

MORNEAU SHEPELL MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2020

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Morneau Shepell Inc. ("Morneau Shepell" or the "Company") was incorporated pursuant to the laws of the Province of Ontario on October 19, 2010, and as of January 1, 2011, is the successor of Morneau Sobeco Income Fund (the "Fund").

This Management's Discussion and Analysis ("MD&A") covers the three and nine months ended September 30, 2020 and should be read in conjunction with the accompanying unaudited condensed consolidated interim financial statements ("interim financial statements") of Morneau Shepell and notes thereto for the three and nine months ended September 30, 2020, and the MD&A and the audited consolidated financial statements and notes thereto for the year ended December 31, 2019. Unless otherwise noted, all financial information presented has been rounded to the nearest thousand and is presented in Canadian dollars in accordance with International Financial Reporting Standards ("IFRS"), unless otherwise noted. Certain totals, subtotals and percentages may not reconcile due to rounding.

This MD&A contains "forward-looking statements" within the meaning of applicable securities laws, such as statements concerning anticipated future events, results, circumstances, performance or expectations that are not historical facts. They are based on certain factors and assumptions, including expected growth, results of operations, business prospects and opportunities. Use of words such as "may", "will", "expect", "believe", or other words of similar effect may indicate a "forward-looking" statement. These statements are not guarantees of future performance and are subject to numerous risks and uncertainties, including those described in our publicly filed documents (available on SEDAR at sedar.com) and in this MD&A under the heading "Risks and Uncertainties". Those risks and uncertainties include the ability to maintain profitability and manage growth, ability to pay dividends, reliance on information systems and technology, reputational risk, dependence on key clients, reliance on key professionals, the ability to successfully integrate acquisitions, general economic conditions and pandemics, natural disasters or other unanticipated events (including the novel coronavirus ("COVID-19") pandemic). Many of these risks and uncertainties can affect our actual results and could cause our actual results to differ materially from those expressed or implied in any forward-looking statement made by us or on our behalf. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. All forward-looking statements in this MD&A are qualified by these cautionary statements. These statements are made as of the date of this MD&A and, except as required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. Additionally, we undertake no obligation to comment on analyses, expectations or statements made by third parties in respect of us, our financial or operating results or our securities.

To assist investors in assessing our financial performance, this discussion also makes reference to certain non-IFRS measures such as EBITDA, adjusted EBITDA, adjusted EBITDA per share, EBITDA margin, adjusted EBITDA margin, Free Cash Flow, Normalized Free Cash Flow, twelve-month rolling Normalized Payout Ratio, and twelve-month rolling Normalized Payout Ratio including changes in adjusted non-cash operating working capital. EBITDA and adjusted EBITDA are intended to represent an indication of Morneau Shepell's capacity to generate profit from operations before taking into account management's financing decisions and costs of consuming tangible capital assets and intangible assets, which vary according to their vintage, technological currency, and management's estimate of their useful life. Accordingly, EBITDA comprises profit before finance costs, income taxes, depreciation and amortization, while Adjusted EBITDA represents EBITDA before taking into account certain unusual expenditures. EBITDA margin represents EBITDA as a percentage of revenue, and Adjusted EBITDA margin represents Adjusted EBITDA as a percentage of revenue. We believe both EBITDA and Adjusted EBITDA are useful measures in evaluating our performance and we utilize them to monitor compliance with debt covenants. We also believe that Free Cash Flow, Normalized Free Cash Flow, the twelve-

month rolling Normalized Payout Ratio, and the twelve-month rolling Normalized Payout Ratio including changes in adjusted non-cash operating working capital, are useful supplemental measures of Morneau Shepell's ability to generate cash after deducting capital expenditures required to maintain or expand the business. We also utilize them to make decisions related to dividends to shareholders. These ratios, however, are non-IFRS measures and therefore, should not be seen as a substitute for cash flow from operating activities. Free Cash Flow is defined as cash provided by operating activities adjusted for capital expenditures. Normalized Free Cash Flow is defined as cash provided by operating activities, adjusted for changes in non-cash operating working capital, capital expenditures, current income taxes (net of income taxes paid) and certain unusual expenditures.

Non-IFRS measures do not have any standard meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers. Non-IFRS measures are reconciled to IFRS measures elsewhere in this MD&A.

OUTSTANDING SHARE DATA

The Company is authorized to issue an unlimited number of common shares and 10 million preferred shares. Each common share entitles the holder to one vote at all meetings of shareholders and represents an interest in dividends declared by the Company and an undivided interest in the net assets of the Company. As at November 10, 2020, Morneau Shepell had 68,514,444 common shares and nil preferred shares outstanding. The number of long-term incentive plan ("LTIP") units, including those that remain unvested, that are outstanding and may be converted to common shares is approximately 2,300,000.

