

# **Genworth MI Canada Inc.**

**Management's Discussion and Analysis**

**For the year ended December 31, 2016**

## Interpretation

The current and prior-period comparative results for Genworth MI Canada Inc. ("Genworth Canada" or the "Company") reflect the consolidation of the Company and its subsidiaries, including Genworth Financial Mortgage Insurance Company Canada (the "Insurance Subsidiary"). The Insurance Subsidiary is engaged in the provision of mortgage insurance in Canada and is regulated by the Office of the Superintendent of Financial Institutions ("OSFI") as well as financial services regulators in each province.

The following Management's Discussion and Analysis ("MD&A") of the financial condition and results of operations as approved by the Company's board of directors (the "Board") on February 6, 2017 is prepared for the three and twelve months ended December 31, 2016. The audited consolidated financial statements of the Company were prepared in accordance with International Financial Reporting Standards ("IFRS"). This MD&A should be read in conjunction with the Company's financial statements.

Unless the context otherwise requires, all references in this MD&A to "Genworth Canada" or the "Company" refer to Genworth MI Canada Inc. and its subsidiaries.

Unless the context otherwise requires, all financial information is presented on an IFRS basis.

## Caution regarding forward looking information and statements

Certain statements made in this MD&A contain forward-looking information within the meaning of applicable securities laws ("forward-looking statements"). When used in this MD&A, the words "may", "would", "could", "will", "intend", "plan", "anticipate", "believe", "seek", "propose", "estimate", "expect", and similar expressions, as they relate to the Company are intended to identify forward-looking statements. Specific forward-looking statements in this document include, but are not limited to, statements with respect to the Company's expectations regarding the effect of the Canadian government guarantee legislative framework, the impact of proposed guideline changes by OSFI (as defined herein) and legislation introduced in connection with the Protection of Residential Mortgage or Hypothecary Insurance Act ("PRMHIA") (as defined herein) and the effect of changes to the government guarantee mortgage eligibility rules, and the Company's beliefs as to housing demand and home price appreciation, unemployment rates, the Company's future operating and financial results, sales expectations regarding premiums written, capital expenditure plans, dividend policy and the ability to execute on its future operating, investing and financial strategies.

The forward-looking statements contained herein are based on certain factors and assumptions, certain of which appear proximate to the applicable forward-looking statements contained herein. Inherent in the forward-looking statements are known and unknown risks, uncertainties and other factors beyond the Company's ability to control or predict, that may cause the actual results, performance or achievements of the Company, or developments in the Company's business or in its industry, to differ materially from the anticipated results, performance, achievements or developments expressed or implied by such forward-looking statements. Actual results or developments may differ materially from those contemplated by the forward-looking statements.

The Company's actual results and performance could differ materially from those anticipated in these forward-looking statements as a result of both known and unknown risks, including: the continued availability of the Canadian government's guarantee of private mortgage insurance on terms satisfactory to the Company; the Company's expectations regarding its revenues, expenses and operations; the Company's plans to implement its strategy and operate its business; the Company's expectations regarding the compensation of directors and officers; the Company's anticipated cash needs and its estimates regarding its capital expenditures, capital requirements, reserves and its needs for additional financing; the Company's plans for and timing of expansion of service and products; the Company's ability to accurately assess and manage risks associated with the policies that are written; the Company's ability to accurately manage market, interest and credit risks; the Company's ability to maintain ratings, which may be affected by the ratings of its majority shareholder, Genworth Financial, Inc.; interest rate fluctuations; a decrease in the volume of high loan-to-value mortgage originations; the cyclical nature of the mortgage insurance industry; changes in government regulations and laws mandating mortgage insurance; the acceptance by the Company's lenders of new technologies and products; the Company's ability to attract lenders and develop and maintain lender relationships; the Company's competitive position and its expectations regarding competition from other providers of mortgage insurance in Canada; anticipated trends and challenges in the Company's business and the markets in which it operates; changes in the global or Canadian economies; a decline in the Company's regulatory capital or an increase in its regulatory capital requirements; loss of members of the Company's senior management team; potential legal, tax

and regulatory investigations and actions; the failure of the Company's computer systems; and potential conflicts of interest between the Company and its majority shareholder, Genworth Financial, Inc.

This is not an exhaustive list of the factors that may affect any of the Company's forward-looking statements. Some of these and other factors are discussed in more detail in the Company's Annual Information Form (the "AIF") dated March 16, 2016. Investors and others should carefully consider these and other factors and not place undue reliance on the forward-looking statements. Further information regarding these and other risk factors is included in the Company's public filings with provincial and territorial securities regulatory authorities (including the Company's AIF) and can be found on the System for Electronic Document Analysis and Retrieval ("SEDAR") website at [www.sedar.com](http://www.sedar.com). The forward-looking statements contained in this MD&A represent the Company's views only as of the date hereof. Forward-looking statements contained in this MD&A are based on management's current plans, estimates, projections, beliefs and opinions and the assumptions related to these plans, estimates, projections, beliefs and opinions may change, and are presented for the purpose of assisting the Company's security holders in understanding management's current views regarding those future outcomes and may not be appropriate for other purposes. While the Company anticipates that subsequent events and developments may cause the Company's views to change, the Company does not undertake to update any forward-looking statements, except to the extent required by applicable securities laws.

#### **Non-IFRS financial measures**

To supplement the Company's consolidated financial statements, which are prepared in accordance with IFRS, the Company uses non-IFRS financial measures to analyze performance. The Company's key performance indicators and certain other information included in this MD&A include non-IFRS financial measures. Such non-IFRS financial measures used by the Company to analyze performance include interest and dividend income, net of investment expenses, net operating income, operating earnings per common share (basic) and operating earnings per common share (diluted).

Other non-IFRS financial measures used by the Company to analyze performance for which no comparable IFRS measure is available include insurance in-force, new insurance written, loss ratio, expense ratio, combined ratio, operating return on equity, investment yield and Minimum Capital Test ("MCT") ratio. The Company believes that these non-IFRS financial measures provide meaningful supplemental information regarding its performance and may be useful to investors because they allow for greater transparency with respect to key metrics used by management in its financial and operational decision making. Non-IFRS financial measures do not have standardized meanings and are unlikely to be comparable to any similar measures presented by other companies.

See the "Non-IFRS financial measures" section at the end of this MD&A for a reconciliation of net operating income to net income, investment income to interest and dividend income, net of investment expenses, operating earnings per common share (basic) to earnings per common share (basic) and operating earnings per common share (diluted) to earnings per common share (diluted).

Definitions of key non-IFRS financial measures and explanations of why these measures are useful to investors and management can be found in the Company's "Non-IFRS financial measures glossary", in the "Non-IFRS financial measures" section at the end of this MD&A.

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## Business profile

### Business background

Genworth Canada is the largest private-sector residential mortgage insurer in Canada and has been providing mortgage default insurance in the country since 1995. The Company has built a broad underwriting and distribution platform across the country that provides customer-focused products and support services to the vast majority of Canada's residential mortgage lenders and originators. Genworth Canada underwrites mortgage insurance for residential properties in all provinces and territories of Canada and has the leading market share among private mortgage insurers. The Canada Mortgage and Housing Corporation ("CMHC"), a crown corporation, is the Company's main competitor.

The Company offers both transactional and portfolio mortgage insurance.

Federally regulated lenders are required to purchase transactional mortgage insurance in respect of a residential mortgage loan whenever the loan-to-value ratio exceeds 80%. The Company's transactional mortgage insurance covers default risk on mortgage loans secured by residential properties to protect lenders from any resulting losses on claims. By offering insurance for transactional mortgages, the Company plays a significant role in providing access to homeownership for Canadian residents. Homebuyers who can only afford to make a smaller down payment can, through the benefits provided by mortgage insurers such as Genworth Canada, obtain mortgages at rates comparable to buyers with more substantial down payments.

The Company also provides portfolio mortgage insurance to lenders for loans with loan-to-value ratios of 80% or less. Portfolio insurance is beneficial to lenders as they provide the ability to manage capital and funding requirements and mitigate risk. The Company views portfolio mortgage insurance as an extension of its relationship with existing transactional customers. Therefore, the Company carefully manages the level of its portfolio mortgage insurance relative to its overall mortgage insurance business. Premium rates on portfolio mortgage insurance have historically been lower than those on transactional mortgage insurance due to the lower risk profile associated with portfolio loans.

### Seasonality

The transactional mortgage insurance business is seasonal. Premiums written vary each quarter, while premiums earned, investment income, underwriting and administrative expenses tend to be relatively stable from quarter to quarter. The variations in premiums written are driven by mortgage origination activity and associated transactional new insurance written, which typically peak in the spring and summer months. Losses on claims vary from quarter to quarter, primarily as the result of prevailing economic conditions, changes in employment levels and characteristics of the insurance in-force portfolio, such as size, age, seasonality and geographic mix of delinquencies. Typically, losses on claims increase during the winter months, due primarily to an increase in new delinquencies, and decrease during the spring and summer months.

The Company's new insurance written from portfolio mortgage insurance varies from period to period based on a number of factors including: the amount of portfolio mortgages lenders seek to insure; the competitiveness of the Company's pricing, underwriting guidelines and credit enhancement for portfolio insurance; and the Company's risk appetite for such mortgage insurance.

### Distribution and marketing

The Company works with lenders, mortgage brokers and real estate agents across Canada to make homeownership more accessible for first-time homebuyers. Mortgage insurance customers consist of originators of residential mortgage loans, such as banks, mortgage loan and trust companies, credit unions and other lenders. These lenders typically determine which mortgage insurer they will use for the placement of mortgage insurance written on loans originated by them. The five largest Canadian chartered banks have been the largest mortgage originators in Canada and provide the majority of financing for residential mortgages.

## Overview

### Fourth quarter financial highlights

**Table 1: Selected financial information**

(in millions of dollars, unless otherwise specified)	Fourth Quarter			Full Year	
	2016	2015		2016	2015
Premiums written	\$ 171	\$ 213		\$ 760	\$ 809
Premiums earned	\$ 164	\$ 151		\$ 638	\$ 586
Losses on claims	29	35		139	122
Expenses	33	27		124	108
Total losses on claims and expenses	62	62		263	230
Net underwriting income	103	90		375	356
Interest and dividend income, net of investment expenses	46	44		176	169
Net investment gains	47	3		38	32
Investment income	93	47		214	201
Interest expense	6	6		23	23
Income before income taxes	190	131		566	534
Net income	\$ 140	\$ 98		\$ 417	\$ 398
Net operating income <sup>1</sup>	\$ 105	\$ 95		\$ 388	\$ 375
<b>Weighted average number of common shares outstanding</b>					
Basic	91,856,165	91,795,125		91,828,701	92,296,521
Diluted <sup>2</sup>	92,266,264	92,218,209		91,874,244	92,771,849
<b>Earnings per common share</b>					
Earnings per common share (basic)	\$ 1.52	\$ 1.06		\$ 4.54	\$ 4.32
Earnings per common share (diluted) <sup>2</sup>	\$ 1.52	\$ 1.03		\$ 4.54	\$ 4.22
<b>Selected non-IFRS financial measures <sup>1</sup></b>					
Operating earnings per common share (basic)	\$ 1.15	\$ 1.04		\$ 4.23	\$ 4.07
Operating earnings per common share (diluted) <sup>2</sup>	\$ 1.14	\$ 1.03		\$ 4.23	\$ 4.05
Insurance in-force <sup>3</sup>	\$ 464,291	\$ 404,963		\$ 464,291	\$ 404,963
Transactional new insurance written	\$ 5,120	\$ 6,231		\$ 21,171	\$ 25,243
Portfolio new insurance written	\$ 4,918	\$ 9,595		\$ 41,881	\$ 25,696
Loss ratio	18%	23%		22%	21%
Expense ratio	20%	18%		19%	18%
Combined ratio	38%	41%		41%	39%
Operating return on equity	12%	12%		11%	12%
MCT ratio	245%	234%		245%	234%
Delinquency ratio <sup>4</sup>	0.10%	0.10%		0.10%	0.10%

Note: Amounts may not total due to rounding.

<sup>1</sup>These financial measures are not calculated based on IFRS. See the “Non-IFRS financial measures” section at the end of this MD&A for additional information.

<sup>2</sup>The difference between basic and diluted number of Common Shares outstanding, basic and diluted earnings per common share, and basic and diluted operating earnings per common share is caused by the potentially dilutive impact of share-based compensation awards.

<sup>3</sup>The Company estimates that the outstanding balance of insured mortgages was approximately \$223 billion as at December 31, 2016.

<sup>4</sup>Based on original insured loans in-force for which coverage terms have not expired and excludes delinquencies that have been incurred but not reported.

**Key fourth quarter financial metrics:**

The Company reported net income of \$140 million and net operating income of \$105 million in the fourth quarter of 2016, as compared to \$98 million and \$95 million, respectively, in the same quarter in the prior year.

- Premiums written of \$171 million decreased by \$42 million, or 20%, as compared to the same quarter in the prior year. Premiums written from transactional insurance of \$149 million were lower by \$32 million, or 17%, from the prior year's period due to an 18% decrease in new insurance written, primarily as a result of targeted underwriting changes in select markets and a smaller transactional insurance market size. Premiums written of \$22 million from portfolio insurance were lower by \$10 million, or 32%, from the prior year's period. The volume of portfolio insurance varies from quarter to quarter based on lender demand.
- Premiums earned of \$164 million were \$13 million, or 9%, higher than the same quarter in the prior year due to the relatively larger contributions from premiums written in the 2015 and 2016 books of business.
- Losses on claims of \$29 million were \$6 million, or 17%, lower than the same quarter in the prior year, primarily due to strong economic conditions in the Pacific region and favourable development from Québec case reserves, partially offset by pressure in oil-producing regions. The loss ratio was 18% for the quarter as compared to 23% in the same quarter in the prior year.
- Expenses of \$33 million were \$6 million, or 22%, higher than the same quarter in the prior year, primarily due to higher share-based compensation expense. The expense ratio for the quarter was 20%, as compared to 18% in the same quarter in the prior year, consistent with the Company's expected operating range of 18% to 20%.
- Investment income, excluding net investment gains, of \$46 million was \$2 million, or 4%, higher than the same quarter in the prior year, primarily due to an increase in the amount of invested assets.
- Net investment gains of \$47 million, primarily from net gains on derivatives and foreign exchange, are \$44 million higher than the same quarter in the prior year. The increase is primarily from the impact of movement in interest rates on the Company's interest rate swaps, as well as movement in foreign exchange rates on the Company's invested assets denominated in U.S. dollars. These gains are largely offset by decreases in fair value of available for sale assets in other comprehensive income ("OCI").

**Key 2016 financial metrics:**

The Company reported 2016 net income of \$417 million and net operating income of \$388 million, as compared to \$398 million and \$375 million, respectively, in the prior year. The prior year's net income and net operating income included a non-recurring favourable tax item of \$5 million.

- Premiums written of \$760 million decreased by \$49 million, or 6%, in 2016 as compared to the prior year. Premiums written from transactional insurance of \$619 million were lower by \$86 million, or 12%, primarily due to a 16% decrease in new insurance written, as a result of targeted underwriting changes in select areas and a smaller transactional insurance market size. This was partially offset by a 5% increase in the average transactional insurance premium rate resulting from the June 2015 premium rate increase. Portfolio insurance premiums written of \$140 million were higher by \$37 million, which was driven by higher demand from lenders prior to the July 1, 2016 regulatory changes, which generally limits portfolio insurance to only those mortgages that will be used in government securitization programs.
- Premiums earned of \$638 million increased by \$52 million, or 9%, in 2016 as compared to the prior year due to the relatively larger contributions from premiums written in the 2015 and 2016 books of business. The unearned premiums reserve was \$2.1 billion at December 31, 2016, up \$122 million, or 6%, from December 31, 2015.
- Losses on claims of \$139 million were \$17 million, or 14%, higher in 2016 as compared to the prior year, primarily due to an increase in new delinquencies, net of cures, and an increase in the average reserve per delinquency in oil-producing regions.
- Expenses of \$124 million increased by \$16 million, or 14%, in 2016 as compared to the prior year primarily due to share-based compensation expense. The expense ratio was 19% as compared to 18% in the prior year, consistent with the Company's expected operating range of 18% to 20%.

- Investment income, excluding net investment gains, of \$176 million was \$7 million, or 4%, higher than the prior year due to an increase in invested assets. The Company's investment portfolio had a market value of \$6.2 billion at December 31, 2016 and earned an investment yield of 3.2% in 2016.

The regulatory capital ratio or MCT ratio was approximately 245%, 11 percentage points higher than the prior year's period and 25 percentage points higher than the Company's operating MCT holding target of 220%.

## 2016 performance against strategic priorities

The Company met or exceeded the majority of its key strategic priorities for the year ended December 31, 2016 highlighted by the following accomplishments:

- Maintained strong insurance portfolio quality with an average transactional credit score of 751;
- Grew net operating income by 3.4%; and
- Achieved an operating return on equity of 11%.

