FRONTENAC

MORTGAGE INVESTMENT CORPORATION

MANAGEMENT DISCUSSION & ANALYSIS

QUARTER ENDED MARCH 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 May 7, 2020 and should be read in conjunction with the unaudited financial statements of the Corporation and the notes thereto for the three months ended March 31, 2020 and 2019, the audited financial statements and the notes thereto for the years ended December 31, 2019 and 2018, as well as the MD&A, including the section on Risks and Uncertainties for the years then ended.

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 at March 31, 2020 with an annualized dividend yield, assuming dividends are re-invested under the Corporation's dividend re-investment plan, of 5.20% for the first quarter of 2020.

As at March 31, 2020, the Corporation's assets totaled $180.9 million including a mortgage investment portfolio totaling $167.2 million with shareholder's equity of $178.8 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 increased 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 it 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 $167,262,298 as at March 31, 2020 as compared to $173,315,185 as at December 31, 2019.

Breakdown of the mortgage investment portfolio by type as at March 31, 2020 and December 31, 2019:

	Mar 31, 2020			**Dec 31, 2019**		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
Residential	298	65,244	39.0%	309	69,254	39.9%
Residential construction	115	47,892	28.6%	128	49,443	28.5%
Residential developments	11	39,038	23.3%	11	39,110	22.6%
Commercial	9	3,759	2.3%	10	4,087	2.4%
Vacant land	47	11,329	6.8%	47	11,421	6.6%
Total	480	167,262	100.0%	505	173,315	100.0%

Residential construction comprise 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 eleven loans reported in this category relate to three separate and unrelated development projects. The total outstanding principal balances for each of these three projects individually represent approximately 7% of the shareholders' equity of the Corporation. As discussed further in the impairments section below, one of these projects is impaired.

The power-of-sale process for this project was completed in October 2018 and the related lands are available for sale under power-of-sale. Breakdown of the mortgage investment portfolio by location as at March 31, 2020 and December 31, 2019:

	Mar 31, 2020			Dec 31, 2019		
	#	$ (000's)	% of total	#	$ (000's)	% of total
Ontario – East	344	115,306	68.9%	366	116,774	67.4%
Ontario – Southwest	45	25,004	14.9%	42	27,755	16.0%
Ontario – Central	39	17,843	10.7%	45	19,007	11.0%
Ontario – North	51	9,077	5.4%	51	9,747	5.5%
Quebec	1	32	0.1%	1	32	0.1%
Total	480	167,262	100.0%	505	173,315	100.0%
Loans on Ontario rural property	315	112,313	67.1%	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 grows, management is targeting to diversify primarily to the rural areas of Ontario – Southwest to further mitigate any geographic concentration risk in the mortgage portfolio. The reduction in the percentage of the portfolio represented by Ontario – East from 75.3% at the end of 2018 to 67.4% at the end of 2019 is a reflection of that strategy. As at March 31, 2020 and December 31, 2019, substantially none (Mar 31, 2020 – 0%; Dec 31, 2019 – 0.2%) 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 March 31, 2020 and December 31, 2019:

	Mar 31, 2020			Dec 31, 2019		
	#	$ (000's)	% of total	#	$ (000's)	% of total
5%	2	1,614	1.0%	2	1,622	.9%
6%	1	7,528	4.5%	1	7,528	4.3%
7%	5	1,816	1.1%	5	1,785	1.0%
8%	22	19,661	11.7%	25	20,150	11.6%
9%	120	34,416	20.5%	126	36,572	21.1%
10%	271	78,906	47.2%	288	81,406	47.0%
11%	35	7,653	4.6%	32	8,485	4.9%
12%	24	15,668	9.4%	26	15,767	9.1%
Total	480	167,262	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 March 31, 2020 was 9.43%, substantially unchanged from 9.44% as at December 31, 2019.