BUSINESS OVERVIEW

Morneau Shepell is a leading provider of technology-enabled HR services that deliver an integrated approach to employee well-being through our cloud-based platform. Our focus is providing world class solutions to our clients to support the mental, physical, social and financial well-being of their people. By improving lives, we improve business. Our approach spans services in employee and family assistance, health and wellness, recognition, pension and benefits administration, retirement consulting, actuarial and investment services. Morneau Shepell employs approximately 6,000 employees who work with some 24,000 client organizations that use our services in Canada, the United States and around the globe.

The Company has four operating segments, consistent with our four core lines of business, named as follows: Well-Being Solutions, Administrative Solutions, Retirement Solutions, and Health and Productivity Solutions.

The Well-Being Solutions business integrates what was formerly Employee Support Solutions ("ESS") with the people, assets and capabilities of the LifeWorks organization, including its cloud-based user platform for deploying technology-enabled HR services. The business is focused on delivering an integrated employee experience for solutions that encompass the full continuum of care for achieving mental, physical, social and financial well-being. These solutions include a broad range of clinical services offered within employee and family assistance plans, along with corporate reward, recognition and perks programs focusing on driving engagement and productivity in workplace culture.

In the Administrative Solutions business, the Company provides a full range of user-friendly solutions from software to full outsourcing for the administration of employee pension and benefits plans, leveraging its Ariel software platform. The Company provides employees and organizations with self-serve portals, mobile applications and contact centre support to ensure they have the tools and resources to manage their benefits, save for retirement and ultimately ensure their long-term financial well-being.

The Retirement Solutions business helps organizations design, build and operate sustainable retirement programs that provide a strong return on investment while ensuring compliance with all governance and regulatory requirements. The Company leverages actuarial, recordkeeping and risk-management technology and data analytics across the entire defined-benefit to defined-contribution spectrum to provide strategic consulting support and innovative solutions to pension and asset management, minimizing risk and supporting the long-term financial security and well-being of employees.

In Health and Productivity Solutions, the Company serves as strategic advisors to help organizations of all sizes design, develop and manage disability programs and policies with a focus on best-in-class employee experience, health prevention, measurable health outcomes, and help people return to work using the tools and resources available on the state-of-the-art Abiliti platform. The business supports the complex end of the Company's continuum of care through its AbilitiCBT product and non-occupational absence management solutions.

2020 THIRD QUARTER SUMMARY

<i>In thousands of Canadian dollars, except per share amounts</i>	Three months ended September 30, 2020	Three months ended September 30, 2019	Nine months ended September 30, 2020	Nine months ended September 30, 2019
Revenue	\$ 240,300	\$ 223,980	\$ 729,517	\$ 641,341
Adjusted EBITDA ⁽¹⁾	49,634	43,811	149,027	134,411
Adjusted EBITDA margin ⁽¹⁾	20.7%	19.6%	20.4%	21.0%
Adjusted EBITDA per share (basic) ⁽¹⁾	0.71	0.66	2.14	2.03
Normalized Free Cash Flow ⁽¹⁾	21,919	24,212	73,627	75,846
Profit (loss)	(2,069)	1,332	45,095	16,320
Earnings (loss) per share (basic)	(0.03)	0.02	0.65	0.25

(1) These items are non-GAAP measures and should not be considered a substitute or alternative for GAAP measures. Refer to the 2020 Third Quarter Operating Results Summary for a reconciliation of these non-GAAP measures to IFRS measures.

THIRD QUARTER:

We had a solid third quarter of 2020 and continued to deliver revenue and adjusted EBITDA growth versus the comparative quarter in 2019. Highlights of the third quarter include:

- Organic revenue growth for the quarter was 4.3% including 8.4% organic growth in our U.S. and International regions.
- Overall, revenue growth of \$16.3 million or 7.3% versus the comparative period is primarily due to previously mentioned organic growth and the mid-year 2019 acquisition of Mercer's standalone, large market, health and defined benefit pension plan administration business, offset by the divestiture of our benefits consulting business in the first quarter of 2020.
- An increase in adjusted EBITDA of \$5.8 million, or 13.3%, to \$49.6 million versus \$43.8 million in the comparative period due to organic growth and the Mercer acquisition.
- Adjusted EBITDA margin was 20.7% versus 19.6% in the comparative period. The slight increase in margin is due to lower operating expenses during the quarter compared to the same period in the prior year.

- An increase in Adjusted EBITDA per share (basic) of \$0.05 or 7.6% to \$0.71 versus \$0.66 in the comparative period.
- Loss for the period was \$2.1 million compared to a profit of \$1.3 million in the same period in prior year. The loss is mainly due to a sublease loss provision of \$10.3 million, before taxes. The sublease loss provision relates to the Company's planned relocation of its current head office and two other offices in the Greater Toronto Area to a new head office location in downtown Toronto at the end of 2021, prior to the end of their respective lease terms. The loss provision recorded is associated with leases of excess office space and other related lease exit costs, net of estimated sublease income. The move downtown will allow the Company to benefit from cost savings and reduce the overall square feet in a more collaborative and modern workspace with better access to clients and labour markets.

