assets is included in Other expenses in the Consolidated statements of income.

2.7 Foreign currency translation

The Consolidated financial statements are presented in Canadian dollars, which is the Company's presentation currency. The functional currency is the currency of the primary economic environment in which an entity operates. The functional currency of most foreign subsidiaries is their local currency, mainly the USD.

Foreign currency transactions

Transactions denominated in foreign currencies are initially recorded in the functional currency of the related entity using the exchange rates in effect at the date of the transaction.

- Monetary assets and liabilities denominated in foreign currencies are translated using the closing exchange rates. Any resulting exchange difference is recognized in income.
- Non-monetary assets and liabilities denominated in foreign currencies and measured at historical cost are translated using historical exchange rates, and those measured at fair value are translated using the exchange rate in effect at the date the fair value is determined.
- Revenues and expenses are translated using the average exchange rates for the period or the exchange rate at the date of the transaction for significant items.
- Net foreign exchange gains and losses are recognized in income with the exception of AFS equity securities where unrealized foreign exchange gains and losses are recognized in OCI until the asset is sold or becomes impaired.

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Foreign operations

- Assets and liabilities of foreign operations whose functional currency is other than the Canadian dollar are translated into Canadian dollars using closing exchange rates.
- Revenues and expenses, as well as cash flows, are translated using the average exchange rates for the period.
- Translation gains or losses are recognized in OCI and are reclassified to income on disposal or partial disposal of the investment in the related foreign operation.

The exchange rates used in the preparation of the consolidated financial statements were as follows:

Table 2.7 – Exchange rates used

	As at			Average rate for the periods		
	Dec. 31, 2017	Sept. 28, 2017	Dec. 31, 2016	2017	Q4-2017	2016
USD vs CAD	1.25730	1.25030	1.34265	1.29832	1.27076	1.32495

2.8 Investments in associates and joint ventures

The Company's investments in associates and joint ventures are initially recorded at the amount of consideration paid, which includes the fair value of tangible assets, intangible assets and goodwill identified on acquisition, plus post-acquisition changes in the Company's share of their net assets. They are subsequently measured using the equity method.

The Company's profit or loss from such investments is shown in Share of profit from investments in associates and joint ventures and reflects the after-tax share of the results of operations of the associates and joint ventures. The Company determines at each reporting date whether there is any objective evidence that investments in associates and joint ventures are impaired.

2.9 Property and equipment

Property and equipment are carried at cost less accumulated depreciation. Depreciation terms are established to depreciate the cost of the assets over their estimated useful lives. Depreciation methods and terms are shown below.

Table 2.8 – Depreciation methods and terms of property and equipment

Property and equipment	Method	Term
Buildings	Straight-line	15 to 40 years
Furniture and equipment	Straight-line	2 to 7 years
Leasehold improvements	Straight-line	Over the terms of related leases

2.10 Leases

Leases which do not transfer to the Company substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Payments made under operating leases are recognized on a straight-line basis over the lease term and reported in underwriting expenses.

2.11 Income taxes

a) Income tax expense (benefit)

Income tax is recognized in Net income, except to the extent that it relates to items recognized in OCI, or directly in equity where it is recognized in OCI or equity. Income tax expense (benefit) comprises current and deferred tax.

- **Current income tax** is based on current year's results of operations, adjusted for items that are not taxable or not deductible. Current income tax is calculated based on income tax laws and rates enacted or substantively enacted as at the balance sheet date. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and provisions are established where appropriate on the basis of amounts expected to be paid to the tax authorities.

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- **Deferred income tax** is provided using the liability method on temporary differences between the carrying value of assets and liabilities and their respective tax values. Deferred tax is calculated using income tax laws and rates enacted or substantively enacted as at the balance sheet date, which are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled. Deferred tax assets are recognized for all deductible temporary differences as well as unused tax losses and tax credits to the extent that it is probable that taxable profit will be available against which the losses can be utilized. For each entity for which there is a history of tax losses, deferred tax assets are only recognized in excess of deferred tax liabilities if there is convincing evidence that future profit will be available.

b) Recognition and offsetting of current tax assets and liabilities

For each legal entity consolidated, current tax assets and liabilities are offset when they relate to the same taxation authority, which allows the legal entity to receive or make one single net payment, and when it intends to settle the outstanding balances on a net basis. Upon consolidation, a current tax asset of one entity is offset against a current tax liability of another entity if, and only if, entities concerned have a legally enforceable right to make or receive a single net payment and entities intend to make or receive such net payment or to recover the asset or settle the liability simultaneously.

2.12 Share-based payments

The Company has three types of shared-based payment plans:

a) LTIP

Certain key employees are eligible to participate in the LTIP. Participants are awarded notional share units referred to as PSUs and RSUs. The payout for the PSUs is based on a specific target composed of the difference between the three-year average adjusted return on equity of the Company and that of the Canadian P&C industry. Most RSUs automatically vest three years from the year of the grant. Vesting for RSUs is not linked to the Company's performance.

Certain participants meeting a defined share ownership threshold ("eligible participants") can elect annually to receive cash in lieu of shares of the Company, subject to the Company's Board of Directors' approval. At the time of the payout, the plan administrator purchases in the market the amount of common shares based upon the vested PSUs and RSUs, and elections of eligible participants.

The awards are estimated and valued at fair value at grant date, which corresponds to the average share price of the Company over the last quarter of the preceding year.

The LTIP is accounted for as an equity-settled plan, except for the participants that are eligible to receive cash in lieu of shares of the Company (accounted for as a cash-settled plan).

Equity-settled plan

The cost of the awards is recognized as an expense over the vesting period, with a corresponding entry to Contributed surplus. The value of each award is not revalued subsequently, but the Company re-estimates the number of awards that are expected to vest at each reporting period. The difference between the market price of the shares purchased and the cumulative cost for the Company of these vested units, net of income taxes, is recorded in Retained earnings.

Cash-settled plan

The cost of the awards is recognized as an expense over the vesting period, with a corresponding entry to Other liabilities. The liability is re-measured at each reporting period based on the number of awards that are expected to vest and the current share price, with any fluctuations in the liability also recorded as an expense until it is settled.

b) ESPP

Employees who are not eligible for the LTIP are entitled to make contributions to a voluntary ESPP. Eligible employees can contribute up to 10% of their annual base salary through a payroll deduction to purchase IFC common shares in the market. As an incentive to participate in the plan the Company matches, at the end of each year, a number of shares equal to 50% of the common shares purchased by the employees during the year (subject to certain conditions). During the following year, the common shares contributed by the Company are purchased by an independent broker at each pay period and deposited in the employee account evenly each pay. The common shares contributed by the Company are awarded and vested at the time they are deposited in the employee account.

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Equity-settled plan

The fair value of awards is estimated at the grant date and is not revalued subsequently, but the Company re-estimates the number of awards that are expected to vest at each reporting period. The cost of awards is recognized as an expense over the vesting period, with a corresponding entry to Contributed surplus. The difference between the market price of the common shares purchased and the cumulative cost for the Company of these vested awards, net of income taxes, is recorded in Retained earnings.

c) DSU

Non-employee directors of the Company are eligible to participate in the Company's DSU. A portion of the remuneration of non-employee directors of the Company must be received in DSUs or common shares of the Company. For the remainder of their compensation, the directors are given the choice of cash, common shares of the Company, DSUs or a combination of the three. Both DSUs and common shares vest at the time of the grant. The DSUs are redeemed upon director retirement or termination and are settled for cash after that time. When directors elect to receive shares, the Company makes instalments to the plan administrator for the purchase of shares of the Company on behalf of the directors.

Cash-settled plan

The DSUs are cash-settled awards which are expensed at the time of granting with a corresponding financial liability reported in Other liabilities. This liability is re-measured at each reporting date based on the current share price, with any fluctuations in the liability also recorded as an expense until it is settled.

2.13 Employee future benefits – pension

The actuarial determination of the DB obligation uses the projected unit credit method and management's best estimate assumptions.

DB pension expense

Cost recognized in Net income in the current period includes:

- service cost: benefits cost provided in exchange for employees' services rendered during the year (current service cost) or prior years (past service cost);
- net interest expense: change in the DB obligation and the plan assets as a result of the passage of time; and
- administrative expenses paid from the pension assets.

The discount rate methodology used to determine the DB expense is determined with reference to the yields on high quality corporate bonds with durations that match the various components of the DB expense.

Re-measurement of net DB liability (asset)

The rate used to discount the DB obligation is determined by reference to market yields on high quality corporate bonds with cash flows that match the timing and amount of expected benefit payments, determined at the end of each reporting period.

Re-measurements are recognized directly in OCI in the period in which they occur and include:

- return on plan assets, which represents the difference between the actual return on plan assets and the return based on the discount rate determined using high quality corporate bonds;
- actuarial gains and losses arising from plan experience; and
- changes in actuarial methods and assumptions, such as discount rate used to discount the DB obligation.

Such re-measurements are also immediately reclassified to Retained earnings as they will not be reclassified to Net income in subsequent periods.

2.14 Current vs non-current

In line with industry practice for insurance companies, the Company's balance sheets are not presented using current and non-current classifications, but are rather presented broadly in order of liquidity. Most of the Company's assets and liabilities are considered current given they are expected to be realized or settled within the Company's normal operating cycle. All other assets and liabilities are considered as non-current and generally include: Investments in associates and joint ventures, Deferred tax assets, Property and equipment, Intangible assets, Goodwill, Deferred tax liabilities and Debt outstanding.

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Note 3 – Significant accounting judgments, estimates and assumptions

The preparation of financial statements in conformity with IFRS requires management to use judgments, estimates and assumptions that can have a significant impact on the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as at the balance sheet date, as well as reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from these estimates.

The key estimates and assumptions that have a risk of causing a material adjustment to the carrying value of certain assets and liabilities within the next financial year are as follows:

Description	Reference	Description	Reference
Business combinations	<i>Note 4.3</i>	Impairment of financial assets	<i>Note 22.2</i>
Valuation of claims liabilities	<i>Note 10.3</i>	Measurement of income taxes	<i>Note 23.3</i>
Impairment of goodwill and intangible assets	<i>Note 14.2</i>	Valuation of DB obligation	<i>Note 26.6</i>

Note 4 – Business combinations

4.1 OneBeacon

On September 28, 2017, the Company completed the acquisition of OneBeacon, a leading U.S. specialty insurer, for a cash consideration of US\$1.7 billion (\$2.3 billion). OneBeacon became a wholly owned subsidiary of the Company and the results of operations are included in the Consolidated financial statements from that date. The acquisition will bolster the Company's Canadian business with new products and cross-border capabilities, and better position it to compete with international insurers. Furthermore, it provides an additional growth pipeline in the U.S. and enables IFC to leverage its consolidation expertise in a fragmented specialty lines market.

The following table summarizes the consideration paid for OneBeacon, and the amounts recognized for the assets acquired and liabilities assumed (determined in accordance with IFRS) as of acquisition date (September 28, 2017).

Table 4.1 – Business combination – OneBeacon

As at December 31, 2017	USD	CAD
Preliminary purchase price		
Cash consideration paid	1,702	2,128
Purchase price hedge	-	200
Total preliminary purchase price	1,702	2,328
Provisional fair value of assets acquired and liabilities assumed		
Investments ¹	2,706	3,383
Premium receivables	275	343
Reinsurance assets	287	358
Distribution networks and other intangibles	626	782
Other assets	379	474
Claims liabilities	(1,630)	(2,038)
Unearned premiums	(650)	(813)
Deferred tax liabilities	(35)	(43)
Debt outstanding	(292)	(364)
Other liabilities	(426)	(532)
Total identifiable net assets	1,240	1,550
Goodwill	462	778
USD/CAD exchange rate as at September 28, 2017		1.25030

¹ Included net cash acquired of US\$151 million.

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As at December 31, 2017, the fair value of the acquired distribution networks, trade names and other intangible assets are based on a preliminary discounted cash flow analysis. The distribution networks are amortized over a 20 year period. The fair value of the claims liabilities reflected the impact of discounting and risk margin. Goodwill reflects the quality of the acquired business and the synergies expected following the integration of OneBeacon. The goodwill is not deductible for tax purposes. The final determination of the fair value of identifiable assets and liabilities acquired will be completed within the prescribed period of one year following the acquisition.

For the year ended December 31, 2017, OneBeacon's contribution to NEP and comprehensive income before income taxes on an IFRS basis was \$354 million and \$24 million respectively, using an exchange rate of 1.27076. On a pro-forma basis, the NEP and income before income taxes would have increased by \$998 million and \$40 million (excluding acquisition-related costs) respectively had OneBeacon been consolidated from January 1, 2017, using an exchange rate of 1.30736.

The integration costs in connection with the acquisition of OneBeacon are reported in Integration and restructuring costs in the Statements of income. These integration costs include items such as the initial net impact of a reinsurance coverage which provides protection against certain negative reserve developments (*see Note 13 – Reinsurance*), pre-acquisition finance costs and acquisition-related expenses.

The Company has hedged the purchase price and book value exposure associated with CAD/USD exchange rate fluctuations (*see Note 7.3 – Currency hedging in relation with the acquisition of OneBeacon*).

4.2 InnovAssur

On November 30, 2016, the Company acquired all of the remaining outstanding shares of InnovAssur, assurances générales inc. ("InnovAssur"), a joint venture previously held with National Bank of Canada, for a cash consideration of \$30 million and a contingent consideration of \$21 million. The contingent consideration is payable over a 15-year period based on annual DPW of InnovAssur. With this transaction, InnovAssur became a wholly owned subsidiary of the Company.

As at December 31, 2016, the excess of the purchase price over the provisional fair value of assets acquired and liabilities assumed was preliminarily recorded to Goodwill for \$63 million. During the year ended December 31, 2017, the Company completed its final assessment of the fair value of assets acquired and liabilities assumed within the prescribed period of one year. The fair value of acquired customer relationships and distribution network was assessed at \$34 million (\$25 million net of deferred tax liabilities) and Goodwill recorded was at \$38 million.

4.3 Significant accounting judgments, estimates and assumptions

Upon initial recognition, the acquiree's assets and liabilities have been included in the Consolidated balance sheets at fair value. Management estimated the fair values using estimates on future cash flows and discount rates. However, actual results can be different from those estimates. The changes in the estimates that relate to new information obtained about facts and circumstances that existed as of the acquisition date, made at initial recognition with regard to items for which the valuation was incomplete, would have an impact on the amount of goodwill recognized. Any other changes in the estimates made at initial recognition would be recognized in income.

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Note 5 – Investments

5.1 Classification of investments

Table 5.1 – Classification of investments

As at	Fair value			Amortized cost	Total carrying amount
	AFS	Classified as FVTPL	Designated as FVTPL	Cash and cash equivalents and loans	
December 31, 2017					
Cash and cash equivalents	-	-	-	163	163
Short-term notes	120	97	-	-	217
Fixed income					
Investment grade					
Government	1,775	-	3,432	-	5,207
Corporate	1,505	-	2,368	-	3,873
Asset-backed ¹	500	-	487	-	987
Mortgage-backed					
Agency ²	90	-	250	-	340
Non-agency	109	-	218	-	327
Below investment grade					
Corporate	-	-	117	-	117
Mortgage backed – non agency	-	-	7	-	7
Non-rated ³	122	-	32	-	154
Debt securities	4,221	97	6,911	-	11,229
Investment grade					
Retractable	24	-	-	-	24
Fixed-rate perpetual	285	-	-	-	285
Other perpetual	1,100	-	-	-	1,100
Preferred shares	1,409	-	-	-	1,409
Common shares	2,272	357	1,030	-	3,659
Loans	-	-	-	393	393
	7,902	454	7,941	556	16,853
December 31, 2016					
Cash and cash equivalents	-	-	-	168	168
Short-term notes	105	-	-	-	105
Fixed income					
Investment grade					
Government	2,029	-	3,329	-	5,358
Corporate	1,485	-	1,642	-	3,127
Asset-backed ¹	144	-	33	-	177
Non-rated	34	-	-	-	34
Debt securities	3,797	-	5,004	-	8,801
Investment grade					
Retractable	46	-	-	-	46
Fixed-rate perpetual	308	-	-	-	308
Other perpetual	1,023	-	-	-	1,023
Preferred shares	1,377	-	-	-	1,377
Common shares	2,184	420	1,031	-	3,635
Loans	-	-	-	405	405
	7,358	420	6,035	573	14,386

¹ Credit card receivables and auto loans.

² Publicly traded mortgage-backed securities which carry the full faith and credit guarantee of the U.S. government or are guaranteed by a government sponsored entity.

³ Included \$40 million of mortgage-backed securities.

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The Company uses data from various rating agencies to rate debt securities and preferred shares. When there are two ratings for the same instrument, the Company uses the lower of the two. When there are three ratings for the same instrument, the Company uses the median. Debt securities with a rating equal to or above 'BBB-' are classified as investment grade. Preferred shares with a rating equal to or above 'P3L' are classified as investment grade.

5.2 Carrying value of investments

Table 5.2 – Carrying value of investments

As at	FVTPL				Other	Total
	investments				investments	investments
	Carrying value	Amortized cost	Unrealized gains	Unrealized losses	Carrying value	Carrying value
December 31, 2017						
Cash and cash equivalents	-	163	-	-	163	163
Debt securities	7,008	4,199	43	(21)	4,221	11,229
Preferred shares	-	1,330	95	(16)	1,409	1,409
Common shares	1,387	2,060	263	(51)	2,272	3,659
Loans	-	393	-	-	393	393
	8,395	8,145	401	(88)	8,458	16,853
December 31, 2016						
Cash and cash equivalents	-	168	-	-	168	168
Debt securities	5,004	3,714	92	(9)	3,797	8,801
Preferred shares	-	1,444	56	(123)	1,377	1,377
Common shares	1,451	1,931	273	(20)	2,184	3,635
Loans	-	405	-	-	405	405
	6,455	7,662	421	(152)	7,931	14,386

5.3 Market neutral equity investment strategy

Table 5.3 – Market neutral equity investment strategy

As at December 31,	2017		2016	
	Fair value	Collateral	Fair value	Collateral
Long positions – common shares	121	-	324	-
Short positions (Table 6.1)	(122)	126	(327)	338

5.4 Securities lending

The Company participates in a securities lending program to generate fee income. This program is managed by the Company's custodian, a major Canadian financial institution. The Company lends securities it owns to other financial institutions to allow them to meet their delivery commitments. Collateral, mainly consisting of government securities, is provided by the counterparty and held in trust by the custodian for the benefit of the Company until the underlying security has been returned to the Company. The collateral cannot be sold or re-pledged externally by the Company, unless the counterparty defaults on its financial obligations. Additional collateral is obtained or refunded on a daily basis as the market value of underlying loaned securities fluctuates.

The Company loaned securities with a fair value of \$1,087 million as at December 31, 2017 (December 31, 2016 – \$720 million) that are reported in Investments. The collateral amounted to \$1,144 million as at December 31, 2017 (December 31, 2016 – \$758 million), representing approximately 105% of the securities loaned fair value as at December 31, 2017 and 2016.

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Note 6 – Financial liabilities related to investments

Table 6.1 – Financial liabilities related to investments

As at December 31,	2017	2016
Equities sold short positions (<i>Table 5.3</i>)	122	327
Embedded derivatives (<i>Note 8.1</i>)	79	39
Accounts payable to investment brokers on unsettled trades	24	29
Derivative financial liabilities (<i>Table 7.2</i>)	21	38
Net asset value attributable to third party unit holders	-	96
	246	529

During the year ended December 31, 2017, the Company sold an investment in a mutual fund, which was previously consolidated. As a result of this sale, the Company's investments and related financial liabilities no longer include the net asset value attributable to third party unit holders and related NCI.

