FRONTENAC

MORTGAGE INVESTMENT CORPORATION

MANAGEMENT DISCUSSION & ANALYSIS

YEAR ENDED DECEMBER 31, 2020

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BASIS OF PRESENTATION

The Corporation has adopted International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") as its basis of financial reporting. The Corporation's functional and reporting currency is the Canadian dollar. This Management Discussion & Analysis ("MD&A") is prepared in accordance with National Instrument 51-102 "Continuous Disclosure".

This Management Discussion & Analysis ("MD&A") is dated March 26, 2021 and should be read in conjunction with the audited financial statements of the Corporation and the notes thereto for the years ended December 31, 2020 and 2019.

OUR BUSINESS

Frontenac Mortgage Investment Corporation (the "Corporation") is a non-bank lender that operates as a mortgage investment corporation as defined under the Income Tax Act (Canada).

The Corporation's primary investment objective is the preservation of shareholders' equity while providing shareholders with a stable stream of dividends from the Corporation's investments.

The Corporation achieves its investment objective predominantly by lending on the security of short-term residential first mortgages in the province of Ontario. The mortgage loans transacted by the Corporation will not generally meet the underwriting criteria of conventional lenders and/or involve borrowers in rural areas generally not well serviced by major lenders. As a result, the Corporation's investments are expected to earn a higher rate of interest than what is generally obtainable through conventional mortgage lending activities.

W.A. Robinson Asset Management Ltd. (the "Manager") manages the Corporation's investment portfolio and manages the distribution of the Corporation's shares. Pillar Financial Services Inc. (the "Administrator") serves as the Corporation's loan originator, underwriter, and servicer.

As a mortgage investment corporation, the Corporation does not pay corporate income taxes on any earnings that are distributed out to its shareholders provided that it continues to meet the requirements of subsection 130.1(6) of the Income Tax Act (Canada). Dividends received by shareholders are generally treated as interest income for personal income tax purposes.

HIGHLIGHTS

Frontenac Mortgage Investment Corporation continues to meet its primary objective of offering its shareholders capital preservation while providing a stable stream of monthly dividend income. The carrying value per share remained stable at $30 throughout 2020 and as at December 31, 2020 and an annualized dividend yield, assuming dividends are re-invested under the Corporation's dividend re-investment plan, of 5.17% was achieved for 2020.

As at December 31, 2020, the Corporation's assets totaled $172.3 million including a mortgage investment portfolio totaling $160.8 million with shareholder's equity of $171.6 million. Total assets and mortgage investments are down slightly from December 31, 2019, when the Corporation's assets totaled $186.3 million including a mortgage investment portfolio of $173.3 million while shareholders' equity has decreased from $174.5 million as at December 31, 2019.

The outbreak of the novel strain of coronavirus, specifically identified as "COVID-19", has resulted in a widespread health crisis that has affected economies and financial markets around the world resulting in significant economic uncertainty. As at the date of this MD&A, the performance of the Corporation has not been materially impacted; however, the Corporation continues to monitor the potential impact COVID-19 could have on its business activities including potential changes related to default rates from borrowers, demand for borrowing or the value of the underlying security of the mortgage portfolio. Further discussion of the potential impacts on the Corporation of this continuing outbreak is included in this MD&A under Results of Operations.

MORTGAGE INVESTMENT PORTFOLIO

The carrying value of the Corporation's mortgage investment portfolio totaled $160,810,418 as at December 31, 2020 as compared to $173,315,185 as at December 31, 2019.

Breakdown of the mortgage investment portfolio by type as at December 31:

	Dec 31, 2020			Dec 31, 2019		
	#	$ (000's)	% of total	#	$ (000's)	% of total
Residential	230	51,751	32.2%	309	69,254	39.9%
Residential construction	132	51,765	32.2%	128	49,443	28.5%
Residential developments	10	41,886	26.0%	11	39,110	22.6%
Commercial	10	3,863	2.4%	10	4,087	2.4%
Vacant land	47	11,545	7.2%	47	11,421	6.6%
Total	429	160,810	100.0%	505	173,315	100.0%

Residential construction comprises construction loans for single residential buildings for housing one to three units, typically single-family residences. Residential development mortgages comprise larger multi-unit construction or land development projects including sub-division developments or multi-unit housing builds. Commercial mortgages have a municipal commercial zoning component but typically also involve a residential component.

The Corporation has strategically decided that the percentage of the portfolio dedicated to residential developments will be reduced over the next few years to instead focus on its rural residential and residential construction core business. Nine of the ten loans reported in the residential developments category relate to three separate and unrelated development projects. The total outstanding principal balances for each of these three projects individually represent approximately 6% of the shareholders' equity of the Corporation. As discussed further in the impairments section below, one of these projects is impaired.