2020 THIRD QUARTER OPERATING RESULTS SUMMARY

Results of Operations	Three Months Ended		Nine months Ended	
	September 30,		September 30,	
Selected Unaudited Consolidated Financial Information	2020	2019	2020	2019
<i>(In thousands of dollars except per share amounts)</i>				
Revenue	\$ 240,300	\$ 223,980	\$ 729,517	\$ 641,341
Deduct/(Add):				
Salaries, benefits and contractor expenses	167,162	153,305	496,113	429,491
Other operating expenses	29,538	35,590	104,375	97,091
Depreciation and amortization	28,931	24,155	81,392	68,613
Sublease loss provision	10,300	–	10,300	–
Finance costs	6,665	7,578	20,962	21,540
Gain on business divestiture	–	–	(39,843)	–
Transaction costs	–	719	–	719
Share of (income) loss of joint ventures	(367)	75	(469)	(399)
Income tax expenses	140	1,226	11,592	7,966
Profit (Loss) for the period	\$ (2,069)	\$ 1,332	\$ 45,095	\$ 16,320
Add:				
Finance costs	6,665	7,578	20,962	21,540
Depreciation and amortization	28,931	24,155	81,392	68,613
Depreciation, amortization, and income tax expense on share of income of joint ventures	166	168	509	511
Income tax expenses	140	1,226	11,592	7,966
EBITDA⁽¹⁾	\$ 33,833	\$ 34,459	\$ 159,550	\$ 114,950
Add/(Deduct) adjustments:				
LifeWorks integration	619	2,449	2,508	7,164
Mercer integration and transactions	2,954	2,986	11,131	2,986
New ERP implementation costs	1,928	–	5,381	–
Gain on business divestiture	–	–	(39,843)	–
Sublease loss provision	10,300	–	10,300	–
Transformation project costs	–	3,917	–	9,311
Adjusted EBITDA⁽²⁾	\$ 49,634	\$ 43,811	\$ 149,027	\$ 134,411
EBITDA margin⁽³⁾	14.1%	15.4%	21.9%	17.9%
Adjusted EBITDA margin⁽³⁾	20.7%	19.6%	20.4%	21.0%
Cash provided by operating activities	50,762	37,085	96,731	57,846
Deduct: Capital expenditures ⁽⁴⁾	(19,788)	(11,444)	(50,594)	(30,680)
Free Cash Flow⁽⁵⁾	\$ 30,974	\$ 25,641	\$ 46,137	\$ 27,166
Add (deduct):				
Changes in non-cash operating working capital	(15,980)	(2,247)	12,333	40,048
Current income taxes, net of income taxes paid	724	(8,533)	(4,563)	(10,829)
Adjustments to EBITDA ⁽⁶⁾	6,201	9,351	19,720	19,461
Normalized Free Cash Flow⁽⁷⁾	\$ 21,919	\$ 24,212	\$ 73,627	\$ 75,846
Earnings (loss) per Share:				
Basic	\$ (0.03)	\$ 0.02	\$ 0.65	\$ 0.25
Diluted	\$ (0.03)	\$ 0.02	\$ 0.64	\$ 0.25
EBITDA per Share (basic)	\$ 0.48	\$ 0.52	\$ 2.29	\$ 1.74
Adjusted EBITDA per Share (basic)	\$ 0.71	\$ 0.66	\$ 2.14	\$ 2.03
Dividends declared	\$ 13,358	\$ 12,596	\$ 39,971	\$ 37,715
Twelve-month rolling Normalized Payout Ratio ⁽⁸⁾	57.8%	53.3%	57.8%	53.3%
Twelve-month rolling Normalized Payout Ratio, including changes in adjusted non-cash operating working capital ⁽⁹⁾	64.6%	82.9%	64.6%	82.9%

Footnotes:

- (1) "EBITDA" is defined as profit before finance costs, income taxes, depreciation and amortization.
- (2) "Adjusted EBITDA" is defined as "EBITDA" before adjusted items, which do not constitute a part of the Company's on-going operating expenses.
- (3) "EBITDA margin" represents EBITDA as a percentage of revenue, and "Adjusted EBITDA margin" represents Adjusted EBITDA as a percentage of revenue.
- (4) "Capital Expenditures" includes additions to capital assets and intangible assets but excludes additions to capital assets and intangible assets acquired through business acquisitions, and is presented net of disposals.
- (5) "Free Cash Flow" is defined as cash provided by operating activities adjusted for capital expenditures.
- (6) "Adjustments to EBITDA" for the purpose of calculating normalized free cash flow do not include non-cash portion of sublease loss provisions. The amount has been excluded as it has already been added back in cash from operating activities before the change in non-cash operating working capital.
- (7) "Normalized Free Cash Flow" is defined as cash provided by operating activities, adjusted for changes in non-cash operating working capital, capital expenditures, current income taxes (net of income taxes paid) and certain unusual expenditures.
- (8) "Twelve-month rolling Normalized Payout Ratio" is defined as dividends declared divided by Normalized Free Cash Flow for the rolling twelve month period.
- (9) "Twelve-month rolling Normalized Payout Ratio, including changes in adjusted non-cash operating working capital" is defined as dividends declared divided by the Twelve-month rolling Normalized Free Cash Flow, including changes in non-cash operating working capital adjusted for unusual fluctuations.