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Note 7 – Derivative financial instruments

7.1 Types of derivatives used

Table 7.1 – Types of derivatives used

Derivatives	Description	Objective	Intent to hold instrument
Forwards	Contractual obligations to exchange:		
Currency	one currency for another on a predetermined future date	Mitigate risk arising from foreign currency fluctuations on foreign currency cash inflows and outflows impacting the Company's Canadian operations Mitigate risk arising from foreign currency fluctuations on the Company's net investment in a U.S. subsidiary Mitigate risk arising from foreign currency fluctuations on the U.S. debt portfolio supporting the Company's Canadian operations	Cash flow hedges Risk management purposes Risk management purposes
Futures	Contractual obligations to buy or sell:		
Interest rate	an interest rate sensitive financial instrument on a predetermined future date at a specified price	Modify or mitigate exposure to interest rate fluctuations	Mostly for risk management purposes
Equity	a specified amount of stocks, a basket of stocks or an equity index at an agreed price on a specified date	Mitigate exposure to Canadian equity market	Risk management purposes
Swaps	Over-the-counter contracts:		
Swap agreements	in which two counterparties exchange a series of cash flows based on a basket of stocks, applied to a notional amount	Mitigate exposure to equity market fluctuations	Risk management purposes
Credit default	that transfer credit risk related to an underlying financial instrument from one counterparty to another	Modify exposure to credit	Risk management purposes
Options	Contractual agreements under which the seller grants to the buyer the right, but not the obligation either to buy (call option) or sell (put option):		
Inflation caps	an index at a predetermined price, at or by a specified future date	Mitigate exposure to inflation risk	Trading purposes

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7.2 Fair value and notional amount of derivatives

Derivative financial assets are presented on the Consolidated balance sheets as part of Other assets and derivative financial liabilities are presented as part of Financial liabilities related to investments.

Table 7.2 – Fair value and notional amount of derivatives by nature of risk

As at December 31,	2017			2016		
	Notional amount	Fair value		Notional amount	Fair value	
		Asset	Liability		Asset	Liability
Foreign currency contracts						
Forwards ¹	1,852	8	13	1,098	6	-
Interest rate contracts						
Futures and forwards	1,317	-	-	949	-	-
Equity contracts						
Swap agreements	1,022	-	8	1,023	-	38
Futures	247	-	-	167	-	-
Credit contracts						
Swap agreements	-	-	-	39	1	-
Inflation options						
Options	63	-	-	93	-	-
	4,501	8	21	3,369	7	38
Net investment hedges (Note 7.3)	383	6	-	-	-	-
Held for risk management purposes	3,954	2	21	2,957	6	38
Held for trading purposes	164	-	-	412	1	-
	4,501	8	21	3,369	7	38
Term to maturity:						
less than one year	4,279			3,266		
from one to five years	222			103		
over five years	-			-		
	4,501			3,369		

¹ Include net investment hedges of OneBeacon.

7.3 Currency hedging in relation with the acquisition of OneBeacon

Purchase price hedges – On May 2, 2017, in connection with the acquisition of OneBeacon, the Company entered into foreign currency forward contracts to hedge the purchase price exposure to fluctuations in the CAD/USD exchange rate. These derivatives for a notional amount of US\$1.7 billion were designated and qualified as cash flow hedges. At closing, losses recognized in AOCI have been included in the acquisition cost of OneBeacon.

Net investment hedges (Book value hedge) – On May 2, 2017, the Company entered into foreign currency forward contracts for a notional amount of US\$600 million to reduce its book value exposure to the USD. These derivatives were recorded at fair value and gains and losses were recorded in net income up to closing. At closing, the Company designated these forward contracts as net investment hedges to cover U.S. operations. On December 20, 2017, the Company terminated the hedging relationship on half of the US\$600 million. The effective portion of gains or losses and the foreign exchange impact were recorded in OCI, while the ineffective portion was recorded in net gains (losses) in the Consolidated statements of income.

See Note 4 – Business Combinations for more details on the acquisition of OneBeacon.

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Note 8 – Fair value measurement

8.1 Categorization of fair values

In 2017 the Company refined its methodology to categorize the fair value measurements according to a three-level fair value hierarchy (see *Note 2 – Summary of significant accounting policies*).

Table 8.1 – Fair value hierarchy of financial assets and financial liabilities

As at	Level 1 Valued using quoted (unadjusted) market prices	Level 2 Valued using models (with observable inputs)	Level 3 Valued using models (without observable inputs)	Total
December 31, 2017				
Short-term notes	217	-	-	217
Fixed income				
Investment grade				
Government	2,902	2,305	-	5,207
Corporate	-	3,873	-	3,873
Asset-backed	-	987	-	987
Mortgage-backed				
Agency	-	340	-	340
Non-agency	-	327	-	327
Below investment grade				
Corporate	-	117	-	117
Mortgage backed – non agency	-	7	-	7
Non-rated	-	43	111	154
Debt securities	3,119	7,999	111	11,229
Preferred shares	1,330	-	79	1,409
Common shares	3,595	35	29	3,659
Derivative financial assets (Table 7.2)	-	8	-	8
Total financial assets measured at fair value	8,044	8,042	219	16,305
Total financial liabilities measured at fair value	122	21	79	222
December 31, 2016				
Short-term notes	105	-	-	105
Fixed income				
Investment grade				
Government	3,090	2,268	-	5,358
Corporate	-	3,127	-	3,127
Asset-backed	-	177	-	177
Non-rated	-	-	34	34
Debt securities	3,195	5,572	34	8,801
Preferred shares	1,338	-	39	1,377
Common shares	3,635	-	-	3,635
Derivative financial assets (Table 7.2)	-	7	-	7
Total financial assets measured at fair value	8,168	5,579	73	13,820
Total financial liabilities measured at fair value	423	38	39	500

The fair value of loans was \$384 million as at December 31, 2017 (December 31, 2016 – \$400 million).

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Note 9 – Financial risk

The Company has a comprehensive risk management framework and internal control procedures designed to manage and monitor various risks in order to protect the Company’s business, clients, shareholders and employees. The risk management programs aim to manage risks that could materially impair the Company’s financial position, accept risks that contribute to sustainable earnings and growth and disclose these risks in a full and complete manner.

Effective risk management consists in identifying, understanding and communicating all material risks that the Company is exposed to in the course of its operations. In order to make sound business decisions, both strategically and operationally, management must have continual direct access to the most timely and accurate information possible. Either directly or through its committees, the Board of Directors ensures that the Company’s management has put appropriate risk management programs in place. The Board of Directors, directly and in particular through its Risk Management Committee, oversees the Company’s risk management programs, procedures and controls and, in this regard, receives periodic reports from, among others, the Risk Management Department through the Chief Risk Officer and internal auditors.

Table 9.1 – Financial risk

	Market risk	Basis risk	Credit risk	Liquidity risk
Risk definition	Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in equity market prices, interest rates or spreads, foreign exchange rates or commodity market.	Risk that offsetting investments in an economic hedging strategy will not experience price changes that entirely offset each other.	Possibility that counterparties may not be able to meet payment obligations when they become due.	Risk that the Company will encounter difficulty in raising funds to meet obligations associated with financial liabilities.
Reference	<i>Notes 9.1 and 9.2</i>	<i>Note 9.3</i>	<i>Note 9.4</i>	<i>Note 9.5</i>

9.1 Market risk

Table 9.2 – Market risk

	Equity price risk	Interest rate risk	Currency risk
Risk definition	Risk of losses arising from changes in equity market prices.	Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in interest rates or spreads.	Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.
Risk exposure	Significant exposure to price changes for common shares and preferred shares.	Significant exposure to changes in interest rates from debt securities and preferred shares.	A portion of the Company’s net investment in a foreign subsidiary. Investments supporting the Company’s Canadian operations denominated in foreign currencies, mainly USD. A portion of foreign currency inflows and outflows impacting the Company’s Canadian operations.
Risk management investment policy	Set forth limits in terms of equity exposure.	Set forth limits in terms of interest rate and credit spread duration.	Set forth limits in terms of currency exposure.
Risk mitigation	Through asset class and economic sector diversification and, in some cases, the use of derivatives.	Through the use of interest-rate derivatives. Changes in the discount rate applied to the Company’s claims liabilities offers a partial offset to the change in price of interest sensitive assets.	Through the use of foreign-currency derivatives.

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The Operational Investment Committee and Compliance Review and Corporate Governance Committee regularly monitor and review compliance, respectively, with the Company's investment policies.

a) Sensitivity analyses to market risk

Sensitivity analyses are one risk management technique that assists management in ensuring that risks assumed remain within the Company's risk tolerance level. Sensitivity analyses involve varying a single factor to assess the impact that this would have on the Company's results and financial condition, excluding any management action. Actual results can differ materially from these estimates for a variety of reasons and therefore, these sensitivities should be considered as directional estimates.

Table 9.3 – Sensitivity analyses (after tax)

For the years ended December 31,	2017		2016	
	Net income	OCI	Net income	OCI
Equity price risk				
Common share prices (10% decrease) ¹	(1)	(201)	9	(193)
Preferred share prices (5% decrease) ²	13	(62)	8	(57)
Interest rate risk (100 basis point increase)	9	(64)	4	(75)
Currency risk (strengthening of Canadian dollar by 10% vs all currencies) ³				
U.S. investments supporting the Company's Canadian operations	6	(1)	2	(47)
International equities supporting the Company's Canadian operations	-	(19)	-	-
Consolidated net assets of a U.S. subsidiary	-	(176)	-	-

¹ Net of any equity hedges, including the impact of any impairment.

² Including the impact on related embedded derivatives.

³ After giving effect to foreign exchange derivatives.

These sensitivity analyses were prepared using the following assumptions:

- shifts in the yield curve are parallel;
- interest rates, equity prices and foreign currency move independently;
- credit, liquidity and basis risks have not been considered;
- impact on the Company's pension plans has been considered; and
- risk reduction measures perform as expected, with no material basis risk and no counterparty defaults.

AFS debt or equity securities in an unrealized loss position, as reflected in AOCI, may be realized through sale in the future.

b) Exposure to currency risk

Table 9.4 – Net currency exposure to the USD

As at December 31,	USD	
	2017	2016
Fixed-income securities	1,031	730
Common shares	3	476
Other net assets (liabilities)	(21)	1
	1,013	1,207
Less: USD foreign-currency derivatives, notional amount	(1,016)	(792)
Net U.S. exposure - Canadian operations	(3)	415
Consolidated net assets of U.S. subsidiary	1,755	-
Less: net investment hedges	(300)	-
Net currency exposure – U.S. subsidiary	1,455	-
Total net exposure	1,452	415

The Company's investment portfolio is mainly comprised of Canadian securities. As a means to provide geographic and sector diversification to its portfolio, the Company also invests in high-quality international common shares. The Company's net exposure to a particular foreign currency (other than the USD) was not significant as at December 31, 2017 and 2016.

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9.2 Interest risk

The following table presents the fair value and respective duration of the Company's assets and liabilities measured at fair value, as well as financial instruments that are sensitive to movements in interest rates.

Table 9.5 – Interest risk

As at December 31,	2017		2016	
	Fair value	Duration (in years)	Fair value	Duration (in years)
Investments				
Debt securities	11,229	3.43	8,801	4.01
Preferred shares	1,409	2.94	1,377	3.24
Pension plan debt securities assets (Note 26.3)	1,308	12.0	1,213	13.1
Net claims liabilities (Note 10.1)	9,746	2.37	8,071	2.4
Pension DB obligation (Note 26.2)	2,263	17.3	2,014	18.2

The Company manages the interest rate risk exposure of its investments portfolio in accordance with its investment policies. Compliance with interest rate risk exposure ranges and targets established in these policies is monitored regularly.

9.3 Basis risk

The Company's use of derivatives exposes the Company to a number of risks, including credit and market risks. The hedging of certain risks with derivatives results in basis risk. The imperfect correlation between the hedging instrument and hedged item creates the potential for excess gains or losses in a hedging strategy, thus adding risk to the position. The Company monitors the effectiveness of its economic hedges on a regular basis. Basis risk is controlled by limits prescribed in the investment policy, which are monitored regularly.

9.4 Credit risk

The Company's credit risk exposure is concentrated primarily in its debt securities and preferred shares and, to a lesser extent, in its premium receivables, reinsurance assets, and structured settlement agreements entered into with various life insurance companies. The Company is also subject to counterparty credit risk arising from reinsurance, over-the-counter derivatives, as well as securities lending and borrowing transactions. A counterparty is any person or entity from which cash or other forms of consideration are expected to extinguish a liability or obligation to the Company. These exposures and the Company's risk management policy and practices used to mitigate credit risk are explained below.

a) Credit exposure

The table below presents the Company's maximum exposure to credit risk without taking into account any collateral held or other credit enhancements available to the Company to mitigate this risk. For on-balance sheet exposures, maximum exposure to credit risk is defined as the carrying value of the asset.

Table 9.6 – Maximum exposure to credit risk

As at December 31,	2017	2016
Cash and cash equivalents	163	168
Debt securities	11,229	8,801
Preferred shares	1,409	1,377
Loans	393	405
Premium receivables	3,351	3,057
Reinsurance assets	822	482
Other financial assets ¹	613	356
On-balance sheet credit risk exposure	17,980	14,646
Structured settlements	1,229	1,170
Off-balance sheet credit risk exposure	1,229	1,170

¹Include restricted funds, other receivables and recoverables, financial assets related to investments, industry pools receivable, accrued investment income and guaranteed loan.

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Structured settlements

The Company has obligations to pay certain fixed amounts to claimants on a recurring basis and has purchased annuities from life insurers to provide for those payments. In the event that the life insurers are in default, the Company may have to assume a financial guarantee obligation. Therefore, the net risk to the Company is any credit risk related to the life insurers. Since the Company deals with registered life insurers with credit rating of at least 'A-' at the inception of the contract, this credit risk is minimal.

b) Credit quality

The Company's risk management strategy is to invest in debt securities and preferred shares of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer by imposing limits based upon credit quality. The Company's investment policy requires that, at the time of the investment, all debt securities have a minimum credit rating of 'BBB' and of 'P3' for preferred shares. This credit quality restriction excludes indirect investments through debt funds. In the case of funds, specific policy limits apply to manage the overall exposure to these investments. Management monitors subsequent credit rating changes on a regular basis.

As of December 31, 2017, approximately 90% of the fixed-income securities were rated 'A-' or better and 79% of the preferred shares were highly-rated with at least a 'P2L' credit rating (December 31, 2016 – 98% and 79% respectively). The decrease in the rating of the fixed-income securities reflected the addition of OneBeacon investments.

c) Credit risk concentration

Concentration of credit risk exists where a number of borrowers or counterparties are engaged in similar activities, are located in the same geographic area or have comparable economic characteristics. Their ability to meet contractual obligations may be similarly affected by changing economic, political or other conditions. The Company's investments could be sensitive to changing conditions in specific geographic regions or industries.

Investments

The Company has a significant concentration of its investments in the financial sector and in Canada. These risk concentrations are closely monitored. As a means to provide sector diversification, the Company holds investment-grade non-financial U.S. corporate bonds. The acquisition of OneBeacon, as well as the existing U.S. and international equity portfolio, reduce the concentration risk in Canada.

Table 9.7 – Investment breakdown by country of incorporation and by industry

As at December 31,	Investments		Pension assets	
	2017	2016	2017	2016
By country of incorporation				
Canada	71%	87%	84%	85%
U.S.	25%	11%	8%	7%
Other	4%	2%	8%	8%
	100%	100%	100%	100%
By industry				
Government	33%	39%	44%	45%
Banks, insurance and diversified financial services	28%	33%	23%	23%
ABS and MBS	10%	1%	-%	-%
Energy	6%	8%	6%	6%
Other	23%	19%	27%	26%
	100%	100%	100%	100%

For the Company's federally regulated subsidiaries, the assets invested in any entity or group of related entities are limited by OSFI to 5% of the subsidiaries' assets. The Company also monitors aggregate concentrations of credit risk by country of issuer and by industry regardless of the asset class (see Note 13.4 – Risk management and counterparty credit risk). The Company applies limits against that aggregate exposure, which are more conservative than OSFI's limits. Investment portfolio diversification helps to mitigate credit risk and is monitored against established guidelines with respect to exposure to individual issuers.

The majority of the investment portfolio is invested in well established, active and liquid markets.

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d) Counterparty credit risk

Counterparty credit risk arises from reinsurance (*see Note 13.4 – Risk management and counterparty credit risk*), over-the-counter derivatives, as well as securities lending and borrowing transactions.

Over-the-counter derivatives, as well as securities lending and borrowing transactions

Credit risk from over-the-counter derivative transactions reflects the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the Company. Therefore, derivative-related credit risk is represented by the positive fair value of an over-the-counter instrument and is normally a small fraction of the contract's notional amount. In addition, the Company may be subject to wrong-way risk arising from certain derivative transactions. Wrong-way risk occurs when exposure to a counterparty is adversely correlated with the credit quality of that counterparty.

Credit risk from securities lending and borrowing transactions arises when the counterparty is allowed to re-hypothecate or re-pledge the collateral externally. Credit risk from securities borrowing is the potential for the counterparty to default when the value of the collateral posted is higher than the value of the security borrowed.

The Company subjects its derivative-related, as well as securities lending and borrowing credit risk to the same credit approval, limit and monitoring standards that it uses for managing other transactions that create credit exposure. This includes evaluating the creditworthiness of counterparties, and managing the size, diversification and maturity structure of the portfolio. Credit utilization for all products is compared with established limits on a continual basis and is subject to a monthly review by the Operational Investment Committee. The Company has adopted a policy whereby, upon signing the derivative contract, the counterparty is required to have a minimum credit rating of 'A-' and an issuer credit spread below established thresholds, or has a guarantee from a company rated 'A-' or better.

The Company uses netting clauses in master derivative agreements to reduce derivative-related credit exposure. Netting clauses in master derivative agreements provide for a single net settlement of all financial instruments covered by the agreement in the event of default. However, credit risk is reduced only to the extent that the Company's financial obligations toward the counterparty to such an agreement can be set off against obligations such counterparty has toward the Company. The overall exposure to credit risk that is reduced through the netting clauses may change substantially following the reporting date as the exposure is affected by each transaction subject to the agreement as well as by changes in underlying market rates and values.

The Company's rigorous collateral management process is another significant credit mitigation tool used to manage counterparty credit risk arising from over-the-counter derivative and securities lending and borrowing transactions. Most of the Company's legal agreements allow for daily collateral movement. Consequently, the Company regularly validates that the collateral that it pledges is not too high and that mark-to-market provisions for derivatives are sufficient. Mark-to-market provisions provide the Company with the right to request that the counterparty pay down or collateralize the current market value of its derivative positions when the value exceeds a specified threshold amount.

The aggregate credit risk exposure was \$95 million as at December 31, 2017 (December 31, 2016 – \$90 million) and is the sum of the replacement cost net of collateral plus an add-on amount for potential future credit exposure. The risk-weighted amount represents the credit risk equivalent, weighted according to the creditworthiness of the counterparty, as prescribed by OSFI.

9.5 Liquidity risk

The Company's liquidity management is governed by establishing a prudent policy that identifies oversight responsibilities as well as by setting limits and implementing effective techniques to monitor, measure and control exposure to liquidity risk. As a result of the nature of the Company's P&C insurance activities, cash flows may be highly volatile and unpredictable.

The Company's liquidity needs are rigorously managed by matching asset and liability cash flows and by establishing forecasts for cash inflows and outflows. The Company invests in various types of assets in order to match them to its liabilities. This method maps the obligations towards insured clients to asset life and performance. The Company reviews the matching status on a quarterly basis. To manage its cash flow requirements, a portion of the Company's investments is maintained in short-term (less than one year) highly liquid money market securities. A large portion of the investments are unencumbered and held in highly liquid federal and provincial government debt to protect against any unanticipated large cash requirements. In addition, the Company also has an unsecured committed credit facility (*see Note 18.3 – Credit facility*).