Breakdown of the mortgage investment portfolio by location as at December 31:

	Dec 31, 2020			Dec 31, 2019		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
Ontario – East	304	107,487	66.8%	366	116,774	67.4%
Ontario – Southwest	36	26,711	16.6%	42	27,755	16.0%
Ontario – Central	37	16,472	10.2%	45	19,007	11.0%
Ontario – North	51	10,109	6.3%	51	9,747	5.5%
Quebec	1	31	0.1%	1	32	0.1%
Total	429	160,810	100.0%	505	173,315	100.0%
Loans on Ontario rural property	279	105,593	65.7%	339	119,400	68.9%

The above location allocations are made using Canadian postal codes for the related real estate. Ontario – East comprises the K postal code; Ontario – Southwest comprises the N postal code; Ontario- Central comprises the L and M postal codes; and Ontario – North comprises the P postal code. Rural properties comprise postal codes designated as rural general delivery.

The Corporation's mortgage portfolio has been historically centered on the Ontario – East market, which aside from the Ottawa and Kingston markets is primarily a rural and small-town market area. As the Corporation's assets grow, management is targeting to diversify the mortgage loan portfolio to include a greater allocation to the rural areas of Ontario – Southwest to further mitigate any geographic concentration risk in the mortgage portfolio. As at December 31, 2020 and December 31, 2019, none of the Ontario – Central allocation was for properties located in the Toronto market (postal code M).

Breakdown of the mortgage investment portfolio by interest rate as at December 31:

	Dec 31, 2020			Dec 31, 2019		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
5%	2	1,057	.6%	2	1,622	.9%
6%	1	7,529	4.7%	1	7,528	4.4%
7%	3	1,080	.7%	5	1,785	1.0%
8%	17	16,886	10.5%	25	20,150	11.6%
9%	85	26,594	16.5%	126	36,572	21.1%
10%	267	81,938	51.0%	288	81,406	47.0%
11%	37	23,877	14.8%	32	8,485	4.9%
12%	13	1,259	.8%	26	15,767	9.1%
13%	4	590	.4%	-	-	-
Total	429	160,810	100.0%	505	173,315	100.0%

Substantially all of the mortgage loans are issued with either 1 or 2 year terms, have fixed interest rates and can be repaid in full before maturity without penalty. The weighted average interest rate of the mortgage loans as at December 31, 2020 was 9.54% as compared to 9.44% as at December 31, 2019.

Breakdown of the gross mortgage investment portfolio by maturity date:

	Dec 31, 2020			Dec 31, 2019		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
Within one year	403	159,835	97.2%	450	162,378	92.0%
Within following year	26	4,623	2.8%	55	14,086	8.0%
Total	429	164,458	100.0%	505	176,464	100.0%

The amounts shown in the table represent principal repayments based on contractual maturity dates at their gross amounts before any provisions for impairment losses. The new mortgage loans are offered under terms of one to two years with the vast majority of loans offered under a one year term. The Corporation targets borrowers that do not meet the underwriting criteria of the major banks and that require short-term financing in order to do so. The Corporation benefits from this short-term financing strategy as it allows the mortgage portfolio of the Corporation to be repriced frequently to current market interest rates, allows loan-to-value figures to be reset to current real estate market prices, and mitigates duration risk with borrowers.

Other key metrics related to the mortgage investment portfolio as at December 31:

	Dec 31, 2020			Dec 31, 2019		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
First mortgage loans	427	160,667	99.9%	504	173,053	99.9%
Average gross loan balance		383			349	

Mortgage impairments and provision for impairment losses:

As at December 31, 2020, there were 9 mortgages totaling $17,060,636 (December 31, 2019 – 16 mortgages totaling $18,155,907) which were considered by management to be impaired with a total provision for impairment losses of $3,202,839 and $2,838,653 against those loans as at December 31, 2020 and December 31, 2019 respectively.

The breakdown of the impaired loans and related provision for impairment losses by mortgage type is as follows:

(All figures $000's)	Dec 31, 2020			Dec 31, 2019		
	Gross loan amount (1)	**Allowance for impairment losses**	**Net carrying amount**	**Gross loan amount (1)**	**Allowance for impairment losses**	**Net carrying amount**
Residential	3,012	453	2,559	2,635	214	2,421
Residential construction	149	-	149	340	8	332
Residential developments	13,714	2,750	10,964	14,476	2,317	12,159
Commercial	-	-	-	-	-	-
Vacant land	186	-	186	705	300	405
Total	17,061	3,203	13,858	18,156	2,839	15,317

(1) Gross amount shown at amortized cost

Based on its risk profile of the mortgage loan borrowers for its niche in the mortgage marketplace, the Corporation expects that and would consider normal that, on average in any given year, 5% of the Corporation's mortgage portfolio would be considered impaired. A definition of impairment is included in the section "Critical Accounting Estimates and Policies – (i) Mortgage Investments" of this MD&A. On those impaired loans, the Corporation would project losses of capital of 0.50% of shareholders' equity or $0.15 per share based on the Corporation's historical carrying value per share of $30. Once a mortgage is considered impaired, the Corporation ceases to accrue additional interest revenue on that mortgage which in turn reduces total revenue per share. For 2020, the Corporation averaged 10.88% of its shareholders' equity as impaired mortgages and incurred mortgage provisions and realized losses of $0.18 per share. For 2019, the Corporation averaged 10.06% of its shareholders' equity as impaired mortgages and incurred mortgage provisions and realized losses of $0.20 per share.