The following table summarizes the Company's performance in comparison to the objectives:

2016 Objective	Performance
<b>Premiums Written and Premiums Earned</b>	
<b>Flat or modestly lower premiums written from transactional insurance compared to 2015</b> as the full year impact of the June 2015 price increase partially offsets the impact of an expected decline in mortgage originations.	Transactional premiums written decline: <b>12%</b> Premiums written from transactional insurance declined by 12% year-over-year primarily due to a 5% – 10% smaller high loan-to-value mortgage originations market as estimated by the Company and a modestly lower market share resulting from targeted underwriting actions in select markets.
Total premiums written moderately higher compared to 2015, primarily due to higher portfolio insurance volumes.	Total premiums written decline: <b>6%</b> Total premiums written declined by 6% year-over-year as the 36% increase in premiums written from portfolio insurance was more than offset by the decrease from transactional insurance.
<b>Moderate growth in premiums earned of 5% or greater for the full year.</b>	Premiums earned growth: <b>9%</b>
<b>Losses on Claims</b>	
<b>Proactive risk management and focused loss mitigation strategies:</b> <ul style="list-style-type: none"> <li>• Loss ratio range of 25% to 40%</li> <li>• Workout penetration rate greater than 55%</li> </ul>	Loss ratio: <b>22%</b> Workout penetration rate: <b>57%</b>  The Company achieved a loss ratio of 22%, 3 percentage points below the lower end of the Company's anticipated range of 25 to 40% for 2016. The loss ratio performance was favorably impacted by strong home price appreciation, stable unemployment, resilience in oil-producing regions and continued strong underwriting discipline. The workout penetration rate of 57% was 2 percentage points higher than the target of 55%.

2016 Objective	Performance
<b>Portfolio Quality and Risk Management</b>	
<p><b>Maintain a high quality insurance portfolio through prudent underwriting guidelines, proactive risk management and disciplined underwriting:</b></p> <ul style="list-style-type: none"> <li>• Average transactional credit score of greater than 735</li> <li>• Average transactional gross debt service ratio of less than 26%</li> <li>• Average transactional credit score below 660 of less than 5%</li> </ul>	<p>Average transactional credit score: <b>751</b>  Average transactional gross debt service ratio: <b>24%</b>  Average transactional credit score below 660: <b>3%</b></p> <p>The Company originated a high quality insurance portfolio with an 8-point average credit score year-over-year improvement to 751 primarily due to a smaller proportion of credit scores below 660. Gross debt service ratio was stable at 24%.</p>
<b>Capital Management</b>	
<p><b>Proactively manage capital to balance capital strength, flexibility and efficiency:</b></p> <ul style="list-style-type: none"> <li>• Ordinary dividend payout ratio of 35% to 45%</li> <li>• Debt-to-total capital ratio of less than or equal to 15%</li> <li>• MCT ratio modestly above 220%</li> </ul>	<p>Ordinary dividend payout ratio: <b>40%</b>  Debt-to-total capital ratio as at December 31, 2016: <b>11%</b>  MCT ratio as at December 31, 2016: <b>245%</b></p> <p>The Company maintained a strong and efficient capital base with an MCT ratio of 245%, 25 percentage points above the holding target, increased ordinary dividends by 5%, and maintained capital flexibility through \$180 million in liquid investments and entering into a \$100 million undrawn credit facility. On January 1, 2017, a new regulatory capital framework took effect and the pro forma MCT ratio under the new regulatory capital framework is 158% to 162% compared to the new PRMHIA minimum and regulatory supervisory ratio of 150%. The Company has established an internal target of 157% under the new regulatory capital framework.</p> <p>See "Recent business and regulatory developments" for further information.</p>
<b>Investments Management</b>	
<p><b>Optimize investment portfolio to maximize investment yield while maintaining a high quality investment portfolio to minimize the correlation of risk with our insurance in-force.</b></p>	<p>The Company maintained a high quality investment portfolio including an allocation of 91% to investment grade bonds and debentures and a modest increase in preferred shares. Overall, the Company achieved an average investment yield of 3.2%.</p>

## Recent business and regulatory developments

### Price increase

The Company reviews its underwriting, pricing and risk selection strategies on an annual basis to ensure that its products remain competitive and consistent with its marketing and profitability objectives. The Company's pricing approach takes into consideration long-term historical loss experience on loans with similar loan-to-value ratios, terms and types of mortgages, borrower credit histories and capital required to support the product.

On January 17, 2017, the Company announced it will increase its transactional mortgage insurance premium rates for homebuyers. The new pricing is a reflection of higher regulatory capital requirements that came into effect on January 1, 2017 and supports the long-term safety and sustainability of the Canadian housing finance system.

The new premium rates on transactional new insurance written for standard owner-occupied purchase applications submitted on or after March 17, 2017 are as follows:

Transactional New Insurance Written Loan-to-Value Ratio	Standard Premium (Prior to March 17, 2017)	Standard Premium (Effective March 17, 2017)
Up to and including 65%	0.60%	0.60%
Up to and including 75%	0.75%	1.70%
Up to and including 80%	1.25%	2.40%
Up to and including 85%	1.80%	2.80%
Up to and including 90%	2.40%	3.10%
Up to and including 95%	3.60%	4.00%
90.01% to 95% (Non-Traditional Payment Program)	3.85%	4.50%

Based on the expected loan-to-value mix, the average transactional premium rate increase is approximately 18% to 20% and is expected to result in an average transactional premium rate of 330 to 335 basis points for 2017, compared to 293 basis points in 2016. The average transactional premium rate after 2017 is expected to be 345 to 350 basis points. The Company believes the new premium rates adequately reflect the increased capital requirements and allows the Company to earn the targeted operating return of equity of 13% on new business.

Similarly, the Company has increased its premium rates for portfolio insurance as a result of the higher regulatory capital that came into effect on January 1, 2017. There may be a one-time increase in portfolio insurance volumes in the first quarter of 2017, as the Company ended 2016 with a number of pending portfolio applications which are expected to close in early 2017.

### Changes to the mortgage insurance rules

On October 3, 2016, the Minister of Finance announced a number of changes in the Canadian housing finance system. Building on measures announced in late 2015, the government will:

- Bring consistency to mortgage insurance rules by standardizing eligibility criteria for high- and low- loan-to-value ratio insured mortgages, including a mortgage rate stress test;
- Improve tax fairness by closing loopholes surrounding the capital gains tax exemption on the sale of a principal residence; and
- Consult on how to better protect taxpayers by ensuring that the distribution of risk in the housing finance system is balanced.

Key changes to the mortgage insurance rules are described below.

#### *Applying a Mortgage Rate Stress Test to All Insured Mortgages*

Effective October 17, 2016, all insured homebuyers must qualify for mortgage insurance at an interest rate that is the greater of their contract mortgage rate or the Bank of Canada's conventional five-year fixed posted rate, which is currently 4.64%. This requirement

was already in place for high loan-to-value ratio insured mortgages with variable interest rates or fixed interest rates with terms less than five years. To qualify for mortgage insurance, borrower debt-servicing ratios cannot exceed the maximum allowable levels of 39% and 44%, for gross debt service ratio and total debt service ratio, respectively.

#### *Changes to Low-Ratio Mortgage Insurance Eligibility Requirements*

Effective November 30, 2016, for insured mortgages with a loan-to-value ratio less than or equal to 80%, the following mortgage insurance criteria applies to both transactional mortgage insurance loans and portfolio mortgage insurance loans:

1. A loan whose purpose includes the purchase of a property or subsequent renewal of such a loan;
2. A maximum amortization length of 25 years commencing from when the loan was originally made;
3. A property value below \$1,000,000;
4. For variable-rate loans that allow fluctuations in the amortization period, loan payments that are recalculated at least once every five years to conform to the established amortization schedule;
5. A minimum credit score of 600 at the time the loan is approved;
6. A maximum gross debt service ratio of 39% and a maximum total debt service ratio of 44% at the time the loan is approved, calculated by applying the greater of the mortgage contract rate or the Bank of Canada conventional five-year fixed posted mortgage interest rate; and,
7. If the property is a single unit, it must be owner-occupied.

#### *Impact of Changes Related to Mortgage Rate Stress Tests and Low-Ratio Mortgage Insurance Eligibility Requirements*

Based on the Company's review of the mortgage insurance eligibility rule changes announced October 3, 2016, it expects that the transactional market size and its transactional new insurance written in 2017 may decline by approximately 15% to 25%, reflecting expected changes to borrower home buying patterns, including the purchase of lower-priced properties and/or larger downpayments.

The Company also expects that portfolio new insurance written in 2017 may decline by approximately 25% to 35% as compared to the normalized run rate after the July 1, 2016 regulatory changes for portfolio insurance. The new mortgage rules prohibit insuring low loan-to-value refinances and most investor mortgages originated by lenders on or after October 17, 2016.

The impact on any future premiums written from the smaller market size will be partially offset by the premium rate increase in March 2017, in response to the higher capital requirements arising from OSFI's new capital framework. With an unearned premiums reserve of \$2.1 billion as at December 31, 2016, premiums earned in the next 12 to 18 months will continue to benefit from the relatively higher level of premiums written in 2014 through 2016. As a result, there should be limited near-term impact on the level of premiums earned.

#### *Forthcoming Consultation on Lender Risk Sharing*

On October 21, 2016, the government launched a public consultation on a policy option that would require mortgage lenders to manage a portion of loan losses on insured mortgages that default, known as "lender risk sharing". This could transfer some risk borne by mortgage insurers to lenders. The comment period for this consultation ends on February 28, 2017. The Company will participate in the consultation; however, the Company believes it is premature to determine the potential impact of this process and its ultimate outcome.

#### **Portfolio mortgage insurance**

Effective July 1, 2016, portfolio mortgage insurance is only available on mortgages used in CMHC securitization programs and is prohibited on mortgages used in private securitizations after a phase-in period for existing private securitizations. The government announced these amendments on February 3, 2016 in the "*Eligible Mortgage Loan Regulations*" and the "*Insurable Housing Loan Regulations*" also referred to as the "Portfolio Insurance Purpose Test". Although it is difficult to determine the long term impact of these changes at this time, the Company believes that the regulations may result in a decrease in demand for portfolio mortgage insurance.

## Changes to the regulatory capital framework

On December 15, 2016, OSFI released the final capital advisory titled “*Capital Requirements for Federally Regulated Mortgage Insurers*”. This advisory provides a new standard framework for determining the capital requirements for residential mortgage insurance companies. The new framework is more risk sensitive and incorporates additional risk attributes, including credit score, remaining amortization and outstanding loan balance. The advisory came into effect on January 1, 2017, replacing OSFI’s advisory, “*Interim Capital Requirements for Mortgage Insurance Companies*”, which had been in effect since January 2015.

The advisory focuses on capital requirements for insurance risk, which consists primarily of:

- i. A base requirement that applies to all insured mortgages at all times; plus
- ii. A supplementary requirement that applies only to mortgages originated during periods when the housing market for the region that corresponds to the mortgage has a house price-to-income ratio that exceeds a specified threshold (with this supplementary requirement not applying to mortgages insured prior to January 1, 2017); less
- iii. Premium liabilities, consisting of unearned premiums reserve and the reserve for incurred but not reported (IBNR) claims.

The advisory states that:

- i. By using outstanding loan balance as the exposure measure, a mortgage’s actual pay down rate is captured and capital is only held against insured mortgages that are still outstanding;
- ii. By using a modified loan-to-value ratio (outstanding loan balance/original property value), the borrower’s equity position in the property is better captured;
- iii. Differentiating requirements by borrower credit score ensures that more capital is held for borrowers who have a greater risk of default;
- iv. Differentiating requirements by remaining amortization recognizes the importance of the expected future pay-down rate and progression of the borrower’s equity position.

Supplementary capital will be tied to the behavior of property prices, both in terms of recent housing price trends and the behavior of housing prices relative to household incomes. The Teranet – National Bank House Price Index™ (“**Teranet Index**”) is used to measure house prices and Statistics Canada household disposable income and population data are used to measure per capita income. The Supplementary Capital Requirement Indicators (“**SCRIs**”), based primarily on the ratio of the Teranet Index for a metropolitan area index to the national per capita income, is compared to a prescribed threshold value for that particular area. For a mortgage loan originated in any period after January 1, 2017, where the SCRI exceeds the threshold value for a metropolitan area, supplementary capital applies for the life of that mortgage. SCRI thresholds are calculated on a one quarter lag based on availability of household disposable income and population data.

The Company has reviewed the methodology for calculating SCRIs and observed that Calgary, Edmonton, Toronto, Vancouver and Victoria are breaching their SCRI thresholds, as prescribed by OSFI, at the end of the third quarter of 2016. These metropolitan areas represented approximately 35% - 40% of transactional new insurance written in 2016.

The advisory also includes a phase-in period to allow for a smooth transition to the new standard framework. For the segments of Genworth Canada’s insurance in-force listed below, these transition arrangements will keep the required capital unchanged from the 2016 MCT guideline level at 220% MCT ratio at December 31, 2016 until such time as the required capital under the new standard framework at the OSFI Supervisory MCT Target of 150% is less than the aforementioned required capital at a 220% MCT ratio:

- Transactional insured mortgages originated prior to December 31, 2016 with original amortizations greater than twenty-five years; and
- Portfolio insured mortgages for which the application for portfolio insurance was received prior to December 31, 2016 and the effective date of insurance is prior to March 31, 2017.

Additionally, the advisory provides for a three year phase-in period of the rising impact on capital required for operational risk.

Under the new capital framework, the holding target of 220% has been recalibrated, under PRMHIA, to the OSFI Supervisory MCT Target of 150% and the minimum MCT under PRMHIA has been reduced to 150%. Based on the new framework, the Company estimates that its pro forma MCT ratio as at December 31, 2016 would have been in the range of 158% to 162%. As a result, the Company was compliant with the new framework upon its implementation on January 1, 2017.

It is important to note that further changes to the new standard framework may be made by OSFI as a result of comments and input it receives in the future. The Company continues to work with OSFI to further refine this new standard framework in specific areas, including the proposed, but deferred, requirement to update credit scores.

#### **Additional property tax on purchases of residential property in Metro Vancouver by foreign buyers**

In order to help improve housing affordability, on July 25, 2016, the British Columbia government introduced a four-pronged plan that includes an additional land transfer tax on foreign buyers. As of August 2, 2016, foreign individuals and corporations are subject to an additional 15% land transfer tax on the purchase of residential property in Metro Vancouver. The Company does not expect these changes to have a material impact on its business, as foreign borrowers are typically not eligible for high loan-to-value mortgage insurance.

#### **Financial strength ratings**

On August 18, 2016, Standard & Poor's ("S&P") affirmed the Insurance Subsidiary's A+ rating with a stable outlook and the Company's BBB+ rating with a stable outlook.

On May 17, 2016, DBRS confirmed the Insurance Subsidiary's AA financial strength rating with a stable trend. DBRS downgraded the Company's issuer rating and senior unsecured debentures rating one notch to A (high) with a stable trend citing "DBRS's concern that there is now a greater risk that OSFI, in a stressed mortgage market situation, may place restrictions on dividend payments from the Insurance Company."<sup>1</sup>

#### **Dividends**

On November 25, 2016, the Company paid a quarterly dividend of \$0.44 per common share.

#### **Share repurchase**

On April 28, 2016, the Company received approval by the Toronto Stock Exchange for the Company to undertake a normal course issuer bid ("NCIB"). Pursuant to the NCIB, the Company can purchase, for cancellation, up to 4,589,958 shares representing approximately 5% of its outstanding common shares as of April 25, 2016. Purchases of common shares under the NCIB may commence on or after May 5, 2016 and will conclude on the earlier of May 4, 2017 and the date on which the Company has purchased the maximum number of shares under the NCIB.

The Company's prior NCIB, which commenced on April 28, 2015, expired on May 4, 2016. The Company did not purchase any shares under either NCIB during the three and twelve months ended December 31, 2016. The Company had made purchases of \$50 million in 2015 pursuant to the NCIB.

#### **E-21 – Operational Risk Management Guideline**

In June 2016, OSFI released its E-21 Operational Risk Management Guideline (the "E-21 Guideline"). In the E-21 Guideline, OSFI defines operational risk "as the risk of loss resulting from people, inadequate or failed internal processes and systems, or from external events. This includes legal risk but excludes strategic and reputational risk". The E-21 guideline sets out four principles: i) integrated and documented operational risk management framework; ii) support of a corporate governance structure including a risk appetite statement; iii) use of a "three lines of defense" approach to ensure accountability; and iv) comprehensive identification and assessment process. The E-21 Guideline is generally consistent with the Company's current operational risk management framework.

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<sup>1</sup> DBRS May 17, 2016 press release: DBRS Confirms Ratings on Genworth Financial Mortgage Insurance Company Canada and Downgrades Genworth MI Canada Inc.

**Maximum outstanding insured exposure for all private insured mortgages**

The Company estimates that its outstanding insured mortgage balances as at December 31, 2016 was \$223 billion, or 48% of the original insured amount. On December 15, 2016, the maximum outstanding insured exposure for all private insured mortgages permitted by PRMHIA was increased to \$350 billion from the previous maximum of \$300 billion. The Company estimates, that as at September 30, 2016, the outstanding insured mortgage balances for all privately insured mortgages was \$282 billion.