ANALYSIS OF THE THREE MONTHS ENDED SEPTEMBER 30, 2020 OPERATING RESULTS

Revenue

Revenue for the three months ended September 30, 2020 increased by \$16.3 million, or 7.3%, to \$240.3 million compared to \$224.0 million for the same period in 2019. The increase is primarily due to strong organic growth and the Mercer acquisition, offset by the divestiture of our benefits consulting business.

Salaries, Benefits and Contractor Expenses

Salaries, benefits and contractor expenses for the three months ended September 30, 2020 increased by \$13.9 million, or 9.1%, to \$167.2 million compared to \$153.3 million for the same period in 2019. The increase is mainly due to the Mercer acquisition, business growth and general merit increases. The increases were partially offset by a reduction in salaries expense related to the benefits consulting business sold in the first quarter of 2020.

Other Operating Expenses

Other operating expenses for the three months ended September 30, 2020 decreased by \$6.1 million, or 17.1%, to \$29.5 million compared to \$35.6 million for the same period in 2019. The decrease is mainly due to lower operating and integration costs related to acquired businesses and a reduction in operating expenses related to the benefits consulting business sold in the first quarter of 2020. The decrease was partially offset by higher implementation costs related to the new ERP system.

Finance Costs

Finance costs for the three months ended September 30, 2020 decreased by \$0.9 million, or 11.8%, to \$6.7 million compared to \$7.6 million for the same period in 2019 primarily due to a reduction of interest expense on convertible debentures and lower borrowings under the Company's credit facility agreement.

Depreciation and Amortization

Depreciation and amortization for the three months ended September 30, 2020 increased by \$4.7 million, or 19.4%, to \$28.9 million compared to \$24.2 million for the same period in 2019. The increase is primarily due to \$1.4 million of accelerated depreciation of right-of-use assets and capital assets due to the planned office

relocation as well as amortization and depreciation of acquired intangibles, capital additions related to the Mercer acquisition and internally developed software additions.

Sublease loss

The Company signed a lease agreement for a new Toronto head office location which became effective in July 2020. The new location will replace the current head office and two other offices in the Greater Toronto Area. As a result, the Company incurred a penalty to terminate one lease early and plans to exit the other leases prior to the end of their respective lease terms. Due to the planned relocation, the Company recognized a loss provision, net of estimated sublease income, of \$10,300 associated with leases of excess office space and other related lease exit costs. The Company will also record accelerated depreciation of the right-of-use assets and fixed assets related to these locations of \$7,620 (\$1,402 for the three months ended September 30, 2020) from this quarter until the end of 2021, when the move is expected to be completed.

Income Taxes

Income tax expense for the three months ended September 30, 2020 was \$0.1 million compared to \$1.2 million for the same period in 2019. The decrease in income tax expense is due to pre-tax loss for the quarter.

Loss for the Period

As a result of the changes noted above, loss for the three months ended September 30, 2020 was \$2.1 million compared to a profit of \$1.3 million for the same period in 2019.

Key Financial Measures: Adjusted EBITDA, EBITDA, Free Cash Flow and Normalized Free Cash Flow

Adjusted EBITDA and EBITDA

Adjusted EBITDA increased by \$5.8 million, or 13.3%, to \$49.6 million compared to \$43.8 million for the same period in 2019. The increase is primarily due to growth in revenue of \$16.3 million, partially offset by an increase in salaries and other operating expenses of \$10.5 million after EBITDA adjustments.

EBITDA decreased by \$0.7 million to \$33.8 million compared to \$34.5 million for the same period in 2019. The decrease in EBITDA is primarily due to the sublease loss provision of \$10.3 million.

Free Cash Flow

Free Cash Flow for the three months ended September 30, 2020 increased by \$5.4 million from \$25.6 million for the same period in 2019 to \$31.0 million in the current quarter. The increase is mainly due to higher cash generated from operating activities of \$22.5 million mainly due to favourable changes in non-cash working capital, partially offset by higher capital expenditures of \$8.3 million and higher income taxes paid of \$8.8 million.

Normalized Free Cash Flow

Normalized Free Cash Flow for the three months ended September 30, 2020 decreased by \$2.3 million to \$21.9 million compared to \$24.2 million for the same period in 2019. The decrease is mainly due to higher capital expenditures of \$8.3 million, partially offset by higher cash generated from operating activities before changes in non-cash operating working capital and EBITDA adjustments of \$5.4 million.

Revenue

Revenue for the nine months ended September 30, 2020 increased by \$88.2 million, or 13.7%, to \$729.5 million compared to \$641.3 million for the same period in 2019. The increase is primarily due to the Mercer acquisition, net of the divestiture of our benefits consulting business in the first quarter of 2020, and strong organic growth in the U.S.