The impairments as at December 31, 2020 include a group of mortgages totaling $13,713,369 (December 31, 2019 - $14,463,944) related to a single development project. The Corporation has recognized provisions for losses totaling $2,750,000 (December 31, 2019 - $2,226,000) related to these loans which represent management's comparison of the discounted expected net proceeds from the sale of the underlying real estate security against the loan amounts outstanding. The power-of-sale process for this group of loans was completed in October 2018 and the related properties are listed for sale.

If this single large group of loans is excluded, as at December 31 2020, the remainder of the mortgage portfolio was performing within normal expectations as there were 8 impaired mortgages totaling $3,347,267 (1.95% of shareholders' equity) and the largest impaired mortgage was $1,622,014. If the same single large group of loans is excluded as at December 31, 2019, there were 15 impaired mortgages totaling $3,691,963 (2.1% of shareholders' equity) and the largest impaired mortgage was $666,670.

RESULTS OF OPERATIONS

Financial Summary

(all figures presented are for year ended December 31)

	2020 $	2019 $	2018 $
Interest income	15,086,513	15,810,099	18,134,892
Management & administration fees	3,880,095	4,117,383	4,608,592
Interest on credit line	87,574	124,846	707,639
Provision for mortgage impairment losses	1,071,835	1,292,201	738,184
Other operating expenses	910,690	618,686	747,488
Total operating expenses	5,950,194	6,153,116	6,801,903
Net income and comprehensive income	9,136,319	9,656,983	11,332,989
Total mortgage investments – at Dec 31	160,810,418	173,315,185	180,967,671
Total assets – at Dec 31	172,300,744	186,286,656	192,344,235
Total shareholders' equity – at Dec 31	171,641,472	174,530,552	177,787,465
Per share data:			
Revenue	2.51	2.46	2.74
Earnings – basic & fully diluted	1.52	1.50	1.71
Dividends per common share	1.52	1.50	1.54
Carrying value per common share – at Dec 31	30.00	30.00	30.00

Results of Operations – Year Ended December 31, 2020

Net income and comprehensive income for the Corporation for the year ended December 31, 2020 decreased on a gross basis to $9,136,319 from $9,656,983 for the year ended December 31, 2019 while, on a per share basis, net earnings increased slightly to $1.52 from $1.50 per common share.

Revenues for the Corporation for the year ended December 31, 2020 were substantially unchanged on a gross basis at $15,086,513 as compared to $15,810,099 for the year ended December 31, 2019 while, on a per share basis, revenues increased slightly to $2.51 from $2.46 per common share.

Total operating expenses, excluding provision for impairment losses, for the year ended December 31, 2020 increased on a gross basis to $4,878,359 from $4,860,915 for the year ended December 31, 2019 while, on a per share basis, these expenses increased to $0.812 from $0.757 per common share. The period-over period increase is a reflection of a period-over-period increase in legal and audit expenses related to the transition in regulatory oversight from investment funds to corporate finance.

A detailed discussion of impairments and impairment losses in 2020 is presented in the Mortgage Impairments section of the "Mortgage Investment Portfolio" section of this MD&A.

Impact and Potential Impact of COVID-19 Outbreak

The coronavirus disease 2019 ("**COVID-19**") outbreak, ongoing as of the date of this MD&A, was declared a pandemic by the World Health Organization in March, 2020. Steps taken over the course of 2020 by governments around the world, including in Frontenac's primary lending market in the Province of Ontario, to contain the spread of the COVID-19 virus included legislated closures of non-essential businesses and services and social distancing measures slowing economic activity and resulting in layoffs and lost jobs as businesses struggle with the economic effects. What follows is a commentary on how the Corporation has fared during the pandemic and the potential impact of a continuance of the current economic conditions under COVID-19 on the Corporation's future performance.

Beginning in late March, the Corporation began operating under its business continuity plan with most management and staff of the Corporation, and of the Manager and the Administrator, working remotely pursuant to social distancing guidelines. Despite working remotely, the Manager and Administrator have been able to execute their respective functions effectively under the business continuity plan.

The Corporation has been able to have substantially all of its available equity invested in mortgage loan assets throughout the second, third, and fourth quarters of 2020, while at the same time preserving its line of credit to meet redemption requests and as a reserve to meet any unexpected future cash needs arising in this COVID-19 environment.

As at December 31 2020, the Corporation had one credit impaired mortgage resulting from COVID-19 economic effects and had made deferral arrangements for six loans in its portfolio. Deferral arrangements are made on a month-to-month basis. Any deferral arrangements offered by the Corporation are not interest-free and therefore do not have a negative impact on interest revenues of the Corporation. Over the course of 2020, the Corporation experienced just the one credit impaired mortgage resulting from COVID-19 economic effects and had a maximum number of only twelve loans with COVID-19 related deferral arrangements outstanding at any given time. These results compare favourably to an average monthly number of 469 total mortgage loans outstanding in its loan portfolio throughout 2020.

