**MORNEAU SHEPELL MANAGEMENT'S DISCUSSION AND ANALYSIS**

*FOR THE YEAR ENDED DECEMBER 31, 2018*


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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 year ended December 31, 2018 and should be read in conjunction with the consolidated financial statements of Morneau Shepell and notes thereto for the years ended December 31, 2018 and 2017. Unless otherwise noted, all financial information presented has been rounded to the nearest thousand.

All financial information is presented in Canadian dollars and 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 www.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, integration of an acquired business and related operations and general economic conditions. 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, 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 intangible and tangible capital 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 tax expenses, 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. 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. These ratios, however, are non-IFRS measures and therefore, should not be seen as a substitute for cash flow from operating activities.

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 March 6, 2019, Morneau Shepell had 64,213,879 common shares, nil preferred shares and $86.0 million aggregate principal amount of 4.75% convertible debentures outstanding. In the event all of the outstanding 4.75% convertible debentures are converted into common shares of the Company by the holders prior to their maturity date, the total number of common shares issuable will be approximately 3,400,000. 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 2,500,000.

## BUSINESS OVERVIEW

Morneau Shepell is the largest Canadian firm providing health and productivity, administrative and retirement solutions. We deliver solutions to assist employers in managing the financial security, health and productivity of their employees. With almost 5,000 employees in offices worldwide, we offer services to approximately 24,000 clients, ranging from small businesses to some of the largest corporations and associations in Canada, the United States and around the globe, directly and through our distribution channel partners.

We derive our revenue primarily from fees charged to clients for wellness and employee support solutions ("Well-being," formerly "Employee Support Solutions"), administrative solutions engagements, consulting engagements, and absence management services.

In billing for Well-being services, clients generally are billed based on one of the following arrangements: payment of a minimum retainer and incremental usage-based fees, actual usage, or fixed fees. In addition, subscriptions revenues are generated from the agreement entered into with customers for unlimited access to and usage of the Company's platform for a specified period. Most Well-being agreements may be terminated by the client upon 30 to 90 days' notice to us. It is typical, however, for agreements to continue for multiple years and many automatically renew on an annual basis.

Our Administrative Solutions practice is characterized by fixed contracts, which typically have three-year to five-year terms. Most Administrative Solutions contracts contain an upfront implementation fee and an ongoing monthly service fee. Implementations usually take three to twelve months and involve transferring the administration of a client's pension and/or benefits plans onto our systems, tailoring our systems and training our employees. Additional services provided that are outside the scope of the contract are usually paid on a fee-for-service basis. A small number of contracts contain a large up front customization and

implementation fee, with lower ongoing maintenance fees. Note that as a result of the Company's adoption of IFRS 15, Revenue from Contracts with Customers ("IFRS 15"), on January 1, 2018 the timing of revenue recognition and accounting for deferred implementation costs for certain groups of clients within our Administrative Solutions line of business was impacted. Please refer to note 3 of the Company's consolidated financial statements for the year ended December 31, 2018 for details.

Fees from consulting engagements are charged based on billable hours or on a fee-for-service basis. In some cases, consulting engagements may be billed on a fixed-fee basis, although these engagements are typically much smaller and the services are delivered over a shorter period of time. For some benefits consulting assignments which involve the purchase of an insurance policy underwritten by an insurance company, we may be paid commissions (in lieu of fees) by the client's insurance company, which is a common practice in the industry. These commissions are based on a percentage of the premiums paid by the client to the insurance company and our policy is to disclose them to our client. We assume no underwriting risk as the insurance policy is underwritten by the insurance company.

Fees from Absence Management Solutions ("AMS") services, such as attendance support and disability management are generally based on negotiated fees or a formula tied to the nature of the service being provided. Fees for workers' compensation services are charged based on billable hours or on a fee-for-service basis. Most AMS agreements may be terminated by the client upon 30 to 60 days' notice to us. It is typical, however, for these agreements to continue for multiple years and many automatically renew on an annual basis.

Our largest operating expense is compensation and related costs. This includes salaries, annual performance-based bonuses, benefits, payroll taxes, independent service providers and temporary staffing services.

The remaining operating expenses include rent and occupancy costs, technology costs (including equipment leases, telecommunications, and software licenses and maintenance), non-recoverable client service costs, training, marketing, office costs, professional services and insurance.

## 2018 SUMMARY AND OUTLOOK

| *(In thousands of dollars)* | **Three months ended December 31, 2018** | **Three months ended December 31, 2017 (1)** | **Year ended December 31, 2018** | **Year ended December 31, 2017 (1)** |
|---|---|---|---|---|
| Revenue | $200,761 | $156,787 | 722,284 | 625,089 |
| Adjusted EBITDA | 35,652 | 27,487 | 136,960 | 118,424 |
| Adjusted EBITDA margin | 17.8% | 17.5% | 19.0% | 18.9% |
| Normalized Free Cash Flow | 18,284 | 18,949 | 75,112 | 69,938 |
| Profit | 3,450 | 3,452 | 21,797 | 33,024 |

Footnote:

(1) Certain comparative figures for the three months and year ended December 31, 2017 have been restated as a result of the Company's adoption of IFRS 15. Please refer to note 3 of the Company's consolidated financial statements for the year ended December 31, 2018 for details.

**Fourth quarter:**

We had a solid fourth quarter of 2018 and continued to deliver revenue and adjusted EBITDA growth versus the comparative quarter in 2017. Highlights of the fourth quarter include:

- Revenue growth of 28.0%, or $44.0 million versus the comparative period to $200.8 million, of which 19.0%, or $29.8 million relates to revenue from the LifeWorks acquisition.

- An increase in Adjusted EBITDA of 29.7%, or $8.2 million, to $35.7 million versus the comparative period, with Adjusted EBITDA margin increasing to 17.8%.

- Profit for the quarter was $3.5 million, which is comparable to profit in the same quarter last year; the current quarter included LifeWorks acquisition related expenses, which total approximately $7.8 million ($5.7 million after tax) including amortization charges from acquired intangibles of $6.2 million and integration costs of $1.6 million.

**Highlights of 2018:**

- Revenue grew by 15.5%, or $97.2 million versus last year to $722.3 million as a result of the LifeWorks acquisition, which contributed 8.3% or $51.9 million of revenue growth. The remaining increase came from new business wins and continued growth with existing clients from all four lines of our business.

- Adjusted EBITDA increased by $18.5 million to $137.0 million, or 15.7% versus the prior year with Adjusted EBITDA Margin increasing to 19.0% from 18.9%.

- Profit for the year was $21.8 million compared to a profit of $33.0 million last year due to LifeWorks acquisition related expenses which total approximately $24.9 million ($19.7 million after tax) including amortization charges from acquired intangibles of $12.3 million, transaction expenses to complete the acquisition of $10.0 million and integration costs of $2.6 million.

- LifeWorks Acquisition:

  On July 27, 2018, the Company completed the acquisition of all of the issued and outstanding shares of LifeWorks Corporation Limited (“LifeWorks”) for a purchase price of approximately $434.8 million (US$332.2 million), after the finalization of the working capital adjustments. The purchase price was satisfied by delivering cash in the amount of $402.5 million (US$307.4 million) and issuing approximately 1.2 million common shares of the Company equivalent to $32.3 million (US$24.8 million). LifeWorks is a global employee assistance program (“EAP”) provider, offering employee assistance, wellness, recognition and incentive programs in Canada, the United States, the UK and Australia. This acquisition allows the Company’s Well-being line of business to deliver an expanded set of well-being services in a more integrated way to our clients as well as bolster the Company’s geographic footprint through LifeWorks’ established presence in the U.S., U.K., Australia and Canada. In 2017, LifeWorks generated revenue of $105.2 million. For details on the purchase consideration and net assets acquired please refer to the business acquisition note of the audited consolidated financial statements for the year ended December 31, 2018.

  In order to finance this acquisition, the Company amended and restated the Company’s existing credit facility agreement (see the ‘Capital Resources’ section of the MD&A below for further details), and raised $231.0 million of gross proceeds through the issuance of 8.7 million common shares of the Company through a public share offering.

We expect our continued investments in our business, including the LifeWorks acquisition, and our established and prospective client base will continue to yield positive results for the Company.