**Credit facility**

During the second quarter of 2016 the Company entered into a \$100 million senior unsecured revolving credit facility, which matures on May 20, 2019. The Company has not drawn on the credit facility as at December 31, 2016. The credit facility provides further financial flexibility in an efficient and cost effective manner.

**Genworth Financial, Inc. transaction**

On October 21, 2016, Genworth Financial, Inc., the Company's majority shareholder, entered into a definitive agreement with China Oceanwide Holdings Group Co., Ltd., a limited liability company incorporated in the People's Republic of China ("China Oceanwide"), under which China Oceanwide has agreed to acquire all of the outstanding shares of Genworth Financial Inc. through a merger. Upon completion of the transaction, Genworth Financial, Inc. will be a standalone subsidiary of China Oceanwide. The transaction is subject to approval by the shareholders of Genworth Financial Inc. as well as other closing conditions, including the receipt of required regulatory approvals.

## Economic environment

The mortgage insurance business is influenced by macroeconomic conditions. Specifically, the level of premiums written is influenced by economic growth, interest rates, unemployment, housing activity, home prices and government policy among other factors. Losses on claims are primarily impacted by unemployment rates, home prices and housing activity.

Key Macroeconomic Factors Influencing Business Performance	
Full Year 2016 or as at December 31, 2016	Full Year 2017 or as at December 31, 2017 Estimate
Housing Resales Y/Y: <b>6.3%</b> <sup>1</sup>	Housing resales Y/Y: <b>(3.3)%</b> <sup>1</sup>
National Composite House Price Index change: <b>12.3%</b> <sup>2</sup>	National Composite House Price Index change: <b>-1% to +1%</b> <sup>2</sup>
Average Oil Price: <b>US \$43</b> <sup>3</sup>	Average Oil Price: <b>US \$50 to \$60</b> <sup>3</sup>
5 year Government of Canada Bond Yields: <b>1.11%</b> <sup>4</sup>	5 year Government of Canada Bond Yields: <b>1.30% to 1.50%</b> <sup>4</sup>
GDP Estimate <b>1.3%</b> <sup>5</sup>	GDP Estimate <b>2.1%</b> <sup>5</sup>
Average Unemployment <b>7.0%</b> <sup>6</sup>	Average Unemployment <b>7.0% to 7.5%</b> <sup>6</sup>

### Macroeconomic environment

The Bank of Canada estimates economic growth, as measured by real Canadian Gross Domestic Product ("GDP"), to be 1.3% in 2016 and 2.1% in 2017. The expected improvement in GDP reflects higher oil prices, stronger exports related to a weaker Canadian dollar, steady consumer spending and increased government investment on infrastructure projects, partially offset by lower residential housing demand.

The overnight interest rate in Canada remained flat at 0.50% in 2016 and is not expected to increase in 2017. The 5-year Government of Canada bond yield has risen approximately 50 basis points since October, to 1.11% as at December 2016 in response to global economic events and is expected to continue to rise modestly in 2017.

Canada's unemployment rate was at 6.9% at the end of the fourth quarter of 2016 and averaged 7.0% in 2016. The average oil price for 2016 was US\$43, recovering from its historic low in early 2016. The Company estimates that the average unemployment rate will be between 7.0% and 7.5% for 2017 and oil prices will be in the range of US\$50 and US\$60 for the year.

### Housing market

Home resales for the full year 2016 were up 6.3% as compared to the prior year and the National Composite House Price Index increased by 12.3% in 2016. These increases were driven primarily by strong housing markets in British Columbia and Ontario, partially offset by continued weakness in the oil-producing regions.

The Canadian Real Estate Association expects housing resales to decline by 3.3% in 2017 and the Company expects the National Composite House Price Index for 2017 to be in the range of 1% to -1%. Recently announced federal mortgage rule changes with respect to mortgage insurance qualification and a modest increase in mortgage rates are expected to adversely impact first time homebuyers.

<sup>1</sup> Canadian Real Estate Association ("CREA")

<sup>2</sup> Teranet – National Bank Home Price Index (2016); Management estimate (2017)

<sup>3</sup> U.S. Energy Information Administration - WTI Light Crude Oil US\$/barrel (2016); Management estimate (2017)

<sup>4</sup> Bloomberg

<sup>5</sup> Monetary Policy Report, January 2017; 2016 Real GDP quarter over quarter percentage change at annual rates and 2017 estimate

<sup>6</sup> Statistics Canada – Labour Force Survey (2016); Management estimate (2017).

## 2017 objectives

In pursuit of being Canada's mortgage insurer of choice, the Company seeks to enhance stakeholder value through working with its lender partners, regulators and influencers to:

- Maintain strong claim paying ability and financial strength;
- Help Canadians responsibly achieve and maintain homeownership;
- Promote strong and sustainable communities across Canada; and
- Advance prudent risk management practices to enhance the safety and soundness of the mortgage finance system.

The Company's long term objective is to enhance shareholder value by achieving a return on equity that exceeds its cost of capital and by increasing net income over time. The Company's priorities to achieve its long-term objective are identified below:

### 2017 Objectives

#### Premiums Written and Premiums Earned

##### Moderate decline in premiums written despite expected higher premium rates.

- The Company expects that the transactional market size and its transactional new insurance written in 2017 may decline by approximately 15% to 25% as a result of regulatory changes that took effect in the fourth quarter of 2016. Transactional premiums written are expected to be moderately lower compared to 2016, primarily due to a smaller mortgage originations market partially offset by the average transactional premium rate increase of approximately 18% to 20% which is expected to result in an average transactional premium rate of 330 to 335 basis points for 2017, compared to 293 basis points in 2016.
- Portfolio insurance premiums written are expected to be significantly lower compared to 2016, primarily due to the prohibition on government guaranteed mortgage insurance on refinance mortgages originated after November 30, 2016 and the impact of the July 1, 2016 regulatory change, or purpose test rule, which restricts the use of portfolio mortgage insurance.
- The Company expects that the average premium rate for portfolio insurance will increase substantially as a result of the new capital framework that became effective January 1, 2017.

##### Modest increase in premiums earned due to seasoning of recent books of business

Given the single upfront premium model, the Company is generally able to reliably estimate the proportion of unearned premiums that will be earned into revenues as premiums earned as long as there are no significant changes to the Company's current premiums recognition curve. The Company expects to earn between \$615 and \$625 million of premiums earned in 2017 from the unearned premiums reserve of \$2.1 billion as at December 31, 2016. In addition, premiums earned in 2017 will benefit from the portion of 2017 premiums written that will be earned in 2017.

#### Losses on Claims

##### Proactive risk management and focused loss mitigation strategies:

- Loss ratio range of 25% to 35%
- Workout penetration rate greater than 55%

#### Portfolio Quality and Risk Management

##### Maintain a high quality insurance portfolio through prudent underwriting guidelines, proactive risk management and disciplined underwriting:

- Average transactional credit score of greater than 735
- Average transactional credit score below 660 or less than 5%

#### Capital Management

##### Prudently manage capital to balance capital strength, flexibility and efficiency:

- Ordinary dividend payout ratio of 35% to 45%
- Debt-to-total capital ratio of less than or equal to 15%
- MCT ratio in the range of 160% to 165%

#### Investment Management

##### Optimize investment portfolio to maximize investment yield while maintaining a high quality investment portfolio to minimize the correlation of risk with our insurance in-force.

- Investment income expected to be modestly higher as a result of higher average assets

## Fourth Quarter Review

**Table 2: Results of operations**

(in millions of dollars, unless otherwise specified)	Fourth Quarter						Full Year						
	2016		2015		Change		2016		2015		Change		
	\$	171	\$	213	\$	(42)	\$	760	\$	809	\$	(49)	
Premiums written	\$	171	\$	213	\$	(42)	\$	760	\$	809	\$	(49)	
Premiums earned	\$	164	\$	151	\$	13	\$	638	\$	586	\$	52	
Losses on claims and expenses:													
Losses on claims	29		35		(6)	(17)%	139		122		17	14%	
Expenses	33		27		6	22%	124		108		16	14%	
Total losses on claims and expenses	62		62		-	-	263		230		33	14%	
Net underwriting income	103		90		13	15%	375		356		19	5%	
Investment income:													
Interest and dividend income, net of investment expenses	46		44		2	4%	176		169		7	4%	
Net investment gains	47		3		44	NM	38		32		6	20%	
Investment income	93		47		45	96%	214		201		13	6%	
Interest expense	6		6		-	-	23		23		-	-	
Income before income taxes	190		131		58	44%	566		534		31	6%	
Provision for income taxes	50		34		16	48%	149		136		13	10%	
Net income	\$	140	\$	98	\$	42	43%	\$	417	\$	398	\$	19
Adjustment to net income, net of taxes:													
Net investment (gains) losses	(35)		(3)		(32)	NM	(29)		(23)		(6)	25%	
Net operating income <sup>1</sup>	\$	105	\$	95	\$	10	11%	\$	388	\$	375	\$	13
Effective tax rate	26.1%		25.6%		-	0.6 pts	26.3%		25.4%		-	0.9 pts	
<b>Selected non-IFRS financial measures <sup>1</sup></b>													
Transactional new insurance written	\$	5,120	\$	6,231	\$	(1,111)	(18)%	\$	21,171	\$	25,243	\$	(4,072)
Portfolio new insurance written	\$	4,918	\$	9,595	\$	(4,677)	(49)%	\$	41,881	\$	25,696	\$	16,185
Loss ratio	18%		23%		-	(5) pts	22%		21%		-	1 pts	
Expense ratio	20%		18%		-	2 pts	19%		18%		-	1 pts	
Combined ratio	38%		41%		-	(3) pts	41%		39%		-	2 pts	
Operating return on equity	12%		12%		-	- pts	11%		12%		-	- pts	
Investment yield	3.2%		3.3%		-	(0.1) pts	3.2%		3.3%		-	(0.1) pts	

Note: Amounts may not total due to rounding. NM means Not Meaningful.

<sup>1</sup> These financial measures are not calculated based on IFRS. See the "Non-IFRS financial measures" section at the end of this MD&A for additional information.

**Table 3: New insurance written, premiums written and premiums earned**

<i>(in millions of dollars, unless otherwise specified)</i>	Fourth Quarter				Full Year			
	2016	2015	Change	2016	2015	Change		
<b>New insurance written</b>								
Transactional Portfolio	\$ 5,120	\$ 6,231	\$ (1,111)	(18)%	\$ 21,171	\$ 25,243	\$ (4,072)	(16)%
Portfolio	4,918	9,595	(4,677)	(49)%	41,881	25,696	16,185	63%
Total	<b>\$ 10,038</b>	<b>\$ 15,826</b>	<b>\$ (5,787)</b>	<b>(37)%</b>	<b>\$ 63,051</b>	<b>\$ 50,938</b>	<b>\$ 12,113</b>	<b>24%</b>
<b>Premiums written</b>								
Transactional Portfolio	149	181	(32)	(17)%	619	705	(86)	(12)%
Portfolio	22	32	(10)	(32)%	140	104	37	36%
Total	<b>\$ 171</b>	<b>\$ 213</b>	<b>\$ (42)</b>	<b>(20)%</b>	<b>\$ 760</b>	<b>\$ 809</b>	<b>\$ (49)</b>	<b>(6)%</b>
<b>Average premium rate (in basis points)</b>								
Transactional Portfolio	292	290	2	1%	293	279	14	5%
Portfolio	45	34	11	33%	34	40	(7)	(17)%
Total	<b>171</b>	<b>135</b>	<b>36</b>	<b>27%</b>	<b>121</b>	<b>158</b>	<b>(38)</b>	<b>(24)%</b>
<b>Premiums earned</b>								
	\$ 164	\$ 151	\$ 13	9%	\$ 638	\$ 586	\$ 52	9%

Note: Amounts may not total due to rounding.

#### Current quarter

Transactional new insurance written was \$5.1 billion in the fourth quarter of 2016, representing a decrease of \$1.1 billion, or 18%, as compared to the same quarter in the prior year. This decrease resulted primarily from targeted underwriting changes in select markets and a smaller transactional insurance originations market. New insurance written from portfolio insurance was \$4.9 billion in the fourth quarter of 2016, as compared to \$9.6 billion in the prior year. The volume and mix of portfolio insurance varies from quarter to quarter based on lender demand.

Premiums written from transactional insurance were \$149 million in the fourth quarter of 2016, a decrease of \$32 million, or 17%, as compared to the prior year's period. The \$32 million decrease was primarily due to lower volumes of transactional insurance business. Premiums written from portfolio insurance were \$22 million in the fourth quarter of 2016 as compared to \$32 million in the prior year's period.

Premiums earned increased by \$13 million, or 9%, to \$164 million in the fourth quarter of 2016, as compared to the prior year's period due to the relatively larger contributions from premiums written in 2015 and 2016.

#### Full year

In 2016, transactional new insurance written was \$21.2 billion, a decrease of \$4.1 billion, or 16%, as compared to the prior year primarily as a result of targeted underwriting changes in select markets and a smaller transactional insurance originations market. New insurance written from portfolio insurance was \$41.9 billion in 2016, as compared to \$25.7 billion in the prior year. This increase was driven by higher demand from lenders prior to the July 1, 2016 regulatory changes which generally limits portfolio insurance to only those mortgages that will be used in government securitization programs.

Premiums written from transactional insurance were \$619 million for the full year of 2016, a decrease of \$86 million, or 12%, as compared to the prior year. The \$86 million decrease was primarily due to lower volumes of transactional insurance, partially offset by a 5% increase in the average premium rate to 2.93% as a result of the June 2015 premium rate increase. Premiums written from portfolio insurance were \$140 million in 2016, an increase of \$37 million or 36%, due to higher volumes of portfolio insurance. The average portfolio insurance premium rate of 0.34% in 2016 reflects the high quality portfolio and higher proportion of portfolio insured mortgages with loan-to-values below 65%.

Premiums earned increased by \$52 million, or 9%, to \$638 million in 2016, as compared to the prior year due to higher premiums earned from the relatively larger contributions from the 2014, 2015 and 2016 books of business.

**Table 4: Losses on claims**

	Fourth Quarter				Full Year			
	2016	2015	Change		2016	2015	Change	
New delinquencies	1,228	1,198	30	3%	4,940	4,466	474	11%
Cures	792	711	81	11%	3,091	2,788	303	11%
New delinquencies, net of cures	436	487	(51)	(10)%	1,849	1,678	171	10%
<b>Average reserve per delinquency</b> (in thousands of dollars)	\$ 79	\$ 72	\$ 7	10%	\$ 79	\$ 72	\$ 7	10%
<b>Losses on claims</b> (in millions of dollars)	\$ 29	\$ 35	\$ (6)	(17)%	\$ 139	\$ 122	\$ 17	14%
<b>Loss ratio</b>	18%	23%	-	(5) pts	22%	21%	-	1 pts

Note: Amounts may not total due to rounding.

#### Current quarter

New delinquencies, net of cures, of 436 were 51 lower than the same quarter in the prior year primarily due to a decrease of 65 largely from non-oil producing regions of Canada, partially offset by a modest increase of 14 in Alberta. The decrease of 65 new delinquencies net of cures included 28 in Québec, 18 in the Pacific region and 14 in Ontario, which was consistent with strong or improving economic conditions in these regions. The Atlantic region decreased marginally by 5 and the Prairies region did not change. The increase of 14 delinquencies in Alberta consisted of an increase in new reported delinquencies of 127 due to economic and housing market pressure which was largely offset by an increase in cures of 113.

Average reserve per delinquency increased by approximately \$7 thousand primarily due to a shift in regional mix towards oil-producing regions with higher average insured amounts and modest declines in house prices.

The resulting loss ratio was 18% in the fourth quarter of 2016, 5 percentage points lower than the same period in the prior year due to lower losses on claims and higher earned premium.

#### Full year

In 2016, new delinquencies, net of cures, of 1,849 were 171 higher than the prior year primarily due to pressure in oil-producing regions with an increase of 391 in Alberta, 82 in the Prairies region, and 2 in the Atlantic region, partially offset by a decrease of 137 in Ontario, 99 in Québec and 68 in the Pacific region consistent with strong or improving economic conditions in these regions.

Average reserve per delinquency increased by approximately \$7 thousand primarily due to a shift in regional mix towards oil-producing regions with higher average insured amounts and modest declines in house prices, partially offset by favourable development from Québec case reserves related to improving economic conditions in this region.

The resulting loss ratio was 22% in 2016, 1 percentage point higher than the prior year due to higher losses on claims partially offset by higher earned premium.