The majority of Frontenac's loans relate to owner-occupied principal residences and, in down economic times, cash outflows related to personal housing are among the last to be cut by people. Essentially, impairment or default is several steps down the road for most borrowers only after they have exhausted cash reserves, cut down on other expenses, worked with government assistance, and worked on potential deferral arrangements. In response to the COVID impacts on the general economy, there have been unprecedented government financial supports introduced throughout 2020 that have helped borrowers in staying current with their mortgage obligations. The Canada Emergency Response Benefit (CERB) that was introduced by the Government of Canada in early 2020 to assist those adversely affected economically by COVID ended in September 2020, but was replaced by the commencement of enhanced Employment Insurance (EI) benefits for people who were still unemployed and other special support programs for those otherwise affected by COVID-19. These government programs extend into 2021.

The expectations for any significant change or increase in the Corporation's impairments over the next four to six months is uncertain. General economic forecasts point to a return to pre-COVID 19 economic forecasts in Canada by the end of 2021. Government financial supports are expected to continue as necessary. Multiple vaccines have now been approved and vaccinations are proceeding. These positive signs may be offset by the emergence of COVID-19 variants and the potential for subsequent waves of new infections that offset the progress made. If the Corporation experiences an increase in impairments, such an increase would translate into lower earnings due to the unlikely collectability of further interest on those loans.

The potential for increase in capital losses on impaired loans requires a decline in home values below the carrying value of the related loans. Frontenac's underwriting policies of focusing on first mortgage loans (99.9% firsts) to a maximum loan-to-value at origination of 80% or less provides some room for a decline in home values. Based on Canadian Real Estate Association ("CREA") data for 2020, the volume of home sales recovered from March 2020 lows and total home sales for 2020 exceeded 2019 sales volumes. In addition, there has not been a decline in home values in the Corporation's lending area. There has been increased consumer demand for rural properties and this demand has led to a significant increase in home prices of up to 20% year-over-year in the Corporation's lending areas. Based on these market conditions, the Corporation does not anticipate that the effects of COVID-19 will lead to any unusual capital losses on the Corporation's impaired loans in the near term.

The impact of COVID-19 on the future performance of the Corporation continues to depend largely on the scope and duration of the pandemic and the related economic shutdown and the speed of the subsequent economic recovery. Although, as discussed above, there are positive indicators that the pandemic may be nearing the end, there is no certainty as at the date of this MD&A as to how long the pandemic will last and when people and businesses will be able to fully return to normalcy.

Summary of Quarterly Results - (Unaudited)

(All figures in thousands except per share figures. Q1 is three months ended March 31; Q2 is three months ended June 30; Q3 is three months ended September 30; Q4 is three months ended December 31)

	Q4 2020 $	Q3 2020 $	Q2 2020 $	Q1 2020 $	Q4 2019 $	Q3 2019 $	Q2 2019 $	Q1 2019 $
Interest income	3,778	3,893	3,567	3,848	4,229	4,113	3,699	3,769
Management & admin fees	974	992	949	965	1,083	1,075	962	997
Interest on credit line	6	5	3	73	68	2	-	56
Provision for impairment losses	348	325	118	281	627	358	120	(187)
Other operating expenses	160	263	248	240	153	152	138	176
Total operating expenses	1,488	1,585	1,318	1,559	1,931	1,587	1,220	1,416
Net income and comprehensive income	2,290	2,308	2,249	2,289	2,298	2,526	2,479	2,353
Earnings per share – basic and fully diluted	.379	0.378	0.376	0.387	0.352	0.378	0.385	0.387

Management and administration fees fluctuate as total assets of the Corporation fluctuate as they are determined based on a fixed percentage of total assets of the Corporation with 1% per annum paid by the Manager and 1% per annum paid to the Administrator calculated and paid on a monthly basis. The Corporation does not use leverage but does maintain a line of credit as a reserve to meet redemption requests and to allow the Corporation to smooth out its cash inflows and outflows related to mortgage advances and repayments. The amount of interest expense in any quarter fluctuates with the actual utilization of the available credit line. Other operating expenses comprise legal, audit, directors fees and expenses, and other operating costs of the Corporation and may fluctuate based on the timing of these expenses throughout the year.

For Q4 2019, the Corporation recognized impairment losses totaling $626,574. As explained in more detail in the above discussion of impairments in the "Mortgage Investment Portfolio" section of this MD&A, the impairments include a group of mortgages related to a single development project. The Corporation increased its provisions for losses by $660,000 in Q4 2019 related to these loans representing management's updated comparison of the discounted expected net proceeds from the sale of the underlying real estate security against the loan amounts outstanding.

Results of Operations – Three Months Ended December 31, 2020

Net income and comprehensive income for the Corporation for the three months ended December 31, 2020 ("Q4 2020") decreased slightly on a gross basis to $2,290,242 from $2,297,949 for the three months ended December 31, 2019 ("Q4 2019") while, on a per share basis, net earnings increased slightly to $0.379 for Q4 2020 as compared to $0.352 per common share for Q4 2019.

