

REVIEW OF FINANCIAL PERFORMANCE

All tabular amounts are in millions of Canadian dollars, unless otherwise noted.

MARCH 13, 2013

This Annual Report is intended to provide interested shareholders and others with selected information concerning Power Financial Corporation. For further information concerning the Corporation, shareholders and other interested persons should consult the Corporation's disclosure documents, such as its Annual Information Form and Management's Discussion and Analysis (MD&A). Copies of the Corporation's continuous disclosure documents can be obtained at www.sedar.com, on the Corporation's website at www.powerfinancial.com, or from the office of the Secretary at the addresses shown at the end of this report.

FORWARD-LOOKING STATEMENTS > Certain statements in this document, other than statements of historical fact, are forward-looking statements based on certain assumptions and reflect the Corporation's current expectations, or with respect to disclosure regarding the Corporation's public subsidiaries, reflect such subsidiaries' disclosed current expectations. Forward-looking statements are provided for the purposes of assisting the reader in understanding the Corporation's financial performance, financial position and cash flows as at and for the periods ended on certain dates and to present information about management's current expectations and plans relating to the future and the reader is cautioned that such statements may not be appropriate for other purposes. These statements may include, without limitation, statements regarding the operations, business, financial condition, expected financial results, performance, prospects, opportunities, priorities, targets, goals, ongoing objectives, strategies and outlook of the Corporation and its subsidiaries, as well as the outlook for North American and international economies for the current fiscal year and subsequent periods. Forward-looking statements include statements that are predictive in nature, depend upon or refer to future events or conditions, or include words such as "expects", "anticipates", "plans", "believes", "estimates", "seeks", "intends", "targets", "projects", "forecasts" or negative versions thereof and other similar expressions, or future or conditional verbs such as "may", "will", "should", "would" and "could".

By its nature, this information is subject to inherent risks and uncertainties that may be general or specific and which give rise to the possibility that expectations, forecasts, predictions, projections or conclusions will not prove to be accurate, that assumptions may not be correct and that objectives, strategic goals and priorities will not be achieved. A variety of factors, many of which are beyond the Corporation's and its subsidiaries' control, affect the operations, performance and results of the Corporation and its subsidiaries and their businesses, and could cause actual results to differ materially from current expectations of estimated or anticipated events or results. These factors include, but are not limited to: the impact or unanticipated impact of general economic, political and market factors in North America and internationally, interest and foreign exchange rates, global equity and capital markets, management of market liquidity and funding risks,

changes in accounting policies and methods used to report financial condition (including uncertainties associated with critical accounting assumptions and estimates), the effect of applying future accounting changes, business competition, operational and reputational risks, technological change, changes in government regulation and legislation, changes in tax laws, unexpected judicial or regulatory proceedings, catastrophic events, the Corporation's and its subsidiaries' ability to complete strategic transactions, integrate acquisitions and implement other growth strategies, and the Corporation's and its subsidiaries' success in anticipating and managing the foregoing factors.

The reader is cautioned to consider these and other factors, uncertainties and potential events carefully and not to put undue reliance on forward-looking statements. Information contained in forward-looking statements is based upon certain material assumptions that were applied in drawing a conclusion or making a forecast or projection, including management's perceptions of historical trends, current conditions and expected future developments, as well as other considerations that are believed to be appropriate in the circumstances, including that the list of factors in the previous paragraph, collectively, are not expected to have a material impact on the Corporation and its subsidiaries. While the Corporation considers these assumptions to be reasonable based on information currently available to management, they may prove to be incorrect.

Other than as specifically required by applicable Canadian law, the Corporation undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made, or to reflect the occurrence of unanticipated events, whether as a result of new information, future events or results, or otherwise.

Additional information about the risks and uncertainties of the Corporation's business and material factors or assumptions on which information contained in forward-looking statements is based is provided in its disclosure materials, including its most recent MD&A and Annual Information Form, filed with the securities regulatory authorities in Canada and available at www.sedar.com.