Breakdown of the mortgage investment portfolio by maturity date:

	Mar 31, 2020			**Dec 31, 2019**		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
2020	427	156,728	91.9%	450	162,378	92.0%
2021	53	13,713	8.1%	55	14,086	8.0%
Total	480	170,441	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 March 31, 2019 and December 31, 2019:

	Mar 31, 2020			Dec 31, 2019		
	#	**$ (000's)**	**% of total**	**#**	**$ (000's)**	**% of total**
First mortgage loans	477	167,004	99.9%	502	173,053	99.9%
Average gross loan balance		355			349	

Mortgage impairments and provision for impairment losses:

As at March 31, 2020, there were 19 mortgages totaling $21,574,756 (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 $2,841,502 and $2,838,653 against those loans as at March 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)	Mar 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	3,885	163	3,722	2,635	214	2,421
Residential construction	1,423	8	1,415	340	8	332
Residential developments	14,512	2,368	12,144	14,476	2,317	12,159
Commercial	993	-	993	-	-	-
Vacant land	762	303	459	705	300	405
Total	21,575	2,842	18,733	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 the first three months of 2020, the Corporation averaged 11.3% of its shareholders' equity as impaired mortgages and incurred mortgage provisions and realized losses of $0.05 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 for each of 2019 and 2018 include a group of mortgages totaling $14,511,789 (December 31, 2019 - $14,463,944) related to a single development project. The Corporation has recognized provisions for losses totaling $2,226,000 (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 March 31, 2020, the remainder of the mortgage portfolio was performing within normal expectations as there were 18 impaired mortgages totaling $7,062,967 (3.9% of shareholders' equity) and the largest impaired mortgage was $1,618,615. 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

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)

	Q1 2020 $	Q4 2019 $	Q3 2019 $	Q2 2019 $	Q1 2019 $	Q4 2018 $	Q3 2018 $	Q2 2018 $
Interest income	3,848	4,229	4,113	3,699	3,769	4,218	4,654	4,824
Management & admin fees	965	1,083	1,075	962	997	1,125	1,196	1,173
Interest on credit line	73	68	2	-	56	95	208	235
Provision for impairment losses	281	627	358	120	187	(172)	180	393
Other operating expenses	240	153	152	138	176	246	178	166
Total operating expenses	1,559	1,931	1,587	1,220	1,416	1,294	1,762	1,967
Net income and comprehensive income	2,289	2,298	2,526	2,479	2,353	2,924	2,892	2,857
Earnings per share – basic and fully diluted	0.387	0.352	0.378	0.385	0.387	0.443	0.429	0.434

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 March 31, 2020

Net income and comprehensive income for the Corporation for the three months ended March 31, 2020 (“Q1 2020”) decreased on a gross basis to $2,288,851 from $2,353,334 for the three months ended March 31, 2019 (“Q1 2019”) while, on a per share basis, net earnings remained constant at $0.387 per common share.

Revenues for the Corporation for Q1 2020 increased slightly on a gross basis to $3,848,376 from $3,768,868 for Q1 2019 while, on a per share basis, revenues increased slightly to $0.651 from $0.620 per common share.

Total operating expenses, excluding realized and unrealized gains and losses, were largely unchanged at $1,278,659, or $0.213 per common share, for Q1 2020 compared to $1,228,368, or $0.203 per common share, for Q1 2019.

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 by governments around the world to contain the spread of the COVID-19 virus including legislated closures of non-essential businesses and services and social distancing measures have slowed economic activity and have resulted in layoffs and lost jobs as businesses struggle with the economic effects. The Province of Ontario, Frontenac's primary lending market, did not implement the closure of non-essential businesses until late March 2020. Accordingly, the operating results of Frontenac for the first quarter ended March 31, 2020 were largely unaffected by COVID-19 related issues.

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 impact of COVID-19 on the future performance of the Corporation will 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 at the date of this MD&A, several provinces including the Province of Ontario have taken small steps to reopen their economies, 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. What follows is a commentary on the potential impact of a continuance of the current economic conditions under COVID-19 on the Corporation's future performance.