Revenues for the Corporation for Q4 2020 decreased on a gross basis to $3,777,951 from $4,228,684 for Q4 2019 while, on a per share basis, revenues decreased slightly to $0.625 from $0.650 per common share.

Total operating expenses, excluding provision for impairment losses, decreased slightly to $1,140,153, or $0.188 per common share, for Q4 2020 compared to $1,304,160, or $0.198 per common share, for Q4 2019.

LIQUIDITY AND CAPITAL RESOURCES

The Corporation is authorized to issue an unlimited number of common shares. Under the terms of the Corporation's continuous offering prospectus, Frontenac issues common shares on up to a monthly basis. Shareholders may redeem shares in the Corporation only once per year, in November, except in certain exceptional circumstances. As at December 31, 2020, there were 5,721,384 common shares issued and outstanding with a total book value of $171,532,472.

Growth in the mortgage portfolio is financed by the issuance of common shares. We expect to be able to generate sufficient funds for future growth in net mortgage loans by utilizing this funding source only. The Corporation has not historically, and does not intend in the future, to supplement this funding using leverage.

The Corporation is a public issuer under Canadian securities law and, in May 2020, completed a transition from regulatory oversight as an investment fund to regulatory oversight as a corporate finance issuer. This change did not have any material impact how the Corporation raises new capital through the issuance of new common shares nor its ability to do so.

The Corporation has a revolving line of credit with a major Canadian chartered bank with a limit equal to 15% of shareholders' equity of the Corporation to a maximum limit of $29.0 million. The line of credit is secured by a General Security Agreement and a first ranking interest in the mortgages, is repayable on demand, and bears interest at bank prime rate plus 1%. Financial covenants require the Corporation to maintain minimum levels for equity, debt to equity ratio, and percentage of residential mortgages. As at December 31, 2020 and December 31, 2019, the Corporation was in compliance with the bank's financial covenants, and management expects to remain in compliance with such covenants going forward.

The line of credit is used to smooth out the cash flows of the Corporation and as a reserve for unexpected share redemptions and is not used to extend the Corporation's investment capacity beyond its available equity. As at December 31, 2020, the Corporation was using $nil (December 31, 2019 - $11,330,000) of its available credit line. The maximum borrowings at any time during 2020 was $11,690,000 (2019 year - $17,880,000).

CHANGES IN FINANCIAL POSITION

The Corporation is authorized to issue an unlimited number of common shares. Under the terms of the its continuous offering prospectus, the Corporation issues common shares on a monthly basis. The following table presents a summary of outstanding share data and transactions for the year ended December 31:

	Year ended December 31, 2020		**Year ended December 31, 2019**	
Common shares:	#	$	#	$
Balance – beginning of period	5,817,686	174,421,552	5,926,249	177,678,465
Issued for cash	441,568	13,247,035	861,616	25,848,472
Issued under dividend re-investment plan	143,821	4,314,616	192,263	5,767,877
Redeemed	(681,691)	(20,450,731)	(1,162,442)	(34,873,262)
Balance – end of period	5,721,384	171,532,472	5,817,686	174,421,552

Under the Corporation's dividend policy and dividend re-investment plan, unless a shareholder elects to receive their dividends in cash, monthly dividends are automatically re-invested into additional shares of the Corporation at the then prevailing carrying value per share.

Under the terms of the Corporation's prospectus, shareholders may redeem shares in the Corporation only once per year, on November 30, except in certain exceptional circumstances. 90% of the redemptions for 2020 occurred in November of that year.

CONTRACTUAL OBLIGATIONS

Contractual obligations due at December 31, 2020 are all due within one year and are as follows:

	$
Dividends payable	490,470
Accounts payable and accrued liabilities	121,523
	611,993

As at December 31, 2020, the Corporation has commitments to advance additional funds of $30,477,000 under existing mortgages (Dec 31, 2019 - $26,104,000). These outstanding commitments are generally expected to be funded over the next 12 months. These commitments relate primarily to residential construction mortgages where funds are advanced as projects are completed subject to third party inspections and other underwriting controls and procedures. In our experience, a portion of the unfunded commitments on existing mortgage loans will never be drawn.

TRANSACTIONS WITH RELATED PARTIES

Transactions with related parties are in the normal course of business.

Pillar Financial Services Inc. (“Pillar”) is the administrator and W.A. Robinson Asset Management Ltd. (“W.A.”) is the manager for the Corporation. These companies are related parties in that they share common management. The Corporation signed new contracts for these services in 2008 under which Pillar and W.A. each charge an annual fee of 1% of the total asset value calculated on a monthly basis. These contracts were renewed for further five-year periods in 2013 and 2018.

Administration and management fees paid under these agreements totaled $974,079 for the three months ended December 31, 2020 (three months ended December 31, 2019 - $1,083,178) including applicable sales taxes. Administration and management fees paid under these agreements totaled $3,880,095 for the year ended December 31, 2020 (year ended December 31, 2019 - $4,117,383) including applicable sales taxes. The decrease in the dollar value of the administration and management fees in 2020 from 2019 reflects a year-over-year decrease in the average total assets of the Corporation.