Readers are reminded that a list of the abbreviations used throughout can be found at the beginning of this Annual Report. In addition, the following abbreviations are used in the Review of Financial Performance and in the Financial Statements and Notes thereto: Audited Consolidated Financial Statements of Power Financial and Notes thereto for the year ended December 31, 2012 (the 2012 Consolidated Financial Statements or the Financial Statements); International Financial Reporting Standards (IFRS); previous Canadian generally accepted accounting principles (previous Canadian GAAP).

OVERVIEW

Power Financial, a subsidiary of Power Corporation, is a holding company with substantial interests in the financial services sector in Canada, the United States and Europe, through its controlling interests in Lifeco and IGM. Power Financial also holds, together with the Frère group of Belgium, an interest in Pargesa.

As at December 31, 2012, Power Financial and IGM held 68.2% and 4.0%, respectively, of Lifeco's common shares, representing approximately 65% of the voting rights attached to all outstanding Lifeco voting shares. As at December 31, 2012, Power Financial and Great-West Life, a subsidiary of Lifeco, held 58.7% and 3.7%, respectively, of IGM's common shares.

Power Financial Europe B.V., a wholly owned subsidiary of Power Financial, and the Frère group each hold a 50% interest in Parjointco, which, as at December 31, 2012, held a 55.6% equity interest in Pargesa, representing 75.4% of the voting rights of that company. These figures do not reflect the dilution which could result from the potential conversion of outstanding debentures convertible into new bearer shares issued by Pargesa in 2006 and 2007.

On December 17, 2012, Power Financial and the Frère group extended the term of the agreement governing their strategic partnership in Europe to December 31, 2029, with provision for possible further extension of the agreement.

RECENT DEVELOPMENTS

On February 19, 2013, Lifeco announced that it had reached an agreement with the Government of Ireland to acquire, through its subsidiary Canada Life Limited, all of the shares of Irish Life Group Limited (Irish Life) for \$1.75 billion (€1.3 billion). Established in 1939, Irish Life is the largest life and pensions group and investment manager in Ireland.

Lifeco also announced a \$1.25 billion offering of subscription receipts exchangeable into Lifeco common shares by way of a \$650 million bought deal public offering as well as concurrent private placements of subscription receipts to Power Financial and IGM for an aggregate amount of \$600 million.

On March 12, 2013, Power Financial purchased \$550 million of Lifeco subscription receipts. On that date, IGM also purchased \$50 million of Lifeco subscription receipts. Each subscription receipt entitles the holder to receive one common share of Lifeco upon closing of the acquisition of Irish Life, without any action on the part of the holder and without payment of additional consideration. Power Financial and IGM completed the purchase

The Pargesa group has holdings in major companies based in Europe. These investments are held by Pargesa through its affiliated Belgian holding company, Groupe Bruxelles Lambert. As at December 31, 2012, Pargesa held a 50% equity interest in GBL, representing 52% of the voting rights.

As at December 31, 2012, Pargesa's portfolio was composed of interests in various sectors, including primarily mineral-based specialties for industry through Imerys; cement and other building materials through Lafarge; oil, gas and alternative energies through Total; electricity, natural gas, and energy and environmental services through GDF Suez; water and waste management services through Suez Environnement; and wines and spirits through Pernod Ricard. On March 14, 2012, GBL sold its interest in Arkema for proceeds of €433 million and realized a gain of €221 million. On March 15, 2012, GBL sold 6.2 million shares of Pernod Ricard, representing approximately 2.3% of the share capital of Pernod Ricard, for proceeds of €499 million and a gain of €240 million. Following this transaction, GBL held 7.5% of Pernod Ricard's share capital.

In addition, Pargesa and GBL have also invested, or committed to invest, in the area of French private equities, including in equity funds Sagard 1 and Sagard 2, whose management company is a subsidiary of Power Corporation.

of subscription receipts by private placements concurrently with the closing of the bought deal public offering of Lifeco's subscription receipts. The public offering and private placements of subscription receipts are at the same price of \$25.70 per subscription receipt.