Over the next quarter, the Corporation may start to build cash as it becomes more difficult to close new mortgage loans as a result of: (i) slowdowns in applications for new home purchases due to the dramatic decline in housing sales, (ii) delays in closing new residential construction loans due to a government restrictions on the issuance of new building permits, (iii) delays in closing deals due to processing slowdowns by appraisers and outside legal firms and other key suppliers in the mortgage process, and (iv) delays in or cancellation of closings due to changes on new mortgages due to changes in the employment status of otherwise approved borrowers. An increase in cash translates into lower earnings as cash reserves earn little to no income.

As at March 31, 2020, the Corporation had not experienced any loan impairments resulting from COVID-19 economic effects. Assuming no change to current economic circumstances, any COVID-19 related increase in impairments is not likely to be noticeable for a period of four to six months in the future for the following reasons: (i) 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, (ii) there are unprecedented government financial supports available that will assist borrowers in staying current with their mortgage obligations; and (iii) the current situation has created an industrywide willingness to work with borrowers under deferred payment programs for qualified borrowers. Essentially, impairment or default is several steps down the road for most borrowers after they have exhausted cash reserves, cut down on other expenses, worked with government assistance, and worked on potential deferral arrangements. 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. If the Corporation experiences an increase in impairments that would translate into lower earnings due to the unlikely collectability of further interest on those loans.

The Corporation does not anticipate that the effects of COVID-19 will lead to capital losses on any of the Corporation's impaired loans in the near term. 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 the most recent available CREA data, for March 2020, the number of home sales has declined dramatically, but there has not yet been a decline in home values in the Corporation's lending area.

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 March 31, 2020, there were 5,961,040 common shares issued and outstanding with a total book value of $178,722,200.

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 2020, expects to complete a transition from regulatory oversight as an investment fund to regulatory oversight as a corporate finance issuer. Management does not expect this change to 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 March 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 March 31, 2020, the Corporation was using $1,600,000 (December 31, 2019 - $11,330,000) of its available credit line. The maximum borrowings at any time during the first quarter of 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 quarter ended March 31, 2020 and the year ended December 31, 2019:

	Three months ended Mar 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	123,046	3,691,392	861,616	25,848,472
Issued under dividend re-investment plan	48,986	1,469,588	192,263	5,767,877
Redeemed	(28,678)	(860,332)	(1,162,442)	(34,873,262)
Balance – end of period	5,961,040	178,722,200	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. Substantially all of the redemptions for 2019 and 2018 occurred in November of each year.

CONTRACTUAL OBLIGATIONS

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

	$
Bank line of credit	1,600,000
Dividends payable	275,492
Accounts payable and accrued liabilities	129,084
	2,004,576

As at March 31, 2020, the Corporation has commitments to advance additional funds of $21,280,000 under existing mortgages (March 31, 2019 - $13,679,000). 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 $965,293 for the quarter ended March 31, 2020 (quarter ended March 31, 2019 - $996,981) including applicable sales taxes. The decrease in the dollar value of the administration and management fees 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, management 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 firm 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 firm 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 March 31, 2020, the Corporation has not made any adjustments to its ECL modelling to account for potential impacts arising from the COVID-19 pandemic. As at March 31, 2020, the Corporation had not experienced any significant increases in credit risk resulting from COVID-19 economic effects nor had any deferral arrangements been made with borrowers on account of COVID-19. 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 1 of the interim financial statements and under the Operating Results section of this MD&A.

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 of the interim financial statements, 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 interim 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 interim financial statements present the fair values of the Corporation's financial instruments as at March 31, 2020 and December 31, 2019.

CHANGES IN ACCOUNTING POLICIES

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

IAS 1 - Presentation of Financial Statements and IAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors

Effective January 1, 2020 the IASB implemented amendments to IAS 1, Presentation of Financial Statements and IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors. The amendments 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 amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

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 MDA 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 March 31, 2020.

ADDITIONAL INFORMATION

Additional information about Frontenac Mortgage Investment Corporation, including the unaudited financial statements for the three months ended March 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 dawn.reiser@robinsonsgroup.com.