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a) Investments and derivative financial instruments by contractual maturity

Table 9.8 – Investments and derivative financial instruments by contractual maturity

	Less than 1 year	From 1 to 5 years	Over 5 years	No specific maturity	Total
As at December 31, 2017					
Cash and cash equivalents	163	-	-	-	163
Debt securities	1,338	5,781	3,999	111	11,229
Preferred shares	4	17	3	1,385	1,409
Common shares	-	-	-	3,659	3,659
Loans	11	42	340	-	393
	1,516	5,840	4,342	5,155	16,853
Derivative financial instruments	21	-	-	-	21
	1,537	5,840	4,342	5,155	16,874
As at December 31, 2016					
Cash and cash equivalents	168	-	-	-	168
Debt securities	995	4,695	3,077	34	8,801
Preferred shares	22	16	8	1,331	1,377
Common shares	-	-	-	3,635	3,635
Loans	6	49	350	-	405
	1,191	4,760	3,435	5,000	14,386
Derivative financial instruments	38	-	-	-	38
	1,229	4,760	3,435	5,000	14,424

b) Financial liabilities by contractual maturity

Table 9.9 – Financial liabilities by contractual maturity

	Less than 1 year	From 1 to 5 years	Over 5 years	No specific maturity	Total
As at December 31, 2017					
Claims liabilities – undiscounted value	4,139	4,463	1,808	-	10,410
Debt outstanding	-	974	1,267	-	2,241
Other financial liabilities	763	81	35	558	1,437
	4,902	5,518	3,110	558	14,088
As at December 31, 2016					
Claims liabilities – undiscounted value	3,295	3,328	1,614	-	8,237
Debt outstanding	-	549	844	-	1,393
Other financial liabilities	737	119	30	629	1,515
	4,032	3,996	2,488	629	11,145

The expected maturity of claims liabilities is determined by estimating when claims liabilities will be settled. Unearned premiums have been excluded because they do not constitute actual obligations.

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Note 10 – Claims liabilities

On the Consolidated balance sheets, claims liabilities are reported gross of the reinsurers' share, which is included in Reinsurance assets. Changes in claims liabilities, net of reinsurance, are reported in Net claims incurred.

10.1 Movements in claims liabilities

As a result of the acquisition of OneBeacon, the Company has refined its estimate when determining the overall risk margin assumption to recognize the benefit of diversification of insurance risk across lines of businesses and geographic regions. This refinement in estimate recognized in the third quarter of 2017 resulted in a decrease in Net claims incurred of \$196 million (see Note 2 – Summary of significant accounting policies).

Table 10.1 – Movements in claims liabilities

For the year ended	Direct	Ceded	Net
December 31, 2017			
Balance, beginning of year	8,536	465	8,071
Current year claims	5,705	54	5,651
Unfavourable (favourable) prior-year claims development	(299)	(46)	(253)
Decrease (increase) due to changes in discount rate	(89)	(2)	(87)
Total claims incurred	5,317	6	5,311
Claims paid	(5,478)	(180)	(5,298)
Business combinations ¹ (Note 4)	2,090	437	1,653
Exchange rate differences	10	1	9
Balance, end of year	10,475	729	9,746
December 31, 2016			
Balance, beginning of year	8,094	253	7,841
Current year claims	5,884	353	5,531
Unfavourable (favourable) prior-year claims development	(396)	(6)	(390)
Decrease (increase) due to changes in discount rate	(34)	(1)	(33)
Total claims incurred	5,454	346	5,108
Claims paid	(5,028)	(134)	(4,894)
Business combinations (Note 4)	16	-	16
Balance, end of year	8,536	465	8,071

¹ Net of positive impact on claims liabilities resulting from the purchase of adverse development coverage (see Note 13 – Reinsurance).

10.2 Fair value of claims liabilities

The Company estimates that the fair value of its net claims liabilities approximate their carrying values. There was no premium deficiency as at December 31, 2017 and 2016.

Table 10.2 – Carrying value of claims liabilities

As at	Direct	Ceded	Net
December 31, 2017			
Undiscounted value	10,410	656	9,754
Effect of time value of money using a discount rate of 2.33%	(553)	(33)	(520)
Risk margin (Note 2.3b)	618	106	512
	10,475	729	9,746
December 31, 2016			
Undiscounted value	8,237	447	7,790
Effect of time value of money using a discount rate of 1.84%	(344)	(9)	(335)
Risk margin	643	27	616
	8,536	465	8,071

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10.3 Significant accounting judgments, estimates and assumptions

The Company establishes claims liabilities to cover the estimated liability for the payment of all losses, including LAE incurred with respect to insurance contracts underwritten by the Company. The ultimate cost of claims liabilities is estimated by using a range of standard actuarial claims projection techniques in accordance with generally accepted actuarial methods.

The main assumption underlying these techniques is that a company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim (severity) and average number of claims (frequency) based on the observed development of earlier years and expected loss ratios. Historical claims development is analyzed by accident years, by geographical area, as well as by significant business line and claim type. Large catastrophic events are separately addressed, either by being reserved at the face value of loss adjuster estimates in the case of very large losses or separately projected in order to reflect their future development which might differ from historical data in the case of catastrophic events. Expected claim cost inflation is also taken into account when estimating claims liabilities.

Additional qualitative judgment is used to assess the extent to which past trends may not apply in the future, in order to arrive at the estimated ultimate cost of claims that present the likely outcome from the range of possible outcomes, taking into account the uncertainties involved ("best estimate"). To recognize the uncertainty in establishing this best estimate, to allow for possible deterioration in experience and to provide greater comfort that the actuarial liabilities are sufficient to pay future benefits, actuaries are required to include margins in some assumptions.

The determination of the overall risk margin takes into account:

- the level of uncertainty in the best estimate due to estimation error, variability of key inflation assumptions and possible economic and legislative changes; and
- the volatility of each line of business and the diversification between the lines of business and geographic regions (referred to as diversification benefit).

At a fixed probability of adequacy, the appropriate risk margin for two or more classes of business or for two or more geographic locations combined is likely to be less than the sum of the risk margins for the individual classes. The level of diversification assumed between classes takes into account industry analysis, historical experience and the judgement of experienced and qualified actuaries. With operations in Canada and the U.S., the risk margin assumption used reflects this diversification benefit as at December 31, 2017.

10.4 Key assumptions and sensitivity analysis

The claims liabilities' sensitivity to certain of these key assumptions is outlined below. It is not possible to quantify the sensitivity to certain assumptions such as legislative changes or uncertainty in the estimation process. The analysis is performed for possible movements in the assumptions with all other assumptions held constant, showing the impact on Net income. Movements in these assumptions may be non-linear and may be correlated with one another.

Table 10.3 – Sensitivity analysis (claims liabilities) – Impact on Net income

As at December 31,		2017		2016
		Canada	U.S.	Canada
Average claim costs (severity)	+5%	(279)	(20)	(279)
Average number of claims (frequency)	+5%	(54)	(62)	(53)
Discount rate	+1%	137	29	137

A portion of the Company's investments backing its claims liabilities has been voluntarily designated as FVTPL to reduce the volatility caused by fluctuations in fair values of underlying claims liabilities due to changes in discount rates.

10.5 Prior-year claims development

The claims development table below demonstrates the extent to which the original claim cost estimates in any one accident year has subsequently developed favourably (lower than originally estimated) or unfavourably. This table illustrates the variability and inherent uncertainty in estimating the claims estimate on a yearly basis. The ultimate claims cost for any particular accident year is not known until all claims payments have been made. For property insurance, payout of claims liabilities generally occurs shortly after the occurrence of the loss. For casualty (long-tailed) coverages, the loss may not be paid, or even reported, until well after the loss occurred. The estimated ultimate claims payments at the end of each subsequent accident year demonstrate how the original estimate has been revised over time.

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The following table presents the estimates of cumulative incurred claims, including IBNR, with subsequent developments during the periods and together with cumulative payments to date.

Table 10.4 – Prior-year claims development – net

As at December 31, 2017	Total	Accident year										
		2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	earlier
Undiscounted claims liabilities outstanding at end of accident year		2,771	2,683	2,493	2,461	2,524	2,375	2,312	2,038	1,799	1,627	4,294
Revised estimates												
One year later			2,720	2,390	2,390	2,463	2,342	2,213	1,923	1,740	1,625	4,136
Two years later				2,425	2,384	2,427	2,262	2,142	1,896	1,739	1,596	4,069
Three years later					2,401	2,418	2,220	2,058	1,860	1,715	1,586	3,985
Four years later						2,414	2,194	2,018	1,836	1,679	1,562	3,910
Five years later							2,171	1,986	1,792	1,656	1,525	3,821
Six years later								1,956	1,768	1,628	1,511	3,807
Seven years later									1,745	1,602	1,493	3,794
Eight years later										1,589	1,482	3,753
Nine years later											1,482	3,731
Ten years later												3,728
Current estimate		2,771	2,720	2,425	2,401	2,414	2,171	1,956	1,745	1,589	1,482	3,728
Claims paid to date			(1,099)	(1,253)	(1,523)	(1,824)	(1,832)	(1,744)	(1,602)	(1,506)	(1,387)	(3,496)
Undiscounted claims liabilities	8,136	2,771	1,621	1,172	878	590	339	212	143	83	95	232
Discounting and risk margin	(38)											
Net claims discounted – Business combination	1,648	659	349	244	172	86	58	30	20	10	9	11
Claims liabilities - net	9,746											

The original reserve estimates are evaluated quarterly for redundancy or deficiency. The evaluation is based on actual payments in full or partial settlement of claims and current estimates of claims liabilities for claims still open or claims still unreported.

The operations of OneBeacon are integrated into the Company's operations since September 28, 2017 (closing date). The estimate of net ultimate claims payments attributable to OneBeacon as at December 31, 2017 was included in the prior year claims development table on a separate line (Business combination) and allocated to the original accident years in which the underlying claims were incurred. To eliminate the distortion resulting from changes in foreign currency rates, all amounts denominated in currencies other than the CAD have been translated into CAD using the exchange rate in effect as at December 31, 2017.

10.6 Industry pools

Canadian operations – When certain automobile owners are unable to obtain insurance via the voluntary insurance market in Canada, they are insured via the FA. In addition, entities can choose to cede certain risks to the FA administered RSP. The related risks associated with FA insurance policies and policies ceded to the RSP are aggregated and shared by the entities in the Canadian P&C insurance industry, generally in proportion to market share and volume of business ceded to the RSP.

U.S. operations – As a condition of its license to do business in certain states in the U.S., the Company is required to participate in various mandatory shared market mechanisms commonly referred to as residual or involuntary markets. Each state dictates the type of insurance and the level of coverage that must be provided.

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Note 11 – Unearned premiums

11.1 Movements in unearned premiums

Unearned premiums represent the portion of DPW that the Company has not yet earned as it represents insurance coverage to be provided by the Company after the balance sheet date.

Table 11.1 – Movements in unearned premiums

For the years ended	Direct	Ceded	Net
December 31, 2017			
Balance, beginning of year	4,573	17	4,556
Business combinations (Note 4)	813	71	742
Premiums written	8,748	221	8,527
Premiums earned	(8,774)	(216)	(8,558)
Exchange rate differences	5	-	5
Balance, end of year	5,365	93	5,272
December 31, 2016			
Balance, beginning of year	4,390	21	4,369
Business combinations (Note 4)	104	-	104
Premiums written	8,197	212	7,985
Premiums earned	(8,118)	(216)	(7,902)
Balance, end of year	4,573	17	4,556

Note 12 – Insurance risk

The Company principally underwrites automobile, home, as well as commercial P&C contracts to individuals and businesses. On September 28, 2017, the Company completed its acquisition of OneBeacon, a specialty P&C insurance provider that offers a wide range of insurance products in the U.S.

The majority of the insurance risk to which the Company is exposed is of a short-tail nature. The average duration of claims liabilities was approximately 2.4 years for Canadian operation and 2.2 years for the U.S. operation as at December 31, 2017 (December 31, 2016 – 2.4 years for Canada). Policies generally cover a 12-month period.

Insurance contract risk is the risk that a loss arises from the following reasons:

- underwriting and pricing (Note 12.1);
- fluctuation in the timing, frequency and severity of claims relative to expectations (Note 12.2);
- inadequate reinsurance protection (Note 13.4); and
- large unexpected losses arising from a single event such as a catastrophe (Note 12.3).

Insured events can occur at any time during the coverage period and can generate losses of variable amounts. An objective of the Company is to ensure that sufficient claims liabilities are established to cover future insurance claim payments related to past insured events. The Company's success depends upon its ability to accurately assess the risk associated with the insurance contracts underwritten by the Company. The Company establishes claims liabilities to cover the estimated liability for the payment of all losses, including LAE incurred with respect to insurance contracts underwritten by the Company.

Claims liabilities do not represent an exact calculation of the liability. Rather, claims liabilities are the Company's best estimates of its expected ultimate cost of resolution and administration of claims. Expected claim cost inflation is taken into account when estimating claims liabilities, thereby mitigating inflation risk. The composition of the Company's insurance risk, as well as the methods employed to mitigate risks, are described hereafter.

12.1 Underwriting and pricing risks

The insurance business is cyclical in nature whereby the industry generally reduces insurance rates following periods of increased profitability, while it generally increases rates following periods of sustained loss. The Company's profitability tends to follow this cyclical market pattern and can also be affected by demand and competition. In addition, the Company is at risk from changes in automobile insurance legislation, the economic environment and climate patterns.

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In order to properly monitor the Company's risk appetite, pricing targets are set by the Insurance Risk Department. Pricing targets are established using an internal return on equity model and a risk-based capital model.

a) Concentration by countries and lines of business

Table 12.1 – Concentration by countries and lines of business

As at December 31,	2017		2016	
	DPW	Net claims liabilities	DPW	Net claims liabilities
By countries				
Canada	96%	83%	100%	100%
U.S. ¹	4%	17%	-%	-%
	100%	100%	100%	100%
By lines of business				
Personal auto	44%	48%	46%	58%
Personal property	24%	7%	24%	8%
Commercial lines- Canada	28%	28%	30%	34%
Commercial lines- U.S. ¹	4%	17%	-%	-%
	100%	100%	100%	100%

¹ Includes only Q4 results of our U.S. operations.

Risks associated with commercial lines and personal property insurance contracts may vary in relation to the geographical area of the risk insured by the Company. For automobile insurance, legislation is in place at a provincial level and this creates differences in the benefits provided among the provinces.

The Company's exposure to concentration of insurance risk, in terms of type of risk and level of insured benefits, is mitigated by careful selection and implementation of underwriting strategies, which is in turn largely achieved through diversification across industry sectors and geographical areas. Diversification also reduces the uncertainty associated with the unfavourable development of claims liabilities for both our Canadian and U.S. operations.

The Enterprise Risk Committee monitors the Company's overall risk profile, aiming for a balance between risk, return and capital and determines policies concerning the Company's risk management framework. Its mandate is to identify, measure and monitor risks, as well as avoid risks that are outside of the Company's risk tolerance level. Further, in order to minimize unforeseen risks, new products are subject to an internal product and approval review process. The Company also uses reinsurance under its strategy for managing the underwriting risk. The availability and cost of reinsurance are subject to prevailing market conditions, both in terms of price and available capacity, which can affect the Company's ceded premium volume and profitability. Reinsurance companies exclude some types of coverage from the contracts that the Company purchases from them or may alter the terms of such contracts from time to time. These gaps in reinsurance protection expose the Company to greater risk and greater potential loss and could adversely affect its ability to underwrite future business. Where the Company cannot successfully mitigate risk through reinsurance arrangements, consideration is given to reducing premiums written in order to lower its risk.

12.2 Risk related to the timing, frequency and severity of claims

The occurrence of claims being unforeseeable, the Company is exposed to the risk that the number and the severity of claims could exceed the estimates.

Strict claim review policies are in place to assess all new and ongoing claims. Regular detailed reviews of claims handling procedures and frequent investigations of possible fraudulent claims reduce the Company's risk exposure. Further, the Company enforces a policy of actively managing and promptly pursuing claims, in order to reduce its exposure to unpredictable future developments that could negatively impact the business. The Company has established a Large Loss Committee responsible for analyzing large losses and contentious matters to ensure that appropriate claims liabilities are established and approved.

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12.3 Catastrophe risk

Catastrophe risk is the risk of occurrence of a catastrophe defined as any one claim, or group of claims related to a single event such as large fires, hurricanes, earthquakes, hail or wind storms, and acts of terrorism. Catastrophes can have a significant impact on the underwriting income of an insurer. Changing climate conditions may add to the unpredictability and frequency of natural disasters and create additional uncertainty as to future trends and exposures.

The Company has limited its exposure to catastrophe risk by imposing maximum claim amounts on certain contracts, as well as by using reinsurance arrangements. The placement of ceded reinsurance is almost exclusively on an excess-of-loss basis (per event or per risk). Ceded reinsurance complies with regulatory guidelines. Retention limits for the excess-of-loss reinsurance vary by product line. *See Note 13 – Reinsurance for the Company's reinsurance net retention and coverage limits by nature of risk.*

12.4 Exposure to insurance risk

The principal assumption underlying the claims liability estimates is that the Company's future claims development will follow a similar pattern to past claims development experience. Claims liabilities estimates are also based on various quantitative and qualitative factors, including:

- average claim costs, including claim handling costs (severity);
- average number of claims by accident year (frequency);
- trends in claim severity and frequency;
- payment patterns;
- other factors such as inflation, expected or in-force government pricing and coverage reforms, and level of insurance fraud;
- discount rate; and
- risk margin.

Most or all of the qualitative factors are not directly quantifiable, particularly on a prospective basis, and the effects of these and unforeseen factors could negatively impact the Company's ability to accurately assess the risk of insurance contracts that the Company underwrites. There may also be significant lags between the occurrence of the insured event and the time it is actually reported to the Company and additional lags between the time of reporting and final settlement of claims.

The Company refines its claims liabilities estimates on an ongoing basis as claims are reported and settled. Establishing an appropriate level of claims liabilities is an inherently uncertain process. Reserving policies are overseen by the Company's Reserve Review Committee.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 13 – Reinsurance

13.1 Company's reinsurance net retention and coverage limits by nature of risk

In the ordinary course of business, the Company reinsures certain risks with other reinsurers to limit its maximum loss in the event of catastrophic events or other significant losses. The following table shows the Company's reinsurance net retention and coverage limits by nature of risk.

Canadian operations

Table 13.1 – Company's reinsurance net retention and coverage limits by nature of risk

As at December 31	2017	2016
Single risk events		
Retentions:		
on property policies	7.5	7.5
on liability policies	3 - 10	3 - 10
Multi-risk events and catastrophes		
Retention	100	100
Coverage limits	3,600	3,575

For certain special classes of business or types of risks, the retention for single risk events may be lower through specific treaties or the use of facultative reinsurance. For multi-risk events and catastrophes, the Company retains participations averaging 5.1% as at December 31, 2017 (December 31, 2016 – 5.3%) on reinsurance layers between the retention and coverage limit. The coverage limit prudently exceeds the Company's risk assessment of an earthquake in Western Canada at a 1-in-500 year return period.

U.S. operations

As at December 31, 2017, the newly acquired U.S. operations of the Company are covered by their own reinsurance program for single risk events but also for multi-risk events and catastrophes. Under the property catastrophe reinsurance program, the first US\$20 million of losses resulting from any single catastrophe are retained, with the coverage limit for the next US\$110 million of losses being entirely reinsured. In addition to the corporate catastrophe reinsurance protection, the Company also purchases dedicated reinsurance protection for certain lines of business. Among these, the retention for single risk events is US\$3 million on property policies and main liability policies.

In connection with the acquisition of OneBeacon, the Company entered into a reinsurance contract pursuant to which a major reinsurer will assume 80% of negative reserve development with respect to OneBeacon's claims liabilities for accident years 2016 and prior. The maximum amount recoverable under the reinsurance agreement is US\$200 million and is subject to some exclusions and limitations.