Should the subscription receipts be converted into common shares of Lifeco, Power Financial will hold, directly and indirectly, a 69.4% economic interest in Lifeco.

The acquisition is expected to close in July of 2013, and is subject to customary regulatory approvals, including approvals from the European Commission under the EU Merger Regulation, and certain closing conditions.

The Corporation also announced, on February 28, 2013, the closing of an offering of 12,000,000 4.80% Non-Cumulative First Preferred Shares, Series S priced at \$25.00 per share for gross proceeds of \$300 million. Proceeds from the issue were used to acquire the subscription receipts of Lifeco referred to above and to supplement the Corporation's financial resources.

BASIS OF PRESENTATION

The 2012 Consolidated Financial Statements have been prepared in accordance with IFRS and are presented in Canadian dollars.

INCLUSION OF PARGESA'S RESULTS

The investment in Parjointco is accounted for by Power Financial under the equity method as the Corporation has joint control over its activities. Parjointco's only investment is its controlling interest in Pargesa. As described above, the Pargesa portfolio currently consists primarily of investments in Imerys, Lafarge, Total, GDF Suez, Suez Environnement and Pernod Ricard, which are held through GBL, which is consolidated in Pargesa. Imerys' results are consolidated in the financial statements of GBL, while the contribution from Total, GDF Suez, Suez Environnement and Pernod Ricard to GBL's operating earnings consists of the dividends received from these companies. GBL accounts for its investment in Lafarge under the equity method, and consequently, the contribution from Lafarge to GBL's earnings consists of GBL's share of Lafarge's net earnings.

NON-IFRS FINANCIAL MEASURES

In analyzing the financial results of the Corporation and consistent with the presentation in previous years, net earnings attributable to common shareholders are subdivided in the section "Results of Power Financial Corporation" below into the following components:

- > **operating earnings** attributable to common shareholders; and
- > **other items** or non-operating earnings, which include the after-tax impact of any item that management considers to be of a non-recurring nature or that could make the period-over-period comparison of results from operations less meaningful, and also include the Corporation's share of any such item presented in a comparable manner by its subsidiaries and jointly controlled corporation. Please also refer to the comments above related to the inclusion of Pargesa's results.

Management has used these financial measures for many years in its presentation and analysis of the financial performance of Power Financial, and believes that they provide additional meaningful information to readers in their analysis of the results of the Corporation.

Operating earnings attributable to common shareholders and operating earnings per share are non-IFRS financial measures that do not have a standard meaning and may not be comparable to similar measures used by other entities. For a reconciliation of these non-IFRS measures to results reported in accordance with IFRS, see the "Results of Power Financial Corporation—Earnings Summary—Condensed Supplementary Statements of Earnings" section below.

RESULTS OF POWER FINANCIAL CORPORATION

This section is an overview of the results of Power Financial. In this section, consistent with past practice, the contributions from Lifeco and IGM, which represent most of the earnings of Power Financial, are accounted for using

the equity method in order to facilitate the discussion and analysis. This presentation has no impact on Power Financial's net earnings and is intended to assist readers in their analysis of the results of the Corporation.

EARNINGS SUMMARY—CONDENSED SUPPLEMENTARY STATEMENTS OF EARNINGS

The following table shows a reconciliation of non-IFRS financial measures used herein for the periods indicated, with the reported results in accordance with IFRS for net earnings attributable to common shareholders and earnings per share.

TWELVE MONTHS ENDED DECEMBER 31	2012	2011
Contribution to operating earnings from subsidiaries and Parjointco		
Lifeco	1,335	1,298
IGM	433	480
Pargesa	106	110
	1,874	1,888
Results from corporate activities	(71)	(55)
Dividends on perpetual preferred shares	(117)	(104)
Operating earnings attributable to common shareholders	1,686	1,729
Other items	(60)	(7)
Net earnings attributable to common shareholders	1,626	1,722
Earnings per share (attributable to common shareholders)		
—operating earnings	2.38	2.44
—non-operating earnings (other items)	(0.08)	(0.01)
—net earnings	2.30	2.43

OPERATING EARNINGS ATTRIBUTABLE TO COMMON SHAREHOLDERS

Operating earnings attributable to common shareholders for the year ended December 31, 2012 were \$1,686 million or \$2.38 per share, compared with \$1,729 million or \$2.44 per share in the corresponding period in 2011, a decrease of 2.5% on a per share basis.