**Table 5: Expenses**

(in millions of dollars, unless otherwise specified)	Fourth Quarter						Full Year					
	2016		2015		Change		2016		2015		Change	
<b>Expenses</b>												
Premium taxes and underwriting fees	\$ 13	\$ 15	\$ (2)	(13)%	\$ 58	\$ 60	\$ (2)	(3)%				
Employee compensation	12	9	3	36%	49	40	9	23%				
Other	9	8	1	10%	30	29	1	4%				
Expenses before net change in deferred policy acquisition costs	34	32	2	6%	138	129	9	7%				
Net change in deferred policy acquisition costs	(1)	(5)	4	(75)%	(14)	(21)	7	(34)%				
<b>Total</b>	<b>\$ 33</b>	<b>\$ 27</b>	<b>\$ 6</b>	<b>22%</b>	<b>\$ 124</b>	<b>\$ 108</b>	<b>\$ 16</b>	<b>14%</b>				
<b>Expense ratio</b>	<b>20%</b>	<b>18%</b>	-	2 pts	<b>19%</b>	<b>18%</b>	-	1 pts				

Note: Amounts may not total due to rounding.

### Current quarter

Expenses, before net change in deferred policy acquisition costs, increased by \$2 million, or 6%, to \$34 million in the fourth quarter of 2016 as compared to the same quarter in the prior year. The increase was primarily due to a \$3 million increase in employee compensation, including higher share based compensation, and a moderate increase in other expenses of \$1 million, which consists primarily of professional fees and office expenses, partially offset by a \$2 million decrease in premium taxes and underwriting fees related to lower levels of premiums written. Total expenses increased by \$6 million primarily due to a \$4 million increase in the net change in deferred policy acquisition costs, largely from the amortization of previously deferred policy acquisition costs in line with higher premiums earned and the increase in non-deferrable expenses including share based compensation in the current quarter.

The expense ratio increased 2 percentage points to 20% for the fourth quarter of 2016, as compared to the same quarter in the prior year due to higher expenses, partially offset by higher earned premium.

### Full year

Expenses before net change in deferred policy acquisition costs increased by \$9 million, or 7%, to \$138 million in 2016 as compared to the prior year. The increase was primarily due to a \$9 million increase in employee compensation, including higher share based compensation, and a moderate increase in other expenses of \$1 million, which consists primarily of professional fees and office expenses, partially offset by a \$2 million decrease in premium taxes and underwriting fees related to lower levels of premiums written. Total expenses increased by \$16 million due to a \$7 million increase in the net change in deferred policy acquisition costs, largely from the amortization of previously deferred policy acquisition costs in line with higher premiums earned and the increase in non-deferrable expenses including share based compensation expense.

The expense ratio increased 1 percentage point to 19% in 2016 as compared to the prior year due to higher expenses partially offset by higher earned premium.

**Table 6: Investment income**

(in millions of dollars, unless otherwise specified)	Fourth Quarter				Full Year			
	2016	2015	Change	2016	2015	Change		
Interest and dividend income, net of investment expenses	\$ 46	\$ 44	\$ 2	4%	\$ 176	\$ 169	\$ 7	4%
Net realized gains / (losses) on sale of investments	1	(2)	3	NM	3	23	(20)	(87)%
Net gains on derivatives and foreign exchange	46	5	41	NM	38	9	29	NM
Impairment loss	-	-	-	NM	(3)	-	(3)	NM
<b>Investment income</b>	<b>\$ 93</b>	<b>\$ 47</b>	<b>\$ 45</b>	<b>95%</b>	<b>\$ 214</b>	<b>\$ 201</b>	<b>\$ 13</b>	<b>6%</b>
<b>Invested assets, end of period</b>	<b>\$ 6,226</b>	<b>\$ 5,917</b>	<b>\$ 309</b>	<b>5%</b>	<b>\$ 6,226</b>	<b>\$ 5,917</b>	<b>\$ 309</b>	<b>5%</b>
<b>Investment yield, average over period</b>	<b>3.2%</b>	<b>3.3%</b>	<b>-</b>	<b>(0.1) pts</b>	<b>3.2%</b>	<b>3.3%</b>	<b>-</b>	<b>(0.1) pts</b>

Note: Amounts may not total due to rounding. NM means Not Meaningful.

#### Current quarter

Interest and dividend income, net of investment expenses, increased by \$2 million, or 4%, to \$46 million in the fourth quarter of 2016, primarily due to an increased level of invested assets and higher dividend income, partially offset by the impact of the low interest rate environment on the reinvestment of fixed income maturities. The average investment yield for the quarter was 3.2%, as compared to 3.3% in the prior year's period. Invested assets increased by \$309 million as a result of premiums written in 2016.

The Company recorded \$1 million of net realized gains in the fourth quarter of 2016 primarily due to the sale of fixed income securities as compared to \$2 million of net realized loss in the same period in the prior year.

Net gains on derivatives and foreign exchanges were \$46 million in the fourth quarter of 2016, as compared to \$5 million in the same period in the prior year, an increase of \$41 million. The increase is primarily from the impact of movement in interest rates on the Company's interest rate swaps as well as movement in foreign exchange rates on the Company's invested assets denominated in U.S. dollars partially offset by foreign exchange-related derivatives activity. These gains are largely offset by decreases in fair value of available for sale assets in OCI.

#### Full year

Interest and dividend income, net of investment expenses, increased by \$7 million, or 4%, to \$176 million in 2016, primarily due to an increased level of invested assets and higher dividend income, partially offset by the impact of the low interest rate environment on the reinvestment of fixed income maturities as compared to the prior year. The average investment yield for 2016 was 3.2%, as compared to 3.3% in the prior year. Invested assets increased by \$309 million as a result of premiums written in 2016.

The Company recorded \$3 million of realized gains in 2016 primarily from the sales of fixed income securities as compared to \$23 million of realized gains, primarily from the sale of its common shares holdings, in the prior year.

Net gains on derivatives and foreign exchanges were \$38 million in 2016, as compared to \$9 million in the prior year, an increase of \$29 million. The increase is primarily from the impact of movement in interest rates on the Company's interest rate swaps and foreign exchange-related derivatives activity partially offset by movement in foreign exchange rates on the Company's invested assets denominated in U.S. dollars.

The Company also recorded an impairment loss of \$3 million on a Brazilian bond.

**Table 7: Net Income**

<i>(in millions of dollars, unless otherwise specified)</i>	Fourth Quarter						Full Year									
	2016		2015		Change		2016		2015		Change					
	\$	190	\$	131	\$	58	44%	\$	566	\$	534	\$	31	6%		
Income before income taxes	\$	190	\$	131	\$	58	44%	\$	566	\$	534	\$	31	6%		
Provision for income taxes	50		34		16		48%	149		136		13	10%			
<b>Net income</b>	<b>\$</b>	<b>140</b>	\$	98	\$	42	43%	\$	417	\$	398	\$	19	5%		
Effective tax rate	26.1%		25.6%		-		0.6 pts		26.3%		25.4%		-		0.9 pts	

Note: Amounts may not total due to rounding.

#### Current quarter

The effective tax rate was 26.1% in the fourth quarter of 2016, an increase of approximately 0.6 percentage points from 25.6% in the prior year's period. The increase was primarily the result of an increase in tax rates in certain provinces and higher non-deductible items partially offset by higher non-taxable dividend income in the current year's period.

Net income increased by \$42 million, or 43%, to \$140 million, primarily as a result of higher investment income, higher earned premium and lower losses on claims partially offset by higher expenses.

#### Full year

The effective tax rate was 26.3% in 2016, an increase of approximately 0.9 percentage points from 25.4% in the prior year. The increase was primarily the result of an approximately \$5 million favourable non-recurring tax adjustment related to prior years that was recorded in the first quarter of 2015, an increase in tax rates in certain provinces in 2016, and higher non-deductible items partially offset by higher non-taxable dividend income in 2016.

Net income increased by \$19 million, or 5%, to \$417 million, in 2016 primarily as a result of higher earned premium and higher investment income, partially offset by higher losses on claims, higher expenses, and the prior period favourable tax adjustment.

## Summary of annual information

Table 8 presents select income statement line items and certain key performance indicators for the last three years.

**Table 8: Summary of Annual Information**

<i>(in millions of dollars, unless otherwise specified)</i>	<b>2016</b>	<b>2015</b>	<b>2014</b>
Net premiums written	<b>\$760</b>	\$809	\$640
Net premiums earned	<b>638</b>	586	565
Losses on claims	<b>139</b>	122	111
Expenses	<b>124</b>	108	107
Net underwriting income	<b>375</b>	356	346
Investment income	<b>214</b>	201	195
Net income	<b>417</b>	398	377
Adjustment to net income net of taxes:			
Fee on early redemption of long term debt	-	-	5
Net investment gains	<b>(29)</b>	(23)	(16)
Net operating income <sup>1</sup>	<b>\$388</b>	\$375	\$366
<b>Earnings per common share:</b>			
Earnings per common share (basic)	<b>\$4.54</b>	\$4.32	\$3.97
Earnings per common share (diluted)	<b>\$4.54</b>	\$4.22	\$3.97
<b>Selected non-IFRS financial measures<sup>1</sup></b>			
Loss ratio	<b>22%</b>	21%	20%
Expense ratio	<b>19%</b>	18%	19%
Combined ratio	<b>41%</b>	39%	39%
Operating earnings per common share (basic) <sup>2</sup>	<b>\$4.23</b>	\$4.07	\$3.86
Operating earnings per common share (diluted) <sup>2</sup>	<b>\$4.23</b>	\$4.05	\$3.86
Operating return on equity	<b>11%</b>	12%	12%

Note: Amounts may not total due to rounding

<sup>1</sup>The financial measures are not calculated based on IFRS. See the “Non-IFRS financial measures” section at the end of this MD&A for additional information.

<sup>2</sup>The difference between basic and diluted earnings per common share and basic and diluted operating earnings per common share is caused by the potentially dilutive impact of share-based compensation awards.

**Table 9: Statement of Financial Position Highlights**

<i>(in millions of dollars, unless otherwise specified)</i>	2016	2015	2014
Total investments	<b>\$6,226</b>	\$5,917	\$5,443
Other assets	<b>319</b>	261	260
Subrogation recoverable	<b>67</b>	61	67
<b>Total assets</b>	<b>6,612</b>	6,239	5,770
Unearned premiums reserves	<b>2,143</b>	2,021	1,799
Loss reserves	<b>163</b>	132	115
Long-term debt	<b>433</b>	433	432
Other liabilities	<b>224</b>	234	153
<b>Total liabilities</b>	<b>2,963</b>	2,819	2,499
Shareholders' equity excluding Accumulated other comprehensive income ("AOCI")	<b>3,556</b>	3,293	3,086
AOCI	<b>93</b>	127	185
<b>Shareholders' equity</b>	<b>3,649</b>	3,420	3,271
<b>Total liabilities and shareholders' equity</b>	<b>6,612</b>	6,239	5,770
<b>Book value per common share</b>			
Number of common shares outstanding (basic)	<b>91,864,100</b>	91,795,125	93,147,778
Book value per common share including AOCI (basic)	<b>\$39.72</b>	\$37.26	\$35.12
Book value per common share excluding AOCI (basic)	<b>\$38.71</b>	\$35.88	\$33.13
Number of common shares outstanding (diluted) <sup>1</sup>	<b>92,885,377</b>	92,872,626	93,403,036
Book value per common share including AOCI (diluted) <sup>1</sup>	<b>\$39.28</b>	\$36.82	\$35.02
Book value per common share excluding AOCI (diluted) <sup>1</sup>	<b>\$38.28</b>	\$35.46	\$33.04
<b>Dividends paid per common for the full year ended</b>	<b>\$1.70</b>	\$1.59	\$1.87

Note: Amounts may not total due to rounding.

<sup>1</sup> The difference between basic and diluted number of common shares outstanding, book value per common share including AOCI and book value per common share excluding AOCI is caused by the potentially dilutive impact of share-based compensation awards.

## Summary of quarterly results

**Table 10: Summary of quarterly results**

(in millions of dollars, unless otherwise specified)	Q4'16	Q3'16	Q2'16	Q1'16	Q4'15	Q3'15	Q2'15	Q1'15
Premiums written	<b>\$ 171</b>	\$ 223	\$ 249	\$ 117	\$ 213	\$ 260	\$ 205	\$ 130
Premiums earned	<b>\$ 164</b>	162	158	154	151	148	144	143
Losses on claims	<b>29</b>	41	32	37	35	31	25	31
Expenses	<b>33</b>	33	30	28	27	28	29	24
Net underwriting income	<b>103</b>	88	95	88	90	89	90	87
Investment Income	<b>93</b>	52	33	37	47	39	58	57
Net income	<b>140</b>	98	91	88	98	90	103	107
Adjustment to net income net of taxes:								
Net investment (gains) losses	<b>(35)</b>	(5)	8	3	(3)	3	(12)	(11)
Net operating income <sup>1</sup>	<b>\$ 105</b>	\$ 93	\$ 99	\$ 91	\$ 95	\$ 92	\$ 92	\$ 97
<b>Earnings per common share:</b>								
Earnings per common share (basic)	<b>\$1.52</b>	\$ 1.07	\$ 0.99	\$ 0.96	\$ 1.06	\$ 0.98	\$ 1.12	\$ 1.15
Earnings per common share (diluted) <sup>2</sup>	<b>\$1.52</b>	\$ 1.07	\$ 0.99	\$ 0.96	\$ 1.03	\$ 0.96	\$ 1.12	\$ 1.08
<b>Selected non-IFRS financial measures <sup>1</sup></b>								
Loss ratio	<b>18%</b>	25%	21%	24%	23%	21%	17%	22%
Expense ratio	<b>20%</b>	20%	19%	19%	18%	19%	20%	17%
Combined ratio	<b>38%</b>	45%	40%	42%	41%	40%	37%	39%
Operating earnings per common share (basic)	<b>\$1.15</b>	\$ 1.02	\$ 1.07	\$ 1.00	\$ 1.04	\$ 1.01	\$ 0.99	\$ 1.04
Operating earnings per common share (diluted) <sup>2</sup>	<b>\$1.14</b>	\$ 1.02	\$ 1.07	\$ 0.99	\$ 1.03	\$ 1.00	\$ 0.99	\$ 1.03
<b>Operating return on equity</b>	<b>12%</b>	11%	12%	11%	12%	12%	12%	12%

Note: Amounts may not total due to rounding.

<sup>1</sup> These financial measures are not calculated based on IFRS. See the “Non-IFRS financial measures” section at the end of this MD&A for additional information.

<sup>2</sup> The difference between basic and diluted earnings per common share and basic and diluted operating earnings per common share is caused by the potentially dilutive impact of share-based compensation awards.

The Company's key financial measures for each of the last eight quarters are summarized in table 10 above. These highlights illustrate the Company's profitability, return on equity, loss ratio, expense ratio and combined ratio. The transactional mortgage insurance business is seasonal. Premiums written vary each quarter, while premiums earned, investment income, underwriting and administrative expenses tend to be relatively stable from quarter to quarter. The variations in premiums written are driven by mortgage origination activity and associated mortgage insurance policies written, which typically peak in the spring and summer months, in addition to changes in market share and premium rates. Portfolio mortgage insurance volume and mix varies from quarter to quarter based on lender demand. Losses on claims vary from quarter to quarter, primarily as the result of prevailing economic conditions and characteristics of the insurance in-force portfolio, such as loan size, age, seasonality and geographic mix of delinquencies. Typically, losses on claims increase during the winter months, due primarily to an increase in new delinquencies, and decrease during the spring and summer months. In the third quarter of 2016, losses increased significantly from the prior quarter, and the same quarter in the prior year, primarily due to an increase in new delinquencies in Alberta specifically related to wild fires in the Fort McMurray area. In the fourth quarter of 2016 losses, decreased from the prior quarter, and the same quarter in the prior year, primarily due to an increase in cures in Alberta.

The Company's financial results for the fourth quarter of 2016 were driven by increasing premiums earned in recent quarters, a relatively consistent expense ratio and a lower loss ratio compared to the prior year.

## Reserve development analysis

Table 11 below shows the one-year development of the Company's loss reserves for the five most recent completed years.

**Table 11: Reserve Development Analysis**

<i>(in millions, unless otherwise specified)</i>	As at December 31				
	2016	2015	2014	2013	2012
Total loss reserves, at the beginning of the year	\$132	\$115	\$118	\$139	\$169
Loss reserves for prior years' delinquent loans, remaining at the end of the year (A)	22	23	16	10	26
Change in loss reserves for prior years' delinquent loans	109	93	101	129	143
Paid claims for prior years' delinquent loans	(91)	(82)	(94)	(139)	(193)
Favourable (unfavourable) development	\$18	\$11	\$7	(\$10)	(\$51)
As a percentage of total loss reserves, at the beginning of the year	14%	10%	7%	-7%	-30%
Loss reserves for current year's delinquent loans, at the end of the year (B)	141	109	99	108	113
<b>Total loss reserves at the end of the year (A+B)</b>	<b>\$163</b>	<b>\$132</b>	<b>\$115</b>	<b>\$118</b>	<b>\$139</b>

Note: Amounts may not total due to rounding.

The Company's loss-reserving methodology, including reserve development, is reviewed on a quarterly basis and incorporates the most current available information. The Company's outstanding reserves represent the Company's current best estimate of the ultimate cost of settling claims, in each case as of the date such reserves are established and based on the information available at such time.