## 2018 OPERATING RESULTS SUMMARY

| **Results of Operations** | **Three months ended December 31,** | | **Year ended December 31,** | |
|---|---|---|---|---|
| Selected Consolidated Financial Information | **2018** | **2017 [1]** | **2018** | **2017 [1]** |
| *(In thousands of dollars, except per share amounts)* | | | | |
| **Revenue** | $200,761 | $156,787 | $722,284 | $625,089 |
| Deduct: | | | | |
| Salaries, benefits and contractor expenses | 136,678 | 110,989 | 483,281 | 425,356 |
| Other operating expenses | 36,285 | 28,025 | 123,648 | 100,992 |
| Finance costs | 6,020 | 3,277 | 17,419 | 13,165 |
| Transaction costs | – | – | 9,924 | – |
| Depreciation and amortization | 17,026 | 9,808 | 54,138 | 38,200 |
| Share of loss of joint venture | 24 | – | 220 | – |
| Income tax expenses | 1,278 | 1,236 | 11,857 | 14,352 |
| **Profit** | **3,450** | **3,452** | **21,797** | **33,024** |
| Add: | | | | |
| Finance costs | 6,020 | 3,277 | 17,419 | 13,165 |
| Depreciation and amortization | 17,026 | 9,808 | 54,138 | 38,200 |
| Depreciation, amortization and income tax expense on share of loss of joint ventures | 68 | – | 685 | – |
| Income tax expenses | 1,278 | 1,236 | 11,857 | 14,352 |
| **EBITDA [2]** | **27,842** | **17,773** | **105,896** | **98,741** |
| Adjustments: | | | | |
| Mercer Canada Outsourcing conversions costs | – | 1,319 | – | 7,157 |
| Transformation project costs | 6,245 | – | 18,523 | – |
| Sublease loss provision | – | 1,225 | – | 1,225 |
| Retirement allowance | – | – | – | 4,131 |
| Reorganization and operational effectiveness initiatives | – | 6,241 | – | 6,241 |
| Lease exit costs | – | 929 | – | 929 |
| LifeWorks transaction costs | – | – | 9,924 | – |
| LifeWorks integration | 1,565 | – | 2,617 | – |
| **Adjusted EBITDA** | **35,652** | **27,487** | **136,960** | **118,424** |
| **EBITDA margin [3]** | 13.9% | 11.3% | 14.7% | 15.8% |
| **Adjusted EBITDA margin [3]** | 17.8% | 17.5% | 19.0% | 18.9% |
| **Cash provided by operating activities** | 25,919 | 44,005 | 64,792 | 77,588 |
| Deduct: Capital expenditures [4] | (12,021) | (11,677) | (36,430) | (31,415) |
| **Free Cash Flow [5]** | **13,898** | **32,328** | **28,362** | **46,173** |
| Add (deduct): | | | | |
| Changes in non-cash operating working capital | (6,468) | (22,012) | 11,371 | 12,078 |
| Current income taxes, net of income taxes paid | 3,044 | 338 | 4,315 | (4,550) |
| Adjustments to EBITDA [6] | 7,810 | 8,295 | 31,064 | 16,237 |
| **Normalized Free Cash Flow [7]** | **18,284** | **18,949** | **75,112** | **69,938** |
| Earnings per Share (basic) | 0.05 | 0.06 | 0.36 | 0.60 |
| Earnings per Share (diluted) | 0.05 | 0.06 | 0.36 | 0.59 |
| EBITDA per share (basic) | 0.42 | 0.32 | 1.76 | 1.79 |
| Adjusted EBITDA per Share (basic) | 0.54 | 0.49 | 2.28 | 2.14 |
| Dividends declared | 12,493 | 10,457 | 46,000 | 41,779 |
| Twelve-month rolling Normalized Payout Ratio [8] | 61.2% | 59.7% | 61.2% | 59.7% |
| Twelve-month rolling Normalized Payout Ratio, including changes in adjusted non-cash operating working capital [9] | 71.0% | 73.6% | 71.0% | 73.6% |

Footnotes:

(1) Certain comparative figures for the three and twelve months ended December 31, 2017 have been restated as a result of the Company's adoption of IFRS 15. Please refer to note 3 of the Company's audited consolidated financial statements for the year-ended December 31, 2018 for details.

(2) "EBITDA" is defined as profit before finance costs, income tax expenses, depreciation and amortization.

(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) For the comparative twelve month period ended December 31, 2017, adjustments to EBITDA do not include the non-cash component of the retirement allowance of $2,027. This 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. For the twelve-month period ended December 31, 2017, the non-cash operating working capital was adjusted for by $1,181 which represents the working capital impact of the retirement allowance.

## ANALYSIS OF FOURTH QUARTER 2018 OPERATING RESULTS

### *Revenue*

Revenue for the three months ended December 31, 2018 increased by $44.0 million, or 28.0%, to $200.8 million compared to $156.8 million for the same period in 2017. LifeWorks generated revenue of $29.8 million for the period, representing 19.0% of the revenue growth, while other acquisitions closed in the fourth quarter of 2017 generated revenue of $2.0 million for the period, representing 1.2% of the revenue growth. The remaining increase of $12.2 million, or 7.8%, from the same period in 2017 is coming from new business wins and continued growth from existing clients in all four of our lines of business, with Administrative Solutions contributing 6.5% and Well-being 0.9% of the revenue growth.

### *Salaries, Benefits and Contractor Expenses*

Salaries, benefits and contractor expenses for the three months ended December 31, 2018 increased by $25.7 million, or 23.1%, to $136.7 million compared to $111.0 million for the same period in 2017. Excluding the net increase in compensation expense of $24.4 million resulting from acquisitions not in the comparative period, compensation expense increased by $1.3 million. The increase is mainly attributable to general increases to support the Company's continued growth of $5.0 million, compensation costs for the transformation project of $3.0 million, and $0.8 million of LifeWorks integration cost, partially offset by reorganization and operational effectiveness initiative costs of $6.2 million and Mercer Canada Outsourcing conversion of $1.3 million in the comparative period.

### *Other Operating Expenses*

Other operating expenses for the three months ended December 31, 2018 increased by $8.3 million, or 29.5%, to $36.3 million compared to $28.0 million for the same period in 2017. Excluding the net increase in other operating expenses of $5.9 million resulting from acquisitions not in the comparative period, other operating expenses grew by $2.4 million. The increase is attributable to transformation project costs of $3.2 million, general increase to support the Company's continued growth of $0.5 million and $0.8 million of LifeWorks integration cost, partially offset by sublease loss provision of $1.2 million and lease exit costs of $0.9 million all in the comparative period.

***Finance Costs***

Finance costs for the three months ended December 31, 2018 increased by $2.7 million, or 83.7%, to $6.0 million compared to $3.3 million for the same period in 2017, due to increased borrowings under the Company's credit facility agreement to finance the LifeWorks acquisition.

***Depreciation and Amortization***

Depreciation and amortization for the three months ended December 31, 2018 increased by $7.2 million, or 73.6%, to $17.0 million compared to $9.8 million for the same period in 2017. The increase is due to higher amortization of $6.7 million related to acquired intangibles from LifeWorks and other acquisitions, and higher amortization of internally developed software of $0.5 million.

***Income Tax Expense***

Income tax expenses for the three months ended December 31, 2018 was $1.3 million compared to income tax expense of $1.2 million for the same period in 2017 due to slightly higher profit from operations before tax.

***Profit for the period***

As a result of the changes noted above, the profit for the three months ended December 31, 2018 was $3.5 million, which is comparable to the same period in 2017.

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

***Adjusted EBITDA and EBITDA***

Adjusted EBITDA increased by $8.2 million, or 29.7%, to $35.7 million compared to $27.5 million for the same period in 2017. The increase is primarily due to growth in revenue of $44.0 million, partially offset by an increase in salaries and other operating expenses of $35.8 million after EBITDA adjustments. These adjusted EBITDA items are described in the analysis of the year ended December 31, 2018 operating results section below.

EBITDA increased by $10.0 million to $27.8 million compared to $17.8 million for the same period in 2017.

***Free Cash Flow***

Free Cash Flow for the three months ended December 31, 2018 decreased by $18.4 million to $13.9 million compared to $32.3 million for the same period in 2017. The decrease is mainly due to lower cash generated from operating activities of $12.8 million compared to the same period in 2017, higher finance costs paid of $3.8 million, higher income taxes paid of $1.5 million, and higher capital expenditures of $0.3 million.

***Normalized Free Cash Flow***

Normalized Free Cash Flow for the three months ended December 31, 2018 decreased by $0.6 million to $18.3 million compared to $18.9 million for the same period in 2017. The decrease is mainly due to higher finance costs paid of $3.8 million and capital expenditures of $0.3 million partially offset by higher cash generated from operating activities before changes in non-cash operating working capital and EBITDA adjustments of $2.3 million and lower current income tax expense of $1.2 million.

## ANALYSIS OF YEAR ENDED DECEMBER 31, 2018 OPERATING RESULTS

***Revenue***

Revenue for the year ended December 31, 2018 increased by $97.2 million, or 15.5%, to $722.3 million compared to $625.1 million for 2017. LifeWorks generated revenue of $51.9 million for the year, representing 8.3% of the revenue growth, while other acquisitions closed in the fourth quarter of 2017 generated revenue of $12.2 million for the year, representing 1.9% of the revenue growth. The remaining increase of $33.1 million, or 5.3%, compared to 2017 is due to new business wins and continued growth from existing clients in all four of our lines of business, with Administrative Solutions contributing 3.1% and the other three lines of business providing the remaining growth evenly.