A discussion of the reasons for period-over-period changes in operating earnings attributable to common shareholders is included in the following sections.

CONTRIBUTION TO OPERATING EARNINGS FROM SUBSIDIARIES AND INVESTMENT IN PARJOINTCO

Power Financial's share of operating earnings from its subsidiaries and investment in Parjointco for the year ended December 31, 2012 was \$1,874 million, compared with \$1,888 million in the same period in 2011.

Lifeco's contribution to Power Financial's operating earnings was \$1,335 million for the year ended December 31, 2012, compared with \$1,298 million for the corresponding period in 2011. Details are as follows:

- > Lifeco reported operating earnings attributable to common shareholders of \$1,955 million or \$2.059 per share for the year ended December 31, 2012, compared with \$1,898 million or \$2.000 per share in the corresponding period in 2011, an increase of 3.0% on a per share basis.
- > Lifeco in Canada: operating earnings attributable to common shareholders for the year ended December 31, 2012 were \$1,040 million, compared with \$986 million in the corresponding period in 2011.
- > Lifeco in the United States: operating earnings attributable to common shareholders for the year ended December 31, 2012 were \$325 million, compared with \$370 million in the corresponding period in 2011.
- > Lifeco in Europe: operating earnings attributable to common shareholders for the year ended December 31, 2012 were \$618 million, compared with \$562 million in the corresponding period in 2011. The 2011 results include catastrophe provisions of \$84 million relating to earthquake events in Japan and New Zealand.

IGM's contribution to Power Financial's operating earnings was \$433 million for the twelve-month period ended December 31, 2012, compared with \$480 million for the corresponding period in 2011. Details are as follows:

- > IGM reported operating earnings available to common shareholders of \$750 million or \$2.94 per share for the twelve-month period ended December 31, 2012, compared with \$833 million or \$3.22 per share in the same period in 2011, a decrease of 8.7% on a per share basis.
- > IGM's earnings are primarily dependent on the level of assets under management. Average daily mutual fund assets for the three-month periods ended December 31, 2012, September 30, 2012, June 30, 2012 and March 31, 2012 were \$102.4 billion, \$101.0 billion, \$100.9 billion and \$103.6 billion, respectively, compared with \$99.6 billion, \$103.5 billion, \$109.9 billion and \$110.0 billion, in the corresponding three-month periods of 2011.

- > On May 18, 2012, Investors Group announced a number of changes in the pricing of its mutual funds and product enhancements designed to expand its services to clients. Investors Group reduced the fees of many of its mutual funds when their prospectuses renewed on June 30, 2012. This has resulted in a decrease in management fees in the third and fourth quarters of 2012.

Pargesa's contribution to Power Financial's operating earnings was \$106 million for the twelve-month period ended December 31, 2012, compared with a contribution of \$110 million in the corresponding period in 2011. Details are as follows:

- > Pargesa's operating earnings for the twelve-month period ended December 31, 2012 were SF359 million, compared with operating earnings of SF343 million in the corresponding period in 2011.
- > The contribution of Pargesa to the Corporation's earnings was negatively affected in 2012 as a result of the weakening of the euro and the Swiss franc against the Canadian dollar.
- > Although the results of Imerys for the twelve-month period ended December 31, 2012 were 2.3% higher than in the corresponding period in 2011, the contribution from Imerys to Pargesa's earnings decreased by 8.9% in 2012, due to the decrease in percentage of ownership as a result of Pargesa having sold its direct interest in Imerys to GBL in April 2011, as previously disclosed.
- > The contribution of Lafarge to Pargesa's earnings increased from SF56 million in 2011 to SF102 million in 2012.
- > The Pargesa results for 2011 include an additional quarterly dividend of SF30 million received from Total as a result of Total paying its dividend on a quarterly basis starting in 2011.