Salaries, Benefits and Contractor Expenses

Salaries, benefits and contractor expenses for the nine months ended September 30, 2020 increased by \$66.6 million, or 15.5%, to \$496.1 million compared to \$429.5 million for the same period in 2019. The increase is mainly due to the Mercer acquisition, business growth and general merit increases. The increases were partially offset by a reduction in salaries expense related to the benefits consulting business sold in the first quarter of 2020.

Other Operating Expenses

Other operating expenses for the nine months ended September 30, 2020 increased by \$7.3 million, or 7.5%, to \$104.4 million compared to \$97.1 million for the same period in 2019. The increase is mainly due to operating and integration costs related to acquired businesses and implementation costs related to a new ERP system. The increases were partially offset by a reduction in operating expenses related to the benefits consulting business sold in the first quarter of 2020.

Finance Costs

Finance costs for the nine months ended September 30, 2020 decreased by \$0.5 million, or 2.3%, to \$21.0 million compared to \$21.5 million for the same period in 2019 primarily due to lower borrowings under the Company's credit facility agreement and a reduction of interest expense on convertible debentures, partially offset by higher accretion expense on future consideration related to acquisitions.

Depreciation and Amortization

Depreciation and amortization for the nine months ended September 30, 2020 increased by \$12.8 million, or 18.7%, to \$81.4 million compared to \$68.6 million for the same period in 2019. The increase is primarily due to \$1.4 million of accelerated depreciation of right-of-use assets and capital assets due to the planned office relocation as well as amortization and depreciation of acquired intangibles, capital additions related to the Mercer acquisition and internally developed software additions.

Gain on Business Divestiture

On March 1, 2020, the Company sold its benefits consulting business to HUB International Limited for a purchase price of \$70.0 million subject to working capital adjustments, which were finalized during the third quarter. The gain recognized on the sale was \$39.8 million before tax. Refer to note 4 of the interim financial statements for the three and nine months ended September 30, 2020 for further details.

Sublease loss provision

Refer to the 'Analysis of the Three Months Ended September 30, 2020 Operating Results' section above.

Income Tax Expenses

Income tax expenses for the nine months ended September 30, 2020 increased by \$3.6 million to \$11.6 million compared to \$8.0 million for the same period in 2019. The increase is mainly due to higher pre-tax profit.

Profit for the Period

As a result of the changes noted above, profit for the nine months ended September 30, 2020 was \$45.1 million compared to a profit of \$16.3 million for the same period in 2019.

Key Financial Measures: Adjusted EBITDA, EBITDA, Free Cash Flow and Normalized Free Cash Flow

Adjusted EBITDA and EBITDA

Adjusted EBITDA increased by \$14.6 million, or 10.9%, to \$149.0 million compared to \$134.4 million for the same period in 2019. The increase is primarily due to the Mercer acquisition and organic growth. Adjusted EBITDA excludes adjusted items, which do not constitute a part of the Company's on-going operating expenses.

Below is a description of the adjustments for the three and nine months ended September 30, 2020 and 2019:

- Mercer and LifeWorks integration costs represent the costs incurred to integrate the clients, employees and operations acquired with our existing businesses. The LifeWorks integration was completed during the third quarter of 2020. The Mercer integration is also largely complete and no additional costs are expected beyond the fourth quarter of 2020.
- New ERP system implementation costs represent costs incurred by the Company to implement a new comprehensive enterprise resource planning solution. The new solution will help with the Company's growth, realize efficiencies, streamline integrations of acquisitions and eliminate redundancies.
- Transformation project costs relate to initiatives that increase long term value in the form of earnings and cash flow improvement through operational efficiency. These costs represent fees payable to a third-party firm, severance and other transition costs. The transformation project was completed in the fourth quarter of 2019.

EBITDA increased by \$44.6 million to \$159.6 million compared to \$115.0 million for the same period in 2019 mainly due to the Mercer acquisition and gain on business divestiture, partially offset by the sublease loss provision.

Free Cash Flow

Free Cash Flow for the nine months ended September 30, 2020 increased by \$18.9 million to \$46.1 million compared to \$27.2 million for the same period in 2019. The increase is mainly due to higher cash generated from operating activities of \$43.1 million mainly due to favourable changes in non-cash working capital, organic growth and the Mercer acquisition, partially offset by higher income tax paid of \$4.4 million and higher capital expenditures of \$19.9 million.

Normalized Free Cash Flow

Normalized Free Cash Flow for the nine months ended September 30, 2020 decreased by \$2.2 million to \$73.6 million compared to \$75.8 million the same period in 2019. The decrease is mainly due to higher capital expenditures of \$19.9 million, partially offset by higher cash generated from operating activities before changes in non-cash operating working capital of \$15.4 million.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

The following table provides an overview of the Company's cash flows for the periods indicated:

Cash Flow Information

Selected Consolidated Financial Information:

<i>Cash provided by (used in): (In thousands of dollars)</i>	Nine months ended September 30, 2020	Nine months ended September 30, 2019
Operating activities	\$ 96,731	\$ 57,846
Financing activities	(104,353)	37,573
Investing activities	9,244	(88,363)
Increase in cash	\$ 1,622	\$ 7,056

Cash provided by operating activities for the nine months ended September 30, 2020 increased by \$38.9 million to \$96.7 million compared to \$57.8 million for the same period in 2019. The increase is mainly due to higher cash generated from operating activities of \$43.0 million mainly due to favourable changes in working capital and lower finance costs paid of \$0.2 million, partially offset by higher income taxes paid of \$4.4 million.