The Company experienced favourable reserve development in 2016 of \$18 million, or 14% of the total loss reserves at the beginning of the year. The province of Québec experienced \$11 million of the favourable development due to improving economic conditions. Favourable development also occurred in Ontario and the Pacific and Atlantic regions offsetting modest unfavorable development in Alberta and the Prairies.

The Company regularly reviews the underlying drivers of its loss reserves development and adjusts its reserving practices accordingly.

## Financial condition

### Financial instruments

As at December 31, 2016, the Company had total cash and cash equivalents and invested assets of \$6.2 billion in its investment portfolio. All of the Company's invested assets are classified as available-for-sale ("AFS") with the exception of cash and cash equivalents, and accrued investment income and other receivables which are classified as loans and receivables, and derivative financial instruments which are classified as Fair Value through Profit and Loss. Fair value measurements for AFS securities are based on quoted market prices for identical assets when available. In the event an active market does not exist, estimated fair values are obtained primarily from industry-standard pricing sources using market observable information and through processes such as benchmark curves, benchmarking of like securities and quotes from market participants.

**Table 13: Invested assets by asset class for the portfolio**

Asset Class (in millions of dollars, unless otherwise specified)	As at December 31, 2016			As at December 31, 2015		
	Fair value	%	Unrealized gains <sup>2</sup> (losses)	Fair value	%	Unrealized gains <sup>2</sup> (losses)
Collateralized loan obligations	\$ 207	3%	\$ 27	\$ 178	3%	\$ 32
Corporate bonds and debentures:						
Financial	910	15%	24	923	16%	33
Energy	356	6%	19	264	4%	18
Infrastructure	101	2%	5	117	2%	7
All other sectors	930	15%	56	733	12%	65
Total corporate bonds and debentures	2,297	37%	105	2,037	34%	124
Short-term investments:						
Canadian federal government treasury bills <sup>1</sup>	206	3%	-	78	1%	-
Total short term investments	206	3%	-	78	1%	-
Government bonds and debentures:						
Canadian federal government <sup>1</sup>	1,976	32%	45	1,963	33%	79
Canadian provincial and municipal governments	988	16%	55	1,023	17%	74
Total government bonds and debentures	2,964	48%	100	2,986	50%	152
Preferred shares:						
Financial	247	4%	(16)	155	3%	(20)
Energy	80	1%	1	33	1%	(6)
All other sectors	99	2%	(4)	59	1%	(7)
Total preferred shares	426	7%	(19)	248	4%	(33)
Total invested assets	\$ 6,100	98%	\$ 212	\$ 5,527	93%	\$ 276
Cash and cash equivalents	126	2%	-	391	7%	-
Total investments	\$ 6,226	100%	\$ 212	\$ 5,917	100%	\$ 276
Accrued investment income and other receivables	47	-	-	28	-	-
Derivative financial instruments (assets)	39	-	-	-	-	-
Total Invested assets, accrued investment income and other receivables	\$ 6,312	-	-	\$ 5,946	-	-
Derivative financial instruments (liabilities)	(43)	-	-	(84)	-	-
Total Invested assets, accrued investment income and net derivative financial instruments	\$ 6,269	-	-	\$ 5,862	-	-

Note: Amounts may not total due to rounding.

<sup>1</sup> Canadian federal government bonds and treasury bills includes \$3 million (December 31, 2015 - \$85 million) in collateral posted for the benefit of the Company's counterparties to its derivative financial instrument contracts.

<sup>2</sup> Unrealized gains include unrealized foreign exchange gains of \$79 million (December 31, 2015- \$97 million).

Unrealized gains on AFS securities in the portfolio were \$212 million, which included \$79 million of unrealized foreign exchange gains. Unrealized gains decreased by \$64 million from the end of 2015 primarily as a result of rising interest rates during 2016 leading to a decline in the value of fixed income securities partially offset by an increase in preferred share values.

The Company's average investment yield for the fourth quarter of 2016 and full year was 3.2%, which included the favourable impact of non-taxable dividend income from its preferred shares.

The Company assigns credit ratings based on the asset risk guideline as outlined in OSFI's Interim Capital Requirements for Mortgage Insurance Companies, Minimum Capital Test Guideline effective January 1, 2015. Based on this guideline, the Company assigns ratings from DBRS when available. The majority of the assets in the Company's current investment portfolio have a DBRS rating. In the absence of a DBRS rating, the Company assigns S&P or Moody's ratings.

**Table 14: Invested assets by credit rating for the portfolio**

<b>Credit Rating</b> <i>(in millions of dollars, unless otherwise specified)</i>	<b>As at December 31, 2016</b>			<b>As at December 31, 2015</b>		
	<b>Fair value</b>	<b>%</b>	<b>Unrealized gains (losses)</b>	<b>Fair value</b>	<b>%</b>	<b>Unrealized gains (losses)</b>
Cash and cash equivalents	\$ 126	2%	\$ -	\$ 391	7%	-
AAA	2,262	39%	49	2,160	38%	90
AA	1,164	20%	75	1,024	18%	93
A	1,687	29%	66	1,703	30%	87
BBB	539	9%	37	387	7%	37
Below BBB	22	0%	4	5	-	1
Total investments (excluding preferred shares)	\$ 5,800	100%	\$ 231	\$ 5,670	100%	308
Preferred shares						
P2	338	79%	(19)	227	92%	(32)
P3	88	21%	-	20	8%	(1)
Total Preferred shares	426	100%	(19)	248	100%	(33)
Total invested assets and cash and cash equivalents	\$ 6,226		\$ 212	\$ 5,917		276

Note: Amounts may not total due to rounding.

### **Investment portfolio management**

The Company manages its portfolio assets to meet liquidity, credit quality, diversification and yield objectives by investing primarily in fixed income securities, including federal and provincial government bonds, corporate bonds and preferred shares. The Company also holds short-term investments. In all cases, investments are required to comply with restrictions imposed by law and insurance regulatory authorities as well as the Company's own investment policy, which has been approved by the Board.

To diversify management styles and to broaden credit expertise, the Company has split these assets primarily among five external investment managers. The Company works with these managers to optimize the performance of the portfolios within the parameters of the stated investment objectives outlined in its investment policy. The policy takes into account the current and expected condition of capital markets, the historical return profiles of various asset classes and the variability of those returns over time, the availability of assets, diversification needs and benefits, the regulatory capital required to support the various asset types, security ratings and other material variables likely to affect the overall performance of the Company's investment portfolio. Compliance with the investment policy is monitored by the Company and reviewed at least quarterly with the Company's management-level investment committee and the Risk, Capital and Investment Committee of the Board.

### **Collateralized loan obligations**

The Company held \$207 million in asset-backed bonds as of December 31, 2016, up from \$178 million as of December 31, 2015. These securities are floating rate collateralized loan obligations ("CLOs") denominated in U.S. dollars, of which 89% are rated AA and above and 11% are rated A.

### **Corporate bonds and debentures**

As of December 31, 2016, approximately 37% of the investment portfolio was held in corporate bonds and debentures, up from 34% at December 31, 2015. The investment policy limits the percentage of the portfolio that can be invested in any single issuer or group of related issuers. Financial sector exposure through corporate bonds and debentures represents 15% of the investment portfolio, or approximately 40% of the corporate bonds and debentures. The Company continuously monitors and repositions its exposure to the financial sector, which represents greater than 35% of the corporate issuances of fixed income securities in the Canadian marketplace. Energy sector exposure through corporate bonds and debentures represents \$356 million or 6% of the investment portfolio, of which approximately \$104 million, or 29%, are energy producers who have a direct price movement correlation to the underlying movement of energy pricing.

Securities rated BBB and below were \$561 million, or 9% of invested assets, as of December 31, 2016.

### **Government bonds and debentures**

The Company's investment policy requires that a minimum of 30% of the investment portfolio be invested in sovereign fixed income securities. As of December 31, 2016, 48% of the investment portfolio was invested in sovereign fixed income securities, consisting of 32% in federal fixed income securities and 16% in provincial fixed income securities, as compared to 50% as of December 31, 2015.

Canadian federal government treasury bills held by the Company consist primarily of short-term investments with original maturities greater than 90 days and less than 365 days. The Company held \$206 million in Canadian federal government short-term treasury bills in the investment portfolio as of December 31, 2016 as compared to \$78 million as of December 31, 2015.

### **Preferred shares**

As of December 31, 2016, the Company held \$426 million of preferred shares, of which the financial sector represented 58%. The Company believes that preferred shares have a comparable dividend yield to common shares and offer a more attractive risk and capital adjusted return profile to that of common shares under the current MCT guidelines. As a result of an increase in interest rates in 2016, the unrealized loss of \$33 million at the end of December 31, 2015 declined to \$19 million at the end of December 31, 2016. Energy sector exposure through preferred shares represents \$80 million or 1% of the investment portfolio, of which approximately \$11 million, or 13%, are energy producers who have a direct price movement correlation to the underlying movement of energy pricing.

### **Cash and cash equivalents**

Cash and cash equivalents consist primarily of cash in bank accounts and government treasury bills with original maturities of 90 days or less. The Company determines its target cash holdings based on near-term liquidity needs, market conditions and perceived favourable future investment opportunities. The Company's cash holdings in the investment portfolio were \$126 million as of December 31, 2016, a decrease of \$265 million from the \$391 million in cash holdings as of December 31, 2015. The decrease was primarily due to cash holdings in the fourth quarter of 2015 being higher as a result of the timing of investment maturities.

## Liquidity

The purpose of liquidity management is to ensure there is sufficient cash to meet all of the Company's financial commitments and obligations. The Company has six primary sources of funds, consisting of premiums written from operations, investment income, cash and short-term investments, investment maturities or sales, proceeds from the issuance of debt and equity and a revolving credit facility. The Company believes it has the flexibility to obtain, from current cash holdings and ongoing operations, the funds needed to fulfill its cash requirements during the current financial year and in the future financial years.

**Table 15: Summary of the Company's cash flows**

<i>(in millions of dollars)</i>	<b>Twelve months ended December 31,</b>	
	<b>2016</b>	<b>2015</b>
<b>Cash provided by (used in):</b>		
Operating activities	\$ 544	\$ 653
Financing activities	(155)	(195)
Investing activities	(654)	(258)
Change in cash and cash equivalents	(265)	200
<b>Cash and cash equivalents, beginning of period</b>	<b>391</b>	190
<b>Cash and cash equivalents, end of period</b>	<b>\$ 126</b>	<b>\$ 391</b>

Note: Amounts may not total due to rounding.

The Company generated \$544 million of cash flows from operating activities in 2016, as compared to \$653 million in the prior year. Cash flow from operations in the current period were primarily the result of strong levels of premiums written, and interest income and dividends received on invested assets. As compared to the prior year, premiums written were moderately lower.

The Company utilized \$155 million of cash flows for financing activities in 2016, primarily related to the payment of ordinary dividends of \$1.70 per common share in 2016 as compared to \$195 million primarily related to the payment of ordinary dividends of \$1.59 per common share in 2015 as well as a \$50 million repurchase of common shares under its NCIB in the prior year's period.

The Company utilized \$654 million of cash flows from investing activities in 2016, primarily from the purchase of bonds and debentures, preferred shares and short-term investments, as compared to \$258 million in the prior year's period.

The Company maintains a portion of its investment portfolio in cash and liquid securities to meet working capital requirements and other financial commitments. As of December 31, 2016, the Company held liquid assets of \$821 million, comprised of \$126 million in cash and cash equivalents, and \$695 million in bonds and debentures maturing within one year in order to maintain financial flexibility. Of the \$821 million liquid assets, \$180 million were held outside of the Insurance Subsidiary. As at December 31, 2016, the duration of the fixed income portfolio was 3.8 years.

In addition to cash and cash equivalents, 51%, or \$3,170 million, of the Company's investment portfolio comprises federal and provincial government securities for which there is a highly liquid market. Funds are used primarily for operating expenses, claims payments, and interest expense, as well as dividends and other distributions to shareholders. Potential liquidity risks are discussed in more detail in the "Risk Factors" section of the Company's AIF.

The Company leases office space, office equipment, computer equipment and automobiles. Future minimum rental commitments for non-cancellable leases with initial or remaining terms of one year or more, long-term debt, accounts payable and accrued liabilities and loss reserves, consist of the following at December 31, 2016:

**Table 16: Summary of the Company's contractual obligations**

	Payment dates due by period ( <i>in millions</i> )				
	1 year or less	1–3 years	3–5 years	Over 5 years	Total
Long-term debt <sup>1</sup>	—	—	\$275	\$160	\$435
Accounts payable and accrued liabilities	\$65	—	—	—	\$65
Operating leases	\$3	\$10	—	—	\$12
Loss reserves	\$135	\$29	—	—	\$163
<b>Total contractual obligations</b>	<b>\$203</b>	<b>\$39</b>	<b>\$275</b>	<b>\$160</b>	<b>\$676</b>

Note: Amounts may not total due to rounding.

<sup>1</sup> See "Debt outstanding" section below for more details.

Operating lease expense for 2016 was \$3 million, consistent with the prior year.

## Derivative financial instruments

Derivative financial instruments are used by the Company for hedging purposes and for the purpose of modifying the risk profile of the Company's investment portfolio, subject to exposure limits specified within the Company's investment policy guidelines, which have been approved by the Board.

The Company uses foreign currency forwards and cross currency interest rate swaps to mitigate foreign currency risk associated with bonds and collateralized loan obligations denominated in U.S. dollars. Foreign currency forwards and cross currency interest rate swaps are contractual obligations to exchange one currency for another at a predetermined future date.

The Company uses equity total return swaps to hedge a portion of its economic exposure from the changes in fair market value of the Company's common shares in relation to risks associated with share-based compensation expense.

The Company uses fixed for floating interest rate swaps in conjunction with the management of interest rate risk related to its fixed income securities. The interest rate swaps are derivative financial instruments in which the Company and its counterparty agree to exchange interest rate cash flows based on a specified notional amount from a fixed rate to a floating rate.

**Table 17: Fair value and notional amounts of derivatives by terms of maturity, in Canadian dollars**

	Notional Amount ( <i>in millions</i> )							
	Derivative Asset	Derivative Liability	Net Fair value	1 year or less	1–3 years	3–5 years	Over 5 years	Total
<b>December 31, 2016</b>								
Foreign currency forwards	-	\$(35)	\$(35)	\$161	\$24	\$50	\$187	\$422
Cross currency interest rate swaps	-	\$(7)	\$(7)	\$19	\$39	\$71	\$142	\$271
Equity total return swaps	\$1	-	\$1	\$21	-	-	-	\$21
Interest rate swaps	\$38	-	\$38	-	-	\$2,000	-	\$2,000
<b>Total</b>	<b>\$39</b>	<b>\$(43)</b>	<b>\$(4)</b>	<b>\$201</b>	<b>\$63</b>	<b>\$2,121</b>	<b>\$329</b>	<b>\$2,714</b>
<b>December 31, 2015</b>								
Foreign currency forwards	-	\$(45)	\$(45)	\$14	\$26	\$36	\$213	\$289
Cross currency interest rate swaps	-	\$(37)	\$(37)	\$144	\$28	\$19	\$34	\$225
Equity total return swaps	-	\$(2)	\$(2)	\$20	-	-	-	\$20
<b>Total</b>	<b>-</b>	<b>\$(84)</b>	<b>\$(84)</b>	<b>\$177</b>	<b>\$54</b>	<b>\$55</b>	<b>\$247</b>	<b>\$533</b>

Note: Amounts may not total due to rounding.

## Capital expenditures

The Company's capital expenditures primarily relate to technology investments aimed at improving operational efficiency and effectiveness for sales, underwriting, risk management and loss mitigation. In 2016, the Company invested approximately \$5 million in underwriting, loss mitigation and risk management technologies enhancements. The Company expects that future capital expenditures will continue to be allocated to underwriting, loss mitigation, and risk management technology improvements. The Company expects that capital expenditures in 2017 will be in the \$3 million to \$5 million range and it is anticipated that such expenditures will be funded primarily from operating cash flows.

## Capital management

### Minimum capital test

The Insurance Subsidiary is regulated by OSFI. Under the MCT, an insurer calculates a ratio of capital available to capital required in a prescribed manner. Mortgage insurers are required to maintain a minimum ratio of regulatory capital available, as defined for MCT purposes, to capital required.

Under PRMHIA, the minimum MCT ratio for the Insurance Subsidiary was 175% for 2016. In conjunction with this requirement, the Insurance Subsidiary established an internal MCT target capital ratio of 185%. The Company manages its capital base to maintain a balance between capital strength, efficiency and flexibility. As at December 31, 2016, the Insurance Subsidiary's MCT ratio was approximately 245%, 25 percentage points higher than the Company's holding target of 220%.

Capital above the amount required to meet the Insurance Subsidiary's MCT operating targets could be used to support organic growth of the business or declaration and payment of dividends or other distributions, and if distributed to Genworth Canada, to repurchase common shares of the Company, for acquisitions, for repayment of debt, or for such other uses as permitted by law and approved by the Board.