***Salaries, Benefits and Contractor Expenses***

Salaries, benefits and contractor expenses for the year ended December 31, 2018 increased by $57.9 million, or 13.6%, to $ 483.3 million compared to $425.4 million for the same period in 2017. Excluding the net increase in compensation expense of $47.8 million resulting from acquisitions not in the comparative period, compensation expense increased by $10.2 million. The increase is mainly attributable to general increases to support the Company's continued growth of $17.1 million, compensation costs for the transformation project of $9.0 million, and $1.6 million of LifeWorks integration cost, partially offset by Mercer Canada Outsourcing conversion of $7.2 million, retirement allowance of $4.1 million, and reorganization and operational effectiveness initiative costs of $6.2 million in the comparative period.

***Other Operating Expenses***

Other operating expenses for the year ended December 31, 2018 increased by $22.6 million, or 22.4%, to $123.6 million compared to $101.0 million for the same period in 2017. Excluding the net increase in other operating expenses of $10.8 million resulting from acquisitions not in the comparative period, other operating expenses grew by $11.8 million. The increase is attributable to transformation project costs of $9.4 million, general increase to support the Company's continued growth of $3.5 million, and $1.0 million of LifeWorks integration cost, partially offset by sublease loss provision of $1.2 million and lease exit costs of $0.9 million all in the comparative period.

***Finance Costs***

Finance costs for the year ended December 31, 2018 increased by $4.2 million, or 32.3% to $17.4 million compared to $13.2 million for the same period in 2017. The increase in finance costs is due to increased borrowings under the Company's credit facility agreement to finance the LifeWorks acquisition.

***Depreciation and Amortization***

Depreciation and amortization for the year ended December 31, 2018 increased by $15.9 million, or 41.7%, to $54.1 million compared to $38.2 million for the same period in 2017. The increase is due to higher amortization of $13.6 million related to acquired intangibles from LifeWorks and other acquisitions, higher amortization of internally developed software of $2.0 million and higher amortization of purchased software of $0.3 million.

***Income Tax Expenses***

Income tax expenses for the year ended December 31, 2018 decreased by $2.5 million, or 17.4%, to $11.9 million compared to $14.4 million for the same period in 2017 due to lower profit from operations before tax for the year.

*Profit for the year*

As a result of the changes noted above, the profit for the year ended December 31, 2018 was $21.8 million compared to $33.0 million for the same period in 2017.

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

***Adjusted EBITDA and EBITDA***

Adjusted EBITDA increased by $18.5 million, or 15.7%, to $137.0 million compared to $118.4 million for the same period in 2017. The increase is primarily due to growth in revenue of $97.4 million, partially offset by an increase in salaries and other operating expenses of $78.9 million after EBITDA adjustments. These adjusted EBITDA items are described below for the years ended December 31, 2018 and December 31, 2017.

*2018*

- Transformation project costs: To support the Company's growth strategy, we engaged a third party firm in 2018 to drive long-term value in the form of earnings and cash flow improvement through changes in the way the Company operates. This project is expected to generate improvements over the next 2 years. The fee payable to the third party firm is contingent on the Company achieving the key activities need to realize the value of the initiatives.

- LifeWorks transaction costs represent advisory, legal, as well as other professional and regulators fees incurred with respect to the LifeWorks acquisition, which was completed in July 2018.

- LifeWorks integration represents costs to integrate the LifeWorks business with our existing Well-being business to achieve the target synergies. Costs incurred up to December 31, 2018 of $2.6 million include severances and sublease losses. The integration activities will continue until the end of 2019. The integration of LifeWorks' operations with our existing Well-being practice is going well, remains on schedule and continues to realize the expected synergies.

*2017*

- Mercer Canada Outsourcing conversion costs represent systems and service improvements required to support the clients acquired in November, 2012. The process commenced immediately after the acquisition and as a result of the savings realized from the original conversion, we decided in 2016 to convert the remaining clients acquired which were not included in the original conversion. The Mercer Canada Outsourcing conversion is now complete.

- Retirement allowance costs represent retirement remuneration to the former President and Chief Executive Officer of the Company after his decision to retire after twelve years with the Company, including the past eight as President and CEO.

- Reorganization and operational effectiveness initiatives represents severance costs related to corporate reorganizations, the completion of the Mercer Canada Outsourcing conversion, and employee terminations to achieve post-acquisition planned synergies.

- The sublease loss provision arose as a result of our decision to sublet excess office space now available in one of our U.S. offices as a result of the completion of significant conversion and implementation projects.

- Lease exit costs represents costs for termination penalties paid and write-off of leasehold improvements, net of extinguishment of related liabilities for leasehold inducements and straight-line rent, for early vacating a floor in one of our Montreal offices that was no longer required.

EBITDA increased by $7.2 million to $105.9 million compared to $98.7 million for the same period in 2017.

***Free Cash Flow***

Free Cash Flow for the year ended December 31, 2018 decreased by $17.8 million to $28.4 million compared to $46.2 million for the same period in 2017. The decrease is mainly due to higher income taxes paid of $6.8 million, higher finance costs paid of $6.3 million, and higher capital expenditures of $5.0 million, partially offset by higher cash generated from operating activities of $0.3 million compared to 2017.

***Normalized Free Cash Flow***

Normalized Free Cash Flow for the year ended December 31, 2018 increased by $5.2 million to $75.1 million compared to $69.9 million for the same period in 2017. The increase is mainly due to higher cash generated from operating activities before changes in non-cash operating working capital and EBITDA adjustments of $14.4 million and lower current income tax expense of $2.1 million, partially offset by higher finance costs paid of $6.3 million and capital expenditures of $5.0 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:

| *(In thousands of dollars)*<br>*Cash provided by (used in):* | **Year ended December 31, 2018** | **Year ended December 31, 2017** |
|---|---|---|
| Operating activities | $ 64,792 | $ 77,588 |
| Financing activities | 369,814 | (28,716) |
| Investing activities | (438,331) | (51,232) |
| Decrease in cash | $ (3,725) | $ (2,360) |

Cash provided by operating activities for the year ended December 31, 2018 decreased by $12.8 million to $64.8 million compared to $77.6 million for the same period in 2017. The decrease is due to income taxes paid of $6.8 million and higher finance costs paid of $6.3 million partially offset by higher cash generated from operating activities of $0.3 million.

Cash provided by financing activities for the year ended December 31, 2018 increased by $398.5 million to $369.8 million compared to cash used in financing activity of $28.7 million for the same period in 2017. The increase is due to proceeds from the issuance of shares, net of underwriting fees, of $220.8 million to finance the LifeWorks acquisition and incremental borrowings under the credit facility, net of debt modification costs, of $181.2 million, partially offset by higher dividends payment of $3.5 million.

Cash used in investing activities for the year ended December 31, 2018 increased by $387.1 million to $438.3 million compared to $51.2 million for the same period in 2017. This increase was primarily due to the cash payment for the acquisition of LifeWorks of $402.5 million and higher capital expenditures of $5.0 million, offset slightly by a decrease in cash used for other business acquisitions of $20.4 million.

***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 fourth quarter of 2018. The Company continued to declare the same monthly dividend amount in January and February 2019.

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 December 31, 2018 was 61.2% compared to 59.7% for the same period in 2017. The increase in the Normalized Payout Ratio is due to higher dividends paid due to shares issued as part of the LifeWorks acquisition and on redemption of LTIP. The twelve-month rolling Normalized Payout Ratio, including changes in adjusted non-cash operating working capital at December 31, 2018 was 71.0% compared to 73.6% for the same period in 2017. The decrease in the ratio was mainly due to higher cash generated from operating activities before changes in non-cash operating working capital and EBITDA adjustments.

***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 December 31, 2018 increased by $0.3 million to $12.0 million compared to $11.7 million for the same period in 2017 and for the year ended December 31, 2018 increased by $5.0 million to $36.4 million from $31.4 million in the comparative period. The increase in capital expenditures for both periods is mainly due to higher internally developed software expenditures to support ongoing business growth and needs as well as investing in new technologies that will benefit the business in the long term.

***Contractual Obligations***

**Commitments**

We lease office space and selected equipment under operating lease agreements with terms ranging from one to fifteen years. We also have revolving loans under the credit facility arrangement 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 netted against the operating leases amounts reported below. We consider the risk of default by the subtenants to be low and therefore no accrual has been set up. A summary of contractual obligations, which outlines the year the payments are due is as follows:

| *(In thousands of dollars)* | **Total** | **2019** | **2020** | **2021** | **2022** | **2023** | **2024 and thereafter** |
|---|---|---|---|---|---|---|---|
| Long-term debt | $ 377,923 | $ – | $ – | $ – | $ – | $ 377,923 | $ – |
| Convertible debenture | 86,000 | – | – | 86,000 | – | – | – |
| Operating leases, net | 116,810 | 17,028 | 15,671 | 15,019 | 13,687 | 11,547 | 43,858 |
| Total | **$ 580,733** | **$ 17,028** | **$ 15,671** | **$ 101,019** | **$ 13,687** | **$ 389,470** | **$ 43,858** |

**Contingent Consideration**

The remaining purchase price for past acquisitions is contingent on future business results and the estimated remaining contingent consideration payable for these acquisitions is $1.8 million due from 2019 thru 2022. These contingent future installments have been recognized as an acquisition liability on the statement of financial position at their estimated discounted amounts as at December 31, 2018.