The purchase of this adverse development coverage has reduced the potential volatility in the Company's claims liabilities as at December 31, 2017 and resulted in a release of risk margin. The initial net cost of the coverage is reported in integration and restructuring cost in the statement of income.

13.2 Components of reinsurance assets

Reinsurance assets include the reinsurers' share of claims liabilities and unearned premiums.

Table 13.2 – Components of reinsurance assets

As at December 31,	2017	2016
Reinsurers' share of claims liabilities (Note 10.1)	729	465
Reinsurers' share of unearned premiums (Note 11.1)	93	17
	822	482

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

13.3 Net recovery (expense) from reinsurance

Table 13.3 – Net recovery (expense) from reinsurance

For the years ended December 31,	2017	2016
Ceded earned premiums (<i>Note 11.1</i>)	(216)	(216)
Ceded claims incurred (<i>Note 10.1</i>)	100	346
Commissions earned on ceded reinsurance	25	20
	(91)	150

The net recovery from reinsurance for the year ended December 31, 2016 mainly related to the Fort McMurray wildfires.

13.4 Risk management and counterparty credit risk

The Company relies on reinsurance to manage underwriting risk. Under reinsurance programs, management considers that in order for a contract to reduce exposure to risk, it must be structured to ensure that the reinsurer assumes the significant insurance risk related to the underlying reinsured risks and it is reasonably possible that the reinsurer may realize a significant loss from the reinsurance.

Although reinsurance makes the assuming reinsurer liable to the Company to the extent of the risk ceded, the Company is not relieved of its primary liability to its policyholders as the direct insurer. There is no certainty that its reinsurers will pay all reinsurance claims on a timely basis or at all. As a result, the Company bears credit risk with respect to its reinsurers on potential future recoverables and collectability of balances due from reinsurers is important to the Company's financial strength.

The Company is selective with its reinsurers, placing reinsurance with only those reinsurers having a strong financial condition. The Company's placement of reinsurance is diversified such that it is not dependent on a single reinsurer and the Company's operations are not substantially dependent upon any single reinsurance contract. The Company monitors the financial strength of its reinsurers on a regular basis. Uncollectible amounts historically have not been significant.

Management concluded that the Company was not exposed to significant loss from reinsurers for potentially uncollectible reinsurance as at December 31, 2017 and 2016.

Canadian operations

The Company also has minimum rating requirements for its reinsurers. Substantially all reinsurers are required to have a minimum credit rating of 'A-' at inception of the contract. The Company also requires that its contracts include a special termination and security review clause allowing the Company to replace a reinsurer during the contract period should the reinsurer's credit rating fall below the level acceptable to the Company or for other reasons that might jeopardize the Company's ability to continue doing business with such reinsurer as intended at the time of entering into the reinsurance arrangement.

The Company has collateral in place to support amounts receivable and recoverable from unregistered reinsurers. The Company is the assigned beneficiary of collateral consisting of cash, security agreements and letters of credit totalling \$114 million as at December 31, 2017 (December 31, 2016 – \$127 million) as guarantees from unregistered reinsurers. This collateral is held in support of policy liabilities of \$69 million as at December 31, 2017 (December 31, 2016 – \$94 million) and could be used should these reinsurers be unable to meet their obligations.

U.S. operations

The Company has collateral in place to support amounts receivable and recoverable from unauthorized reinsurers. The Company is the assigned beneficiary of collateral consisting of cash, security agreements and letters of credit totalling \$86 million as at December 31, 2017 as guarantees from unauthorized reinsurers. This collateral is held in support of policy liabilities of \$71 million as at December 31, 2017 and could be used should these reinsurers be unable to meet their obligations.

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 14 – Goodwill and intangible assets

14.1 Summary of goodwill and intangible assets

Table 14.1 – Reconciliation of the carrying value of goodwill and intangible assets.

	Intangible assets				Total intangible assets
	Goodwill	Distribution networks and trade names	Customer relationships	Internally developed software	
Cost					
Balance as at January 1, 2017	1,403	910	365	495	1,770
Acquisitions and costs capitalized	83	1	31	71	103
Business combinations ¹ (Note 4)	753	804	12	18	834
Disposals and write-off	-	-	(1)	(67)	(68)
Exchange rate differences	3	4	-	-	4
Balance as at December 31, 2017	2,242	1,719	407	517	2,643
Accumulated amortization					
Balance as at January 1, 2017	-	(15)	(179)	(274)	(468)
Amortization expense	-	(16)	(32)	(33)	(81)
Disposals	-	-	-	67	67
Balance as at December 31, 2017	-	(31)	(211)	(240)	(482)
Net carrying value	2,242	1,688	196	277	2,161
Cost					
Balance as at January 1, 2016	1,272	910	345	426	1,681
Acquisitions and costs capitalized	82	-	26	69	95
Business combinations (Note 4)	63	-	-	-	-
Disposals	(14)	-	(6)	-	(6)
Balance as at December 31, 2016	1,403	910	365	495	1,770
Accumulated amortization					
Balance as at January 1, 2016	-	(11)	(143)	(242)	(396)
Amortization expense	-	(4)	(37)	(32)	(73)
Disposals	-	-	1	-	1
Balance as at December 31, 2016	-	(15)	(179)	(274)	(468)
Net carrying value	1,403	895	186	221	1,302

¹ Including business combinations of OneBeacon and InnovAssur.

Intangible assets under development amounted to \$103 million as at December 31, 2017 (December 31, 2016 – \$63 million). These intangible assets are not subject to amortization, but are tested for impairment on an annual basis.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

14.2 Significant accounting judgments, estimates and assumptions

a) Allocation of goodwill and intangible assets with indefinite lives to the group of CGUs

Goodwill and intangible assets with indefinite lives are allocated to CGUs, or groups of CGUs, that are expected to benefit from the business combination in which they arose.

Prior to the acquisition of OneBeacon on September 28, 2017, the carrying value of the goodwill and intangible assets with indefinite lives were essentially all allocated to the Canada Insurance CGU, which was the Company's sole operating segment.

In 2017, with the acquisition of OneBeacon, a U.S. P&C insurer, a new group of CGUs has been defined and the goodwill and intangible assets with indefinite useful lives acquired were allocated to it (*see Note 4 – Business combinations*).

Table 14.2 – Allocation of Goodwill and intangible assets with indefinite lives to the groups of CGUs

As at December 31,	Goodwill		Intangible assets	
	2017	2016	2017	2016
Canada Insurance	1,461	1,403	820	820
U.S. Insurance	781	n/a	46	n/a
	2,242	1,403	866	820

b) Impairment testing of goodwill and intangible assets with indefinite lives

The Company determines whether goodwill and intangible assets with indefinite useful lives (not subject to amortization) are impaired at least annually and whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable at the CGU or group of CGUs level.

The annual impairment test was performed as at June 30, 2017 for the Canada Insurance group of CGUs and as at December 31, 2017 for the U.S. Insurance group of CGUs, following the acquisition of OneBeacon. Each group of CGUs was tested for impairment by comparing their carrying value to their recoverable amount, which has been determined based on a value in use calculation using the following key estimates and assumptions.

- Cash flow projections for the next three years based on financial budgets approved by management and determined using budgeted margins based on past performance and management expectations for the group of CGUs and their industry.
- Cash flows beyond the three-year period are extrapolated using estimated growth rates, based mainly on the U.S. and Canadian inflation and demographic growth perspectives.
- Pre-tax discount rate, which represents the weighted-average cost of capital for comparable companies whose activities are similar to the group of CGUs concerned.

Table 14.3 – Key assumptions used

	Growth rate		Pre-tax discount rate	
	2017	2016	2017	2016
Canada Insurance	2.5%	3.0%	9.1%	9.6%
U.S. Insurance	3.9%	n/a	10.7%	n/a

No impairment loss on goodwill or intangible assets with infinite lives has been recognized for these groups of CGUs for the year ended December 31, 2017 or prior.

The key assumptions used to determine the recoverable amount of each group of CGUs were tested for sensitivity by applying a reasonably possible change to those assumptions, with all other assumptions held constant. The results of the sensitivity analysis would not change the conclusion of the Canada Insurance CGUs. For the U.S. Insurance test, since the Company recently acquired the U.S. operations, the allocated goodwill is already at fair value.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 15 – Investments in associates and joint ventures

Table 15.1 – Movement in investments in associates and joint ventures

As at December 31,	2017	2016
Balance, beginning of year	543	396
Acquisitions, net of sales	11	194
Business combinations (<i>Note 4</i>)	-	(45)
Dividends received	(14)	(21)
Share of profit (loss) recorded in:		
net income	16	16
OCI	(6)	3
Balance, end of year	550	543
Of which:		
associates	398	382
joint ventures	152	161

During 2017, there were no events or changes in circumstances that indicated that the carrying values of Company's investments in associates and joint ventures, all of which are investments in private entities, may not be recoverable.

Note 16 – Property and equipment

16.1 Net carrying value of property and equipment

Table 16.1 – Net carrying value of property and equipment

As at December 31,	2017	2016
Land and buildings	37	38
Furniture and equipment	50	47
Leasehold improvements	63	54
	150	139

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 17 – Other assets and other liabilities

17.1 Other assets

Table 17.1 – Components of other assets

As at December 31,	2017	2016
Other receivables and recoverables	210	148
Restricted funds	111	50
Industry pools receivable	100	108
Guaranteed loan ¹	96	-
Accrued investment income	76	63
Investments, at cost	54	54
Prepays	43	23
Financial assets related to investments	34	21
Pension plans in a surplus position (Note 26.1)	5	62
Other	53	20
	782	549

¹ Recorded at fair value based on a discounted cash flow model using information as of the measurement date.

During 2017, there were no events or changes in circumstances that indicated that the carrying values of Investments at cost may not be recoverable.

17.2 Other liabilities

Table 17.2 – Components of other liabilities

As at December 31,	2017	2016
Premium and sale taxes payable	233	215
Commissions payable	199	228
Deposits received in connection with insurance contracts ¹	197	-
Accrued salaries and other short-term benefits	177	162
Accrued expenses	157	52
Pension plans in a deficit position and unfunded plans (Note 26.1)	140	95
Industry pools payable	99	105
Other post-employment benefits and other post-retirement benefits	52	29
Deposits received from reinsurers	25	32
Deferred income	-	72
Other payables	340	343
	1,619	1,333

¹ Unrestricted collateral held by the Company primarily in relation with the surety business.

Note 18 – Debt outstanding

On June 7, 2017, the Company completed an offering of \$425 million principal amount of Series 7 unsecured medium term notes ("Notes"). The Notes bear interest at a fixed annual rate of 2.85% until maturity on June 7, 2027, payable in semi-annual instalments commencing on December 7, 2017. The net proceeds from this offering of Notes was used to partially fund the purchase price for the acquisition of OneBeacon (see Note 4 – Business combinations).

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

18.1 Summary of debt outstanding

Table 18.1 – Carrying value and fair value of debt outstanding

As at December 31,	Maturity date	Initial term (years)	Fixed rate	Coupon (payment)	Principal amount	Carrying value (net of fees)	
						2017	2016
Term notes							
Series 1	Sept. 2019	10	5.41%	Mar. & Sept.	250	250	250
Series 2	Nov. 2039	30	6.40%	May & Nov.	250	248	248
Series 3	July 2061	50	6.20%	Jan. & July	100	99	99
Series 4	Aug. 2021	10	4.70%	Feb. & Aug.	300	299	299
Series 5	June 2042	30	5.16%	June & Dec.	250	249	249
Series 6	Mar. 2026	10	3.77%	Mar. & Sept.	250	249	248
Series 7	June 2027	10	2.85%	June & Dec.	425	422	-
2012 U.S. Senior Notes	Nov. 2022	10	4.60%	May & Nov.	USD275	365	-
Credit facility						60	-
						2,241	1,393

The term notes are accounted for at amortized cost which equals their carrying value. They may be redeemed at the option of the issuer, in whole or in part at any time, at a redemption price equal to the greater of the Government of Canada Yield at the date of redemption plus a margin or their par value.

Fair value of debt outstanding amounted to \$2,449 million as at December 31, 2017 (December 31, 2016 – \$1,624 million) and was established using valuation data from a benchmark firm. As at December 31, 2017, the Company was in compliance with all debts covenants.

18.2 Movement in the Company's debt outstanding

Table 18.2 – Movement in the Company's debt outstanding

For the year ended December 31,	2017	2016
Balance, beginning of year	1,393	1,143
Cash flows from financing activities		
Proceeds from issuance of debt	422	248
Amount drawn under a credit facility	60	-
Business combinations (<i>Note 4</i>)	364	-
Exchange rate differences	2	-
Other	-	2
Balance, end of year	2,241	1,393

18.3 Credit facility

During the year ended December 31, 2017, the Company increased the amount available under its unsecured revolving term credit facility from \$300 million to \$750 million. This five-year credit facility matures on August 28, 2022 and may be drawn as prime loans or base rate (Canada) advances at the prime or U.S. base rate plus a margin, as well as bankers' acceptances or Libor advances at the bankers' acceptance or Libor rate plus a margin.

The amount drawn under its credit facility totalled \$60 million as at December 31, 2017 (December 31, 2016 – nil). As part of the covenants of the loans under the credit facility, the Company is required to maintain certain financial ratios, which were fully met as at December 31, 2017 and 2016.

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 19 – Common shares and preferred shares

19.1 Authorized

Authorized share capital consists of an unlimited number of common shares and Class A Shares.

19.2 New financing in connection with the acquisition of OneBeacon

Common shares	<ul style="list-style-type: none"> On September 28, 2017, concurrent to the acquisition of OneBeacon, 8,210,000 subscription receipts (“receipts”) were converted into 8,210,000 common shares. The Company had completed its offering of the 8,210,000 subscription receipts on May 11, 2017 at \$91.85 per receipt for gross proceeds of \$754 million. Share issuance costs of \$23 million (\$19 million after tax), were accounted for as a reduction in common shares on the Consolidated balance sheets.
Preferred shares	<ul style="list-style-type: none"> On August 18, 2017, the Company completed a Series 6 offering of preferred shares (the “Series 6 Preferred Shares”) by issuing and selling 6,000,000 Series 6 Preferred Shares, at a price of \$25.00 per share, for aggregate gross proceeds of \$150 million. Share issuance costs of \$4 million (\$3 million after tax), were accounted for as a reduction in preferred shares on the interim Consolidated balance sheets. On May 24, 2017, the Company completed a Series 5 offering of preferred shares (the “Series 5 Preferred Shares”) by issuing and selling 6,000,000 Series 5 Preferred Shares, at a price of \$25.00 per share, for aggregate gross proceeds of \$150 million. Share issuance costs of \$4 million (\$3 million after tax), were accounted for as a reduction in preferred shares on the interim Consolidated balance sheets.

19.3 Issued and outstanding

Table 19.1 – Issued and outstanding shares

As at December 31,	2017		2016	
	Number of shares	Amount (in millions)	Number of shares	Amount (in millions)
Common shares	139,188,634	2,816	131,050,134	2,082
Preferred shares - Class A Shares				
Series 1	10,000,000	244	10,000,000	244
Series 3	8,405,004	206	8,405,004	206
Series 4	1,594,996	39	1,594,996	39
Series 5	6,000,000	147	-	-
Series 6	6,000,000	147	-	-
Total Class A	32,000,000	783	20,000,000	489

Issued and outstanding Class A shares rank in priority to common shares with regards to payment of dividends.

Table 19.2 – Reconciliation of number of shares outstanding

As at December 31,	Common shares (in shares)		Preferred shares Class A shares (in shares)	
	2017	2016	2017	2016
Balance, beginning of year	131,050,134	131,543,134	20,000,000	20,000,000
Issued	8,210,000	-	12,000,000	-
Repurchased for cancellation (Note 19.5)	(71,500)	(493,000)	-	-
Balance, end of year	139,188,634	131,050,134	32,000,000	20,000,000

On December 1, 2017, the Company announced that it did not intend to exercise its right to redeem its non-cumulative Rate Reset Class A Series 1 Preferred Shares (“Series 1 Preferred Shares”). On December 18, 2017, the Company also announced that they are not entitled to convert their shares. Subject to certain conditions on December 31, 2022 and on December 31 every five years thereafter, the holders of Series 1 Preferred Shares will have the right to convert their shares into Series 2 Preferred Shares. In addition, the Company has the option to redeem the Series 1 and Series 2 Preferred Shares on the same dates.

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

19.4 Dividends declared and paid per share

Table 19.3 – Dividends declared and paid per share (in dollars)

For the years ended December 31,	2017	2016
Common shares	2.56	2.32
Preferred shares		
Series 1	1.05	1.05
Series 3	0.83	1.00
Series 4	0.81	0.20
Series 5	0.78	n/a
Series 6	0.49	n/a

The holders of record of the Company preferred shares are entitled to receive non-cumulative preferential cash dividends on a quarterly basis, as and when declared by the Board of Directors of the Company.

- **Series 1 Preferred Shares** – The initial fixed-rate period ending on December 31, 2017 was based on an annual rate of 4.20%. The dividend rate that will prevail from and including December 31, 2017 to but excluding December 31, 2022 is 3.396%. Every five years thereafter, the dividend rate will reset at a rate equal to the five-year Government of Canada bond yield plus 1.72%.
- **Series 3 Preferred Shares** – The annual dividend rate for the five-year period from and including September 30, 2016 to but excluding September 30, 2021 is 3.332%.
- **Series 4 Preferred Shares** – The dividend rate for the 3-month floating rate period from and including September 30, 2017 to but excluding December 31, 2017 was 0.85749% (3.402% on an annualized basis). The floating quarterly dividend rate will be reset every quarter.
- **Series 5 Preferred Shares** – The annual dividend rate is 5.20%, and is not subject to a rate reset. The initial dividend paid on September 30, 2017 amounted to \$0.45945 per share.
- **Series 6 Preferred Shares** – The annual dividend rate is 5.30%, and is not subject to a rate reset. The initial dividend paid on December 29, 2017 amounted to \$0.49007 per share.

19.5 Normal course issuer bid (NCIB)

On February 13, 2017, the Company renewed the NCIB to purchase for cancellation during the next 12 months up to 6,551,741 common shares, representing approximately 5% of the issued and outstanding common shares as at February 1, 2017.

Table 19.4 – Common shares repurchased for cancellation under the NCIB

As at December 31,	2017	2016
Common shares repurchased for cancellation (in shares)	71,500	493,000
Average price (in dollars)	94.05	88.54
Total consideration paid	7	44

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The cost paid, including fees, was first charged to Share capital to the extent of the average carrying value of the common shares purchased for cancellation and the excess of \$6 million was charged to Retained earnings as at December 31, 2017 (December 31, 2016 – \$36 million).

Following the announcement of the acquisition of OneBeacon on May 2, 2017, the Company suspended its NCIB in order to maintain excess capital prior to the closing date of the transaction. Following closing, the Company plans to use excess capital for deleveraging, in line with its conservative transaction financing plan.

Note 20 – Capital management

20.1 Capital management objectives

The Company's objectives when managing capital consist of:

- maintaining strong regulatory capital levels (see Regulatory capital section below), while ensuring policyholders are well protected; and
- maximizing long-term shareholder value by optimizing capital used to operate and grow the Company.

The Company seeks to maintain adequate excess capital levels to ensure the probability of breaching the regulatory minimum requirements is very low. Such levels may vary over time depending on the Company's evaluation of risks and their potential impact on capital. The Company also keeps higher levels of excess capital when it foresees growth or actionable opportunities in the near term. Furthermore, the Company intends to return excess capital to shareholders through annual dividend increases and, when excess capital levels permit, through share buybacks.

Regulatory capital

The amount of capital deployed in any particular company or country is dependent upon local regulatory requirements, as well as the Company's internal assessment of capital requirements in the context of its risk profiles, requirements and strategic plans. The Company's practice is to maintain the capitalization of its regulated operating subsidiaries at a level that will exceed the relevant minimum regulatory capital requirements in the jurisdictions in which they operate (referred to as regulator supervisory minimum levels). Regulatory capital guidelines change from time to time and may impact the Company's our capital levels. The Company carefully monitors all changes, actual or proposed.