**Table 18: MCT as at December 31, 2016 and as at December 31, 2015**

<i>(in millions, unless otherwise specified)</i>	As at December 31, 2016	As at December 31, 2015
<b>Minimum Capital Test</b>		
Capital available	<b>\$3,827</b>	\$3,633
Capital required	<b>\$1,560</b>	\$1,552
MCT ratio	<b>245%</b>	234%

The Company's MCT estimate as at December 31, 2016 of 245% was 11 percentage points higher than the MCT as at December 31, 2015. The increase to capital available in 2016 was due primarily to the profitability which was partially offset by the Insurance Subsidiary's dividends and a decrease in unrealized gains in the investment portfolio. The increase in capital required in 2016 was primarily due to an increase in insurance margin risk from premiums written partially offset by a decrease in required capital for interest rate risk, as the Company entered into \$2.0 billion of interest rate swaps. The Company uses fixed for floating interest rate swaps in conjunction with the management of interest rate risk related to its fixed income securities.

On December 15, 2016, OSFI released the final capital advisory titled "*Capital Requirements for Federally Regulated Mortgage Insurers*". This advisory provides a new standard framework for determining the capital requirements for residential mortgage insurance companies. The proposed framework is more risk sensitive and incorporates additional risk attributes, including credit score, remaining amortization and outstanding loan balance. The finalized advisory came into effect on January 1, 2017, replacing OSFI's current advisory, "*Interim Capital Requirements for Mortgage Insurance Companies*", which had been in effect since 2015.

Under the new capital framework, the holding target of 220% has been recalibrated to the OSFI Supervisory MCT Target of 150% and the minimum MCT under PRMHIA has been reduced to 150%. Based on the new framework, the Company has established an internal

MCT target of 157% for 2017 and estimates that its pro forma MCT ratio as at December 31, 2016 would have been in the range of 158% to 162%.

## Debt

The Company proactively manages capital to balance capital strength, flexibility and efficiency. The Company currently has \$433 million in long-term debt, issued in two series, with a debt-to-capital ratio as at December 31, 2016 of 11%.

**Table 19: Details of the Company's long-term debt**

*(in millions unless otherwise specified)*

Series	Series 1	Series 3
Timing of maturity	3–5 years	After 5 years
Principal amount outstanding	\$275	\$160
Date issued	June 29, 2010	April 1, 2014
Maturity date	June 15, 2020	April 1, 2024
Fixed annual rate	5.68%	4.242%
Semi-annual interest payments due each year on	June 15, December 15	October 1, April 1
<b>Debenture Ratings</b>		
S&P <sup>1</sup>	BBB+, (Stable)	BBB+, (Stable)
DBRS <sup>1</sup>	A (High), Stable	A (High), Stable

<sup>1</sup> See "Financial Strength Rating" section of this MD&A for additional information.

The principal debt covenants associated with the debentures are as follows:

- A negative pledge under which the Company will not assume or create any security interest (other than permitted encumbrances) unless the debentures are secured equally and ratably with (or prior to) such obligation;
- The Company will not, nor will it permit any of its subsidiaries to, amalgamate, consolidate or merge with or into any other person or liquidate, wind-up or dissolve itself unless (a) the Company or one of its wholly-owned subsidiaries is the continuing or successor company or (b) if the successor company is not a wholly-owned subsidiary, at the time of, and after giving effect to, such transaction no event of default and no event that, after notice or lapse of time, or both, would become an event of default shall have happened and be continuing under the trust indenture, in each case subject to certain exceptions and limitations set forth in the trust indenture; and
- The Company will not request that the rating agencies withdraw their ratings of the debentures.

In the case of certain events of default under the terms of the debentures issued by the Company in 2010 and 2014, the aggregate unpaid principal amount of such debentures, together with all accrued and unpaid interest thereon and any other amounts owing with respect thereto, shall become immediately due and payable. The events of default that would trigger such an acceleration of payment include if the Company takes certain voluntary insolvency actions, such as instituting proceedings for its winding up, liquidation or dissolution, or consents to the filing of such proceedings against it; or if involuntary insolvency proceedings go uncontested by the Company or are not dismissed within a specified time period, or the final order sought in such proceedings is granted against the Company.

For more specific details on the terms and conditions of the Company's debentures, please see the relevant prospectus, copies of which are available on the SEDAR website at [www.sedar.com](http://www.sedar.com).

## Credit facility

On May 20, 2016, the Company entered into a \$100 million senior unsecured revolving credit facility, which matures on May 20, 2019. Any borrowings under the credit facility will bear interest at a rate per annum equal to, either a fixed rate based on a spread over Bankers' Acceptance or a variable rate based on a spread over the Lender Prime Rate. The Company will also pay a standby fee

based on the unused amount of the commitments. The credit facility includes customary representations, warranties, covenants, terms and conditions for transactions of this type.

As at December 31, 2016 there was no amount outstanding under the credit facility and all of the covenants were fully met.

## Financial strength ratings

The Insurance Subsidiary has financial strength ratings from both S&P and DBRS. Although the Insurance Subsidiary is not required to have ratings to conduct its business, ratings may influence the confidence in an insurer and its products.

On August 18, 2016, Standard & Poor's ("S&P") affirmed the Insurance Subsidiary's A+ rating with a stable outlook and the Company's BBB+ rating with a stable outlook. S&P noted that the Company had a strong competitive position, low industry risk due to the Company's strong portfolio quality, tight regulation, extremely strong earnings and capitalization and adequate financial flexibility with a moderate risk due to monoline focus in a sector prone to capital and earnings volatility.

On May 17, 2016, DBRS confirmed the Insurance Subsidiary's AA financial strength rating with a stable trend citing "the Insurance Company's solid market position, seasoned insurance portfolio and advanced risk analytics, as well as its strong capital position relative to the capital required to meet insurance claim obligations. The confirmation also reflects the Company's strong capital adequacy as assessed through the application of the DBRS residential mortgage-backed securities (RMBS) model, assuming a runoff scenario." DBRS downgraded the Company's issuer rating and senior unsecured debentures rating one notch to A (high) with a stable trend citing "DBRS's concern that there is now a greater risk that OSFI, in a stressed mortgage market situation, may place restrictions on dividend payments from the Insurance Company."<sup>2</sup>

Ratings Summary	S&P	DBRS
<b>Issuer Rating</b>		
Company	BBB+, Stable	A (High), Stable
<b>Financial Strength</b>		
Insurance Subsidiary	A+, Stable	AA, Stable
<b>Senior Unsecured Debentures</b>		
Company	BBB+, Stable	A (High), Stable

## Capital transactions

### Share repurchase

On April 28, 2016, the Company received approval by the Toronto Stock Exchange for the Company to undertake an NCIB. Pursuant to the NCIB, the Company can purchase, for cancellation, up to 4,589,958 shares representing approximately 5% of its outstanding common shares as at April 25, 2016. Purchases of common shares under the NCIB may commence on or after May 5, 2016 and will conclude on the earlier of May 4, 2017 and the date on which the Company has purchased the maximum number of shares under the NCIB.

The Company's prior NCIB which commenced on April 28, 2015, expired on May 4, 2016. The Company did not purchase any shares under either NCIB during the three and twelve months ended December 31, 2016. The Company had made purchases of \$50 million in 2015 pursuant to the NCIB.

The Company's major shareholder, Genworth Financial, Inc., intends to participate proportionately to maintain its approximately 57.2% ownership interest in the Company throughout the course of the NCIB, if any shares are purchased. Shareholders may obtain a copy of the NCIB notice, without charge, by contacting the Company.

<sup>2</sup> DBRS May 17, 2016 press release: DBRS Confirms Ratings on Genworth Financial Mortgage Insurance Company Canada and Downgrades Genworth MI Canada Inc.

## Restrictions on dividends and capital transactions

The Insurance Subsidiary is subject to certain restrictions with respect to dividend and capital transactions. The Insurance Companies Act (“**ICA**”) prohibits directors from declaring or paying any dividend on shares of an insurance company if there are reasonable grounds for believing that the Company is, or the payment of the dividend would cause the company to be, in contravention of applicable requirements to maintain adequate capital, liquidity and assets. The ICA also requires an insurance company to notify OSFI of the declaration of a dividend at least 15 days prior to the date fixed for its payment. Similarly, the ICA prohibits the purchase for cancellation of any shares issued by an insurance company or the redemption of any redeemable shares or other similar capital transactions if there are reasonable grounds for believing that the company is, or the payment would cause the Company to be, in contravention of applicable requirements to maintain adequate capital, liquidity and assets. Share cancellation or redemption would also require the prior approval of OSFI. Finally, OSFI has broad authority to take actions that could restrict the ability of an insurance company to pay dividends.

## Outstanding share data

**Table 20: Changes in the number of common shares outstanding at December 31, 2016 and December 31, 2015**

	December 31, 2016	December 31, 2015
Common shares, beginning of period (January 1)	<b>91,795,125</b>	<b>93,147,778</b>
Common shares issued in connection with share-based compensation plans	<b>68,975</b>	<b>101,543</b>
Common shares repurchased and cancelled	-	<b>(1,454,196)</b>
Common shares, end of period	<b>91,864,100</b>	<b>91,795,125</b>

At December 31, 2016, Genworth Financial, Inc. beneficially owned 52,562,042 common shares of the Company, or approximately 57.2% of the Company's outstanding common shares, through its wholly-owned subsidiaries, Genworth Financial International Holdings LLC (“**GFIH**”), Genworth Mortgage Insurance Corporation (“**GMIC**”) and Genworth Mortgage Insurance Corporation of North Carolina (“**GMICNC**”) which held approximately 40.6%, 14.9% and 1.7% of the common shares of the Company, respectively.

## Risk management

### Enterprise risk management framework

Risk management is a critical part of Genworth Canada's business. The Company's Enterprise Risk Management ("ERM") Framework, comprises the totality of the frameworks, systems, processes, policies, and people for identifying, assessing, mitigating and monitoring risks. The key elements of the ERM Framework are illustrated in the diagram below.



### Governance framework

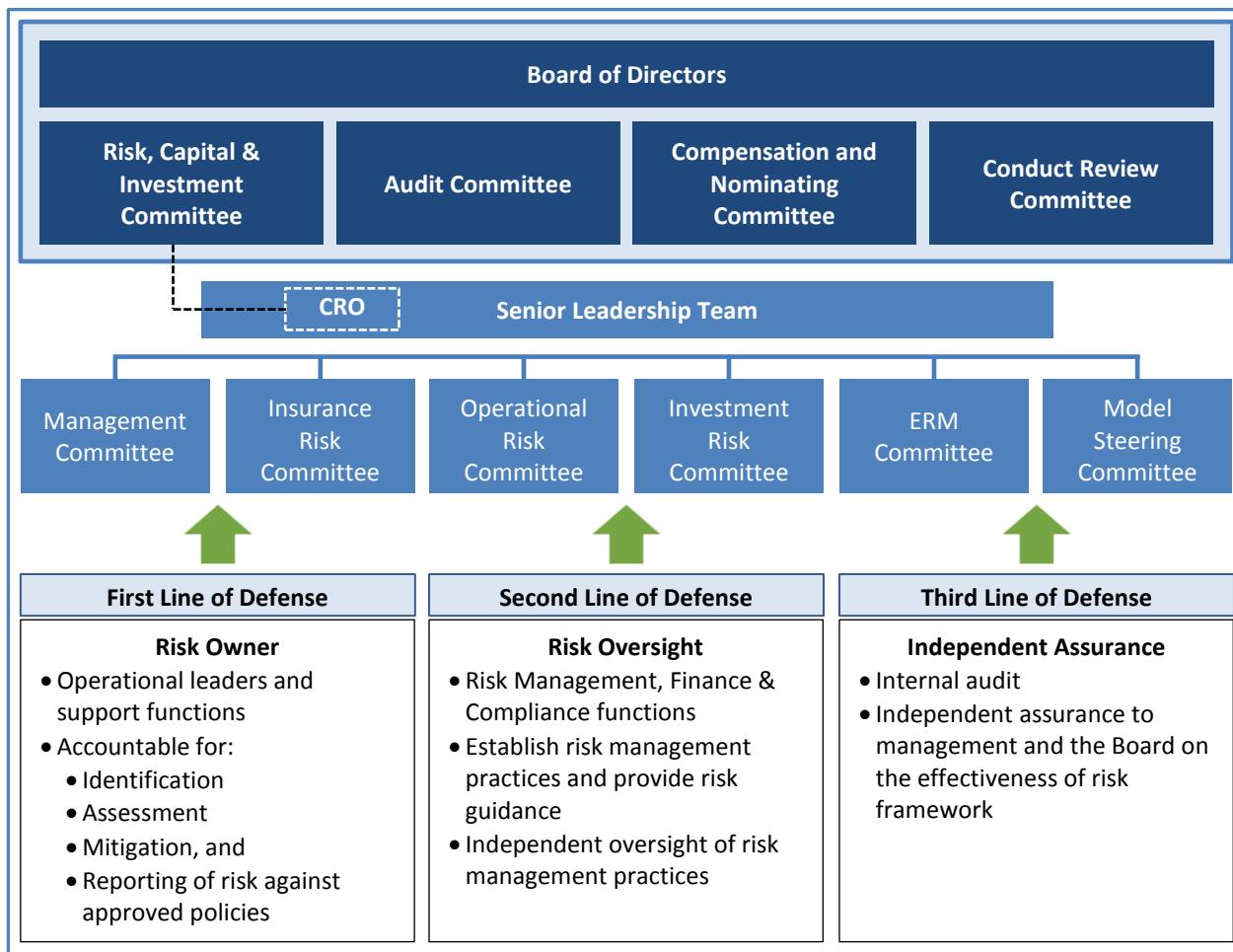
The Company's governance framework is designed to ensure the Board and management have effective oversight of the risks faced by the Company with clearly defined and articulated roles and responsibilities and inter-relationships. The governance framework is comprised of three core elements:

- I. Board's oversight of risk and risk management practices;
- II. Management's oversight of risks; and
- III. The "three lines of defense" operating model.

The Board is responsible for reviewing and approving the Company's Risk Appetite and ensuring that it remains consistent with the Company's short and long-term strategy, business and capital plans. The Board carries out its risk management mandate primarily through its committees, with the Risk, Capital and Investment Committee having responsibility for oversight of insurance, investment and operational risks.

The Company's management is responsible for risk management under the oversight of the Board and fulfills its responsibility through several risk committees, as noted in the chart below. The Chief Risk Officer ("CRO"), who oversees the Risk Management Group, reports to the Chief Executive Officer ("CEO") but has direct access via in-camera sessions with the Risk, Capital and Investment Committee of the Board.

The Board and the board of directors of the Insurance Subsidiary use a '*three lines of defense*' approach to risk management, which serves to allocate accountability and responsibility for risk management within the various business functions, as outlined in the chart below.



## Risk appetite framework

Risk appetite is the maximum amount of risk that the Company is willing to accept in the pursuit of its business objectives. The objective in managing risk is to protect the Company from unacceptable loss or an undesirable outcome with respect to earnings volatility, capital adequacy, liquidity or reputation, while supporting the Company's overall business strategy.

The purpose of the Risk Appetite Framework is to provide a framework for management and the Board for understanding the ultimate level of risk the Company is willing to undertake in pursuit of its strategic objectives with due regard to its commitments and regulatory boundaries. It articulates the desired balance between risk objectives, meeting customer needs and profitability objectives, and is a key communication tool that enables the Board to cascade key messages throughout the organization. It establishes a common understanding around the acceptable level of variability in financial performance and answers the question of how much risk the Company is willing to take under expected and extreme scenarios.

Where possible, the Company has set risk limits and tolerances that guide the business and ensure that risk taking activities are within its risk appetite. The Company's risk tolerances and limits will be assessed for appropriateness no less than annually and on a more frequent basis if there is a major change to the economic or business environment. The Company communicates risk tolerances and limits across the organization through its policies, limit structures and operating procedures.

Where possible, the Company's risk appetite is subject to stress and scenario testing and can be expressed as the tolerance with respect to acceptable variances for earnings, liquidity and capital to deviate from their target levels under adverse scenarios.

## Risk principles

The Company employs the following methods of managing risk that originate from the business objectives of the Company:

- Ensure the expected outcomes of risk taking activities are consistent with the Company's strategies and risk appetite;
- Ensure there is an appropriate balance between risk, return, capital, and liquidity in order to meet policyholder obligations and maximize shareholder value throughout economic cycles;
- Ensure business decisions are based on an understanding of risk;
- Ensure a deep understanding of risk drivers as they relate to our key objectives;
- Employ a "Three Lines of Defense" risk governance model, which ensures that a responsibility for risk management is shared across the business;
- Proactively address emerging risks as they arise; and
- Ensure strict adherence to legal, compliance and regulatory requirements.

The Company's ERM framework and internal control procedures are designed to reduce the level of volatility in its financial results. The Company's ERM framework is linked to its business strategy and decision making framework. One of the key tools is the Own Risk and Self-Assessment ("ORSA") framework. The key elements and considerations of ORSA include: the comprehensive identification and assessment of risks and the adequacy of the Company's risk management; the assessment of the Company's current and likely future capital needs and solvency positions in light of its risk assessments; the distinguishing of Board oversight and management responsibility for such processes; detailing related monitoring and reporting requirements; and detailing the Company's internal controls and objective review process and procedures for such risk assessments. The Company's ORSA is forward looking and is undertaken in conjunction with the Company's business and strategic planning.