CRITICAL ACCOUNTING ESTIMATES AND POLICIES

The preparation of financial statements in accordance with IFRS requires management to make assumptions and estimates and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements, the reported amounts of revenue and expenses for the year, as well as the disclosure of contingent assets and liabilities at the date of the financial statements.

In making estimates and judgements, the Manager relies on external information and observable conditions where possible supplemented by internal analysis as required. Those estimates and judgements have been applied in a manner consistent with the prior period and there are no known trends, commitments, events, or certainties that are believed to materially affect the methodology or assumptions utilized in making those estimates in these financial statements. Actual amounts could differ from these estimates. Changes in estimates are recorded in the accounting period in which they are determined. Significant estimates used in determining the recorded amount for assets and liabilities in the financial statements are as follows:

(i) Mortgage investments:

The Corporation is required to make an assessment as to whether the credit risk of a mortgage has changed significantly since initial recognition and is also required to determine the impairment of mortgage investments. The Corporation considers a number of factors when assessing if there has been a significant increase in credit risk. Mortgages with payments over 30 days in arrears are immediately flagged as potentially being in Stage 2. Other factors that the Corporation considers when confirming if there has been a significant increase in credit risk include changes in the financial condition of the borrower, responsiveness of the borrower, and other borrower or property specific information that may be available. Mortgage investments are considered to be impaired only if objective evidence indicates that one or more events have occurred after its initial recognition that have a negative effect on the estimated future cash flows of that asset. The estimation of future cash flows includes assumptions about local real estate market conditions, market interest rates, availability and terms of financing, underlying value of the security and various other factors. These assumptions are limited by the availability of reliable comparative market data, economic uncertainty and the uncertainty of future events. Accordingly, by their nature, estimates of impairment are subjective and may not necessarily be comparable to the actual outcome. Should the underlying assumptions change, the estimated future cash flows could vary.

The quantitative aspect of the expected credit loss begins with the use of an Autoregressive Distributed Lag ("ARDL") model. The ARDL model indicates that expected credit losses are largely explained by borrower specific information such as credit score, debt servicing ratios, borrower equity and age and are not a function of statistics or forecasts of national economic performance. As a result, the Corporation incorporates borrower specific information to estimate the probability of default over the life of the mortgage to estimate expected credit losses. In instances where qualitative information about a mortgage indicates that the borrower may have experienced an increase in credit risk, the Corporation incorporates the new information and re-estimates the probability of default. This new estimate is then used to evaluate the probability of default between the occurrence of the increased credit risk and the end of the mortgage term. In all cases, the probability of default is used as a weighting factor in determining expected credit losses on each individual mortgage within the portfolio.

IFRS 9 uses an expected credit loss (“ECL”) model to determine the provision for credit losses.
The ECL allowances are calculated through three probability-weighted forward-looking scenarios including base, optimistic, and pessimistic, that measures the expected cash shortfalls on the financial assets related to default events either (i) over the next 12 months or (ii) over the expected life based on the maximum contractual period over which the Corporation is exposed to credit risk. The expected life of certain revolving credit facilities is based on the period over which the Corporation is exposed to credit risk and where the credit losses would not be mitigated by management actions. The three scenarios are updated at each reporting date, and the probability weights and the associated scenarios are determined through a management review process that involves significant judgement and review by the Corporation’s Finance and Risk management groups.

Upon initial recognition of financial assets, the Corporation recognizes a 12-month ECL allowance which represents the portion of lifetime ECL that result from default events that are possible within the next 12 months (Stage 1). If there has been a Significant Increase in Credit Risk (“SICR”), the Corporation then recognizes a lifetime ECL allowance resulting from possible default events over the expected life of the financial asset (Stage 2). The SICR is determined through changes in the lifetime probability of default ("PD") since initial recognition of the financial assets, using a combination of borrower specific and account specific attributes with a presumption that credit risk has increased significantly when contractual payments are more than 30 days past due. This assessment considers all reasonable and supportable information about past events, current conditions and forecasts of future events and economic conditions that impact the Corporation's credit risk assessment. Criteria for assessing SICR are defined at a portfolio level and vary based on the risk of default at the origination of the portfolio. If credit quality subsequently improves such that the increase in credit risk since initial recognition is no longer significant, the loss allowances will revert back to be measured based on a 12-month ECL, and the financial asset will transfer from Stage 2 back to Stage 1. Stages 1 and 2 comprise all non-impaired financial assets.

Management developed a modelling of the Stage 2 estimate which requires a reassessment of the overall credit risk resulting from a SICR. The model developed for SICR assumes a complete degradation in credit quality as proxied by the borrower's Beacon Score. This enters into a logistic regression to estimate lifetime probability of default based on this new assumption. The lifetime probability of default estimate then enters into the Survival Analysis as a parameter to allow probability of default to be estimated over the remaining term to maturity.