Canada	The Company's federally chartered Canadian P&C insurance subsidiaries are subject to the regulatory capital requirements defined by OSFI and the Insurance Companies Act, while its Québec provincially chartered subsidiaries are subject to the requirements of the AMF and the Act respecting insurance. Federal and Québec regulated P&C insurers are required, at a minimum, to maintain a MCT ratio of 100%. OSFI and the AMF have also established a regulator supervisory target capital ratio of 150%, which provides a cushion above the minimum requirement.
U.S.	The Company's U.S. insurance operations are subject to regulation and supervision in each of the states where they are domiciled and licensed to conduct business. State insurance departments have established the insurer solvency laws and regulatory infrastructure to maintain accredited status with the National Association of Insurance Commissioners ("NAIC"). A key solvency-driven NAIC accreditation requirement is a state's adoption of risk-based capital ("RBC") requirements. Dividends from our major U.S. insurance subsidiary are subject to the New York Regulator's prior approval for a two year period ending September 30, 2019.

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Notes to the Consolidated financial statements

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20.2 Capital position

As at December 31, 2017 and 2016, all the of Company's regulated P&C insurance subsidiaries were well capitalized on an individual basis with capital levels well in excess of supervisory minimum levels, as well as CALs. CALs represent the thresholds below which regulator notification is required together with a company action plan to restore capital levels.

U.S. capital levels comprise the RBC levels of OneBeacon's U.S. regulated entities consolidated in Atlantic Specialty Insurance Company (ASIC). As at December 31, 2017, ASIC's RBC level stood at 459%.

Table 20.1 – Estimated aggregate capital position

As at December 31,	2017			2016	
	Canada (MCT)	U.S. (RBC)	IFC Capital margin	Canada (MCT)	IFC Capital margin
Regulatory capital ratios	205%	459%	-	218%	-
Industry-wide supervisory minimum levels	150%	150%	-	150%	-
CALs	170%	200%	-	170%	-
Capital above CALs (capital margin)	618	438	1,056	947	947
Other regulated / unregulated entities ¹	-	-	79	-	23
Total capital margin			1,135		970

¹ Other regulated entities include Split Rock Insurance, Ltd. (Bermuda) and IB Reinsurance Inc. (Barbados).

IFC total capital margin stood at \$1,135 million as at December 31, 2017 (\$970 million as at December 31, 2016). This represents the aggregate of capital in excess of CALs in regulated entities plus available cash in unregulated entities.

Annually, the Company performs Capital Adequacy Testing to ensure that the Company has sufficient capital to withstand significant adverse event scenarios. These scenarios are reviewed each year to ensure appropriate risks are included in the testing process. The 2017 results indicated that the Company's capital position is strong. In addition, the target, actual and forecasted capital position of the Company is subject to ongoing monitoring by management using stress and scenario analysis to ensure its adequacy

Note 21 – Net investment income

Table 21.1 – Net investment income

For the years ended December 31,	2017	2016
Interest income from:		
debt securities		
designated or classified as FVTPL	161	157
classified as AFS	90	85
loans and cash and cash equivalents	24	23
Interest income	275	265
Dividend income (expense) from:		
common shares, net		
designated or classified as FVTPL	62	54
classified as AFS	78	74
preferred shares		
classified as AFS	61	61
equities sold short	(8)	(6)
long-term investments, at cost	1	1
Dividend income	194	184
Investment income	469	449
Expenses	(37)	(35)
	432	414

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 22 – Net gains (losses)

Table 22.1 – Net gains (losses)

Portfolios	2017			2016		
	Fixed Income	Equity	Total	Fixed Income	Equity	Total
Net gains (losses) from:						
financial instruments:						
designated as FVTPL	(127)	12	(115)	(103)	205	102
classified as FVTPL	-	9	9	-	7	7
classified as AFS	2	167	169	2	122	124
	(125)	188	63	(101)	334	233
derivatives ¹ :						
swap agreements	-	(47)	(47)	-	(239)	(239)
futures	5	(19)	(14)	(2)	(29)	(31)
other	-	1	1	-	-	-
	5	(65)	(60)	(2)	(268)	(270)
Embedded derivatives	-	(50)	(50)	-	(13)	(13)
Net foreign currency gains (losses), net	(2)	33	31	(1)	21	20
Impairment losses from common shares	-	(20)	(20)	-	(41)	(41)
	(122)	86	(36)	(104)	33	(71)
Currency derivative gain related to book value hedge of OneBeacon ²			65			-
Other gains (losses) ³			40			1
			69			(70)

¹ Excluding foreign currency contracts, which are reported in Net foreign currency gains (losses).

² See Note 7.3 – Currency hedging in relation with the acquisition of OneBeacon.

³ Including net gains on investments in associates and joint ventures related to a change of control.

22.2 Significant accounting judgments, estimates and assumptions

The Company determines, at each balance sheet date, whether there is objective evidence that financial assets, other than those classified or designated as FVTPL, are impaired. Considerations which form the basis of these objective evidence judgments include a significant or prolonged decline in fair value, a loss event that has occurred which has impaired the expected cash flows, as well as other considerations such as liquidity and credit risk. See Table 2.4 - Objective evidence of impairment for equity impairment model.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 23 – Income taxes

23.1 Income tax expense recorded in Net income

Table 23.1 – Components of income tax expense recorded in Net income

For the years ended December 31,	2017	2016
Current income tax expense		
Current year	216	103
Adjustments to prior years	4	(29)
Deferred income tax expense (benefit)		
Change related to temporary differences	(40)	42
Adjustments related to the U.S. Corporate Tax reform (see below)	(27)	-
Adjustments to prior years	(3)	29
	150	145

On December 22, 2017, the U.S. Tax Cuts and Jobs Act (“U.S. Corporate Tax reform”), which reduces the U.S. corporate tax rate from 35% to 21% effective January 1, 2018, was enacted. This change resulted in a deferred tax benefit of \$27 million for the year ended December 31, 2017.

23.2 Effective income tax rate

The effective income tax rates are different from the combined Canadian federal and provincial income tax rates. The Consolidated statements of comprehensive income contain items that are non-taxable or non-deductible for income tax purposes, which cause the income tax expense to differ from what it would have been if based on statutory tax rates.

The following table presents the reconciliation of the effective income tax rate to the income tax expense calculated at statutory tax rates.

Table 23.2 – Effective income tax rate reconciliation

For the years ended December 31,	2017	2016
Income tax expense calculated at statutory tax rate	26.9%	26.9%
Increase (decrease) in income tax rates resulting from:		
non-taxable dividend income	(3.8)%	(4.8)%
adjustments related to the U.S. Corporate Tax reform	(2.9)%	-%
non-deductible losses (non-taxable gains)	(3.5)%	(0.1)%
non-taxable income from subsidiaries	(0.5)%	(0.7)%
non-taxable income	(0.7)%	(1.5)%
non-deductible expenses	1.0%	1.1%
foreign income taxed at different rates	(0.7)%	-%
other	0.1%	0.2%
Effective income tax rate	15.9%	21.1%

23.3 Significant accounting judgments, estimates and assumptions

Management exercises judgment in estimating the provision for income taxes. The Company is subject to income tax law in various jurisdictions where it operates. Various tax laws are potentially subject to different interpretations by the taxpayer and the relevant tax authority. To the extent that the Company’s interpretations of tax laws differ from those of tax authorities or that the timing of realization of deferred tax assets is not as expected, the provision for income taxes may increase or decrease in future periods to reflect actual experience.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

23.4 Components of deferred tax assets and liabilities

Table 23.3 – Components of deferred tax assets and liabilities

As at December 31,	Consolidated balance sheets Asset (liability)		Consolidated statements of comprehensive income Expense (benefit)	
	2017	2016	2017	2016
Net claims liabilities	100	108	(92)	(2)
Deferred loss for tax purposes	-	-	-	64
Difference between market value and book value of investments	-	-	-	7
Deferred expenses for tax purposes	58	52	(5)	13
Losses available for carry forward	140	3	(30)	4
DB plans	36	18	29	(12)
Other	13	2	11	(1)
Deferred tax assets	347	183	(87)	73
Intangible assets	(437)	(262)	119	(1)
Deferred income for tax purposes	-	(140)	140	140
Deferred gains and losses on specified debt obligations	(11)	(13)	2	(1)
Property and equipment	(36)	(28)	(11)	7
Difference between market value and book value of investments	(8)	(2)	5	2
Deferred tax liabilities	(492)	(445)	255	147
Net deferred tax asset (liability) / expense (benefit)	(145)	(262)	168	220

The Company believes that it is probable that it will generate sufficient taxable income in the future to realize the above deferred tax assets.

23.5 Movement in the net deferred tax asset (liability)

Table 23.4 – Movement in the net deferred tax asset (liability)

As at December 31,	2017	2016
Balance, beginning of year	(262)	(44)
Income tax benefit (expense):		
recorded in net income	70	(71)
recorded in OCI	98	(149)
recorded in equity	9	-
Business combinations (Note 4)	(43)	3
Exchange rate differences and other	(17)	(1)
Balance, end of year	(145)	(262)
Reported in:		
deferred tax assets	112	142
deferred tax liabilities	(257)	(404)

23.6 Tax losses

Operating losses – As at December 31, 2017, there were approximately:

- \$434 million of net operating losses carry forward balances in our U.S. subsidiaries, with the majority of those losses expiring between 2031 and 2035; and
- \$60 million of Canadian net operating losses carry forward balances, which will expire in 2037 (December 31, 2016 – nil).

As at December 31, 2017, a deferred tax asset was recognized in relation to all U.S. net operating losses and on \$57 million of Canadian operating losses.

Tax credits – The Company has \$27 million of tax credits in the United States that can be used to offset U.S. tax payable in the future.

Capital losses – The Company had allowable capital losses of \$81 million as at December 31, 2017 (December 31, 2016 – \$25 million), which had not been recognized when computing the deferred tax asset. These losses, which have no expiry date, can be used to reduce future taxable capital gains.

Non-capital losses – The Company has recognized a deferred tax asset for unused non-capital losses as at December 31, 2017 and 2016.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 24 – Earnings per share

EPS was calculated by dividing the Net income attributable to common shareholders of the Company by the weighted-average number of common shares outstanding during the year. Dilution is not applicable and, therefore, diluted EPS is the same as basic EPS.

Table 24.1 – Earnings per share

For the years ended December 31,	2017	2016
Net income attributable to shareholders	792	541
Less: dividends declared on preferred shares, net of tax	27	20
Net income attributable to common shareholders	765	521
Weighted-average number of common shares outstanding (in millions)	133.1	131.2
EPS – basic and diluted (in dollars)	5.75	3.97

Note 25 – Share-based payments

25.1 Long-term incentive plan

a) Outstanding LTIP units and fair value at grant date

Table 25.1 – Outstanding units and weighted-average fair value at grant date by performance cycle

As at December 31,	2017			2016		
Performance cycles	Number of units	Weighted-average fair value at grant date (in \$)	Amount (in millions of \$)	Number of units	Weighted-average fair value at grant date (in \$)	Amount (in millions of \$)
2014 - 2016	-	-	-	255,253	66.25	17
2015 - 2017	227,572	77.89	19	229,928	77.89	18
2016 - 2018	216,886	90.36	20	217,065	90.36	19
2017 - 2019	210,592	93.30	20	-	-	-
2017 - 2022	119,733	103.88	12	-	-	-
	774,783	92.06	71	702,246	77.51	54

b) Movements in LTIP units

Table 25.2 – Movements in LTIP share units

For the years ended December 31,	2017 (in units)	2016 (in units)
Outstanding, beginning of year	702,246	697,924
Awarded	308,252	182,170
Net change in estimate of units outstanding	20,203	62,802
Units settled	(255,918)	(240,650)
Outstanding, end of year	774,783	702,246

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

c) LTIP expense recognized in Net income

The LTIP is accounted for as an equity-settled plan, except for the participants that are eligible to receive cash in lieu of shares of the Company (accounted for as a cash-settled plan).

Table 25.3 – LTIP expense recognized in Net income

As at December 31,	2017	2016
Cash-settled plans	6	4
Equity-settled plans	14	14
	20	18

d) LTIP settlement in shares

Table 25.4 – Settlement in shares

As at December 31,	2017	2016
Value of common shares repurchased for share-based payments	37	19
Less: cumulative cost of the units for the Company	29	13
Excess of market price over the cumulative cost for the Company	8	6
Amount recognized in Retained earnings, net of taxes	6	5

The cumulative cost of the units that vested during the year and were settled through the plan administrator purchasing common shares on the market and remitting them to the participants was removed from Contributed surplus.

The difference between the market price of the shares and the cumulative cost for the Company of these vested units, net of income taxes, was recorded in Retained earnings.

25.2 ESPP

e) Movements in restricted common shares

Table 25.5 – Movements in restricted common shares

For the years ended December 31,	2017 (in units)	2016 (in units)
Outstanding, beginning of year	145,368	-
Awarded and vested	(139,953)	-
Forfeited	(5,415)	-
	-	-
Accrued during the year	134,865	145,368
Awarded and vested	(2,374)	-
Outstanding, end of year	132,491	145,368

f) ESPP expense recognized in Net income

The ESPP is accounted for as an equity-settled plan. For the years ended December 31, 2017 and 2016, the ESPP expense was \$14 million. For 2016, the \$14 million includes an expense of \$6 million recognized upon the change to the ESPP, representing the value of the unvested shares as at December 31, 2015 that vested on January 1, 2016.

25.3 DSU

The DSU is accounted for as a cash-settled plan. For the years ended December 31, 2017 and 2016, the expense was \$2 million. The DSU provision amounted to \$10 million as at December 31, 2017 (December 31, 2016 – \$8 million).

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 26 – Employee future benefits

The Company has a number of funded and unfunded DB pension plans in Canada that provide benefits to members in the form of a guaranteed pension payable for life based on final average earnings and contingent upon certain age and service requirements. The Company provides active employees in Canada a choice between a DB and a defined contribution pension plan. The Company offers its employees in the U.S. a 401(k) plan.

Subject to applicable pension legislation, the Canadian plans are administered either by the Company or by a pension committee, with assets held in a pension fund that is legally separate from the Company. The assets cannot be used for any purpose other than payment of pension benefits and related administrative fees.

Provincial minimum funding regulations in Canada require special payments from the Company to amortize any shortfall of registered plans' assets relative to the corresponding funding targets. Security in the form of letters of credit is permitted in lieu of those special payments, up to a limit of 15% of the actuarial liability used to determine the funding target.

Subject to applicable legal requirements in Canada, any balance of assets remaining after providing for the accrued benefits of the plan members may be returned to the Company upon termination of the plan. Pension legislation in certain provinces may require that the Company submit a proposal to the members and beneficiaries regarding the allocation of surplus assets. However, on an ongoing basis, a portion of such surplus may be recoverable by the Company through a reduction in future contributions or through payment of eligible administrative expenses.

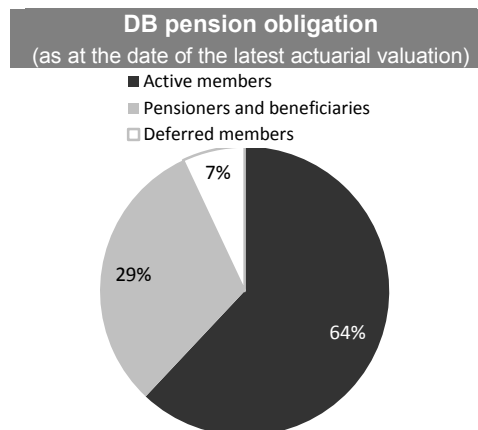
The Company also offers employer-paid post-retirement life insurance and health care benefit plans to a limited number of active employees and retirees as well as post-employment benefit plans that provide health and dental coverage to employees on disability for the duration of their leaves. These post-retirement and post-employment benefit plans are unfunded.

26.1 Funded status

The DB obligation, net of the fair value of plan assets, is recognized on the balance sheets as an asset, when the plan is in a surplus position, or as a liability, when the plan is in a deficit position. This classification is determined on a plan-by-plan basis.

Table 26.1 – Movement in the DB obligation

As at December 31,	Pension plans	
	2017	2016
DB obligation	(2,263)	(2,014)
Fair value of plan assets	2,128	1,981
Net DB asset (liability)	(135)	(33)
Reported in:		
other assets – plans in a surplus position	5	62
other liabilities – unfunded plans	(140)	(95)
	(135)	(33)
Funded status – funded plans	99%	103%



The measurement date for the DB pension plans is December 31. The latest actuarial valuations for the DB pension plans were performed as at December 31, 2016. The Company's liquidity risk with regards to pension plans is not significant, as inflows from contributions receivable generally outweigh outflows for benefit payments. A large portion of the investments are held in short-term notes and highly liquid federal and provincial government debt to protect against any unanticipated large cash requirements.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

26.2 DB obligation

The DB obligation is based on the current value of expected benefit payment cash flows to plan members over their expected lifetime.

Table 26.2 – Movement in the DB obligation

As at December 31,	Pension plans	
	2017	2016
Balance, beginning of year	2,014	1,801
Current service cost	65	63
Past service cost	1	-
Interest expense on DB obligation	72	76
Actuarial losses (gains) due to changes in:		
financial assumptions	103	110
plan experience	52	8
Employee contributions	27	26
Benefit payments	(71)	(70)
Balance, end of year	2,263	2,014

26.3 Fair value of plan assets

The Company makes contributions to the DB pension plans to secure the benefits. The amount and timing of the Company's contributions are made in accordance with applicable pension and tax legislation following the advice of an actuary. Under the provisions of the pension plans, members may annually select between three different DB levels and are required to make contributions to their respective plans based on the benefit level selected. The Company must fund the excess of the required funding over the members' contributions.

a) Movement in the fair value of plan assets

Table 26.3 – Movement in the fair value of plan assets

As at December 31,	Pension plans	
	2017	2016
Balance, beginning of year	1,981	1,812
Employer contributions	60	61
Employee contributions	27	26
Actual return on plan assets		
Interest income on plan assets recognized in Net income	69	75
Actuarial gains recognized in OCI	66	82
Benefit payments	(71)	(70)
Other	(4)	(5)
Balance, end of year	2,128	1,981

b) Composition of pension plan assets

Table 26.4 – Composition of pension plan assets

As at December 31,	2017		2016	
	Fair value	% of total	Fair value	% of total
Cash and short-term notes	43	2%	45	2%
Fixed income				
Investment grade				
Government	867	41%	823	42%
Corporate	438	21%	382	19%
Asset-backed	3	-	8	-
Debt securities	1,308	62%	1,213	61%
Common shares	749	35%	685	35%
Derivative financial instruments	28	1%	38	2%
	2,128	100%	1,981	100%

Plan assets are essentially all quoted in an active market.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Based on the latest projections of the financial position of all its plans, total cash contributions by the Company are expected to be approximately \$62 million in 2018 compared to actual contributions of \$60 million in 2017. The contributions will vary depending on the results of the December 31, 2017 actuarial valuations, the impact of any funding rule changes, the use of funding relief measures, if any, and decisions taken by the Company to use or not use letters of credit as permitted by legislation. The Company is also expected to meet the cost of eligible administrative expenses through the pension funds.

26.4 Employee future benefit expense recognized in Net income

Table 26.5 – Employee future benefit expense recognized in Net income

For the years ended December 31,	Pension plans	
	2017	2016
Current service cost	65	63
Past service cost	1	-
Net interest expense		
Interest expense on DB obligation	72	76
Interest income on plan assets	(69)	(75)
Other	4	5
	73	69

26.5 Actuarial losses (gains) recognized in OCI

Table 26.6 – Actuarial losses (gains) recognized in OCI

For the years ended December 31,	Pension plans	
	2017	2016
Re-measurements related to:		
change in discount rate used to determine the benefit obligation	110	106
actual return on plan assets	(66)	(82)
change in other financial assumptions	(7)	4
changes in plan experience	52	8
	89	36

Net actuarial losses (gains) on employee future benefits recognized in OCI for the year ended December 31, 2016 also include a gain of \$1 million for other post-retirement benefits.