Cash provided by financing activities for the nine months ended September 30, 2020 decreased by \$142.0 million compared to the same period in 2019. The decrease is due to a net change in the revolving loan of \$136.2 million, loan modification fees of \$0.4 million, higher principal payments of lease liabilities of \$1.7 million, \$1.5 million payment related to the redemption of convertible debentures and higher dividend payments of \$2.1 million.

Cash provided by investing activities for the nine months ended September 30, 2020 increased by \$97.6 million to \$9.2 million compared to cash used in investing activities of \$88.4 million for the same period in 2019. The increase was primarily due to \$68.8 million received from the sale of the benefits consulting business and lower business acquisition payments of \$59.2 million compared to the prior year. The increases are partially offset by higher capital expenditures of \$19.9 million, higher deferred and contingent acquisition payments of \$10.2 million and lower principal payments received of \$0.2 million from finance leases.

Dividends to Shareholders

Monthly dividends were declared for shareholders of record on the last business day of each month and were paid on approximately the 15th day of the following month. Monthly dividends were \$0.065 per share each month for the quarter. The Company continued to declare the same monthly dividend amount in October and November 2020.

We consider the amount of cash generated by the business in determining the amount of dividends to pay to shareholders. We do not generally consider profit or loss in setting the level of dividends as this is a non-cash metric and is not reflective of the level of cash flow that we generate.

The twelve-month rolling Normalized Payout Ratio at September 30, 2020 was 57.8% compared to 53.3% for the same period in 2019. The increase is primarily due to higher dividend payments as a result of the conversion of the convertible debentures. The twelve-month rolling Normalized Payout Ratio, including changes in adjusted non-cash operating working capital at September 30, 2020 was 64.6% compared to 82.9% for the same period in 2019. The decrease in the ratio is primarily due to the favourable change in non-cash operating working capital over the comparative period.

Capital Expenditures

Our capital expenditures typically include information technology hardware and software (external and internally developed), leasehold improvements, and office furniture. Such amounts are expected to be funded from our operating cash flow. Additional capital expenditure requirements may result from significant business expansion. Capital expenditures for the three months ended September 30, 2020 increased by \$8.4 million to \$19.8 million compared to \$11.4 million for the same period in 2019, and for the nine months ended September 30, 2020 increased by \$19.9 million to \$50.6 million compared to \$30.7 million for the same period in 2019. The increase is mainly due to capital expenditures related to the Mercer integration and the development of internally developed software, partially offset by lower expenditures on hardware and software purchases.

Contractual Obligations

The Company manages and continually monitors its commitments and contractual obligations to ensure that these can be met with funding provided by operations and capital resources available.

Commitments

We lease office space and selected equipment under lease agreements as well as software licenses with terms ranging from one to fifteen years. We also have revolving loans under the Company's credit facility agreement and convertible debentures described under the "Capital Resources" section.

We are a party to various subleases to which we would be liable for the rental payment in the case of a default by the subtenants. The minimum payments and the aggregate sublease income related to these premises have been presented on a "net" basis below for the purpose of the Commitments disclosure. A summary of contractual obligations, which outlines the year the payments are due is as follows:

<i>(In thousands of dollars)</i>	Total	2020	2021	2022	2023	2024	2025 and thereafter
Long-term debt	\$ 426,371	\$ –	\$ –	\$ –	\$426,371	\$ –	\$ –
Leases (net) and software licenses	203,272	5,280	26,541	27,337	22,840	18,029	103,245
Total	\$ 629,643	\$ 5,280	\$ 26,541	\$ 27,337	\$ 449,211	\$ 18,029	\$ 103,245

Future Consideration Related to Acquisitions

The total undiscounted contingent future consideration remaining to be paid is \$16.2 million due from 2020 through 2022. These contingent future installments have been recognized as future consideration related to acquisitions on the statement of financial position at their estimated discounted amounts as at September 30, 2020.

We have no material contractual obligations other than those described in this MD&A and have no off-balance sheet financing arrangements.

Capital Resources

The following table provides an overview of our capital resources:

<i>(In thousands of dollars)</i>	As at September 30, 2020	As at December 31, 2019
Cash, net of bank indebtedness	\$ 5,273	\$ 3,651
Long- term debt, net of debt issuance costs	424,028	470,456
Convertible debenture, net of issuance costs and equity component of debenture	–	40,699
Shareholders' equity	670,365	618,388

Long-term debt

The long-term debt, net of debt issuance costs, decreased \$46.5 million from \$470.5 million as at December 31, 2019 to \$424.0 million as at September 30, 2020.