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:

| *(In thousands of dollars)* | **As at December 31, 2018** | **As at December 31, 2017** |
|---|---|---|
| Bank indebtedness (net of cash) | $ 9,141 | $ 5,416 |
| Long-term debt, net of debt issuance costs | 374,381 | 179,669 |
| Convertible debentures, net of issuance costs and equity component of debenture | 83,117 | 82,080 |
| Shareholders' equity | 606,404 | 356,271 |

*Long-term debt*

The long-term debt, net of debt issuance costs, increased by $194.7 million from $179.7 million as at December 31, 2017 to $374.4 million as at December 31, 2018. This increase is the result of an increase in borrowings under the Company's credit facility agreement to finance the acquisition of LifeWorks and business growth.

On July 27, 2018, the Company amended and restated the Company's existing Credit Facility Agreement (the "Amended and Restated Credit Facility Agreement"). Under the Amended and Restated Credit Facility Agreement, the Company's revolving facility increases from $300,000 to $500,000 (including a swing line of $14.0 million), and the agreement has a maturity date five years from closing. At December 31, 2018, the Company had utilized approximately $386 million (December 31, 2017 - $188 million) under the Amended and Restated Credit Facility Agreement.

The interest rates for the Amended and Restated Credit Facility Agreement are floating, based on a margin over certain referenced rates of interest. The applicable margin may vary up or down depending on the ratio of the Company's consolidated debt to Adjusted EBITDA, as defined in the agreement. The Amended and Restated Credit Facility Agreement is secured by a general assignment of all the assets of the Company and requires the Company to maintain, on a consolidated basis, a debt to Adjusted EBITDA financial covenant of not more than 3.5:1.0 (or not more than 4.0:1.0 for the 12-month period immediately following the completion of a permitted acquisition, as defined in the agreement, with a purchase price of $50,000 or more), and an EBITDA to interest expense ratio of not less than 2.0:1.0.

We are in compliance with all of the required financial covenants as at December 31, 2018.

The Company entered into interest rate swap agreements to hedge against the variable interest rate component borrowed under the Credit Facility Agreement. The interest rate swaps have been designated as cash flow hedges and their terms are as follows:

- $50.0 million for the period from November 29, 2017 up to and ending December 20, 2020 at an interest rate of 1.79%, before the applicable margin, for the duration of this period

- $130.0 million for the period from September 4, 2018 up to and ending July 27, 2023 at an interest rate of 2.59%, before the applicable margin, for the duration of this period

*Convertible debentures*

In June 2016, the Company issued $86.0 million principal amount of 4.75% Convertible Unsecured Subordinated Debentures (the "4.75% Convertible Debentures") for net proceeds of $82.0 million. The 4.75% Convertible Debentures pay interest semi-annually on June 30 and December 31, commencing with the initial interest payment on December 31, 2016 and have a maturity date of June 30, 2021.

These debentures are convertible at the option of the holder to common shares at a conversion price of $25.10 per common share. The Company has the option to redeem the 4.75% Convertible Debentures on and after June 30, 2019 and at any time prior to June 30, 2020 at a redemption price equal to 100% of their principal plus accrued and unpaid interest provided that the weighted average trading price for the 20 consecutive trading days ending five days preceding the date on which the notice of redemption is given is at least 125% of the conversion price of $25.10. On and after June 30, 2020, but prior to the maturity date, the 4.75% Convertible Debentures are redeemable at a redemption price equal to 100% of their principal amount plus accrued and unpaid interest. On redemption or maturity, the Company may elect to repay the principal and satisfy its interest obligations by issuing common shares.

## SELECTED STATEMENT OF FINANCIAL POSITION DATA

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

| *(in thousands of dollars)* | **As at December 31, 2018** | **As at December 31, 2017** |
|---|---|---|
| Current assets | $ 212,539 | $ 186,070 |
| Non-current assets | 1,135,803 | 635,618 |
| Current liabilities | 142,886 | 118,325 |
| Non-current liabilities | 599,052 | 347,092 |

### Current Assets

Current assets as at December 31, 2018 increased by $26.4 million to $212.5 million from $186.1 million as at December 31, 2017. The increase is primarily attributable to the LifeWorks acquisition, which represented $24.3 million of current assets not included in the comparative period. The remaining increase of $2.1 million relates to an increase in trade and other receivables of $9.9 million due to growth in the business and the revenue billing cycle in accordance with contract terms, an increase in the deferred implementation costs of $2.4 million, an increase in income tax receivable of $0.1 million, and an increase in cash of $0.4 million, partially offset by lower unbilled fees of $5.2 million, a decrease in investment held in trust of $4.9 million, and a decrease in prepaid expenses and other by $0.6 million.

### Non-current Assets

Non-current assets as at December 31, 2018 increased by $500.2 million to $1,135.8 million from $635.6 million as at December 31, 2017. The increase is primarily due to higher intangible assets of $225.4 million due to LifeWorks acquisition in excess of amortization for the period, an increase in goodwill of $270.2 million due to LifeWorks acquisition, an increase in deferred implementations costs of $4.2 million, an

increase in capital assets of $2.5 million due to capital asset additions in excess of depreciation. This was partially offset by a decrease in deferred tax asset of $1.5 million, investments in joint venture of $0.5 million, and unbilled fees of $0.1 million.

**Current Liabilities**

Current liabilities as at December 31, 2018 increased by $24.6 million to $142.9 million from $118.3 million as at December 31, 2017. The increase is primarily attributable to the LifeWorks acquisition, which represented $26.7 million of current liabilities not included in the comparative period. The offsetting decrease of $2.1 million is primarily due to a decrease in income taxes payable of $5.5 million, a decrease in insurance premium liabilities of $4.9 million, and a decrease in the current portion of future consideration related to acquisitions of $1.9 million (primarily as a result of acquisition settlement payments). This was partially offset by higher trade and other payables of $1.7 million due to timing of compensation related accruals and annual incentive payments, an increase in deferred revenue of $0.7 million due to timing of consideration received from customers, an increase in bank indebtedness of $6.6 million, an increase in dividends payable of $0.7 million due to increase in number of shares outstanding, and an increase in interest rate swaps of $0.5 million.

**Non-current Liabilities**

Non-current liabilities as at December 31, 2018 increased by $252.0 million to $599.1 million from $347.1 million as at December 31, 2017. The increase is mainly due to an increase in the long-term debt of $194.7 million due to higher amounts borrowed under the Credit Facility Agreement, an increase of $1.0 million in the Convertible Debentures due to non-cash accretion and amortization of issuance costs, an increase in the deferred tax liability of $54.7 million primarily attributable to LifeWorks, an increase in other liabilities of $1.4 million partially due to leasehold inducements received, an increase of future consideration related to acquisitions of $0.1 million, and interest rate swaps of $1.6 million not in comparative period, which was partially offset by a decrease of deferred revenue non-current portion of $0.8 million, and decrease of $0.7 million in other provisions.

As a result of the changes in current assets and current liabilities discussed above, working capital increased by $1.9 million from $67.7 million as at December 31, 2017 to $69.6 million as at December 31, 2018.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements requires us to make estimates and assumptions that affect the reported values of assets and liabilities as well as disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period.

These estimates are reviewed periodically and, as adjustments become necessary, they are reported in profit or loss in the periods in which they become known. Accordingly, actual results could differ from these estimates. The Company's significant accounting policies are presented in Note 3 of the audited consolidated financial statements and notes thereto for the years ended December 31, 2018 and 2017. The accounting policies and estimates that are critical to our business relate to the following items:

***Revenue recognition and unbilled fees***

Revenues include fees generated from Well-being, Administrative Solutions, Consulting Services, and AMS contracts.

A contract-based five-step analysis of transactions is applied to determine whether, how much, and when to recognize revenue.

Well-being offers counselling and educational services, and targeted health and wellness programs, to support employee and family work, financial, personal and family needs. Most Well-being agreements may be terminated by the client upon 30 to 60 days' notice to us. It is typical, however, for Well-being agreements to continue for multiple years and many automatically renew on an annual basis. Well-being revenue is recognized through a combination of the minimum contracted amount and incremental usage above the minimum thresholds. The minimum contracted amount is recognized on a basis consistent with the provision of Well-being services. Incremental usage is accrued when the minimum usage threshold is exceeded and subsequently billed.

Administrative solutions manages all aspects of the administration of clients' pension and benefit plans on an outsourced basis, as well as providing administration support through software as a service ("SaaS") and application service provider ("ASP"). Administrative Solutions engagements typically involve both an implementation and an ongoing services component. Where a single contract requires the delivery of multiple components, revenue recognition criteria are applied to determine whether each component is distinct and a separate performance obligation. A component is distinct and a separate performance obligation if the component is separately identifiable from the other promised goods and services in the bundled package, and if the customer can benefit from it on its own or with other readily available resources. For a single contract with multiple performance obligations, the consideration is allocated to the separate performance obligations based on their observable price when the Company customarily provide such goods or services on a stand-alone basis. Where the Company does not provide such goods or services on a stand-alone basis, the adjusted market assessment approach or expected cost plus margin approach is then used to allocate the consideration. Revenue is recognized as follows:

- Implementation

  The provision of implementation services in a contract that involves both an implementation component and an ongoing services component, where the implementation component is considered distinct and a separate performance obligation, is recognized as revenue based on the percentage of implementation work completed. The percentage of implementation work completed is estimated based on hours incurred to date relative to the total estimated hours to complete the implementation work. Where the implementation services in a contract are not considered distinct, revenue and related costs are deferred and recognized on a basis consistent with the ongoing services component of the contract (see below).