## Risk controls

The Company's ERM approach is supported by a comprehensive set of risk controls. The controls are embedded through its ERM framework and risk-specific frameworks. These frameworks lay the foundation for the development and communication of management -approved policies and the establishment of formal review and approval processes. The Company's risk management framework and policies are organized as follows:

- **ERM Framework:** provides an overview of the enterprise-wide program for identifying, measuring, controlling and reporting of material risks the Company faces;
- **Risk-Specific Frameworks:** provides an overview of the Company's program for identifying, measuring, controlling and reporting for each of its material risks; and
- **Company-wide Policies and Procedures:** governs activities such as product risk review and approval, project initiatives, stress testing, risk limits and risk approval authorities.

## Risk categories

### Insurance risk

Genworth Canada's mortgage insurance risk management involves actively managing its borrower credit quality, product and geographic exposures. The Company carefully monitors portfolio concentrations by borrower credit quality, product and geography against pre-determined risk tolerances, taking into account the conditions of the housing market and economy in each region of Canada. For Genworth Canada-insured transactional mortgages in 2016, the average credit score increased 8 points to 751 and the average home price has increased to \$325,000, or 1%, over the prior year. The average gross debt service ratio for the 2016 was stable at 24%, over the prior year, and is well below the new mortgage stress test threshold of 26%.

To the extent that home prices appreciate over time and/or the principal amount of the loan is paid down, the effective loan-to-value of the Company's insurance written in a given year decreases.

**Table 21: Estimated effective loan-to-value % of the Company's outstanding mortgage insurance balances<sup>1</sup> by book of business**

	As at December 31, 2016			As at December 31, 2015		
	Transactional	Portfolio	Total	Transactional	Portfolio	Total
2009 & prior	44	21	41	49	25	45
2010	61	27	55	67	32	61
2011	65	34	59	71	41	65
2012	70	34	53	76	42	59
2013	74	39	56	81	46	62
2014	79	44	62	87	53	69
2015	84	50	64	92	59	72
2016	90	53	64	-	-	-
Total	69	46	58	72	49	62

<sup>1</sup> This is based on the amounts reported by lenders surveyed, which represents the vast majority of insurance in-force.

Genworth Canada's extensive historical database and innovative information technology systems are important tools in its approach to risk management. The Company utilizes its proprietary transactional insurance performance database to build and improve its mortgage scoring model. This mortgage scoring model employs a number of evaluation criteria to assign a score to each insured mortgage loan which is an indicator of the likelihood of a future claim. This evaluation criteria includes borrower credit score, loan type and amount, total debt service ratio, property type and loan-to-value. The Company believes these factors, as well as other considerations, significantly enhance the ability of the mortgage scoring model to predict the likelihood of a borrower default, as compared to reliance solely on borrower credit score. The Company also utilizes internally developed stochastic modelling to estimate projected losses on claims and to measure the severity of loss and delinquency rate sensitivity to both changes in the economic environment as well as individual loan or borrower attributes.

The Company's mortgage portfolio risk management function is organized into three primary groups: portfolio analysis, underwriting policies and guidelines, and risk technology and actuarial modeling. The risk management team analyzes and summarizes mortgage portfolio performance, risk concentrations, emerging trends and remedial actions which are reviewed with the Company's management-level Risk Committee on a monthly basis. The Company closely monitors the delinquency performance as a key indicator of insurance portfolio performance.

The Company also employs a quality assurance team to ensure that policies and guidelines established by the Company's mortgage portfolio risk management function are adhered to both internally within the Company and by lenders submitting applications to the Company. The quality assurance team conducts daily reviews of a random sample of loans adjudicated by the Company's underwriters. Similarly, external lender audits are conducted on a routine basis, using a statistically relevant sample of approved loans. In addition, the quality assurance team also reviews the Company's loss reserving and mitigation functions to ensure compliance with relevant Company policies and accounting standards. Audit results of all three areas are reviewed by management on a monthly basis.

## Market and credit risk

The Company monitors and manages the credit risk, liquidity risk and market risk, including interest rate risk, equity price risk, currency risk, emerging markets risk and counterparty risk of its investment portfolio.

**Credit risk**

Credit risk is the risk that one party to a financial instrument fails to discharge an obligation and causes financial loss to another party. The Company is exposed to credit risk principally through its investment assets. The Company's investment management strategy is to invest primarily in debt instruments of Canadian government agencies and other high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer, business sector, or credit rating category, as specified in its investment policy. Credit quality of financial instrument issuers is assessed based on ratings supplied by rating agencies DBRS, S&P and Moody's and credit analysis completed by the Company and its investment managers.

Credit risk from derivative transactions reflects the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the Company. Therefore, derivative-related credit risk is represented by the positive fair value of the instrument and is normally a small fraction of the contract's notional amount. To mitigate credit risk related to derivative counterparties, the Company has adopted a policy whereby, upon signing the derivative contract, the counterparty is required to have a minimum credit rating of A- and to collateralize their derivative obligations.

**Liquidity risk**

Liquidity risk is the risk of having insufficient cash resources to meet policy obligations and other financial commitments as they fall due without raising funds at unfavourable rates or selling assets on a forced basis. To ensure liquidity requirements are met, the Company holds a portion of investment assets in liquid securities. Adverse capital and credit market conditions and the MCT requirements of the Insurance Subsidiary may significantly affect the Company's access to capital and may affect its ability to meet liquidity or debt refinancing requirements in the future. Potential liquidity risks are discussed in more detail in the "Risk Factors" section of the Company's AIF and the "Liquidity" section in this MD&A.

**Market risk**

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, equity market fluctuations, foreign currency exchange rates and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying assets are traded. The market risks to which the Company is exposed are interest rate risk, equity price risk, currency risk, emerging markets risk and counterparty risk.

**Interest rate risk**

Fluctuations in interest rates have a direct impact on the market valuation of the Company's fixed income investment portfolio. Short-term interest rate fluctuations will generally create unrealized gains or losses. Generally, the Company's interest income will be reduced during sustained periods of lower interest rates as higher-yielding fixed income investments are called, mature or are sold and the proceeds are reinvested at lower rates, and this will likely result in unrealized gains in the value of fixed income investments the Company continues to hold, as well as realized gains to the extent that the relevant investments are sold. During periods of rising interest rates, the market value of the Company's existing fixed income investments will generally decrease and gains on fixed income investments will likely be reduced or become losses. To mitigate interest rate risk, the Company uses fixed for floating interest rate swaps to hedge a portion of the interest rate risk.

**Equity price risk**

Equity price risk is the risk that the fair values of equities will decrease as a result of changes in the levels of equity indices and the values of individual stocks. Equity price risk exposure arises from the Company's investment in common shares. The Company did not hold any common shares as at December 31, 2016 and 2015.

**Currency risk**

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company is exposed to currency risk arising from investments denominated in U.S. dollars. The Company uses foreign exchange forward contracts and cross-currency interest rate swaps to mitigate currency risk.

**Emerging markets risk**

Emerging markets risk relates to international investment grade bond holdings which are exposed to greater market volatility, have less availability of reliable financial information, carry higher transactional and custody costs, are subject to taxation by foreign governments, have decreased market liquidity and may be exposed to political instability.

**Counterparty risk**

Counterparty risk relates to the risk that a counterparty will fail to discharge its obligation related to a bond, derivative contract or other trade or transaction.

## Financial reporting controls and accounting disclosures

### Disclosure controls and procedures and internal controls over financial reporting

As required by National Instrument 52-109, the Company has in place disclosure controls and procedures and internal controls over financial reporting, designed under the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") Framework (2013) to ensure the disclosure of all material information or changes relating to the Company to all members of the public in a fair and timely manner. Such controls and procedures ensure that all relevant material is gathered and reported to senior management (including the CEO, CFO and General Counsel) and the Company's management-level disclosure committee on a timely basis so that appropriate decisions can be made regarding public disclosure. An evaluation and certification of the Company's disclosure controls and procedures and internal controls over financial reporting is done regularly under supervision by the Company's CEO and CFO in accordance with the requirements of National Instrument 52-109 of the Canadian Securities Administrators, and such certifications are available with the Company's filings on the SEDAR website at [www.sedar.com](http://www.sedar.com). The certifications filed in connection with certain interim and annual financial disclosure documents, confirm that the CEO and CFO have concluded that the design and operation of the disclosure controls and procedures and internal controls over financial reporting were effective, for such periods. There were no changes in the Company's internal controls over financial reporting during the quarter or year ending December 31, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's controls over financial reporting.

### Changes in accounting standards and future accounting standards

The following amendment to existing standards has been issued by the IASB and is effective for annual periods beginning on or after January 1, 2016.

#### Amendments to IAS 1 - Presentation of financial statements ("IAS 1"):

In December 2014, the IASB issued certain narrow focus amendments to IAS 1 to clarify existing presentation and disclosure requirements. Amendments include the requirement to disaggregate line items on the Statement of Financial Position, Statement of Income and Statement of Comprehensive Income if disaggregation is helpful to users of the financial statements and to aggregate line items on the Statement of Financial Position if immaterial.

Adoption of the amendment on January 1, 2016 did not have a significant impact on the Company's consolidated financial statements.

**Future accounting standards****IFRS 17 - Insurance contracts**

IFRS 17 (previously IFRS 4 phase II) is intended to replace *IFRS 4: Insurance contracts*. Under the IFRS 17 model, insurance contract liabilities will be calculated as the present value of future insurance cash flows with a provision for risk. The discount rate will reflect current interest rates. If the present value of future cash flows would produce a gain at the inception of the contract, the model will also require a "contractual service margin" to offset the day one gain. The contractual service margin will amortize over the life of the contract. Certain types of contracts will be permitted to use a simplified unearned premium liability model until a claim is incurred. Additionally, for the contracts in which the cash flows are linked to underlying items, the liability value will reflect that linkage. There will also be a new income statement presentation for insurance contracts and additional disclosure requirements. IFRS 17 is anticipated to be released in the first half of 2017 and has an expected effective date of January 1, 2021.

The Company is assessing the impact of IFRS 17.

**IFRS 9 - Financial instruments**

In July 2014, the IASB published the final version of IFRS 9, which replaces *IAS 39 - Financial instruments: recognition and measurement*, and includes guidance on the classification and measurement of financial instruments, impairment of financial assets, and a new general hedge accounting model. Financial asset classification is based on the cash flow characteristics and the business model in which an asset is held. The classification determines how a financial instrument is accounted for and measured. IFRS 9 also introduces a single impairment model for financial instruments not measured at Fair Value through Profit or Loss that requires recognition of expected credit losses at initial recognition of a financial instrument and the recognition of lifetime expected credit losses if certain criteria are met. The new model for hedge accounting aligns hedge accounting with risk management activities.

While the new standard is generally effective for years beginning on or after January 1, 2018, on September 12, 2016, the IASB issued amendments to *IFRS 17 Insurance Contracts*, which permits eligible insurer optional transitional relief until the forthcoming insurance accounting standard is available for implementation. The options permit (a) entities whose predominant activity is issuing insurance contracts within the scope of IFRS 17 a temporary exemption to defer the implementation of IFRS 9, which may allow alignment of the implementation of IFRS 9 with the forthcoming insurance accounting standard, or alternatively (b) give entities issuing insurance contracts the option to remove from profit or loss the incremental volatility caused by changes in the measurement of specified financial assets upon application of IFRS 9. Entities that apply either of the options will be required to adopt IFRS 9 on the earlier of the date that IFRS 17 is effective and annual periods beginning on or after January 1, 2021. The Company has concluded that it is an eligible insurer that qualifies for the transitional relief.

The Company is evaluating the impact of IFRS 9 on its financial assets and financial liabilities and the optional transitional relief that permits deferral of the adoption of IFRS 9.

**IFRS 16 - Leases**

IFRS 16 was issued on January 13, 2016. The new standard will replace existing lease guidance in IFRS and related interpretations, and requires companies to bring most leases on-balance sheet. 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. Short-term leases and leases of low value items are optional exemptions under the standard. Lessor accounting remains similar to the current standards, where lessors classify leases as finance or operating leases. The new standard is effective for years beginning on or after January 1, 2019.

The Company is assessing the impact of IFRS 16.

**Amendments to IFRS 2 – Share-based payments (“IFRS 2”)**

Amendments to IFRS 2 were published in June 2016, which clarify how to account for certain types of share-based payment transactions.

The amendments provide requirements on the accounting for:

- the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments
- share-based payment transactions with a net settlement feature for withholding tax obligations; and
- a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled

The amendments are effective for annual periods beginning on or after January 1, 2018, with early adoption permitted if information is available without the use of hindsight.

The Company is currently assessing the impact of the amendments to IFRS 2.

**Significant estimates and judgments**

The preparation of consolidated financial statements in accordance with IFRS requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods covered by the financial statements. The principal financial statement components subject to measurement uncertainty are outlined below as accounting estimates and judgments. Actual results may differ from the estimates used, and such differences may be material.

**Accounting estimates**

Information about assumptions and estimation uncertainties that have a risk of resulting in material adjustment within the next 12 months are as follows:

**Premiums earned**

Mortgage insurance premiums are deferred and then taken into underwriting revenues over the terms of the related policies. The rates or formulae under which premiums are earned relate to the loss emergence pattern in each year of coverage. In order to match premiums earned to losses on claims, premiums written are recognized as premiums earned using a factor-based premium recognition curve.

In constructing the premium recognition curve, the Company applies actuarial forecasting techniques to historical loss data to determine expected loss development and the related loss emergence pattern.

**Loss reserves**

Loss reserves represent the amount needed to provide for the expected ultimate net cost of settling claims including adjustment expenses related to defaults by borrowers (both reported and unreported) that have occurred on or before the reporting date. Loss reserves are discounted to take into account the time value of money and include a supplemental provision for adverse deviation. In determining the ultimate claim amount, the Company estimates the expected recovery from the property securing the insured loan and the legal, property maintenance and other loss adjustment expenses incurred in the claim settlement process. Loss reserves consist of individual case reserves, Incurred But Not Reported ("IBNR") reserves and supplemental loss reserves for potential adverse deviation.

For the purpose of quantifying case reserves, the Company analyzes each reported delinquent loan on a case-by-case basis and establishes a case reserve based on the expected loss, if any. The ultimate expected claim amount is influenced significantly by housing market conditions, changes in property values, and the condition of properties in default.

IBNR is the Company's best estimate of losses that have been incurred but not reported from the time the first scheduled mortgage payment has been missed by a mortgage borrower. The Company establishes reserves for IBNR based on the reporting lag from the date of first missed payment to the reporting date for mortgages in default that have not been reported to the Company. IBNR is calculated using estimates of expected claim frequency and claim severity based on the most current available historical loss data, adjusted for seasonality.

In order to discount loss reserves to present value, the Company's appointed actuary determines a discount rate based on the market yield of the Company's investment portfolio.

The Company recognizes a provision for adverse deviation based on assessment of the adequacy of the Company's loss reserves and with reference to the current and future expected condition of the Canadian housing market and its impact on the expected development of losses.

The process for the establishment of loss reserves relies on the judgment and opinions of a number of individuals, on historical precedent and trends, on prevailing legal and economic trends and on expectations as to future developments. This process involves risks that actual results will deviate, perhaps substantially, from the best estimates made. These risks vary in proportion to the length of the estimation period and the volatility of each component comprising the liability.

#### **Subrogation recoverable**

The Company estimates the fair value of subrogation rights related to real estate included in subrogation recoverable based on third party property appraisals or other types of third party valuations deemed to be more appropriate for a particular property.

The Company estimates borrower recoveries related to claims paid and loss reserves included in subrogation recoverable based on historical recovery experience. Borrower recoveries are discounted to present value and include an actuarial margin for adverse deviation.

#### **Deferred policy acquisition costs**

Deferred policy acquisition costs are comprised of premium taxes, appraisal costs, risk fee, certain employee compensation, and other expenses that relate directly to acquisition of new mortgage insurance business. Deferred policy acquisition costs are deferred and expensed in proportion to and over the periods in which premiums are earned.

The Company estimates expenses eligible for deferral based on the nature of expenses incurred and results of time and activity studies performed to identify the portion of time the Company's employees incur in the acquisition of new mortgage insurance business.

#### **Accounting judgments**

##### **Objective evidence of impairment of AFS financial assets**

As of each reporting date, the Company evaluates AFS financial assets for objective evidence of impairment.

For investments in bonds and preferred shares, evaluation of whether impairment has occurred is based on the Company's assessment that a loss event has occurred and the Company's best estimate of the cash flows to be collected at the individual investment level. The Company considers all available information relevant to the collectability of the investment, including information about past events, current conditions, and reasonable and supportable forecasts. Impairment assessment is a qualitative and quantitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of any underlying collateral for asset-backed investments. Impairment for bonds and preferred shares is deemed to exist when the Company does not expect full recovery of the amortized cost of the investment based on the estimate of cash flows to be collected or when the Company intends to sell the investment prior to recovery from its unrealized loss position.