On April 17, 2020 the Company entered into an amended and restated Credit Facility Agreement (the "Amended and Restated Credit Facility Agreement"). The key changes to the Amended and Restated Credit Facility Agreement include:

- The Company obtained an incremental \$100 million of committed capacity ("Incremental Facility") which matures 364 days from closing.
- The debt to Adjusted EBITDA financial covenant will remain at 4:1 until maturity of the credit agreement.

As at September 30, 2020, the Company had \$315.7 million borrowed in Canadian dollars (December 31, 2019 - \$235.0 million), \$110.7 million (US\$ 83.0 million) borrowed in US dollars (December 31, 2019 - \$238.2 million, US\$ 183.4 million), and had not utilized the swing line available (December 31, 2019 - \$2.9 million utilized), which is included in bank indebtedness. Borrowings under the Amended and Restated Credit Facility Agreement bear interest at CDOR or Canadian Prime plus a specified margin for borrowings in Canadian dollars. Borrowings in US dollars under the Amended and Restated Credit Facility Agreement bear interest at US Base Rate or LIBOR plus a specified margin.

As at September 30, 2020, the Company complied with all the required financial covenants.

Convertible debentures

In January 2020, the Company converted all of the remaining convertible debentures being \$39.2 million, at the holders' request, into 1.6 million common shares of the Company at a conversion price of \$25.10 per common share. The remaining \$1.5 million principal amount was redeemed for cash at a price of one thousand dollars per debenture, plus accrued and unpaid interest.

SELECTED STATEMENT OF FINANCIAL POSITION DATA

The following table provides an overview of our selected statement of financial position data:

<i>(in thousands of dollars)</i>	As at September 30, 2020	As at December 31, 2019
Current assets	\$ 256,906	\$ 270,633
Non-current assets	1,285,174	1,259,585
Current liabilities	174,779	227,471
Non-current liabilities	696,936	684,359

Current Assets

Current assets as at September 30, 2020 decreased by \$13.7 million to \$256.9 million from \$270.6 million as at December 31, 2019. The decrease in current assets is due to a decrease in trade and other receivables and unbilled fees by \$8.2 million primarily due to increased collections as well as decreases in cash of \$4.1 million, prepaid expenses by \$1.0 million, current portion of deferred implementation costs by \$0.5 million and current portion of finance lease receivables by \$0.1 million. The decreases are partially offset by an increase in cash held in trust by \$0.3 million.

Non-current Assets

Non-current assets as at September 30, 2020 increased by \$25.6 million to \$1,285.2 million from \$1,259.6 million as at December 31, 2019. The increase is primarily due to the right-of-use asset recognized for the new head office location, leasehold improvements related to the Mercer acquisition, increases in deferred implementation costs and additions to internally developed software. These increases were partially offset by the disposal of intangible assets and goodwill related to the sale of the benefits consulting business of \$23.3 million and depreciation and amortization of capital and intangible assets.

Current Liabilities

Current liabilities as at September 30, 2020 decreased by \$52.7 million to \$174.8 million from \$227.5 million as at December 31, 2019. The decrease is primarily due to settlement of \$40.7 million of convertible debentures through issuance of common shares and cash repayment, a decrease in trade and other payables of \$9.2 million, a \$7.4 million reduction in the current portion of future consideration related to acquisitions balance mainly due to payments, a \$1.8 million decrease in the fair value of interest and currency swaps liabilities and lower bank indebtedness by \$5.7 million. The decreases are partially offset by increases in current portion of lease liabilities of \$6.8 million, current portion of deferred revenue by \$5.0 million and cash held in trust by \$0.3 million.

Non-current Liabilities

Non-current liabilities as at September 30, 2020 increased by \$12.5 million to \$696.9 million from \$684.4 million at December 31, 2019. The increase is primarily due to increases in lease liabilities of \$39.6 million mainly due to the lease liability recognized for the new head office location, a \$9.9 million increase in provisions mainly related to the sublease loss provision, a \$3.7 million increase in the deferred tax liability, a \$3.1 million increase in deferred revenue and a \$2.9 million higher fair value of interest rate swaps. The increases are offset by decreases in long-term debt of \$46.4 million and future consideration related to acquisitions of \$0.2 million.

As a result of the changes in current assets and current liabilities discussed above, working capital increased by \$38.9 million from \$43.2 million as at December 31, 2019 to \$82.1 million as at September 30, 2020.

CRITICAL ACCOUNTING ESTIMATES

In our year ended December 31, 2019 audited consolidated financial statements and accompanying notes, and in our MD&A for the year ended December 31, 2019, we have identified the accounting estimates that are critical to understanding our business operations and our results from operations. The interim financial statements for the three and nine months ended September 30, 2020 have been prepared using the critical accounting estimates and assumptions consistent with those applied in the audited consolidated financial statements for the year ended December 31, 2019.