- Ongoing services

  Ongoing services can include record-keeping and managing employee information, processing transactions that are required to administer employee pension and benefit plans, hosting client benefits websites, and responding to employee inquiries through call centres. Depending on the nature of the arrangement with the client, the Company can manage all aspects of the administration of clients' pension and benefit plans on an outsourced basis, or provide administration support through SaaS and ASP. Revenue from ongoing services are accrued as revenue as these services are provided and subsequently billed.

Administrative Solutions clients typically sign three-to-five year contracts. There may be an upfront fee charged for implementation services, with ongoing services generally billed on a monthly basis. In estimating the transaction price in a contract, the Company adjusts the transaction price for the time value of money if the contract contains a significant financing component. In making this assessment, the Company considers amongst other factors the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services, the combined effect of the length of time between when the Company transfers the goods or services to the client and when it receives payment for these goods or services, and the prevailing market interest rates. For contracts that contain a significant financing component,

the financing component is recognized as interest expense when the customer pays in advance or as interest income when the customer pays in arrears.

Consulting services entails assisting organizations with the design, determination of funding requirements, management, and financial control of pension and benefit plans. Fees for actuarial and consulting services are billed either on a time-and-material basis or on a fixed-fee basis. Revenue is accrued as services are rendered and expenditures are incurred and subsequently billed.

AMS provides administration and support services to organizations in the area of attendance, disability, and workers' compensation. AMS revenue is recognized on a fixed-fee or time-and-material basis. Most AMS agreements may be terminated by the client upon 30 to 60 days' notice to us. It is typical, however, for these agreements to continue for multiple years and many automatically renew on an annual basis. On fixed-fee basis arrangements, where the provision of service is characterized by an indeterminate number of acts, revenue is recognized on a straight-line basis over the term of the contract. On time-and-material basis arrangements, revenue is accrued as services are rendered and expenditures are incurred and subsequently billed.

Unbilled fees represent contract assets for fees earned for services rendered but not yet invoiced as at the reporting date; upon billing, this balance will be transferred to trade receivables. Unbilled fees are generally billed in the following month and have been classified as current, as they are billed within the following year. Unbilled fees on time and material basis arrangements are recorded at the lower of unbilled hours worked at normal billing rates and at the amount which is estimated to be recoverable upon invoicing. The Company maintains an allowance for amounts expected to be unrecoverable.

Other sources of operating revenue include the following:

(i) Investment income earned in the course of normal business operations, and is recorded on the accrual basis.

(ii) Commissions income is recognized when earned, which is at the later of the billing or the effective date of the policy, net of a provision for return commissions due to policy cancellations or change of brokers.

***Intangible assets***

Intangible assets consist of customer relationships, customer contracts, proprietary software, and trade names acquired through acquisitions or business combinations, internally-developed software and purchased software.

Internally-developed software is recognized at the cost of all eligible development costs, when all the following criteria are met:

- It is technically feasible to complete the software so that it will be available for use;
- Management intends to complete the software and use or sell it;
- Morneau Shepell is able to use or sell the software;
- Future benefits associated with the software can be demonstrated;
- Adequate technical, financial, and other resources to complete the development and to use or sell the software are available; and
- The expenditures attributable to the software during its development can be reliably measured.

Eligible expenditures capitalized as part of internally-developed software include external direct costs of materials and services consumed in development, and payroll and payroll-related costs for employees who are directly associated with and who devote time to the development of the software. All costs incurred in

the preliminary research stage of the projects are expensed as incurred.

Intangible assets acquired through acquisitions or business combinations involve significant estimates and assumptions regarding cash flow projections, growth projections, economic risk, and cost of capital.

Intangible assets with a finite life are amortized on a straight-line basis over their estimated useful lives. Intangible assets with an indefinite life are not amortized, but are tested for impairment annually or whenever impairment indicators are identified. Trade names have been determined to have an indefinite life based on their strength, history, and expected future use.

Amortization expense has been presented in profit or loss as depreciation and amortization. Assets are removed from asset and accumulated amortization balances once they become fully amortized. Proceeds from disposals are netted against the related assets and accumulated amortization, and resulting gains and losses are included in profit or loss.

Amortization on internally-developed software does not commence until the asset is ready for use as management intended.

***Goodwill***

Goodwill represents the excess of the cost of the Company's business acquisitions over the fair value of our share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill is carried at cost less accumulated impairment charges and is not amortized but is subject to an impairment test annually or whenever impairment indicators are identified.

***Deferred implementation costs***

Implementation costs incurred in connection with Administrative Solutions contracts, depending on the nature of the arrangement with the client, either relate to those costs necessary to set up clients and their human resource or benefit programs onto the Company's systems and operating processes, or for costs necessary to set up clients so they can administer their human resource or benefit programs using the Company's proprietary pension and benefits software solutions. Such costs may include internal and external costs for coding and customizing systems, client data conversion costs, and contract negotiation costs. For Administrative Solutions contracts where the implementation component is not distinct and a separate performance obligation, specific, incremental, and direct costs, are deferred and amortized over the term of the service contract plus any expected renewal period.

The Company is required to assess the recoverability of unamortized deferred implementation costs. This assessment requires judgment by management to determine whether costs will be less than fully recoverable based on the future cash flow for each respective client. If a client terminates a contract prior to its end, a loss on the contract may be recorded (if necessary), and any remaining deferred implementation revenues and costs would be recognized into income over the remaining implementation period through to the date of termination.

***Corporate income taxes***

Deferred income tax assets are recognized for all unused tax losses and deductible temporary differences to the extent that it is probable that taxable profit will be available against which the losses and deductible temporary differences can be utilized. Management exercises judgment in determining the provision for income taxes and deferred income tax assets and liabilities. The provision is based on management's expectations regarding the income tax consequences of transactions and events during the period. Management interprets the tax legislation for each jurisdiction in which the Company operates and makes assumptions about the expected timing of the reversal of deferred income tax assets and liabilities. If

management's interpretations of the legislation differ from those of the tax authorities or if the actual timing of the reversals of the deferred income tax assets and liabilities is not as anticipated, the provision for income taxes could increase or decrease in future periods.

***Future consideration related to acquisitions***

The Company may pay future consideration related to acquisitions based upon performance measures contractually agreed at the time of purchase. Management estimates the future consideration payable based on underlying contract terms, and best estimates of the future performance of the acquiree. Depending on the future performance of the acquiree, management estimates of the amounts payable for future consideration related to acquisitions may materially differ from the consideration ultimately paid.

***Impairment of non-financial assets***

The Company's identifiable tangible and intangible assets with finite useful lives are reviewed for indications of impairment at each statement of financial position date and when events or changes in circumstances indicate that they may be impaired. Impairments are recorded when the recoverable amount of assets are less than their carrying amounts. The recoverable amount is the higher of an asset's fair value less cost to sell or its value in use.

Similarly, intangible assets with indefinite useful lives and goodwill are tested for impairment annually or whenever impairment indicators are identified, by estimating their recoverable amounts and comparing it to their carrying amounts. Where individual assets cannot be tested individually, they are grouped together into cash-generating units ("CGUs"), the smallest group of assets that are capable of generating cash inflows from continuing use largely independent of other groups of assets, and tested on this basis. Goodwill acquired through business combinations is allocated to each CGU or groups of CGU's but not larger than an operating segment that is expected to benefit from the synergies of the combination.

An impairment loss is recognized if the carrying amount of the CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss, and those impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the unit, and then to reduce the carrying amount of the other assets in the unit on a pro rata basis.

Impairment losses in respect of goodwill are not reversed. In respect of other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount, and only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization had no impairment charge been recorded.

Goodwill and intangible assets impairment review involves significant estimates and assumptions regarding cash flow projections, growth projections, economic risk, and cost of capital. If future events or results differ adversely from these estimates and assumptions, the Company could incur impairment charges in future periods.

***Trade receivables (expected credit losses)***

We are required to assess whether accounts receivable are collectible from customers. Accordingly, management establishes an allowance for expected credit losses ("ECLs") for non-payment and delinquent accounts based on historic trends of the probability of default timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be great or less than suggested by historical trends. If future collections differ from estimates, future profits could be adversely affected.

***Litigation and claims***

We are involved in litigation and other claims arising in the normal course of business. We must use judgment to determine whether or not a claim has any merit, the amount of the claim and whether to record a provision, which is dependent upon the potential success of the claim. Management believes that adequate provisions have been made where required and the ultimate resolution with respect to any claim will not have a material adverse effect on the financial position or results of operations of the Company.