In addition, management exercises expert credit judgements in assessing exposures that have experienced a SICR and in determining the amount of ECL allowances required at each reporting date by considering reasonable and supportable information that are not already included in the quantitative models. Expert credit judgements are performed by considering emergence of economic, environmental or political events, as well as expected changes to parameters, models or data that are not currently incorporated. Significant judgements made by management may impact the amount of ECL allowances recognized. ECL is calculated as the product of PD, loss given default ("LGD"), and exposure at default ("EAD"), and is calculated over the remaining expected life of the financial asset and discounted to the reporting date at the respective effective interest rate. PD measures the estimated likelihood of default over a given time period. PD estimates are updated for each scenario at each reporting date and is based on current information. LGD provides the estimate of loss when default occurs at a given time, and is determined based on historical write-off events, recovery payments, borrower specific attributes and direct costs. The estimate is updated at each reporting date for each scenario based on current information. EAD estimates the exposure at the future default date.

As at December 31, 2020, no adjustments were deemed necessary to the ECL modelling to account for potential impacts arising from the COVID-19 pandemic. As at December 31, 2020, the Corporation had made 6 deferral arrangements with borrowers on account of COVID-19, which are included with the stage 2 loans in the ECL model. The impact of COVID-19 on the ECL model of the Corporation will depend entirely on the scope and duration of the pandemic and the related economic shutdown and the speed of the subsequent economic recovery. There is no certainty at this time as to how long the pandemic will last and when people and businesses will be able to return to normalcy. Further commentary on the impact of COVID-19 is provided in Note 2 to the Corporation's financial statements.

Financial assets with objective evidence of impairment as a result of loss events that have a negative impact on the estimated future cash flows are considered to be impaired requiring the recognition of lifetime ECL allowances. (Stage 3). Deterioration in credit quality is considered an objective evidence of impairment and includes observable data that comes to the attention of the Corporation, such as significant financial difficulty of the borrower. The Corporation defines default as when there is identification of objective evidence of impairment (which could, for example, be delinquency of 90 days or more). A financial asset is no longer considered impaired when past due amounts have been recovered, and the objective evidence of impairment is no longer present.

Financial assets are written off, either partially or in full against the related allowances for credit losses when the Corporation believes there are no reasonable expected future recoveries through payments or the sale of the related security. Any recoveries of amounts previously written off are credited against provision for credit losses in the statements of income and comprehensive income.

Loan Modification

The Corporation defines loan modification as changes to the original contractual terms of the financial asset that represents a fundamental change to the contract or changes that may have a significant impact on the contractual cash flow of the asset. The Corporation derecognizes the original asset when the modification results in significant change or expiry in the original cash flows; a new asset is recognized based on the new contractual terms. The new asset is assessed for staging and SICR to determine the corresponding ECL measurement required at the date of modification. If the Corporation determines the modifications do not result in derecognition, then the asset will retain its original staging and SICR assessments.

(ii) Fair value measurements:

In accordance with IFRS, the Corporation must classify fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making its fair value measurements. The following hierarchy has been used in determining and disclosing fair value of financial instruments:

> Level 1: quoted prices in active markets for the same instrument (i.e. without modification or repackaging);
> Level 2: quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data; and
> Level 3: valuation techniques for which any significant input is not based on observable market data.

The Corporation's cash and cash equivalents are valued using Level 1 measures and the properties held for sale under foreclosure are valued using Level 3 measures as there are no quoted prices in an active market for these investments. As explained in more detail in Note 12, management makes its determination of fair value of mortgages by discounting future cash flows at the Corporation's prevailing rate of return on new mortgages of similar type, term, and credit risk.

These assumptions are limited by the availability of reliable comparative market data, economic uncertainty and the uncertainty of future events. Accordingly, by their nature, measurements of fair value are subjective and may not necessarily be comparable to the actual outcome. Should the underlying assumptions change, the estimates could vary.

FINANCIAL INSTRUMENTS

The Corporation 's most significant financial asset consists of its mortgage investments. Mortgage investments are classified as measured at amortized cost. The financial risks associated with the

Corporation's mortgage investments and the Corporation 's management of those risks are discussed in Note 8 of the financial statements.

The Corporation 's other financial assets consist of cash and cash equivalents, due from administrator in trust, and accrued interest receivable. The Corporation 's financial liabilities consist of bank line of credit, dividends payable, and accounts payable and accrued liabilities. Unless otherwise noted, it is management's opinion that the Corporation is not exposed to significant interest or currency risks arising from these financial instruments. The fair value of these financial instruments approximate their carrying value, unless otherwise noted.

The Corporation classifies its financial assets as one of the following: measured at amortized cost or fair value through profit or loss ("FVTPL") or fair value through other comprehensive income ("FOCI"). Financial liabilities are classified as: FVTPL or financial liabilities at amortized cost. The Corporation has designated its financial assets and financial liabilities as follows:

(i) Financial assets:
Cash and cash equivalents are classified as FVTPL. Due from administrator in trust, accrued interest receivable, and mortgage investments are classified as measured at amortized cost.

(ii) Financial liabilities:
Bank line of credit, dividends payable, and accounts payable and accrued liabilities are classified as financial liabilities at amortized cost.