26.6 Significant accounting judgments, estimates and assumptions

The cost of the DB plans and the DB obligation are calculated by the Company's independent actuaries using assumptions determined by management. The actuarial valuation involves making assumptions about discount rates, future salary increases, future inflation, the employees' age upon termination and retirement, mortality rates, future pension increases, disability incidence and health and dental care cost trends. If actuarial experience differs from the assumptions used, the expected obligation could increase or decrease in future years.

Due to the complexity of the valuation and its long-term nature, the DB obligation is highly sensitive to changes in the assumptions. Assumptions are reviewed at each reporting date.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

a) Assumptions used and sensitivity analysis

Table 26.7 – Key weighted-average assumptions used in measuring the Company's pension plans

	Obligation		Expense	
	As at December 31,		For the years ended December 31,	
	2017	2016	2017	2016
Discount rate:				
determination of DB obligation	3.5%	3.8%	n/a	n/a
current service cost	n/a	n/a	3.9%	4.1%
interest expense on the DB obligation	n/a	n/a	3.3%-3.5%	4.1%
Rate of increase in future compensation:				
next 3 years	2.75%	2.75%	2.75%	2.75%
beyond 3 years	2.68%	2.75%	2.75%	2.75%
Rate of inflation	1.93%	2.00%	2.00%	1.75%
Life expectancy for pensioners at the age of 65:				
male	21.6	21.6	21.6	21.6
female	24.1	24.1	24.1	24.0

The rate of compensation increase was based on financial plans approved by management for the next 3 years, and on inflation and long-term expectations of wage salary increase beyond 3 years.

Mortality rates have been established in accordance with the final table and improvement scale published in 2014 by the Canadian Institute of Actuaries.

Table 26.8 – Sensitivity of the DB pension obligation to key assumptions

As at December 31,	Change	2017		2016	
		increase	decrease	increase	decrease
Discount rates	1%	(369)	503	(318)	419
Rate of increase in future compensation	1%	108	(107)	79	(76)
Rate of inflation	1%	76	(69)	71	(68)
Life expectancy	One year	60	(60)	50	(50)

The effect on the DB pension obligation at the end of the year has been calculated by changing one assumption for the sensitivity but without changing any other assumptions. The impact of a one-year increase in life expectancy has been approximated by measuring the impact of members being one year younger than their actual age on the valuation date.

26.7 Risk management and investment strategy

Employee DB provisions expose the Company to actuarial risks (such as longevity risk, interest rate risk, inflation risk and market investment risk). The ultimate cost of the DB provisions to the Company will depend upon future events rather than on the assumptions made. In general, the risk to the Company is that the assumptions underlying the disclosures or the calculation of contribution requirements are not borne out in practice and the cost to the Company is higher than expected. This could result in higher contributions required from the Company and a higher deficit disclosed.

Assumptions which may vary significantly include:

- the actual return on plan assets;
- decrease in asset values not being matched by a similar decrease in the value of liabilities; and
- unanticipated future changes in mortality patterns leading to an increase in the DB liabilities.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

The DB obligation and the service cost are sensitive to the assumptions made about salary growth levels and inflation, as well as the assumptions made about life expectancy. It is based on estimates of market yields of highly rated corporate bonds.

The Management Pension Committee is responsible for the oversight of the pension plans, including the review of the funding policy and investment performance. The Statement of Investment Policies and Procedures of the pension plan (the "SIP&P") formulates investments principles, guidelines and monitoring procedures to meet the funds needs and objectives, in conformity with applicable rules. It also establishes principles and limits pertaining to debt and equity market risks. Any deviation from the SIP&P is reviewed by the Operational Investment Committee. The Risk Management Committee, which is a committee of the Company's Board of Directors, is responsible for the approval of the SIP&P and the review of the pension plans investment performance.

The pension plans investment portfolio is managed by Intact Investment Management Inc., a subsidiary of the Company, in accordance with the SIP&P that focuses on asset diversification and asset-liability matching. The Company regularly monitors compliance with the SIP&P.

Asset diversification

The goal of asset diversification is to limit the potential to have significant capital losses.

Debt securities in the pension plans are significantly exposed to changes in interest rates and movements in credit spreads. Investment policies seek a balanced target investment allocation between debt and equity securities, within credit concentration limit. The pension plans' risk management strategy is to invest in debt instruments of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer by imposing limits based upon credit quality. The adopted SIP&P generally requires minimum credit ratings of 'BBB' for investments in debt securities and limits its concentration in any one investee or related group of investees to 5% of the cost of its total assets for debt securities (except for those that are issued or guaranteed by the Government of Canada or by a province of Canada having at least an 'A' rating). The Company has overall limits on credit exposure that include debt and equity securities, as well as off-balance sheet exposure.

Sensitivity analysis is one risk management technique that assists management in ensuring that equity risks assumed remain within the pension plans' risk tolerance level. The Company's pension plans have a significant concentration of their investments in Canada as well as in the Government sector. This risk concentration is closely monitored.

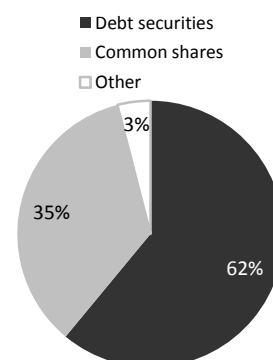
The Company also establishes asset allocation limits to ensure sufficient diversification (*see Note 9.4 – Credit risk*).

Asset-liability matching

One objective established in the SIP&P is to maintain an appropriate balance between the interest rate exposure of the Company's invested assets and the duration of its contractual liabilities. The Company calculates a hedge ratio as the duration of the pension asset portfolio divided by the duration of the funded registered pension plans' obligation. A lower hedge ratio increases the Company's exposure to changes in interest rates. The hedge ratio was 68% as at December 31, 2017 (December 31, 2016 – 74%).

A portion of the pension plan liabilities contain an indexation provision linked to the consumer price index (CPI). The Company invests in inflation sensitive assets to partially mitigate the risk of an unanticipated increase in inflation. As at December 31, 2017 and 2016, 10% of pension plan assets were invested in Canada Government Real Return Bonds.

Pension plan asset mix
(as at December 31, 2017)



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Notes to the Consolidated financial statements

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Note 27 – Segment information

27.1 Reportable segments

In 2017, in connection with the acquisition of OneBeacon, the Company changed the composition of its reportable segments to align with how senior management assesses its operating performance and allocates resources. The Company now has two reportable segments, in line with its management structure and internal financial reporting which is based on country, as well as nature of activities. Prior to the acquisition, the Company's activities used to be captured within a sole reporting and operating segment, P&C insurance operations. The comparative segment information has been reclassified accordingly.

Canada Insurance (“Canada”)

- Underwriting of automobile, home and business insurance contracts to individuals and businesses in Canada distributed through a wide network of brokers and directly to consumers.
- Distribution operations, including the results from the Company's wholly-owned subsidiary (BrokerLink) and broker affiliates.

U.S. Insurance (“U.S.”)

- Underwriting of specialty contracts to small and midsize businesses in the United States. The Company distributes insurance through independent agencies, brokers, wholesalers and managing general agencies.

Corporate and Other (“Corporate”)

- Consists of centralized investing, treasury and capital management activities, as well as other corporate activities.

27.2 Segment operating performance

Table 27.1 – Segment operating performance¹

For the years ended December 31,	2017				2016			
	Canada	U.S.	Corporate	Total	Canada	U.S.	Corporate	Total
Operating income								
NEP	8,204	326	-	8,530	7,946	-	-	7,946
Investment income	-	-	469	469	-	-	449	449
Other	124	-	34	158	111	-	32	143
Segment operating revenues	8,328	326	503	9,157	8,057	-	481	8,538
Net claims incurred (before MYA)	(5,381)	(198)	-	(5,579)	(5,161)	-	-	(5,161)
Underwriting expenses ²	(2,345)	(120)	-	(2,465)	(2,410)	-	-	(2,410)
Investment expenses	-	-	(37)	(37)	-	-	(35)	(35)
Investment gains (losses)	-	-	-	-	2	-	-	2
Share of profit from invest. in associates & JV	46	-	-	46	40	-	-	40
Finance costs	-	-	(82)	(82)	-	-	(72)	(72)
Other	(38)	-	(29)	(67)	(42)	-	(22)	(64)
PTOI³	610	8	355	973	486	-	352	838
Comprised of:								
underwriting income	478	8	-	486	375	-	-	375
net investment income	-	-	432	432	-	-	414	414
net distribution income	132	-	-	132	111	-	-	111
other income (expense)	-	-	5	5	-	-	10	10
finance costs	-	-	(82)	(82)	-	-	(72)	(72)
Investments	-	-	16,853	16,853	-	-	14,386	14,386
Net claims liabilities (Table 10.1)	8,098	1,648	-	9,746	8,071	-	-	8,071

¹ See Table 27.2 for the reconciliation to the Consolidated financial statements of income

² Other underwriting revenues are netted against underwriting expenses when assessing segment performance.

³ See Section 27 – Non IFRS financial measures of the Company's MD&A for the definition of related operating measures.

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Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

All segment revenues presented in *Table 27.1 Segment operating performance* before are generated from external customers.

Management measures the profitability of the Company's segments based on pre-tax operating income ("PTOI"). PTOI exclude elements that are not representative of the Company's operating performance because they relate to special items, bear significant volatility from one period to another, or because they are not part of the Company's normal activities.

The reconciliation of the segment information to the amounts reported in the Consolidated financial statements is presented in the table below. Other underwriting revenues are netted against underwriting expenses when assessing segment performance for MD&A presentation and, as such, are not included in segment operating revenues. Revenues and expenses not allocated to segments mainly represent non-operating items excluded from PTOI.

Table 27.2 – Reconciliation of segment information to amounts reported in the Consolidated statements of income

For the years ended December 31,	2017	2016
Segment operating revenues (<i>Table 27.1</i>)	9,157	8,538
Add: other underwriting revenues	108	122
Add: NEP exited lines	28	-
Less: NEP attributable to jointly held insurance operations	-	(44)
Revenues, as reported	9,293	8,616
Segment PTOI (<i>Table 27.1</i>)	973	838
Non-operating items:		
net gains (losses)	69	(72)
positive (negative) impact on MYA on underwriting	92	34
integration and restructuring costs	(57)	(23)
amortization of intangible assets recognized in business combinations	(62)	(53)
difference between expected return and discount rate on pension assets	(45)	(26)
underwriting results from OneBeacon exited lines	(10)	-
other non-operating costs	(18)	(12)
Pre-tax income, as reported	942	686

27.3 Information by geographic areas

Table 27.3 – Geographic areas

As at December 31,	Revenues		Total assets	
	2017	2016	2017	2016
Canada	8,939	8,616	22,093	22,866
U.S. ¹	354	-	5,835	-
	9,293	8,616	27,928	22,866

¹ Includes only Q4 results of our U.S. operations.

Revenues and assets are allocated based on the country where the risks originate. The Company's significant operating subsidiaries by geographic areas of operations are presented below.

Table 27.4 – Significant operating subsidiaries by geographic areas

Operations	Legal entities	
Canada	<ul style="list-style-type: none"> • Belair Insurance Company Inc. • Canada Brokerlink Inc. • Equisure Financial Network Inc. • Intact Insurance Company • IB Reinsurance Inc. 	<ul style="list-style-type: none"> • Jevco Insurance Company • Novex Insurance Company • The Nordic Insurance Company of Canada • Trafalgar Insurance Company of Canada
U.S.	<ul style="list-style-type: none"> • OneBeacon Insurance Group Holding; Ltd. • Atlantic Specialty Insurance Company 	<ul style="list-style-type: none"> • OneBeacon U.S. Financial Services Inc. • Split Rock Insurance, Ltd.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Note 28 – Additional information on the Consolidated statements of cash flows

28.1 Adjustments for non-cash items

Table 28.1 – Adjustments for non-cash items

For the years ended December 31,	2017	2016
Depreciation of property and equipment	34	37
Amortization of intangible assets	81	73
Net premiums on debt securities classified as AFS	15	10
DB pension expense	73	69
Share-based payments expense (equity-settled plans)	34	32
Share of profit from investments in associates and joint ventures	(16)	(16)
Other	4	3
	225	208

28.2 Changes in other operating assets and liabilities

Table 28.2 – Changes in other operating assets and liabilities

For the years ended December 31,	2017	2016
Unearned premiums, net	(30)	85
Premium receivables, net	52	(98)
Deferred acquisition costs, net	(25)	(23)
Other operating assets	(26)	(27)
Other operating liabilities	(186)	11
Dividends received from investments in associates and joint ventures	14	21
	(201)	(31)

Note 29 – Related-party transactions

The Company enters into transactions with associates and joint ventures in the normal course of business, as well as with key management personnel and pension plans. Transactions with related parties are at normal market prices and mostly comprise commissions for insurance policies and interest and principal payments on loans.

29.1 Transactions with associates and joint ventures

Table 29.1 – Transactions with associates and joint ventures

For the years ended December 31,	2017	2016
Income and expenses reported in:		
net investment income	8	8
underwriting expenses	260	241
Assets and liabilities reported in:		
loans and other receivables	202	203
commissions payable	36	39

29.2 Compensation of key management personnel

Key management personnel comprise all members of the Board of Directors and certain members of the Executive Committee. The compensation of key management personnel comprises salaries, share-based awards, annual incentive plans and pension value. Total compensation amounted to \$42 million for the year ended December 31, 2017 (December 31, 2016 – \$17 million).

Key management personnel can purchase insurance products offered by the Company in the normal course of business. The terms and conditions of such transactions are essentially the same as those available to clients and employees of the Company.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

29.3 Pension plans

Intact Investment Management Inc., a subsidiary of the Company, manages the investment portfolio of the pension plans' Master Trust in return for investment advisory fees charged to the pension plans, for a total of \$7 million for the year ended December 31, 2017 (December 31, 2016 – \$6 million). The Company made contributions to pension plans of \$60 million for the year ended December 31, 2017 (December 31, 2016 – \$61 million).

Note 30 – Commitments and contingencies

30.1 Operating lease commitments

The Company has entered into commercial operating leases, which have a remaining life ranging from one to 14 years.

Table 30.1 – Future minimum rental payments under non-cancellable operating leases

As at December 31, 2017

Less than 1 year	168
From 1 to 5 years	412
Over 5 years	230
	810

30.2 Contingencies

In the normal course of operations, various insurance claims and legal proceedings are instituted against the Company. Legal proceedings are often subject to numerous uncertainties and it is not possible to predict the outcome of individual cases. In management's opinion, the Company has made adequate provisions for, or has adequate insurance to cover all insurance claims and legal proceedings. Consequently, any settlements reached should not have a material adverse effect on the Company's consolidated future operating results and financial position.

The Company provides indemnification agreements to directors and officers, to the extent permitted by law, against certain claims made against them as a result of their services to the Company. The Company has insurance coverage for these agreements.

During Q4-2017, as a participant in the Voluntary Reimbursement Program established by the Government of Quebec, the Company entered into a final settlement with the City of Montreal. The settlement related to allegations against AXA Insurance Inc. ("AXA") and events prior to the acquisition of AXA Canada Inc. by the Company, and related to the provision of surety contracts. The Company denies any liability but elected to participate in the Voluntary Reimbursement Program to resolve this matter expeditiously. The amount of the settlement was not material.

Note 31 – Disclosures on rate regulation

31.1 Canada Insurance

The Company's Canadian insurance subsidiaries are licensed under insurance legislation in each of the provinces and territories in which they conduct business. Personal and commercial automobile insurance is a compulsory product and is subject to different regulations across the provinces and territories in Canada, including those with respect to rate setting. Rate setting mechanisms generally fall under three categories:

Table 31.1 – Rate filing categories

Category	Description
File and approve	Insurers must wait for specific approval of filed rates before they may be used.
File and use	Insurers file their rates with the relevant authorities and wait for a prescribed period of time and then implement the proposed rates.
Use and file	Rates are filed following use.

For Canada, all provinces and territories except Quebec use a rate setting mechanisms file and approve. Quebec uses a rate setting mechanisms use and file. For the years ended December 31, 2017 and 2016, automobile DPW in Canadian provinces excluding Québec totalled \$4 billion, or 98% of the Canadian Company's automobile DPW.

INTACT FINANCIAL CORPORATION

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

31.2 U.S. Insurance

Nearly all states have insurance laws requiring property and casualty insurance companies to file their rates, rules and policy or coverage forms with the state's regulatory authority. In most cases, such rates, rules and forms must be approved prior to use. While pricing laws vary from state to state, their objectives are generally to ensure that rates are not excessive, unfairly discriminatory or used to engage in unfair price competition. Company's ability to increase rates and the timing of the process are dependent upon the regulatory requirements in each state.

Relevant regulatory authorities may, in some circumstances, require retroactive rate adjustments, which could result in a regulatory asset or liability. As at December 31, 2017 and 2016, the Company had no significant regulatory asset or liability.

Note 32 – Standards issued but not yet effective

32.1 Financial instruments

IFRS 9 – *Financial Instruments* ("IFRS 9") is a three-part standard that will replace IAS 39 – *Financial Instruments: Recognition and Measurement* ("IAS 39"). IFRS 9 will be effective for annual periods beginning on or after January 1, 2018. However, the Company meets the eligibility criteria of the temporary exemption from IFRS 9 as provided by IFRS 4 – *Insurance Contracts* ("IFRS 4") (see Note 32.2 - *Insurance contracts – amendments for the application of IFRS 9 Financial Instruments*) and has elected to defer the application of IFRS 9 until the effective date of the new insurance contracts standards IFRS 17 - *Insurance Contracts* ("IFRS 17"), on January 1, 2021. The Company is currently evaluating the impact that IFRS 9, in conjunction with IFRS 17, will have on its Consolidated financial statements.

Classification and measurement

The classification of debt instruments is dependent on the business model and the cash flows characteristics. A debt instrument will be classified in accordance with the table below if its contractual term gives rise on specific dates to cash flows that are solely payments of principal and interest. It would otherwise be classified as FVTPL.

Amortized cost	FVTOCI	FVTPL
Default classification when the objective of the business model is uniquely to receive contractual cash flows of principal and interest.	Default classification when the objective of the business model is equally to receive contractual cash flows of principal and interest and realize cash flows from the sale.	Classification when the debt instrument does not meet the objective of the amortized cost or FVTOCI business models, or election to measure them as FVTPL instead of amortized cost or FVTOCI if doing so eliminates or significantly reduces an accounting mismatch.

Equity instruments and derivatives are usually measured at FVTPL. An entity can also elect on initial recognition to present fair value changes on an equity investment that is not held for trading directly and permanently in OCI, thus gains or losses are not recognized in income when the investment is disposed of.

Hedge accounting

The new model more closely aligns hedge accounting with risk management activities undertaken by companies when hedging their financial and non-financial risk exposures (under IAS 39, hedging non-financial components is not permitted). It will enable more entities to:

- apply hedge accounting to reflect their actual risk management activities; and
- use information produced internally for risk management purposes as a basis for hedge accounting, compared to IAS 39 which imposes eligibility and compliance based on metrics that are designed solely for accounting purposes.

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

Expected credit loss

This new impairment model applies only to financial assets classified as amortized cost and debt securities classified as FVTOCI. Under the expected credit loss model, a loss allowance will be established for all financial assets impaired based on a 12-month expected credit losses or a life-time expected credit losses if the credit risk increases significantly.