Estimates and underlying assumptions are reviewed on an ongoing basis. Estimates are based on historical experience and other assumptions that are considered reasonable in the circumstances. The actual amount or values may vary in certain instances from the assumptions and estimates made. Changes will be recorded, with corresponding effect in profit or loss, when, and if, better information is obtained. The future impact of COVID-19 uncertainties could generate, in future reporting periods, a significant risk of material adjustment to the reported amounts of assets, liabilities, revenue and expenses in the consolidated financial statements. Examples of accounting estimates and judgments that may be impacted by the pandemic include: revenue recognition, impairment of goodwill and intangible assets, allowance for expected credit losses, corporate income taxes, provisions and contingent consideration related to acquisitions.

RISKS AND UNCERTAINTIES

The results of operations, business prospects and financial considerations of Morneau Shepell remain subject to a number of risks and uncertainties and are affected by a number of factors outside of our control. For more information about our risks and uncertainties, please refer to our MD&A for the year ended December 31, 2019.

The risks and uncertainties remain substantially unchanged from those previously disclosed. The reference to pandemics, natural disasters or other unanticipated events in our MD&A for the year ended December 31, 2019 includes the COVID-19 pandemic. The duration and impact of the COVID-19 pandemic on the Company is unknown at this time.

SUPPLEMENTARY SUMMARY OF QUARTERLY RESULTS

Selected Unaudited Consolidated Financial information (in thousands of dollars except per share amounts)

Quarter ended	September 30, 2020 ⁽¹⁾	June 30, 2020	March 31, 2020 ⁽²⁾	December 31, 2019	September 30, 2019	June 30, 2019	March 31, 2019	December 31, 2018 ⁽³⁾
Revenue	240,300	246,175	243,048	247,549	223,980	212,666	204,695	200,761
Profit (loss)	(2,069)	8,258	38,905	2,648	1,332	6,329	8,659	3,450
EBITDA ⁽⁴⁾	33,833	44,386	81,330	39,433	34,459	39,032	41,460	27,842
Adjusted EBITDA ⁽⁴⁾	49,634	52,075	47,318	48,041	43,811	45,882	44,718	35,652
EBITDA margin ⁽⁴⁾	14.1%	18.0%	33.5%	15.9%	15.4%	18.4%	20.3%	13.9%
Adjusted EBITDA margin ⁽⁴⁾	20.7%	21.2%	19.5%	19.4%	19.6%	21.6%	21.8%	17.8%
Earnings(loss) per share (basic)	(0.03)	0.12	0.56	0.04	0.02	0.10	0.13	0.05
Earnings(loss) per share (diluted)	(0.03)	0.12	0.56	0.04	0.02	0.10	0.13	0.05
Normalized Free Cash Flow ⁽⁴⁾	21,919	30,844	20,868	17,636	24,212	27,618	24,013	18,284
Dividends declared	13,358	13,327	13,287	12,739	12,596	12,586	12,533	12,493
Twelve-month rolling normalized payout ratio ⁽⁴⁾	57.8%	55.5%	56.7%	54.0%	53.3%	53.9%	58.4%	61.2%
Twelve-month rolling normalized payout ratio, including changes in adjusted non-cash operating working capital ⁽⁴⁾	64.6%	74.1%	99.0%	89.9%	82.9%	66.5%	64.2%	71.0%
Total assets	1,542,080	1,512,230	1,709,699	1,530,218	1,483,878	1,397,115	1,409,850	1,348,342
Long-term debt	424,028	424,228	586,244	470,456	460,474	408,715	374,752	374,381

Footnotes:

1. September 30, 2020 results included sublease loss of \$10.3 million.
2. March 31, 2020 results included a gain on business divestiture of \$39.8 million.
3. The Company has applied IFRS 16 using the modified retrospective approach. The figures presented have not been restated. Please refer to note 3 of the Consolidated Financial Statements for the year ended December 31, 2019 for further details.
4. These items are non-GAAP measures and should not be considered a substitute or alternative for GAAP measures. Refer to the 2020 Third Quarter Operating Results Summary for a reconciliation of these non-GAAP measures to IFRS measures.

Disclosure Controls and Procedures

Our disclosure controls and procedures have been designed to provide reasonable assurance that all relevant information is identified to our Disclosure Committee to ensure appropriate and timely decisions are made regarding public disclosure.

The Chief Executive Officer and the Chief Financial Officer have concluded that the disclosure controls and procedures are appropriately designed as at September 30, 2020.

Internal Control over Financial Reporting

Management is responsible for designing internal controls over financial reporting, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. In designing these controls, Management used the *Internal Control – Integrated Framework* (COSO 2013 Framework) published by The Committee of Sponsoring Organizations of the Treadway Commission.

The Chief Executive Officer and the Chief Financial Officer have concluded that the internal controls over financial reporting are appropriately designed as at September 30, 2020. No changes were made to our internal controls over financial reporting during the third quarter ended September 30, 2020, that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Additional Information

Morneau Shepell's shares currently trade on the Toronto Stock Exchange under the symbols MSI. Additional information relating to us, including all public filings and our Annual Information Form, is available on the SEDAR website (sedar.com) and on our own website at morneaushepell.com.

The content of this MD&A reflects information known as of November 10, 2020.