The tables in note 12 of the financial statements present the fair values of the Corporation's financial instruments as at December 31, 2020 and December 31, 2019.

CHANGES IN ACCOUNTING POLICIES

Significant accounting policies are described in note 4 of the Corporation's financial statements.

At the date of authorization of this MD&A, certain new standards, and amendments to existing standards have been published by the International Accounting Standards Board ("IASB"). Information on those expected to be relevant to the Corporation's financial statements is provided below.

Management anticipates that all relevant pronouncements will be adopted in the Corporation's accounting policies for the first period beginning after the effective date of the pronouncement. New standards, interpretations, and amendments not either adopted or listed below did not have a material impact on the Corporation's financial statements.

New accounting standards implemented during the year:

IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors

Effective January 1, 2020, the IASB implemented an amendment to IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors. The amendment clarified the definition of "material" and aligned the definition used in the Conceptual Framework and the standards themselves. The information provided in the Company financial statements is compliant with the issued amendment to IAS 8, Accounting

Policies, Changes in Accounting Estimates and Errors. The Corporation adopted the amendments in its financial statements for the period beginning January 1, 2020. The implementation of the amendments did not have a material impact on the Corporation's financial statements.

New accounting standards pending for future periods:

IAS 1 - Presentation of Financial Statements

In January 2020, the IASB issued an amendment to IAS 1, Presentation of Financial Statements to come into effect January 1, 2022. The amendment is to provide clarification on the classification of liabilities as current or non-current. On July 15, 2020 the effective date of these amendments was deferred by one year to January 1, 2023. Early adoption is permitted. The Corporation will adopt the amendments in its financial statements for the annual period beginning January 1, 2023. The Corporation does not expect the amendments to have a material impact on the financial statements.

RISKS AND UNCERTAINTIES

The Corporation is subject to many risks and uncertainties that may limit our ability to execute on our strategies and achieve our objectives. We have processes and procedures in place in an attempt to control or mitigate certain risks, while others cannot be or are not mitigated. Material risks that cannot be mitigated include a significant decline in the general economy and general real estate market, a significant change in interest rates, an inability to make mortgage loans at rates consistent with rates historically achieved, and having an insufficient amount of new mortgage loan opportunities presented.

See "Forward-Looking Information" below and the Risk Factors section of the Corporation's prospectus for further information on risks and uncertainties faced by the Corporation. The Corporation's prospectus is available on www.sedar.com and on the Corporation's website at www.fmic.ca.

A discussion of the impact and potential impact on the operations and performance of the Corporation of the recent and on-going COVID-19 outbreak is included in this MD&A under Operating Results.

FORWARD-LOOKING INFORMATION

From time to time in our public communications we provide forward-looking statements. Such statements are disclosures regarding possible events, conditions, results of operations or changes in financial position that are based upon assumptions and expectations. These are not based on historical facts but are with respect to management's beliefs, estimates, and intentions. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "outlook", "objective", "may", "will", "expect", "intent", "estimate", "anticipate", "believe", "should", "plans", or "continue" or other similar expressions suggesting future outcomes or events. Forward looking statements regarding performance of the economy in general and real estate markets in particular. Forward-looking statements generally assume that our revenues and expenses continue to follow current trends, and that current trends in our mortgage portfolio continue.

All forward-looking statements reflect management's current beliefs and are based on information currently available to management. These statements are not guarantees of future performance and are based on our estimates and assumptions that are subject to risks and uncertainties which could cause our actual results to differ materially from the forward-looking statements contained in this MD&A or elsewhere. Those risks and uncertainties include risks associated with mortgage lending, competition for mortgage lending, real estate values, interest rate fluctuations, environmental matters, and the general economic environment. For other risks and uncertainties, please refer to "Risks and Uncertainties" above and to the "Risk Factors" section of the Corporation's prospectus which is available at www.sedar.com and www.fmic.ca. That list is not exhaustive as other factors could adversely affect our results, performance, or achievements. The reader is cautioned against undue reliance on any forward-looking statements.

Although the forward-looking information contained in this MD&A is based on what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements. We will not publicly update or revise any forward-looking statement, whether as a results of new information, future events, or otherwise, unless required to do so by law.

RESPONSIBILITY OF MANAGEMENT AND THE BOARD OF DIRECTORS

Management is responsible for the information disclosed in this MD&A and has in place the appropriate information systems, procedures and controls to ensure the information used internally by management and externally is materially complete and reliable. In addition, our audit committee and board of directors provide an oversight role with respect to our public financial disclosures and have reviewed and approved this MD&A and the financial statements as at December 31, 2020.

ADDITIONAL INFORMATION

Additional information about Frontenac Mortgage Investment Corporation, including the audited financial statements for the year ended December 31, 2020 and the audited financial statements for the year ended December 31, 2019, is available on SEDAR at www.sedar.com or on our website at www.fmic.ca. You may also obtain information by contacting the Corporate Secretary for Frontenac Mortgage Investment Corporation by telephone at (613) 279-2116 or by email at amber.kehoe@robinsonsgroup.com.