**Related party transactions**

The Company's related parties include key management personnel, unconsolidated structured entities, and joint ventures. Details of these related parties, as well as the Company's related party transactions can be found in note 24 'Related Parties' of the Company's consolidated financial statements for the year ended December 31, 2018.

**Changes in Accounting Policies**

*IFRS 15, Revenue from Contracts with Customers ("IFRS 15")*

On January 1, 2018 the Company adopted IFRS 15 and as a result, changed its accounting policy for revenue recognition. The Company applied IFRS 15 retrospectively, with restatement of comparative periods, using the practical expedient in paragraph C5(c) of IFRS 15, under which the Company does not disclose the amount of consideration allocated to remaining performance obligations or an explanation of when the Company expects to recognize that amount as revenue for all reporting periods presented before the initial date of application of January 1, 2018.

The implementation component and ongoing services components in Administrative Solutions ASP and SaaS contracts that provide the customer with a right to access license to our proprietary pension and benefits software for the term of the contract are now considered a single performance obligation. Previously, the Company considered the implementation component to be a separate unit of accounting, resulting in the recognition of revenue upon commencement of the implementation component.

Furthermore, for implementation costs incurred in connection with Administrative Solutions contracts where the implementation component was not considered a separate performance obligation, these costs were previously deferred and amortized over the initial term of the service contract. Under IFRS 15, the Company considers the renewal period in the contract in addition to the initial term of the service contract, in determining the amortization period of these deferred costs, when contract renewal is highly probable.

Refer to note 3 of the Company's consolidated financial statements for the year ended December 31, 2018 for a description of the changes and the quantitative impact of the adoption of IFRS 15.

*IFRS 9, Financial Instruments ("IFRS 9")*

The Company adopted IFRS 9 on January 1, 2018, which replaces IAS 39, Financial Instruments: Recognition and Measurement ("IAS 39"). As a result of the adoption of IFRS 9, there was no impact on retained earnings as at the date of adoption of January 1, 2018. The adoption of IFRS 9 did not have a significant impact on the Company's classification and measurement of financial assets and financial liabilities, the Company's measurement of impairment losses on its financial assets carried at amortized cost and contract assets or the Company's hedge accounting. Refer to note 3 of the Company's consolidated financial statements for the year ended December 31, 2018 for further details on the adoption of IFRS 9.

## Future Accounting Changes

*IFRS 16, Leases ("IFRS 16")*

The Company is required to adopt IFRS 16 from January 1, 2019. IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

As a lessee, the Company will recognize new assets and liabilities for its operating leases of office premises and equipment. The nature of expenses related to those leases will now change because the Company will recognize a depreciation charge for right-of-use assets and interest expense on lease liabilities. Previously, the Company recognized operating lease expense on a straight-line basis over the term of the lease, and recognized assets and liabilities only to the extent that there was a timing difference between actual lease payments and the expense recognized. The Company does not expect the adoption of IFRS 16 to impact its ability to comply with the financial covenants under the Amended and Restated Credit Facility Agreement, as the covenants will be calculated throughout the term in accordance with existing lease guidance applicable at the date the credit agreement was amended.

The Company expects that it will reclassify its sub-leases in which the Company is a lessor as finance leases, resulting in recognition of a finance lease receivable as at January 1, 2019.

The Company plans to apply IFRS 16 initially on January 1, 2019, using the modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognized as an adjustment to the opening balance of retained earnings at January 1, 2019, with no restatement of comparative information. The Company has assessed the estimated impact that initial application of IFRS 16 will have on its consolidated financial statements, as described in note 3 of the Company's consolidated financial statements for the year ended December 31, 2018.

*Other standards*

*IFRIC Interpretation 23, Uncertainty over Income Tax Treatments ("The Interpretation")*

The Interpretation provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. The Interpretation is applicable for annual periods beginning on or after January 1, 2019 with early adoption permitted. The Interpretation requires the Company to: a) contemplate whether uncertain tax treatments should be considered separately, or together as a group, based on which approach provides better predictions of the resolution; and b) determine if it is probable that the tax authorities will accept the uncertain tax treatment or if it is not probable that the uncertain tax treatment will be accepted, measure the tax uncertainty based on the most likely amount or expected value, depending on whichever method better predicts the resolution of the uncertainty.

The Company will adopt the Interpretation in its consolidated financial statements for the annual period beginning on January 1, 2019. Management does not expect the adoption of IFRIC 23 to have a material impact on the Company's Financial Statements.

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.

**Ability to Maintain Profitability and Manage Growth**

There can be no assurance that Morneau Shepell will be able to sustain profitability in future periods. Morneau Shepell's future operating results will depend on a number of factors, including its ability to continue to successfully execute its strategic initiatives.

There can be no assurance that Morneau Shepell will be successful in achieving its strategic plan or that its strategic plan will enable the firm to maintain its historical revenue growth rates or to sustain profitability. Failure to successfully execute any material part of Morneau Shepell's strategic plan could have a material adverse effect on its business, financial condition and operating results.

There can be no assurance that Morneau Shepell will be able to effectively manage its growth, and any failure to do so could have a material adverse effect on the firm's business, financial condition and operating results.

**Competition**

Morneau Shepell operates in a highly competitive international market. As a result, Morneau Shepell competes with many domestic and international firms. Some of its competitors have achieved substantially more market penetration in certain of the areas in which Morneau Shepell competes. In addition, some of Morneau Shepell's competitors have substantially more financial resources and/or financial flexibility than Morneau Shepell. Furthermore, Morneau Shepell's business relies, in part, upon its ability to develop and implement technology solutions, in a cost effective manner that anticipates and keeps pace with rapid and continuing changes in technology, industry standards and client preferences.

Morneau Shepell's competitors may offer new technologies more efficiently or cost effectively than Morneau Shepell. Competitive forces could result in reduced market share and thus have a material adverse effect on Morneau Shepell's business, financial condition and operating results.

**Reliance on Information Systems and Technology and Confidentiality of Client Information**

Information systems are an integral part of Morneau Shepell's business and the products and services offered to its clients. Morneau Shepell relies on these systems to maintain accurate, accessible and secure records.

In the course of delivering its products and services, Morneau Shepell collects and uses sensitive personal and financial information pertaining to its corporate, institutional and government clients as well as individual users. This information includes personal identification such as date of birth, social insurance numbers and driver's license numbers as well as health, benefits and financial information. The collection, use and protection of such information is governed by data privacy laws in multiple jurisdictions, including the General Data Protection Regulation in the U.K.

Due to the nature of the information involved in its products and services, Morneau Shepell may be subject to greater cybersecurity risks and consequences of disclosure than other companies. These risks can range from internal human error to uncoordinated individual attempts to gain unauthorized access to its information technology systems, to sophisticated and targeted measures directed at Morneau Shepell and its systems, clients or service providers. Any such disruptions in Morneau Shepell's systems or the failure of

the systems to operate as expected could, depending on the magnitude of the problem, result in the loss of client information (including personal information), a loss of current or future business, reputational harm and/or potential claims against Morneau Shepell, all of which could have a material adverse effect on Morneau Shepell's business, financial condition and operating results.

Morneau Shepell continues to enhance its efforts to mitigate these risks.

It invests in technology security initiatives to better identify and address any vulnerabilities. This includes measures such as annual third party internal and external vulnerability assessments and third party code reviews, data monitoring and assessments. Morneau Shepell has also improved the security testing capabilities of its internal teams. In addition, Morneau Shepell continues to increase the awareness its employees have of security policies and procedures through ongoing communications and privacy and security training. Morneau Shepell ensures that its service providers adopt similar measures through the use of security agreements.

From a systems and infrastructure perspective, Morneau Shepell uses a third party co-location site for data storage to decrease the probability of loss in the event of a business interruption or disaster. Internally, it maintains a complete inventory of all servers and infrastructure components and uses data loss prevention features to reduce the likelihood of improper disclosure of personal and confidential information.

Morneau Shepell’s Chief Information Officer and Chief Security Officer are responsible for establishing, monitoring and maintaining the enterprise technology and security processes and policies with support from third party consultants and the Company’s internal information technology, legal and audit departments.

The Company maintains privacy and network liability insurance coverage in the event of a loss arising from a network security failure, privacy event or social engineering fraud commonly referred to a “phishing attack”.

The above referenced insurance policy, technology security initiatives and employee awareness measures are assessed on an annual basis as part of Morneau Shepell’s comprehensive enterprise risk management process.

While Morneau Shepell has invested and continues to invest in technology security initiatives, information technology risk management and disaster recovery plans, these measures cannot fully insulate it from cybersecurity incidents, technology disruptions or data loss, which could adversely impact its competitiveness and result of operations.

**Reputational Risk**

Morneau Shepell depends to a large extent upon its relationships with its clients and its reputation for high-quality services. As a result, the impact of client dissatisfaction with Morneau Shepell’s services or products may be more damaging in Morneau Shepell’s business than in other businesses. Moreover, if the firm fails to meet its contractual or regulatory obligations, Morneau Shepell could be subject to legal liability and a loss of client relationships.