For common shares, the Company recognizes an impairment loss in the period in which it is determined that an investment has experienced significant or prolonged losses.

### **Transactions with related parties**

#### **Services**

The Company enters into related party transactions with Genworth Financial, Inc. and its subsidiaries. Services rendered by Genworth Financial, Inc. and subsidiaries consist of information technology, finance, human resources, legal and compliance, and other specified services. The services rendered by the Company and the Insurance Subsidiary relate mainly to financial reporting and tax compliance support services. These transactions are in the normal course of business and are at terms and conditions no less favourable than market. Balances owing for service transactions are non-interest bearing and are settled on a quarterly basis. The Company incurred net related party charges of approximately \$6 million in 2016, relatively unchanged as compared to in the prior year.

#### **Reinsurance**

During the year ended December 31, 2015, the Company, through its indirect subsidiary MIC Insurance Company Canada, terminated its retrocession agreement with a third party reinsurance company that commenced on December 1, 2013, under which the Company assumed reinsurance risk for approximately 33% of the retroceded liabilities on claims paid by Genworth Financial Mortgage Insurance Pty Limited, an Australian company.

During the year ended December 31, 2016, the Company did not participate in reinsurance transactions and therefore no premiums were recognized or losses incurred in conjunction with reinsurance arrangements. During the year ended December 31, 2015, the Company recognized premiums of \$2 million and incurred no losses.

## Non-IFRS financial measures

To supplement the Company's consolidated financial statements, which are prepared in accordance with IFRS, the Company uses non-IFRS financial measures to analyze performance. The Company's key performance indicators and certain other information included in this MD&A include non-IFRS financial measures. Such non-IFRS financial measures used by the Company to analyze performance include net operating income, operating earnings per common share (basic), operating earnings per common share (diluted). The Company believes that these non-IFRS financial measures provide meaningful supplemental information regarding its performance and may be useful to investors because they allow for greater transparency with respect to key metrics used by management in its financial and operational decision making. Non-IFRS financial measures do not have standardized meanings and are unlikely to be comparable to any similar measures presented by other companies.

**Table 22: Non-IFRS financial measures reconciled to comparable IFRS measures for such periods**

<i>(in millions of dollars, unless otherwise specified)</i>	Fourth Quarter		Full Year	
	2016	2015	2016	2015
Investment income	\$ 93	\$ 47	\$ 214	\$ 201
Adjustment to investment income:				
Net investment (gains)	(47)	(3)	(38)	(32)
Interest and dividend income, net of investment expenses	\$ 46	\$ 44	\$ 176	\$ 169
Net income	140	98	417	398
Adjustments to net income, net of taxes:				
Net investment (gains)	(35)	(3)	(29)	(23)
Net operating income	\$ 105	\$ 95	\$ 388	\$ 375
Earnings per common share (basic)	\$ 1.52	\$ 1.06	\$ 4.54	\$ 4.32
Adjustment to earnings per common share, net of taxes:				
Net investment (gains)	(0.38)	(0.03)	(0.31)	(0.25)
Operating earnings per common share (basic)	\$ 1.15	\$ 1.04	\$ 4.23	\$ 4.07
Earnings per common share (diluted) <sup>1</sup>	\$ 1.52	\$ 1.03	\$ 4.54	\$ 4.22
Adjustment to earnings per common share, net of taxes:				
Share based compensation re-measurement amount	0.00	0.03	0.00	0.08
Net investment (gains)	(0.38)	(0.03)	(0.31)	(0.25)
Operating earnings per common share (diluted) <sup>1</sup>	\$ 1.14	\$ 1.03	\$ 4.23	\$ 4.05

Note: Amounts may not total due to rounding.

<sup>1</sup>The difference between basic and diluted number of common shares outstanding is caused by the potentially dilutive impact of share-based compensation awards.

Other non-IFRS financial measures used by the Company to analyze performance for which no comparable IFRS measure is available include insurance in-force, new insurance written, loss ratio, expense ratio, combined ratio, operating return on equity, investment yield and MCT ratio.

**Table 23: Non-IFRS financial measures for which no comparable IFRS measure is available**

For a more meaningful description of the measure, refer to the “Non-IFRS financial measures glossary”.

<i>(in millions of dollars, unless otherwise specified)</i>	Fourth Quarter		Full Year	
	2016	2015	2016	2015
<b>Selected non-IFRS financial measures</b>				
Insurance in force <sup>1</sup>	\$ 464,291	\$ 404,963	\$ 464,291	\$ 404,963
Transactional new insurance written	5,120	6,231	21,171	25,243
Portfolio new insurance written	4,918	9,595	41,881	25,696
Loss ratio	18%	23%	22%	21%
Expense ratio	20%	18%	19%	18%
Combined ratio	38%	41%	41%	39%
Operating return on equity	12%	12%	11%	12%
Investment yield	3.2%	3.3%	3.2%	3.3%
MCT ratio	245%	234%	245%	234%

<sup>1</sup>The Company estimates that the outstanding balance of insured mortgages was approximately \$223 billion as at December 31, 2016.

**Non-IFRS financial measures glossary**

**“combined ratio”** means the sum of the loss ratio and the expense ratio. The combined ratio measures the proportion of the Company’s total cost to its premium earned and is used to assess the profitability of the Company’s insurance underwriting activities.

**“expense ratio”** means the ratio (expressed as a percentage) of sales, underwriting and administrative expenses to premiums earned for a specified period. The expense ratio measures the operational efficiency of the Company and is a useful comparison to industry benchmarks and internal targets.

**“insurance in-force”** means the amount of all mortgage insurance policies in effect at a specified date, based on the original principal balance of mortgages covered by such insurance policies, including any capitalized premiums. Insurance in-force measures the maximum potential total risk exposure under insurance contracts at any given time and is used to assess potential losses on claims.

**“interest and dividend income, net of investment expenses”** means the total net investment income excluding investment gains (losses). This measure is an indicator of the core operating performance of the investment portfolio.

**“investment yield”** means the annualized investment income before investment fees and excluding net investment gains (losses) tax affected for dividends for such period divided by the average of the beginning and ending investments book value, for such period. For quarterly results, the investment yield is the annualized investment income using the average of beginning and ending investments book value, for such quarter.

**“loss ratio”** means the ratio (expressed as a percentage) of the total amount of losses on claims associated with insurance policies incurred during a specified period to premiums earned during such period. The loss ratio is a key measure of underwriting profitability and the quality of the insurance portfolio and is used for comparisons to industry benchmarks and internal targets.

**“Minimum Capital Test”** or **“MCT”** means the minimum capital test for certain federally regulated insurance companies established by OSFI (as defined herein). Under MCT, companies calculate an MCT ratio of regulatory capital available to regulatory capital required using a defined methodology prescribed by OSFI in monitoring the adequacy of a company’s capital. The MCT ratio is a key metric of the adequacy of the Company’s capital in comparison to regulatory requirements and is used for comparisons to other mortgage insurers and internal targets.

**“net operating income”** means net income excluding after-tax net realized gains (losses) on sale of investments, unrealized gains (losses) on FVTPL securities and the cost of interest rate swaps representing the difference between the fixed rate and floating rate. Net operating income estimates the recurring after-tax earnings from core business activities and is an indicator of core operating performance.

**“portfolio new insurance written”** means the original principal balance of mortgages, insured during a specified period as part of a portfolio of mortgages that have a loan-to-value ratio equal to or less than 80% at the time the loan is insured. New insurance written measures the maximum potential risk exposure under insurance contracts added during a specific time period and is used to determine potential loss exposure.

**“operating earnings per common share (basic)”** means the net operating income divided by the basic average common shares outstanding during the period.

**“operating earnings per common share (diluted)”** means the net operating income divided by the diluted average common shares outstanding during the period. The Company excludes the impact of the share based compensation re-measurement amount from operating earnings per share (diluted) as it believes this results is a better indicator of core operating performance.

**“operating return on equity”** means the net operating income for a period divided by the average of the beginning and ending shareholders’ equity, excluding AOCI, for such period. For quarterly results, the operating return is the annualized operating return on equity using the average of beginning and ending shareholders’ equity, excluding AOCI, for such quarter. Operating return on equity is an indicator of return on invested capital in the core business activities.

**“transactional new insurance written”** means the original principal balance of mortgages, including any capitalized premiums, insured during a specified period predominantly on mortgages with a loan-to-value ratio of greater than 80% at the time the loan is originated. New insurance written measures the maximum potential risk exposure under insurance contracts added during a specific time period and is used to determine potential loss exposure.

## Other Glossary

**“accumulated other comprehensive income”** or **“AOCI”** is a component of shareholders’ equity and reflects the unrealized gains and losses, net of taxes, related to available-for-sale assets. Unrealized gains and losses on assets classified as available-for-sale are recorded in the consolidated statement of comprehensive income and included in accumulated other comprehensive income until recognized in the consolidated statement of income.

**“available-for-sale”** or **“AFS”** means investments recorded at fair value on the balance sheet, using quoted market prices, with changes in the fair value of these investments included in AOCI.

**“average reserve per delinquency”** means the average reserve per delinquent loan calculated by total loss reserves in dollars divided by the number of outstanding delinquent loans reported by lenders. Average reserve per delinquency measures the potential size of the average loss, including delinquent loans with no expected loss, and is used for trending purposes and comparisons against internal targets.

**“average premium rate”** means the average premiums written collected divided by the new insurance written

**“book value per common share”** is a measure of the carrying value of each individual share of the Company and is a key metric used in assessing the market value of the Company.

**“book value per common share excluding AOCI (basic)”** means the per common share amount of shareholders’ equity excluding AOCI to the number of basic common shares outstanding at a specified date.

**“book value per common share excluding AOCI (diluted)”** means the per common share amount of shareholders’ equity excluding AOCI to the number of diluted common shares outstanding at a specified date. Diluted common shares outstanding takes into account all of the outstanding dilutive securities that could potentially be exercised.

**“book value per common share including AOCI (basic)”** means the per common share amount of shareholders’ equity including AOCI to the number of basic common shares outstanding at a specified date.

**“book value per common share including AOCI (diluted)”** means the per common share amount of shareholders’ equity including AOCI to the number of diluted common shares outstanding at a specified date. Diluted common shares outstanding takes into account all of the outstanding dilutive securities that could potentially be exercised.

**“case reserves”** means the expected losses associated with reported delinquent loans. Lenders report delinquent loans to the Company on a monthly basis. The Company analyzes reported delinquent files on a case-by-case basis and derives an estimate of the expected loss. Case reserve estimates incorporate the amount expected to be recovered from the ultimate sale of the residential property securing the insured mortgage.

**“claim”** means the amount demanded under a policy of insurance arising from the loss relating to an insured event.

**“common shares”** means the issued and outstanding common shares of the Company.

**“credit score”** means the lowest average credit score of all borrowers on a mortgage insurance application. Average credit scores are calculated by averaging the score obtained from both Equifax and TransUnion for each borrower on the application. This is a key measure of household financial health.

**“cures”** means previously reported delinquent loans where the borrower has made all scheduled mortgage payments or a successful workout has been completed and the loan is no longer considered a delinquent loan.

**“debt-to-capital ratio”** means the ratio (expressed as a percentage) of debt to total capital (the sum of debt and equity). This is a measure of financial leverage that the Company considers in capital management planning.

**“deferred policy acquisition costs”** means the expenses incurred in the acquisition of new business, comprised of premium taxes and other expenses that relate directly to the acquisition of new business. Policy acquisition costs are only deferred to the extent that they are in excess of the service fees and can be expected to be recovered from unearned premium reserves. Deferred policy acquisition costs are amortized into income in proportion to and over the periods in which premiums are earned.

**“delinquency ratio”** means the ratio (expressed as a percentage) of the total number of delinquent loans to the total original number of policies in-force at a specified date. The delinquency ratio is an indicator of the emergence of losses on claims and the quality of the insurance portfolio and is a useful comparison to industry benchmarks and internal targets.

**“delinquent loans”** means loans where the borrowers have failed to make scheduled mortgage payments under the terms of the mortgage and where the cumulative amount of mortgage payments missed exceeds the scheduled payments due in a three-month period.

**“dividends paid per common share”** means the portion of the Company’s profits distributed to shareholders during a specified period and measures the total amount distributed by the Company to shareholders.

**“effective loan-to-value”** means a Company estimate based on the estimated balance of loans insured divided by the estimated fair market value of the mortgaged property using the Teranet - National Bank Home Price Index Composite 11.

**“effective tax rate”** means the ratio (expressed as a percentage) of provision for income taxes to income before income taxes for a specified period. The effective tax rate measures the actual amount of pre-tax income the Company pays in taxes and is a useful comparison to industry benchmarks and prior periods.

**“Fair Value through Profit or Loss”** or **“FVTPL”** means investments recorded at fair value on the statement of financial position with changes in the fair value of these investments recorded in income.

**“gross debt service ratio”** or **“GDSR”** means the percentage of borrowers’ total monthly debt servicing costs, in respect of the debt in question, as a percentage of borrowers monthly gross income. This is a key measure of household financial health.

**“incurred but not reported”** or **“IBNR”** reserves means the estimated losses on claims for delinquencies that have occurred prior to a specified date, but have not been reported to the Company.

**“investment portfolio”** means invested assets (including cash and cash equivalents, short-term investments, bonds or other fixed income securities and equity investments).

**“loan-to-value ratio”** means the original balance of a mortgage loan divided by the original value of the mortgaged property.

**“loss adjustment expenses”** means all costs and expenses incurred by the Company in the investigation, adjustment and settlement of claims. Loss adjustment expenses include third-party costs as well as the Company’s internal expenses, including salaries and expenses of loss management personnel and certain administrative costs.

**“losses on claims”** means the estimated amount payable under mortgage insurance policies during a specified period. A portion of reported losses on claims represents estimates of costs of pending claims that are still open during the reporting period, as well as estimates of losses associated with claims that have yet to be reported and the cost of investigating, adjusting and settling claims.

**“loss reserves”** means case reserves based on delinquencies reported to the Company, an estimate for losses on claims based on delinquencies that are IBNR, supplemental loss reserves for potential adverse developments related to claim severity and loss adjustment expenses representing an estimate for the administrative costs of investigating, adjusting and settling claims. Loss reserves are discounted to take into account the time value of money.

**“market share”** or **“share”** of a mortgage insurer means the insurer’s gross premiums written as a percentage of the reported gross premiums written of the Canadian mortgage insurance industry.

**“net investment gains or losses”** means the sum of net realized gains or losses on sales of investments, net gains or losses on derivatives and foreign exchanges and impairment losses.

**“net underwriting income”** means the sum of premiums earned and fees and other income, less losses and sales, underwriting and administrative expenses during a specified period.

**“ordinary dividend payout ratio”** means the ratio (expressed as a percentage) of the dollar amount of ordinary dividends paid during a specified period to shareholders as a percentage of net operating income over the same period. This is a measure of the proportion of net operating income returned to shareholders in the form of ordinary dividends.

**“portfolio insurance”** means mortgage insurance covering an individual mortgage that is underwritten as part of a portfolio of mortgages that have a loan-to-value ratio equal to or less than 80% at the time the loan is insured.

**“premium tax”** means a tax paid by insurance companies to provincial and territorial governments calculated as a percentage of gross premiums written.

**“premium written”** means gross payments received from insurance policies issued during a specified period.

**“sales, underwriting and administrative expenses”** means the cost of marketing and underwriting new mortgage insurance policies and other general and administrative expenses, including premium taxes, risk fee and net of the change in deferred policy acquisition costs.

**“severity”** means the dollar amount of losses on claims.

**“share based compensation re-measurement amount”** means the impact of revaluation of stock option liability as required under IFRS due to the cash settlement option. The Company believes that excluding this impact from operating earnings per share (diluted) is a better indicator of core operating performance.

**“total debt service ratio”** or **“TDSR”** means the borrowers’ monthly debt servicing costs as a percentage of borrowers’ monthly gross income.

**“transactional insurance”** means mortgage insurance covering an individual mortgage that typically has been underwritten individually, and which is predominantly a mortgage with a loan-to-value ratio of greater than 80% at the time the loan is originated.

**“underwriter”** means an individual who examines and accepts or rejects mortgage insurance risks based on the Company’s approved underwriting policies and guidelines.

**“unearned premiums reserve”** or **“UPR”** means that portion of premiums written that has not yet been recognized as revenue. Unearned premium reserves are recognized as revenue over the policy life in accordance with the expected pattern of loss emergence as derived from actuarial analysis of historical loss development.

**“workout penetration rate”** means the ratio (expressed as a percentage) of the number of total workouts approved, including shortfall sales, over total workout opportunities. Total workout opportunities include all new and re-delinquencies reported plus total workouts approved over the same period. Workout penetration rate measures the number of workouts performed relative to the number of existing workout opportunities and is used to assess the success of the loss mitigation Homeowner Assistance Program.

The Company’s full glossary is posted on the Company’s website at <http://investor.genworthmicanada.ca> and can be accessed by clicking on the link under the Investor Resources heading on the bottom navigation bar.