32.2 Insurance contracts – amendments for the application of IFRS 9 Financial Instruments

In September 2016, the IASB issued amendments to IFRS 4, to address concerns of insurers about the different effective dates for IFRS 9 and IFRS 17, the new insurance contracts standard. The amendments allow insurance entities to elect one of the two following options:

- the deferral approach provides entities whose predominant activities are to issue contracts within the scope of IFRS 4, a temporary exemption to continue using IAS 39, instead of IFRS 9 until January 1, 2021 (the “deferral approach”).
- the overlay approach can be applied to eligible financial assets and provides an option for all issuers of insurance contracts to reclassify from profit or loss to OCI any additional accounting volatility that may arise from applying IFRS 9 before the new insurance contracts standard.

The Company has opted for the deferral approach and performed an assessment as at September 30, 2017 considering OneBeacon’s acquisition (*see Note 4 – Business combinations*). The Company concluded that its activities are predominantly connected with insurance, since the percentage of liabilities connected with insurance contracts over total liabilities is above the 80% threshold.

Therefore, the Company will apply the temporary exemption and will continue to apply IAS 39 to its financial assets until January 1, 2021.

32.3 Revenues from contracts with customers

In May 2014, the IASB issued IFRS 15 – *Revenue from Contracts with Customers* (“IFRS 15”). The standard supersedes IAS 18 – *Revenue*, IAS 11 – *Construction Contracts*, and a number of revenue-related interpretations. This new standard specifies how and when to recognize revenue and additional relevant disclosure requirements. IFRS 15 applies to nearly all contracts with customers, except for insurance contracts, financial instruments and leases.

IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The adoption of this standard will have limited impact for the Company.

32.4 Leases

In January 2016, the IASB issued IFRS 16 – *Leases* (“IFRS 16”). IFRS 16 will replace IAS 17 – *Leases* and IFRIC 4 – *Determining Whether an Arrangement Contains a Lease*. It requires lessees to recognize most leases on their Balance sheets as lease liabilities, with the corresponding right-of-use assets. Lessees will have the option not to recognize leases with duration of less than one year and those of low-value assets. Generally, the recognition pattern for recognized leases will be similar to today’s finance lease accounting, with interest and depreciation expense recognized separately in the Consolidated statements of income.

IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with early application permitted. Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach. The Company does not anticipate early adoption of IFRS 16. The Company expects significant changes to its Balance sheets mainly due to its real estate leases and is currently evaluating the impact.

32.5 Share-based payments

In June 2016, the IASB issued amendments to IFRS 2 – *Share-based Payment* (“IFRS 2”), which provides additional guidance on the classification and measurement of share-based payment transactions. The amendments clarify the accounting for cash-settled share-based payment transactions that include a vesting condition, the classification of share-based payment transactions with net settlement features for withholding tax obligations, and the accounting for modifications of share-based payment transactions from cash-settled to equity-settled.

The amendments to IFRS 2 are effective for annual periods beginning on or after January 1, 2018, with early application permitted. It should be applied prospectively; however, retrospective application is permitted in certain instances. The adoption of these amendments will not have any impact for the Company.

Notes to the Consolidated financial statements

(in millions of Canadian dollars, except as otherwise noted)

32.6 Insurance contracts

In May 2017, the IASB published IFRS 17 a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure, which replaces IFRS 4 and introduces consistent accounting for all insurance contracts.

IFRS 17 provides a general model for the recognition of insurance contracts, as well as a simplified model (premium allocation approach) for short-duration contracts, which will be applicable to most property and casualty insurance contracts. The standard requires a company to measure insurance contracts using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires a company to recognize profits as it delivers insurance services.

The main features of the simplified new accounting model for property and casualty insurance contracts are as follows:

- the concept of portfolio, which is a group of contracts covering similar risks and managed together as a single pool. As such, contracts will be grouped for allocation of deferred acquisition costs, the calculation of risk adjustment, the determination of onerous contracts and the application of the discount rate;
- insurance liabilities will be discounted at a rate that reflects the characteristics of the liabilities (as opposed to a rate based on asset returns) and the duration of each portfolio. Entities will record the effect of changes in discount rates either in Net income or in OCI, according to their accounting policy choice;
- changes in balance sheet presentation where unearned premiums will correspond to premiums received in advance, while accounts receivable will be constituted of amounts not received when revenue is recognized. In profit or loss, direct premiums written will no longer be presented (only earned premiums). Also, insurance results will be presented without the impact of discounting. Amounts relating to financing and changes in discount rates will be shown separately;
- disclosure: extensive disclosures to provide information on the recognized amounts from insurance contracts and the nature and extent of risks arising from these contracts.

The standard applies to annual periods beginning on or after January 1, 2021. Earlier application is permitted if IFRS 9 – *Financial Instruments* is also applied. Retrospective application is required. However, if full retrospective application for a group of insurance contracts is impracticable, then the entity is required to choose either a modified retrospective approach or a fair value approach. The Company plans to adopt the new standard on the required effective date together with IFRS 9 (see above). The Company started a project to implement IFRS 17 and has been performing a high-level impact assessment of IFRS 17. The Company expects that the new standard will result in important changes to accounting policies for insurance contract liabilities, but the impact has not yet been determined.

32.7 Uncertainty over income tax treatments

In June 2017, the IASB issued IFRIC 23 – *Uncertainty over Income Tax Treatments* (“IFRIC 23”). This interpretation specifies that if an entity concludes it is probable that the taxation authority will accept an uncertain tax treatment, it shall determine the tax result consistently with the tax treatment used or planned to be used in its income tax filing. If it is not probable, the entity shall reflect the effect of uncertainty for each uncertain tax treatment by using either of the following methods, depending on which one the entity expects to better predict the resolution of the uncertainty:

- most likely amount: single most likely amount in a range of possible outcomes.
- expected value: sum of the probability-weighted amounts in a range of possible outcomes.

An entity shall apply IFRIC 23 for annual reporting periods beginning on or after January 1, 2019, with earlier application permitted. The Company will not early adopt IFRIC 23 and does not expect a significant impact.

32.8 Income tax consequences of payments on financial instruments classified as equity

In December 2017, the IASB issued amendments to IAS 12 – *Income Taxes* (“IAS 12”) to clarify that an entity should account for the income tax on dividends in Net income, OCI or equity, according to where the entity originally recognized the past transactions that allowed for having the cash flows to declare a dividend.

The amendments apply to annual periods beginning on or after January 1, 2019, with earlier application permitted. The Company will not early adopt the amendments to IAS 12. The Company is currently assessing the impact of these amendments.

GLOSSARY

Actuarial gains (losses)

Effect of changes in actuarial assumptions and experience adjustments (the effect of differences between the previous actuarial assumptions and what has actually occurred).

Adjusted earnings per share ("AEPS")

A non-IFRS financial measure calculated as net income for a specific period less preferred share dividends, adjusted for the after-tax impact on net income of amortization of intangible assets recognized in business combinations, integration and restructuring costs, acquisition-related currency derivative gains or losses and the positive impact from the U.S. Corporate Tax reform, divided by the weighted-average number of common shares outstanding during the same period.

Adjusted return on equity ("AROE")

A non-IFRS financial measure calculated as net income for a 12-month period less preferred share dividends, adjusted for the after-tax impact on net income of amortization of intangible assets recognized in business combinations, integration and restructuring costs, acquisition-related currency derivative gains or losses and the positive impact from the U.S. Corporate Tax reform, divided by the average shareholders' equity (excluding preferred shares) over the same 12-month period. Net income and shareholders' equity are determined in accordance with IFRS.

Affiliated brokers

Brokers in which we hold an equity investment or provide financing.

Asset-backed security

A financial security whose value and income payments are derived from and collateralized (or backed) by a specified pool of underlying assets such as mortgage-backed securities, auto loan receivables and credit card receivables.

Associates

Entities in which the Company has the power to participate in the relevant decision-making activities of the investee, but does not have control. These investments are accounted for using the equity method.

Average shareholders' equity

Mean of shareholders' equity at the beginning and end of the period, adjusted for significant capital transactions, if appropriate. Shareholder's equity is determined in accordance with IFRS.

Basis risk

Basis risk is the risk that offsetting investments in an economic hedging strategy will not experience price changes that entirely offset each other.

Book value per share

Shareholders' equity (excluding preferred shares) divided by the number of common shares outstanding at the same date. Shareholders' equity is determined in accordance with IFRS.

Case reserves

The liability established to reflect the estimated cost of unpaid claims that have been reported and claims expenses that the insurer will ultimately be required to pay.

Cash flow available for investment activities

A non-IFRS financial measure, which includes net cash flows from cash and cash equivalents and the investment portfolio.

Catastrophe losses

Any one claim or group of claims, equal to or greater than \$7.5 million for P&C Canada (US\$5 million for P&C U.S.) related to a single event.

Claims liabilities

Technical accounting provisions comprising the following: (1) case reserves, (2) claims that are incurred but not reported ("IBNR"), and (3) a risk margin as required by accepted actuarial practice. Claims liabilities are discounted to take into account the time value of money, using a rate that reflects the estimated market yield of the underlying assets backing these claims liabilities at the reporting date.

Claims ratio

Claims incurred, net of reinsurance, during a specific period and expressed as a percentage of net earned premiums for the same period.

Combined ratio

The sum of the claims ratio and the expense ratio. A combined ratio below 100% indicates a profitable underwriting result. A combined ratio over 100% indicates an unprofitable underwriting result.

Company action levels (CALs)

Thresholds below which regulator notification is required together with a company action plan to restore capital levels.

Credit risk

Possibility that counterparties may not be able to meet payment obligations when they become due.

Currency forwards

Contractual obligations to exchange one currency for another on a predetermined future date.

Currency risk

Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

Customer relationships

Relationships that exist with the policyholders, either directly (as a direct insurer) or indirectly (through consolidated brokers).

Debt-to-total capital ratio

Total debt outstanding divided by the sum of total shareholders' equity and total debt outstanding, at the same date.

Derivative financial instruments

A financial contract settled at a future date that requires little or no initial investment, and whose value is derived from an underlying interest rate, foreign exchange rate, equity or commodity instrument or index. The notional amount of the derivative is the contract amount used as a reference point to calculate the payments to be exchanged between the two parties, and the notional amount itself is generally not exchanged by the parties.

Derivative-related credit risk

Potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the Company. Therefore, derivative-related credit risk is represented by the positive fair value of an over-the-counter instrument and is normally a small fraction of the contract's notional amount.

Direct premiums written (DPW)

The total amount of premiums for new and renewal policies billed (written) during a specific period, as reported under IFRS.

Distribution EBITA

Operating results excluding interest and taxes from our wholly owned broker (BrokerLink), as well as our share of results from our broker associates for a specific period.

Distribution networks

Contractual agreements between the Company and unconsolidated brokers for the distribution of its insurance products.

DPW (MD&A basis)

A non-IFRS financial measure calculated as the total amount of premiums for new and renewal policies billed (written) during a specific period, normalized for the effect of multi-year policies, excluding industry pools, fronting and U.S. Commercial exited lines. This measure matches direct premiums written to the year in which coverage is provided, whereas under IFRS, the full value of multi-year policies is recognized in the year the policy is written.

DPW growth (MD&A basis)

Growth normalized for the effect of multi-year policies. This measure matches direct premiums written to accident year, whereas under IFRS, the full value of multi-year policies is recognized in the year the policy is written.

Earnings per share to common shareholders ("EPS"), basic

Net income attributable to common shareholders divided by the weighted-average number of common shares outstanding during the same period.

Earnings per share to common shareholders ("EPS"), diluted

Net income attributable to common shareholders divided by the weighted-average number of common shares outstanding during the same period, adjusted for the dilutive effect of stock options and other convertible securities.

Embedded derivatives

A component of a hybrid (combined) instrument that also includes a non-derivative host contract. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified financial variable.

Equities sold short

A transaction in which the seller sells equities and then borrows the equities in order to deliver them to the purchaser upon settlement. At a later date, the seller buys identical equities in the market to replace the borrowed securities.

Equity price risk

Risk of losses arising from changes in equity market prices.

Expense ratio

Underwriting expenses including commissions, premium taxes and general expenses related to underwriting activities for a specific period and expressed as a percentage of net earned premiums for the same period.

Frequency (of claims)

Average number of claims reported in a specific period.

Incurred but not reported ("IBNR") claims reserve

Reserves for estimated claims that have been incurred but not yet reported by policyholders including a reserve for future developments on claims which have been reported.

Industry pools

Canadian operations – When certain automobile owners are unable to obtain insurance via the voluntary insurance market in Canada, they are insured via the Facility Association ("FA"). In addition, entities can choose to cede certain risks to the FA administered Risk Sharing Pool ("RSP"). The related risks associated with FA insurance policies and policies ceded to the RSP are aggregated and shared by the entities in the Canadian P&C insurance industry, generally in proportion to market share and volume of business ceded to the RSP.

U.S. operations – As a condition of its license to do business in certain states in the U.S., the Company is required to participate in various mandatory shared market mechanisms commonly referred to as residual or involuntary markets. Each state dictates the type of insurance and the level of coverage that must be provided.

Interest rate futures contracts

Contractual obligations to buy or sell interest-rate-sensitive financial instruments on a predetermined future date at a specified price.

Interest rate hedge ratio

A ratio calculated by the Company as the duration of the pension asset portfolio divided by the duration of the registered pension plans' obligation. A lower hedge ratio increases the Company's exposure to changes in interest rates.

Interest rate risk

Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in interest rates or spreads.

Joint venture

Joint arrangement whereby the parties have joint control of the arrangements, requiring unanimous consent of the parties sharing control for strategic and operating decision making. The parties sharing control also have rights to the net assets of the arrangements. These investments are accounted for using the equity method.

Large loss

A single claim larger than \$0.25 million for P&C Canada (US\$0.25 million for P&C U.S.) but smaller than the catastrophe threshold of \$7.5 million for P&C Canada (US\$5 million for P&C U.S.).

Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet obligations associated with financial liabilities.

Market-based yield

Non-IFRS financial measure defined as the annualized total pre-tax investment income (before expenses) divided by the mid-month average fair value of net equity and fixed-income securities held during a period (average net investments).

Market risk

Risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in equity market prices, interest rates or spreads, foreign exchange rates or commodity market.

Market yield adjustment (MYA)

The impact of changes in the discount rate used to discount claims liabilities based on the change in the market-based yield of the underlying assets.

Master netting agreement

An agreement between a company and a counterparty designed to reduce the credit risk of derivative transactions through the creation of a legal right to offset the exposure in the event of a default.

Minimum capital test ("MCT")

Ratio of total capital available to total capital required, as defined by the Office of the Superintendent of Financial Institutions (OSFI) and Autorité des marchés financiers (AMF).

Net distribution income

Operating income excluding interest and taxes from our wholly-owned broker (BrokerLink) and operating income including interest and taxes from our broker associates for a specific period.

GLOSSARY

Net earned premiums

Net premiums written recognized for accounting purposes as revenue during a period.

Net operating income (“NOI”)

A non-IFRS financial measure calculated as net income for a specific period, excluding the after-tax impact of amortization of intangible assets recognized in business combinations, integration and restructuring costs, net gains (losses), difference between expected return and discount rate on pension assets, market yield adjustment, underwriting results of U.S. Commercial exited lines, the positive impact from the U.S. Corporate Tax reform, as well as other costs that we do not believe to be reflective of our operating performance.

Net operating income per share (“NOIPS”)

A non-IFRS financial measure calculated as net operating income for a specific period less preferred share dividends, divided by the weighted-average number of common shares outstanding during the same period.

Net premiums written

Direct premiums written for a given period less premiums ceded to reinsurers during the same period.

Non-catastrophe weather event

A group of claims, which is considered significant but that is smaller than the catastrophe threshold of \$7.5 million for P&C Canada (US\$5 million for P&C U.S.), related to a single weather event.

Non-operating results

A non-IFRS financial measure, which includes elements that are not representative of our operating performance because they relate to special items, bear significant volatility from one period to another, or because they are not part of our normal activities.

Normal course issuer bid (“NCIB”)

A program for the repurchase of the Company’s own common shares, for cancellation through a stock exchange that is subject to the various rules of the relevant stock exchange and securities commission.

Notional amount

Contract amount used as a reference point to calculate cash payments for derivatives.

Operating return on equity (“OROE”)

A non-IFRS financial measure calculated as net operating income for a 12-month period less preferred share dividends, divided by the average shareholders’ equity (excluding preferred shares and accumulated other comprehensive income) over the same 12-month period.

Options

Contractual agreements under which the seller grants to the buyer the right, but not the obligation, either to buy (call option) or sell (put option) an asset (underlying asset) at a predetermined price, at or by a specified future date.

Over-the-counter derivatives

Contracts that are negotiated directly between two parties, without going through a formal exchange or other intermediaries.

Prior year claims development

Change in total prior year claims liabilities in a given period. A reduction to claims liabilities is called favourable prior year claims development. An increase in claims liabilities is called unfavourable prior year claims development.

Regulatory capital ratios

Minimum capital test (MCT), as defined by the Office of the Superintendent of Financial Institutions (OSFI) and the Autorité des marchés financiers (AMF) in Canada and Risk-based capital requirements (RBC) as defined by the National Association of Insurance Commissioners (NAIC) in the U.S.

Reinstatement premium

Premium payable to restore the original reinsurance policy limit as a result of a reinsurance loss payment under catastrophe coverage. Reinstatement premiums are reported in Net earned premiums.

Reinsurer

An insurance company that agrees to indemnify another insurance or reinsurance company, the ceding company, against all or a portion of the insurance or reinsurance risks underwritten by the ceding company, under one or more policies.

Return on equity (“ROE”)

Net income for a 12-month period less preferred share dividends, divided by the average shareholders’ equity (excluding preferred shares) over the same 12-month period. Net income and shareholders’ equity are determined in accordance with IFRS.

Risk-based Capital (“RBC”)

Risk-based capital, as defined by the National Association of Insurance Commissioners (NAIC) in the U.S.

Securities lending

Transactions in which the owner of a security agrees to lend it under the terms of a prearranged contract to a borrower for a fee. The borrower must collateralize the security loan at all times.

Severity (of claims)

Average cost of a claim calculated by dividing the total cost of claims by the total number of claims.

Structured settlements

Periodic payments to claimants for a determined number of years for life, typically in settlement for a claim under a liability policy, usually funded through the purchase of an annuity.

Swap agreements

Over-the-counter contracts in which two counterparties exchange a series of cash flows based on a basket of stocks, applied to a contract notional amount.

Total capital margin

Total capital margin includes the aggregate of capital in excess of company action levels in regulated entities (170% MCT, 200% RBC) plus available cash in unregulated entities.

Underlying current year loss ratio

A non-IFRS financial measure calculated as current year claims ratio excluding catastrophe losses, reinstatement premiums and prior year claims development.

Underwriting income

Net earned premiums less net claims incurred, commissions, premium taxes and general expenses, excluding market yield adjustment, the difference between the expected return and discount rate on pension assets and the underwriting results of U.S. Commercial exited lines.

Written insured risks

The number of vehicles in automobile insurance and the number of premises in personal property insurance.