RESULTS FROM CORPORATE ACTIVITIES

Results from corporate activities include interest on cash and cash equivalents, operating expenses, financing charges, depreciation and income taxes.

Corporate activities represented a net charge of \$71 million in the twelve-month period ended December 31, 2012, compared with a net charge of \$55 million in the corresponding period in 2011.

The variation in the results from corporate activities for the twelve-month period ended December 31, 2012, compared with the corresponding period in 2011, was mainly due to the recognition in the first quarter of 2011 of the tax benefits of loss carry forwards transferred to IGM under a loss consolidation transaction and higher operating expenses in 2012.

OTHER ITEMS / NON-OPERATING EARNINGS

TWELVE MONTHS ENDED DECEMBER 31	2012	2011
Share of Lifeco's other items		
Litigation provisions (charge) reversal	(99)	88
Share of IGM's other items		
Non-cash income tax charge	(4)	
Gain on disposal of M.R.S. Trust Company and M.R.S. Inc.		18
Changes in the status of certain income tax filings	15	17
Share of Pargesa's other items		
Impairment charges	(48)	(133)
Gain on partial disposal of Pernod Ricard	46	
Gain on disposal of Arkema	43	
Other (charge) income	(13)	3
	(60)	(7)

For the twelve-month period ended December 31, 2012, other items represented a net charge of \$60 million, compared with a net charge of \$7 million in the corresponding period in 2011.

Other items in 2012 mainly comprised the following:

- > The Corporation's share of a charge reported by Lifeco relating to a litigation provisions adjustment of \$99 million, net of tax, in the fourth quarter.
- > The Corporation's share of a non-cash income tax charge recorded by IGM in the second quarter resulting from increases in Ontario corporate income tax rates and their effect on the deferred income tax liability related to indefinite life intangible assets arising from prior business acquisitions, as well as the recording in the fourth quarter of 2012 of a favourable change in income tax provision estimates related to certain tax filings.
- > The Corporation's share of GBL's write-down of its investment in GDF Suez in the fourth quarter, representing an amount of \$48 million, net of foreign currency gains recorded by Pargesa and the Corporation. Under IFRS, a significant or prolonged decline in the fair value of an investment in an available-for-sale equity instrument below its cost is objective evidence of impairment. Once impaired, any subsequent decrease in the market price of a stock is automatically recognized as an impairment loss. A recovery of the price of a stock that has been impaired is accounted for through Other comprehensive income. Such recovery will impact earnings only upon the disposal of the investment.
- > The Corporation's share of the gains realized by GBL in the first quarter on the partial disposal of its interest in Pernod Ricard was \$46 million and on the disposal of its interest in Arkema was \$43 million.
- > The Corporation's share of goodwill impairment and restructuring charges recorded by Lafarge in the first and second quarters.

Other items in 2011 mainly comprised the following:

- > A contribution of \$88 million representing the Corporation's share of non-operating earnings of Lifeco. In the fourth quarter of 2011, Lifeco re-evaluated and reduced a litigation provision established in the third quarter of 2010 which positively impacted Lifeco's common shareholders' net earnings by \$223 million. Additionally, in the fourth quarter of 2011, Lifeco established a provision of \$99 million after tax in respect of the settlement of litigation relating to its ownership in a U.S.-based private equity firm. The net impact to Lifeco of these two unrelated matters was \$124 million.
- > The Corporation's share of an amount recorded by IGM in the third quarter relating to changes in the status of certain income tax filings as well as the Corporation's share of the gain on the disposal of M.R.S. Trust Company and M.R.S. Inc. by IGM.
- > The Corporation's share of GBL's write-down of its investment in Lafarge, representing an amount of \$133 million recorded in the third quarter.

NET EARNINGS ATTRIBUTABLE TO COMMON SHAREHOLDERS

Net earnings attributable to common shareholders for the twelve-month period ended December 31, 2012 were \$1,626 million or \$2.30 per share, compared with \$1,722 million or \$2.43 per share in the corresponding period in 2011.