**Satisfactory Performance of Obligations**

In its contracts with clients, Morneau Shepell is sometimes committed to meeting identified service levels and/or timelines. If the service levels/timelines are not met, Morneau Shepell may experience reduced revenues, incur significant additional costs or be held responsible for the costs incurred by the client for failure to meet the service level/timeline. Morneau Shepell's success depends in large part upon whether it fulfills these and other contractual obligations with clients and maintains client satisfaction. If Morneau Shepell fails to satisfactorily perform its contractual obligations, its clients could terminate contracts and/or

take legal action against Morneau Shepell. Such occurrences could result in a loss of its professional reputation and in extra costs needed to defend or rectify the situation and thus have a material adverse effect on Morneau Shepell's business, financial condition and operating results.

**Economic Conditions**

An economic slowdown could cause a decline in demand for Morneau Shepell’s services. Growth in its clients’ businesses may be affected by economic slowdowns and could therefore potentially have an impact on Morneau Shepell’s operating results. During an economic downturn, Morneau Shepell clients and potential clients may reduce their employee populations, delay services or projects, or defer contracts currently underway. This situation could also lead to greater delays and defaults in payments or debt collection, resulting in lower operating results. Because of lower revenue during an economic slowdown, competition may increase and prices may be reduced by certain competitors to maintain or expand their market share. Pricing and profitability could be adversely affected as a result.

**Potential Risks Associated with Acquisitions**

In connection with acquisitions completed by Morneau Shepell, there may be undisclosed or unknown claims against, liabilities of, or issues concerning an acquired business that Morneau Shepell failed to discover or was unable to quantify in its due diligence which it conducted prior to the execution of an acquisition. Morneau Shepell may not be indemnified for some or all of these claims, liabilities or issues. In addition, indemnities given by vendors may not provide Morneau Shepell with sufficient protection against a breach of vendor representations, warranties or covenants. The existence of any material claims, liabilities or issues could have a material adverse effect on Morneau Shepell’s business, financial condition, liquidity and results of operations.

Acquisition transactions involve risks that could materially and adversely affect Morneau Shepell’s business plan, including the failure of Morneau Shepell to realize the results expected from an acquisition. In order to achieve the benefits of a completed acquisition, Morneau Shepell will rely upon its ability to successfully retain staff, consolidate functions and integrate operations, procedures and personnel in a timely and efficient manner, as well as the ability to realize growth opportunities and potential synergies from combining an acquired business and related operations with those of Morneau Shepell. There is a risk that some or all of the expected benefits will fail to materialize, or may not occur within the time periods anticipated by management. The realization of some or all of such benefits may be affected by a number of factors, many of which are beyond the control of Morneau Shepell.

The integration of an acquired business and related operations require the dedication of management effort, time and resources, which may divert management’s focus and resources from other strategic opportunities and from operational matters during the integration process. The integration process may result in the disruption of ongoing business and customer relationships that may adversely affect Morneau Shepell’s ability to achieve anticipated benefits of an acquisition.

**Dependence on Key Clients and Key Channel Partners**

As clients may terminate engagements with minimum notice, there can be no assurance that Morneau Shepell will be able to retain relationships with its largest clients. Moreover, there can be no assurance that such clients will continue to use Morneau Shepell’s services in the future. Any negative change involving any of Morneau Shepell’s largest clients, including but not limited to a client's financial condition or desire to continue using Morneau Shepell’s services, could result in a significant reduction in revenue which could have a material adverse effect on Morneau Shepell’s business, financial condition and operating results. No one Morneau Shepell client makes up more than 10% of Morneau Shepell’s total revenue for the years ended December 31, 2018 and 2017.

Morneau Shepell markets its services directly to end-user employers, associations and universities as well as through certain channel partners, primarily insurance companies (many of which compete amongst themselves directly). There can be no assurance that Morneau Shepell will be able to maintain its existing relationships with all these channel partners, which could have a material adverse effect on Morneau Shepell’s business, financial condition and operating results.

**Reliance on Key Professionals**

Morneau Shepell's operations are dependent upon the abilities, experience and efforts of its professionals, many of whom have excellent reputations and a significant number of contacts in the industries in which Morneau Shepell operates. Morneau Shepell's business depends, in part, on its professionals’ abilities to develop and maintain client relationships and alliances with businesses such as financial services companies, healthcare organizations, insurance companies, business process outsourcing organizations and other companies, in order to develop, market and deliver its services. Profitability could be negatively impacted if Morneau Shepell’s client relationships or business alliances are discontinued due to the loss of professional staff or if the firm has difficulty developing new alliances.

Should any member of its professional staff be unable or unwilling to continue his or her relationship with Morneau Shepell, this change could have a material adverse effect on Morneau Shepell’s business, financial condition and operating results.

**Risk of Future Legal Proceedings**

Morneau Shepell may be threatened with, or may be named as a defendant in, or may become subject to, various legal proceedings in the ordinary course of conducting its business, including lawsuits based upon professional errors and omissions.

Consulting services involves assumptions and estimates concerning future events, the actual outcome of which cannot be known with certainty in advance. In addition, computational, software programming or data management errors could occur. For example, possible legal proceedings could result from a client's assertion that actuarial assumptions used in a pension plan were unreasonable, leading to plan underfunding; a claim that inaccurate data was used, which could lead to an underestimation of plan liabilities; or a claim that employee benefits plan documents were misinterpreted or plan amendments were misstated in plan documents, which could lead to overpayments to beneficiaries. The well-being and health and productivity services involve confidential counseling, occupational health activities and disability case management. Each of these activities could potentially put Morneau Shepell in conflict with its customers, their employees, or both. Possible legal proceedings could also result from matters such as an employee claiming for breach of confidence, failure to provide adequate counsel, or denial of benefits or employment as a result of Morneau Shepell’s actions.

Defending lawsuits of this nature could require much management attention, which could divert its focus from operations. Such claims could produce negative publicity that could harm Morneau Shepell's reputation and business. A significant judgment against Morneau Shepell, or the imposition of a significant fine or penalty as a result of a finding that Morneau Shepell failed to comply with laws or regulations, could have a material adverse effect on Morneau Shepell's business, financial condition and operating results.

**Protection of Intellectual Property**

Morneau Shepell continually develops and improves its proprietary technology solutions for the delivery of its services. No assurance can be given that Morneau Shepell's competitors will not develop substantially similar technology.

Morneau Shepell relies on one or more of the following to protect its proprietary rights: trademarks, copyrights, trade secrets, confidentiality procedures and contractual provisions. Despite Morneau Shepell's efforts to protect its proprietary rights, unauthorized parties may attempt to obtain and use information that Morneau Shepell regards as proprietary. Stopping unauthorized use of Morneau Shepell's intellectual property may be difficult, time-consuming and costly. There can be no assurance that Morneau Shepell will be successful in protecting its proprietary rights and, if it is not, this could have a material adverse effect on Morneau Shepell's business, financial condition and operating results.

**Insurance**

Morneau Shepell believes that its insurance coverage, including professional errors and omissions insurance, cyber liability insurance, crime insurance, director and officer liability insurance, and commercial general liability insurance coverage address all material insurable risks, provides coverage that is similar to that which would be maintained by a prudent operator of a similar business and is subject to deductibles, limits and exclusions which are customary or reasonable given the cost of procuring insurance and current operating conditions.

However, there can be no assurance that such insurance will continue to be offered on economically feasible terms, that all events that could give rise to a loss or liability are insurable, or that the amounts of insurance will at all times be sufficient to cover each and every loss or claim that may occur involving Morneau Shepell's assets or operations.

**Foreign Exchange Risk**

A portion of Morneau Shepell's sales are in U.S. dollars, Australian dollars, and British Pounds and thus Morneau Shepell is exposed to fluctuations in the value of these currencies relative to the Canadian dollar.

The net revenue exposure denominated in foreign currencies was $46.9 million for the year ended December 31, 2018. An increase in foreign revenues would expose Morneau Shepell to fluctuations in exchange rates which may have a material adverse effect on Morneau Shepell's business, financial condition, and operating results.

**Indebtedness and Interest Rates**

The ability of Morneau Shepell to pay dividends or make other payments or advances will be subject to applicable laws and contractual restrictions contained in the instruments governing any indebtedness of Morneau Shepell.

The degree to which Morneau Shepell is leveraged could have important consequences including: Morneau Shepell's ability to obtain additional financing for working capital, capital expenditures or acquisitions in the future may be limited; a significant portion of Morneau Shepell's cash flow from operations may be dedicated to the payment of the principal of and interest on its indebtedness, thereby reducing funds available for future operations; certain borrowings will be at variable rates of interest, which exposes Morneau Shepell to the risk of increased interest rates; and Morneau Shepell may be more vulnerable to economic downturns and be limited in its ability to withstand competitive pressures.

These factors may increase the sensitivity of free cash flow to interest rate variations. Interest rate swap agreements are used as part of Morneau Shepell's program to manage the floating interest rate of Morneau Shepell's Credit Facility.