FIVE-YEAR FINANCIAL HISTORY

(Excluding MYA. In millions of Canadian dollars, except as noted)

	IFRS				
	2017	2016	2015	2014	2013
Consolidated performance					
Direct premiums written	8,747	8,293	7,922	7,461	7,345
Net earned premiums	8,530	7,946	7,535	7,207	7,014
Underwriting income (loss)	486	375	628	519	142
Net investment income	432	414	424	427	406
Net distribution income	132	111	104	75	75
Net operating income	771	660	860	767	500
Non-operating gains (losses)	(31)	(152)	(216)	10	(95)
Income before income taxes	942	686	875	957	465
Effective tax rate	15.9%	21.1%	19.3%	18.3%	7.3%
Net income attributable to shareholders	792	541	706	782	431
Claims ratio	65.4%	64.9%	61.3%	62.6%	66.9%
Expense ratio	28.9%	30.4%	30.4%	30.2%	31.1%
Combined ratio	94.3%	95.3%	91.7%	92.8%	98.0%
Favourable prior year claims development	(238)	(389)	(477)	(364)	(374)
Current year catastrophes claims	313	385	116	243	486
Net gains (losses)	69	(72)	(64)	174	(83)
Per share measures (\$)					
Weighted average number of common shares outstanding (millions)	133.1	131.2	131.5	131.5	132.4
Net operating income per share	5.60	4.88	6.38	5.67	3.62
Earnings per share	5.75	3.97	5.20	5.79	3.10
Adjusted earnings per share	5.82	4.53	5.54	6.01	3.44
Book value per share	48.00	42.72	39.83	37.75	33.94
Return on equity					
Operating return on equity	12.9%	12.0%	16.6%	16.3%	11.2%
Return on equity	12.8%	9.6%	13.4%	16.1%	9.3%
Adjusted return on equity	13.0%	11.0%	14.3%	16.8%	10.3%
Personal auto					
Direct premiums written	3,818	3,792	3,591	3,374	3,383
Written insured risks (thousands)	4,319	4,358	4,159	3,900	3,902
Net earned premiums	3,782	3,704	3,508	3,387	3,349
Underwriting income (loss)	(64)	5	161	186	228
Combined ratio	101.7%	99.9%	95.4%	94.5%	93.2%
Personal property					
Direct premiums written	2,135	2,030	1,864	1,715	1,635
Written insured risks (thousands)	2,413	2,393	2,294	2,192	2,221
Net earned premiums	2,040	1,880	1,736	1,617	1,519
Underwriting income (loss)	222	170	244	177	(66)
Combined ratio	89.1%	90.9%	85.9%	89.0%	104.4%
Commercial lines – CAN					
Direct premiums written	2,487	2,471	2,467	2,372	2,327
Net earned premiums	2,382	2,362	2,291	2,203	2,146
Underwriting income (loss)	320	200	223	156	(20)
Combined ratio	86.5%	91.5%	90.3%	92.9%	100.9%
Commercial lines – U.S.					
Direct premiums written	307	–	–	–	–
Net earned premiums	326	–	–	–	–
Underwriting income (loss)	8	–	–	–	–
Combined ratio	97.4%	–	–	–	–
Financial condition					
Total capital margin	1,135	970	625	681	550
MCT %	205%	218%	203%	209%	203%
RBC %	459%	–	–	–	–
Debt-to-total capital ratio	23.1%	18.6%	16.6%	17.3%	18.7%
Investments					
Performance					
Market-based investment yield	3.20%	3.36%	3.55%	3.65%	3.68%
Total investments	16,853	14,386	13,504	13,440	12,261
Portfolio mix (net of hedging position)					
Cash, cash equivalents and short-term notes	4%	3%	4%	3%	2%
Fixed-income securities	72%	70%	71%	72%	73%
Preferred shares	8%	10%	9%	9%	10%
Common shares	14%	14%	13%	13%	12%
Loans	2%	3%	3%	3%	3%

THREE-YEAR QUARTERLY REVIEW

(Excluding MYA. In millions of Canadian dollars, except as noted)

	IFRS 2017				IFRS 2016				IFRS 2015			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Consolidated performance												
Direct premiums written	2,294	2,209	2,500	1,744	1,961	2,193	2,458	1,681	1,908	2,095	2,344	1,575
Net earned premiums	2,400	2,082	2,051	1,997	2,043	2,036	1,937	1,930	1,948	1,930	1,865	1,792
Underwriting income (loss)	178	170	103	35	153	61	16	145	221	131	158	118
Net investment income	121	101	105	105	104	102	104	104	110	105	104	105
Net distribution income	28	30	50	24	24	30	43	14	22	28	34	20
Net operating income	236	219	193	123	212	137	114	197	265	199	210	186
Non-operating gains (losses)	(58)	(61)	57	31	(52)	(16)	(26)	(58)	(99)	(89)	(14)	(14)
Income before income taxes	246	220	295	181	224	156	112	194	241	161	254	219
Effective tax rate	5.9%	22.3%	17.6%	19.3%	23.7%	19.9%	16.9%	21.6%	17.8%	18.6%	21.7%	18.7%
Net income attributable to shareholders	232	171	243	146	171	125	93	152	198	131	199	178
Claims ratio	63.5%	63.8%	65.6%	69.2%	62.9%	67.4%	67.5%	62.0%	57.6%	63.4%	60.9%	63.2%
Expense ratio	29.1%	28.0%	29.4%	29.0%	29.6%	29.6%	31.7%	30.5%	31.0%	29.8%	30.7%	30.2%
Combined ratio	92.6%	91.8%	95.0%	98.2%	92.5%	97.0%	99.2%	92.5%	88.6%	93.2%	91.6%	93.4%
Favourable prior year claims development	(62)	(53)	(41)	(82)	(62)	(71)	(93)	(163)	(75)	(107)	(106)	(189)
Current year catastrophes claims	31	89	105	88	34	166	164	21	2	81	22	11
Net gains (losses)	(6)	(59)	59	75	(97)	17	28	(20)	(72)	(64)	(29)	101
Per share measures (\$)												
Weighted average number of common shares outstanding (millions)	139.2	131.2	131.0	131.0	131.1	131.1	131.3	131.5	131.5	131.5	131.5	131.5
Net operating income per share	1.63	1.61	1.44	0.90	1.58	1.01	0.83	1.46	1.97	1.47	1.56	1.37
Earnings per share	1.60	1.25	1.82	1.08	1.27	0.91	0.67	1.11	1.46	0.95	1.47	1.32
Adjusted earnings per share	1.55	1.41	1.68	1.18	1.56	1.01	0.76	1.19	1.54	1.06	1.56	1.38
Book value per share	48.00	46.56	42.16	43.14	42.72	41.47	40.57	40.06	39.83	37.84	39.23	38.95
Return on equity												
Operating return on equity	12.9%	13.3%	12.1%	10.6%	12.0%	13.4%	14.6%	16.7%	16.6%	16.9%	16.8%	17.2%
Return on equity	12.8%	12.7%	12.3%	9.5%	9.6%	10.5%	10.5%	12.7%	13.4%	14.2%	15.4%	16.1%
Adjusted return on equity	13.0%	13.6%	13.1%	10.8%	11.0%	11.4%	11.4%	13.6%	14.3%	15.0%	16.1%	16.7%
Personal auto												
Direct premiums written	824	1,028	1,163	803	829	1,032	1,154	777	808	987	1,090	706
Written insured risks (thousands)	917	1,139	1,360	903	928	1,164	1,373	893	899	1,135	1,307	818
Net earned premiums	952	962	949	919	942	944	918	900	909	903	868	828
Underwriting income (loss)	(11)	(50)	22	(25)	(9)	(41)	23	32	28	51	85	(3)
Combined ratio	101.2%	105.1%	97.8%	102.6%	100.9%	104.3%	97.6%	96.4%	96.9%	94.4%	90.3%	100.3%
Personal property												
Direct premiums written	505	591	625	414	486	569	592	383	452	527	542	343
Written insured risks (thousands)	562	671	704	476	562	669	701	461	547	651	664	432
Net earned premiums	522	517	506	495	494	483	447	456	453	444	428	411
Underwriting income (loss)	106	78	2	36	120	2	(30)	78	123	11	31	79
Combined ratio	79.7%	85.0%	99.5%	92.8%	75.6%	99.7%	106.7%	82.9%	72.7%	97.4%	92.7%	80.7%
Commercial lines – CAN												
Direct premiums written	658	590	712	527	646	592	712	521	648	581	712	526
Net earned premiums	600	603	596	583	607	609	572	574	586	583	569	553
Underwriting income (loss)	75	142	79	24	42	100	23	35	70	69	42	42
Combined ratio	87.4%	76.5%	86.7%	95.9%	93.2%	83.5%	95.9%	93.9%	88.0%	88.2%	92.6%	92.5%
Commercial lines – U.S.												
Direct premiums written	307	–	–	–	–	–	–	–	–	–	–	–
Net earned premiums	326	–	–	–	–	–	–	–	–	–	–	–
Underwriting income (loss)	8	–	–	–	–	–	–	–	–	–	–	–
Combined ratio	97.4%	–	–	–	–	–	–	–	–	–	–	–
Financial condition												
Total capital margin	1,135	1,155	1,014	1,034	970	881	857	904	625	389	564	763
MCT %	205%	201%	224%	225%	218%	215%	212%	215%	203%	195%	200%	213%
RBC %	459%	413%	–	–	–	–	–	–	–	–	–	–
Debt-to-total capital ratio	23.1%	24.7%	22.8%	18.5%	18.6%	19.0%	19.3%	19.5%	16.6%	17.3%	16.8%	16.9%
Investments												
Performance												
Market-based investment yield	3.11%	3.10%	3.30%	3.32%	3.27%	3.27%	3.43%	3.47%	3.62%	3.55%	3.62%	3.41%
Total investments	16,853	17,093	14,890	14,227	14,386	14,342	13,812	13,630	13,504	13,339	13,394	13,443
Portfolio mix (net of hedging position)												
Cash, cash equivalents and short-term notes	4%	6%	8%	2%	3%	5%	4%	4%	4%	5%	4%	3%
Fixed-income securities	72%	71%	67%	70%	70%	69%	70%	70%	71%	70%	70%	72%
Preferred shares	8%	8%	9%	10%	10%	9%	9%	9%	9%	8%	9%	9%
Common shares	14%	13%	13%	15%	14%	14%	14%	14%	13%	13%	13%	13%
Loans	2%	2%	3%	3%	3%	3%	3%	3%	3%	4%	4%	3%

BOARD OF DIRECTORS

Claude Dussault

Chairman of the Board of Intact Financial Corporation and President of ACVA Investing Corporation

Charles Brindamour

Chief Executive Officer

Robert W. Crispin^{2,4}

Corporate Director

Janet De Silva^{2,3}

President & CEO of Toronto Region Board of Trade

Robert G. Leary^{1,4}

CEO, Olayan Group

Eileen Mercier^{1,4}

Corporate Director

Sylvie Paquette^{1,4}

Corporate Director

Timothy H. Penner^{2,3}

Corporate Director

Louise Roy^{2,3}

Chancellor and Chair of the Board, Université de Montréal and Invited Fellow, Centre for Interuniversity Research and Analysis on Organizations

Frederick Singer^{1,4}

CEO of Echo360

Stephen G. Snyder^{1,3}

Corporate Director

Carol Stephenson^{2,3}

Corporate Director

EXECUTIVE COMMITTEE MEMBERS

Charles Brindamour

Chief Executive Officer

Louis Gagnon

President, Canadian Operations**

T. Michael Miller

President, U.S. and Specialty Solutions

Patrick Barbeau

Senior Vice President, Claims

Martin Beaulieu

Senior Vice President and Chief Risk Officer**

Alan Blair

Senior Vice President, Atlantic Canada

Jean-François Blais*

President, Intact Insurance

Paul Brehm

Senior Vice President, Specialty Solutions**

Sonya Côté

Senior Vice President and Chief Internal Auditor

Frédéric Cotnoir

Senior Vice President, Corporate and Legal Services and Secretary

Debbie Coull-Cicchini

Executive Vice President, Intact Insurance**

Dennis Crosby

Senior Vice President, Specialty Solutions (U.S.)**

Joe D'Annunzio

Senior Vice President, BrokerLink**

Jean-François Desautels

Senior Vice President, Québec and Digital Distribution, Intact Insurance

Monika Federau

Senior Vice President and Chief Strategy Officer

Anne Fortin

Senior Vice President, Direct Distribution**

Don Fox

Executive Vice President

Darren Godfrey

Senior Vice President, Personal Lines

Karim Hirji

Senior Vice President, International and Ventures

Mathieu Lamy

Executive Vice President and Chief Operating Officer**

Alain Lessard

Senior Vice President, Commercial Lines

Louis Marcotte

Senior Vice President and Chief Financial Officer

Lucie Martel

Senior Vice President and Chief Human Resources Officer

Benoit Morissette

Senior Vice President and Group Chief Actuary**

Jennie Moushos

Senior Vice President, Western Canada

Werner Muehleman

Senior Vice President and Managing Director, Intact Investment Management Inc.

Carla Smith

Senior Vice President, Corporate Development

Richard Taschereau**

Senior Vice President, Marketing (Canada)

Mark A. Tullis

Vice Chairman

Peter Weightman

Senior Vice President, Specialty Solutions and Surety (Canada)**

Notes:

1 Denotes member of the Audit Committee

2 Denotes member of the Compliance Review and Corporate Governance Committee

3 Denotes member of the Human Resources and Compensation Committee

4 Denotes member of the Risk Management Committee

* Retired since Jan. 1, 2018

** Since Jan. 1, 2018

For complete biographies of the members of the Board of Directors, please see www.intactfc.com.

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SHAREHOLDER AND CORPORATE INFORMATION

Credit rating

	A.M. Best	DBRS	Moody's	Fitch
IFC long-term issuer credit ratings	a-	A	Baa1	A-
OneBeacon long-term issuer credit ratings	bbb+	Not rated	Baa2	A-
IFC's principal Canadian P&C insurance subsidiaries' financial strength ratings	A+	AA (low)	A1	AA-
IFC's principal U.S. P&C insurance subsidiaries' financial strength ratings	A	Not rated	A2	AA-

DBRS has assigned a rating of "Pfd-2" with a Stable trend for the Non-cumulative Rate Reset Class A Series 1 preferred shares, Non-cumulative Rate Reset Class A Series 3 preferred shares, Non-cumulative Floating Rate Class A Series 4 preferred shares, Non-cumulative Class A Series 5 preferred shares and Non-cumulative Class A Series 6 preferred shares (the "Series 1 Preferred Shares", "Series 3 Preferred Shares", "Series 4 Preferred Shares", "Series 5 Preferred Shares" and "Series 6 Preferred Shares" respectively) issued on July 12, 2011, August 18, 2011, September 30, 2016, May 24, 2017 and August 18, 2017, respectively. Fitch Ratings has assigned a rating of "BBB" with a Stable outlook to the Series 1 Preferred Shares, Series 3 Preferred Shares, Series 4 Preferred Shares, Series 5 Preferred Shares and Series 6 Preferred Shares.

Eligible dividend designation

For purposes of the enhanced dividend tax credit rules contained in the *Income Tax Act* (Canada) and any corresponding provincial and territorial tax legislation, all dividends (and deemed dividends) paid by Intact Financial Corporation to Canadian residents on our common and preferred shares after December 31, 2005, are designated as eligible dividends. Unless stated otherwise, all dividends (and deemed dividends) paid by the Company hereafter are designated as eligible dividends for the purposes of such rules.

Information for shareholders outside of Canada

Dividends paid to residents of countries with which Canada has bilateral tax treaties are generally subject to the 15% Canadian non-resident withholding tax. There is no Canadian tax on gains from the sale of shares (assuming ownership of less than 25%) or debt instruments of the Company owned by non-residents not carrying on business in Canada. No government in Canada levies estate taxes or succession duties.

Common share prices and volume

	High	Low	Close	Volume Traded
2017 Q1	\$ 97.56	\$ 91.40	\$ 94.58	13,471,916
2017 Q2	\$ 98.29	\$ 91.41	\$ 97.96	15,096,910
2017 Q3	\$ 104.33	\$ 95.14	\$ 103.07	13,125,539
2017 Q4	\$ 109.33	\$ 99.35	\$ 104.99	15,359,434
Year 2017	\$ 109.33	\$ 91.40	\$ 104.99	57,053,799
2016 Q1	\$ 91.08	\$ 77.49	\$ 90.93	16,605,531
2016 Q2	\$ 94.16	\$ 84.88	\$ 92.29	13,312,286
2016 Q3	\$ 97.20	\$ 89.75	\$ 94.84	10,209,134
2016 Q4	\$ 97.34	\$ 90.00	\$ 96.10	13,065,874
Year 2016	\$ 97.34	\$ 77.49	\$ 96.10	53,192,825
2015 Q1	\$ 95.77	\$ 81.74	\$ 95.42	18,432,707
2015 Q2	\$ 95.36	\$ 85.42	\$ 86.79	15,894,652
2015 Q3	\$ 95.82	\$ 86.30	\$ 93.72	14,672,799
2015 Q4	\$ 96.77	\$ 85.81	\$ 88.68	19,056,349
Year 2015	\$ 96.77	\$ 81.74	\$ 88.68	68,056,507

Source: Toronto Stock Exchange

Common share dividend history

Record	Payable	Amount
Dec. 15, 2017	Dec. 29, 2017	\$0.64
Sept. 15, 2017	Sept. 29, 2017	\$0.64
June 15, 2017	June 30, 2017	\$0.64
Mar. 15, 2017	Mar. 31, 2017	\$0.64
Dec. 15, 2016	Dec. 30, 2016	\$0.58
Sept. 15, 2016	Sept. 30, 2016	\$0.58
June 15, 2016	June 30, 2016	\$0.58
Mar. 15, 2016	Mar. 31, 2016	\$0.58
Dec. 15, 2015	Dec. 31, 2015	\$0.53
Sept. 15, 2015	Sept. 30, 2015	\$0.53
June 15, 2015	June 30, 2015	\$0.53
Mar. 16, 2015	Mar. 31, 2015	\$0.53

Toronto Stock Exchange (TSX) listings

Common Shares Ticker Symbol: IFC
 Series 1 Preferred Shares Ticker Symbol: IFC.PR.A
 Series 3 Preferred Shares Ticker Symbol: IFC.PR.C
 Series 4 Preferred Shares Ticker Symbol: IFC.PR.D
 Series 5 Preferred Shares Ticker Symbol: IFC.PR.E
 Series 6 Preferred Shares Ticker Symbol: IFC.PR.F

Annual meeting of the shareholders

Date: Wednesday, May 9, 2018
 Time: 11:30 a.m. (Eastern Time)
 Venue: Art Gallery of Ontario
 317 Dundas Street West
 Toronto, Ontario
 Canada M5T 1G4

Version française

Il existe une version française du présent rapport annuel à la section Investisseurs de notre site Web www.intactfc.com/French/accueil/default.aspx. Les personnes intéressées peuvent obtenir une version imprimée en appelant au 1 866 778 0774 ou en envoyant un courriel à ir@intact.net.

Transfer agent and registrar

Computershare Investor Services Inc.
 100 University Avenue, 8th Floor,
 North Tower
 Toronto, Ontario M5J 2Y1
 1 800 564 6253

Auditors

Ernst & Young LLP

Earnings conference call dates

Q1 – May 9, 2018
 Q2 – August 1, 2018
 Q3 – November 7, 2018
 Q4 – February 6, 2019

Investor inquiries

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 Vice President, Investor Relations
 & Treasurer
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Media inquiries

Stephanie Sorensen
 Director, External Communications
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Dividend reinvestment

Shareholders can reinvest their cash dividends in common shares of Intact Financial Corporation on a commission-free basis either through a broker, subject to eligibility as determined by the broker, or through Canadian ShareOwner Investments Inc. Full details can be obtained by visiting the Investors section of the Company's website at www.intactfc.com.

Why **invest** with Intact

We are the largest provider of P&C insurance in Canada with close to \$10 billion (\$8 billion in Canada) in annual direct premiums written¹. We have consistently outperformed the Canadian industry due to our disciplined approach to underwriting, our scale advantage and our in-house claims expertise. Our record of strong capital generation and disciplined capital deployment has allowed us to pursue our growth objectives while also returning capital to shareholders. We are a proven industry consolidator with a track record of 16 accretive acquisitions since 1988. In 2017 we expanded our reach by entering the U.S. specialty market, representing a significant milestone in building a world-class P&C insurer. Our financial strength is reinforced by prudent risk management, resulting in a consistent track record of favourable reserve development.

¹ DPW (pro-forma) for 2017 comprises the DPW of P&C Canada and the DPW (pro-forma) of P&C U.S., using an exchange rate of 1.30



See the full story online at
intactfc.com/2017annualreport



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