A discussion of period-over-period changes in net earnings attributable to common shareholders is included in the foregoing sections.

CONDENSED SUPPLEMENTARY BALANCE SHEETS

AS AT DECEMBER 31	CONSOLIDATED BASIS		EQUITY BASIS	
	2012	2011	2012	2011
ASSETS				
Cash and cash equivalents ^[1]	3,313	3,385	984	707
Investment in Parjointco	2,149	2,222	2,149	2,222
Investment in subsidiaries at equity			11,464	11,147
Investments	123,587	117,042		
Funds held by ceding insurers	10,537	9,923		
Reinsurance assets	2,064	2,061		
Intangible assets	4,933	5,023		
Goodwill	8,673	8,786		
Other assets	8,389	7,654	102	104
Interest on account of segregated fund policyholders	104,948	96,582		
Total assets	268,593	252,678	14,699	14,180
LIABILITIES				
Insurance and investment contract liabilities	120,658	115,512		
Obligations to securitization entities	4,701	3,827		
Debentures and debt instruments	5,858	5,888	250	250
Capital trust securities	119	533		
Other liabilities	7,937	7,521	420	409
Investment and insurance contracts on account of segregated fund policyholders	104,948	96,582		
Total liabilities	244,221	229,863	670	659
EQUITY				
Perpetual preferred shares	2,255	2,005	2,255	2,005
Common shareholders' equity	11,774	11,516	11,774	11,516
Non-controlling interests ^[2]	10,343	9,294		
Total equity	24,372	22,815	14,029	13,521
Total liabilities and equity	268,593	252,678	14,699	14,180

[1] Under the equity basis presentation, cash equivalents include \$625 million (\$430 million at December 31, 2011) of fixed income securities with maturities of more than 90 days. In the 2012 Consolidated Financial Statements, this amount of cash equivalents is classified in investments.

[2] Non-controlling interests include the Corporation's non-controlling interests in the common equity of Lifeco and IGM as well as the participating account surplus in Lifeco's insurance subsidiaries and perpetual preferred shares issued by subsidiaries to third parties.

CONSOLIDATED BASIS

The consolidated balance sheets include Lifeco's and IGM's assets and liabilities.

Total assets of the Corporation increased to \$268.6 billion at December 31, 2012, compared with \$252.7 billion at December 31, 2011.

Investments at December 31, 2012 were \$123.6 billion, a \$6.5 billion increase from December 31, 2011, primarily related to Lifeco's activities. See also the discussion in the "Cash Flows" section below.

Liabilities increased from \$229.9 billion at December 31, 2011 to \$244.2 billion at December 31, 2012, mainly due to an increase in Lifeco's insurance and investment contract liabilities as well as investment and insurance contracts on account of segregated fund policyholders.

ASSETS UNDER ADMINISTRATION

Assets under administration of Lifeco and IGM are as follows:

AS AT DECEMBER 31 (IN BILLIONS OF CANADIAN DOLLARS)	2012	2011
Assets under management of Lifeco		
Invested assets	120.0	114.6
Other corporate assets	28.8	27.6
Segregated funds net assets	104.9	96.6
Proprietary mutual funds and institutional net assets	134.6	125.4
	388.3	364.2
Assets under management of IGM	120.7	118.7
Total assets under management	509.0	482.9
Other assets under administration of Lifeco	157.5	137.8
Total assets under administration	666.5	620.7

Total assets under administration at December 31, 2012 increased by \$45.8 billion from December 31, 2011:

- > Total assets under administration by Lifeco at December 31, 2012 increased by \$43.8 billion from December 31, 2011. Segregated funds increased by approximately \$8.3 billion and proprietary mutual funds and institutional net assets increased by \$9.2 billion, primarily as a result of lower government bond rates and, to a lesser extent, higher U.S. equity market levels. Other assets under administration increased by \$19.7 billion, primarily as a result of new plan sales and improved U.S. equity market levels. Invested assets increased by approximately \$5.4 billion, primarily due to asset growth and an increase in bond fair values as a result of lower government bond rates.
- > IGM's assets under management, at market value, were \$120.7 billion at December 31, 2012, compared with \$118.7 billion at December 31, 2011. This increase of \$2.0 billion since December 31, 2011 represents market and income gains of \$7.6 billion less net redemptions of \$5.6 billion.