The Credit Facility contains numerous restrictive covenants that limit the discretion of management with respect to certain business matters. These covenants place significant restrictions on, among other things, the ability of Morneau Shepell to create liens or other encumbrances, to pay dividends or make certain

other payments, investments, loans and guarantees and to sell or otherwise dispose of assets and merge or consolidate with another entity.

In addition, the Credit Facility contains financial covenants that require Morneau Shepell to meet certain financial ratios and financial condition tests. A failure to comply with the obligations in the Credit Facility could result in a default which, if not cured or waived, could result in a reduction or termination of dividends by Morneau Shepell and permit acceleration of the relevant indebtedness. If the indebtedness under the Credit Facility was to be accelerated, there can be no assurance that the assets of Morneau Shepell would be sufficient to repay in full that indebtedness. In addition, the Credit Facility matures on July 27, 2023. There can be no assurance that future borrowings or equity financing will be available to Morneau Shepell or available on acceptable terms, in an amount sufficient to fund Morneau Shepell's needs.

**Credit risk**

If a counterparty to a financial instrument held by Morneau Shepell fails to discharge their obligation, this could lead to a financial loss for the Company. As at December 31, 2018, the Company's credit risk was limited to the carrying amount of the cash and accounts receivable as at this date, with one U.S. public sector customer comprised $14,752 (December 31, 2017 - $14,134) of the trade and other receivables balance, of which $8,495 (December 31, 2017 - $10,599) is greater than ninety days past due. The Company believes that the credit risk of accounts receivable, including the customer noted above, is limited for the following reasons:

(a) Risk associated with concentration of credit risk with respect to accounts receivable is limited due to the credit rating of the Company's top 10 clients.

(b) Management regularly reviews and assesses customer accounts and credit risk. Historically, bad debt as a percentage of revenue has been minimal.

The credit risk on cash and investments held in trust is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

**Cash Dividends are not Guaranteed and will Fluctuate with the Business Performance**

As a corporation, Morneau Shepell's dividend policy is at the discretion of its Board of Directors. The ability of Morneau Shepell to make dividend payments, and the actual amount paid is entirely dependent on the operations and assets of its subsidiaries and is subject to various factors applicable to Morneau Shepell and its subsidiaries including financial performance, obligations under credit facilities, fluctuations in working capital, the sustainability of margin and capital expenditure requirements, and applicable laws and regulations.

**Market Price and Dilution of Common Shares**

The market price of Morneau Shepell's common shares may be subject to wide fluctuations in response to many factors, including variations in operating results of Morneau Shepell, divergence in financial results from expectations, changes in business prospects for Morneau Shepell, general economic conditions, legislative changes, and other events and factors outside Morneau Shepell's control.

Sales of a substantial number of common shares by a significant shareholder in the public market or otherwise could adversely affect the prevailing market prices of the common shares and could impair the Company's ability to raise additional capital through an offering of common shares. The possible perception among the public that these sales will occur could also produce the same effect.

Pursuant to its articles of incorporation, Morneau Shepell is authorized to issue an unlimited number of

common shares and 10 million preferred shares for the consideration and on such terms established by the Board of Directors without the approval of any shareholders. Any further issuance of common shares may dilute the interests of existing shareholders. Furthermore, Morneau Shepell may make future acquisitions or enter into financings or other transactions involving the issuance of securities of Morneau Shepell which may be dilutive. In addition, Morneau Shepell may issue shares upon the conversion, redemption or maturity of payment of interest on its convertible debentures. Accordingly, if the debentures are converted this may have a dilutive impact on the Company's earnings per share.

## SELECTED ANNUAL INFORMATION

| *(In thousands of dollars, except per share amounts)* | Year ended December 31, 2018 | Year ended December 31, 2017[2] | Year ended December 31, 2016 |
|---|---|---|---|
| Revenue | $722,284 | $625,089 | $592,057 |
| Profit for the year | 21,797 | 33,024 | 26,000 |
| Earnings per share (basic) | 0.36 | 0.60 | 0.49 |
| Earnings per share (diluted) | 0.36 | 0.59 | 0.49 |
| Dividends declared per share | 0.78 | 0.78 | 0.78 |
| Total assets | 1,348,342 | 821,688 | 773,626 |
| Total long-term debt [1] | 457,498 | 261,749 | 247,395 |

Footnotes:

(1) Includes convertible debentures.

(2) Certain figures have been restated as a result of the Company's adoption of IFRS 15 on January 1, 2018. Note that figures for the year ended December 31, 2016 have not been restated. Please refer to note 3 of the audited consolidated financial statements for the year ended December 31, 2018 for further details.

## SUPPLEMENTARY SUMMARY OF QUARTERLY RESULTS

Selected Unaudited Consolidated Financial information:

*(in thousands of dollars except per share amounts)*

| Quarter ended | December 31, 2018 | September 30, 2018 | June 30, 2018 | March 31, 2018 | December 31, 2017 [2] | September 30, 2017 [2] | June 30, 2017 [2] | March 31, 2017 [2] |
|---|---|---|---|---|---|---|---|---|
| Revenue | 200,761 | 182,805 | 171,191 | 167,526 | 156,787 | 152,528 | 159,193 | 156,582 |
| Profit (loss) [4] | 3,450 | (9,556) | 13,672 | 14,229 | 3,452 | 9,178 | 12,117 | 8,280 |
| EBITDA[4] | 27,842 | 11,684 | 32,785 | 33,584 | 17,773 | 26,325 | 29,094 | 25,552 |
| Adjusted EBITDA | 35,652 | 33,989 | 33,734 | 33,584 | 27,487 | 28,333 | 31,332 | 31,275 |
| EBITDA margin | 13.9% | 6.4% | 19.2% | 20.0% | 11.3% | 17.3% | 18.3% | 16.3% |
| Adjusted EBITDA margin | 17.8% | 18.6% | 19.7% | 20.0% | 17.5% | 18.6% | 19.7% | 20.0% |
| Earnings(loss) per share (basic) | 0.05 | (0.15) | 0.25 | 0.26 | 0.06 | 0.17 | 0.22 | 0.15 |
| Earnings(loss) per share (diluted) | 0.05 | (0.15) | 0.24 | 0.25 | 0.06 | 0.16 | 0.22 | 0.15 |
| Normalized Free Cash Flow | 18,284 | 23,075 | 16,922 | 16,832 | 18,949 | 17,227 | 15,422 | 18,340 |
| Dividends declared | 12,493 | 12,505 | 10,504 | 10,498 | 10,457 | 10,525 | 10,417 | 10,380 |
| Twelve-month rolling normalized payout ratio | 61.2% | 58.0% | 60.0% | 61.2% | 59.7% | 59.0% | 58.7% | 55.4% |
| Twelve-month rolling normalized payout ratio, including changes in adjusted non-cash operating working capital | 71.0% | 54.2% | 80.2% | 74.0% | 73.6% | 97.5% | 70.7% | 72.4% |
| Total assets [3] | 1,348,342 | 1,331,245 | 833,815 | 820,939 | 821,688 | 797,158 | 804,983 | 788,946 |
| Total long-term debt [1][3] | 457,498 | 467,321 | 288,124 | 264,608 | 261,749 | 266,082 | 267,277 | 247,638 |

Footnotes:

(1) Includes convertible debentures.

(2) Certain figures have been restated as a result of the Company's adoption of IFRS 15 on January 1, 2018. Please refer to note 3 of the audited consolidated financial statements for the year ended December 31, 2018 for further details.

(3) The Company acquired LifeWorks in Q3 2018 for approximately $434.8 million, which resulted in the increase in total assets. Total long–term debt also increased as the acquisition was partially financed by a draw down from the Company's Credit Facility.

(4) The loss and the decline in EBITDA for the quarter ended September 30, 2018 is due to transaction costs of $9.0 million incurred to complete the LifeWorks acquisition.

## 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 and operating effectively as at December 31, 2018.

## 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.

With the exception of internal controls related to the acquired LifeWorks business, the Chief Executive Officer and the Chief Financial Officer have concluded that the internal controls over financial reporting are appropriately designed and operating effectively to provide this assurance based on the evaluation of these controls conducted as of December 31, 2018. No changes were made in our internal controls over financial reporting during the fourth quarter ended December 31, 2018, that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting,

As discussed in the '2018 Summary and Outlook' section of the MD&A above, Morneau Shepell acquired the LifeWorks business on July 27, 2018. The Company is integrating internal controls over financial reporting for that business. The documentation and evaluation of these controls will be carried out in 2019.

The following is a summary of the financial information of LifeWorks:

- Revenue of $51.9 million and a loss of $7.9 million (which include a pre-tax amortization charge of $12.3 million for acquisition related intangibles) for the period from the date of acquisition to December 31, 2018.

- Current and non-current assets as at December 31, 2018 of $24.3 million and $499.2 million respectively.

- Current and non-current liabilities as at December 31, 2018 of $27.2 million and $54.4 million respectively.

**Additional Information**

Morneau Shepell's shares and convertible debentures currently trade on the Toronto Stock Exchange under the symbols MSI and MSI.DB.A, respectively. 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 March 6, 2019.