EQUITY BASIS

Under the equity basis presentation, Lifeco and IGM are accounted for by the Corporation using the equity method. This presentation has no impact on Power Financial's shareholders' equity and is intended to assist readers in isolating the contribution of Lifeco and IGM to the assets and liabilities of the Corporation.

Cash and cash equivalents held by Power Financial amounted to \$984 million at December 31, 2012, compared with \$707 million at the end of December 2011 (see "Cash Flows—Equity Basis" section below for details). The amount of quarterly dividends declared by the Corporation but not yet paid was \$278 million at December 31, 2012. The amount of dividends declared by IGM but not yet received by the Corporation was \$80 million at December 31, 2012.

In managing its own cash and cash equivalents, Power Financial may hold cash balances or invest in short-term paper or equivalents, as well as deposits, denominated in foreign currencies and thus be exposed to fluctuations in exchange rates. In order to protect against such fluctuations, Power Financial may, from time to time, enter into currency-hedging transactions with counterparties with high credit ratings. As at December 31, 2012, approximately 90% of the \$984 million of cash and cash equivalents was denominated in Canadian dollars or in foreign currencies with currency hedges in place.

The carrying value under the equity method of accounting of Power Financial's investments in Lifeco, IGM and Parjointco increased to \$13,613 million at December 31, 2012, compared with \$13,369 million at December 31, 2011. This increase is explained as follows:

	LIFECO	IGM	PARJOINTCO	TOTAL
Carrying value, at the beginning	8,476	2,671	2,222	13,369
Share of operating earnings	1,335	433	106	1,874
Share of other items	(95)	7	28	(60)
Share of other comprehensive income (loss)	(67)	(2)	(100)	(169)
Dividends	(797)	(318)	(65)	(1,180)
Other, including effect of change in ownership	(6)	(173)	(42)	(221)
Carrying value, at the end	8,846	2,618	2,149	13,613

EQUITY

Common shareholders' equity was \$11,774 million at December 31, 2012, compared with \$11,516 million at December 31, 2011. This \$258 million increase was primarily due to:

- > A \$405 million increase in retained earnings, reflecting mainly net earnings of \$1,743 million, less dividends declared of \$1,109 million and a decrease of \$229 million representing:
 - > The effect on equity of the repurchase by a subsidiary of common shares at a price in excess of the stated value of such shares and the issuance of common shares by subsidiaries in the amount of \$167 million.
 - > A negative amount of \$55 million composed of the Corporation's share of retained earnings adjustments in subsidiaries and Parjointco.
 - > Share issue expenses of the Corporation for an amount of \$7 million.
- > A loss of \$171 million, which represents essentially the Corporation's share of other comprehensive income of its subsidiaries and Parjointco.

There were 930,400 common shares issued by the Corporation in the twelve-month period ended December 31, 2012 pursuant to the Corporation's Employee Stock Option Plan for proceeds of \$20 million.

As a result of the above, the book value per common share of the Corporation was \$16.60 at December 31, 2012, compared with \$16.26 at the end of 2011.

On February 23, 2012, the Corporation issued 10,000,000 5.5% Non-Cumulative First Preferred Shares Series R for gross proceeds of \$250 million.

The Corporation filed a short-form base shelf prospectus dated November 23, 2012, pursuant to which, for a period of 25 months thereafter, the Corporation may issue up to an aggregate of \$1.5 billion of First Preferred Shares, common shares and unsecured debt securities, or any combination thereof. This filing provides the Corporation with the flexibility to access debt and equity markets on a timely basis to make changes to the Corporation's capital structure in response to changes in economic conditions and changes in its financial condition.

As noted under "Recent Developments", on February 28, 2013, the Corporation issued 12,000,000 4.8% Non-Cumulative First Preferred Shares Series S for gross proceeds of \$300 million.

OUTSTANDING NUMBER OF COMMON SHARES

As of the date hereof, there were 709,104,080 common shares of the Corporation outstanding, compared with 708,173,680 as at December 31, 2011. The increase in the number of outstanding common shares reflects the exercise of options under the Corporation's Employee Stock Option Plan. As of the date hereof, options were outstanding to purchase up to an aggregate of 8,835,797 common shares of the Corporation under the Corporation's Employee Stock Option Plan.

CASH FLOWS**CONDENSED CONSOLIDATED CASH FLOWS**

FOR THE YEARS ENDED DECEMBER 31	2012	2011
Cash flow from operating activities	5,369	5,505
Cash flow from financing activities	(561)	(2,406)
Cash flow from investing activities	(4,872)	(3,106)
Effect of changes in exchange rates on cash and cash equivalents	(8)	24
Increase (decrease) in cash and cash equivalents—continuing operations	(72)	17
Cash and cash equivalents, at the beginning	3,385	3,656
Less: cash and cash equivalents from discontinued operations—beginning of period	—	(288)
Cash and cash equivalents, at the end—continuing operations	3,313	3,385

On a consolidated basis, cash and cash equivalents from continuing operations decreased by \$72 million in the twelve-month period ended December 31, 2012, compared with an increase of \$17 million in the corresponding period of 2011.

Operating activities produced a net inflow of \$5,369 million in the twelve-month period ended December 31, 2012, compared with a net inflow of \$5,505 million in the corresponding period of 2011.

Operating activities during the twelve-month period ended December 31, 2012, compared to the same period in 2011, included:

- > Lifeco's cash flow from operations was a net inflow of \$4,722 million, compared with a net inflow of \$4,844 million in the corresponding period in 2011. Cash provided by operating activities is used by Lifeco primarily to pay policy benefits, policyholder dividends and claims, as well as operating expenses and commissions. Cash flows generated by operations are mainly invested by Lifeco to support future liability cash requirements.
- > Operating activities of IGM which, after payment of commissions, generated cash flows of \$710 million, compared with \$777 million in the corresponding period of 2011.

Cash flows from financing activities, which include dividends paid on the common and preferred shares of the Corporation, as well as dividends paid by subsidiaries to non-controlling interests, resulted in a net outflow of \$561 million in the twelve-month period ended December 31, 2012, compared with a net outflow of \$2,406 million in the corresponding period of 2011.

Financing activities during the twelve-month period ended December 31, 2012, compared to the same period in 2011, included:

- > Dividends paid by the Corporation and by its subsidiaries to non-controlling interests of \$1,764 million, compared with \$1,735 million in the corresponding period of 2011.
- > Issuance of common shares of the Corporation for an amount of \$20 million, compared with \$3 million in the corresponding period in 2011, pursuant to the Corporation's Employee Stock Option Plan.
- > Issuance of common shares by subsidiaries of the Corporation for an amount of \$44 million, compared with \$61 million in the corresponding period of 2011.
- > Issuance of preferred shares by the Corporation for an amount of \$250 million, compared to no issuance in the corresponding period of 2011.

- > Issuance of preferred shares by subsidiaries of the Corporation for an amount of \$650 million, compared to no issuance in the corresponding period of 2011.
- > Repurchase for cancellation by subsidiaries of the Corporation of their common shares for an amount of \$215 million, compared with \$186 million in the corresponding period of 2011.
- > No repayment of long-term debentures by IGM, compared with repayment of long-term debentures of \$450 million in the corresponding period of 2011.
- > Net inflow of \$874 million arising from obligations to securitization entities at IGM, compared with a net inflow of \$319 million in the corresponding period of 2011.
- > Net payment of \$2 million by IGM arising from obligations related to assets sold under repurchase agreements, compared to a net payment of \$408 million in 2011. The net payment in 2011 included the settlement of \$428 million in obligations related to the sale of \$426 million in Canada Mortgage Bonds, which is reported in investing activities.

- > Redemption of capital trust securities by subsidiaries of Lifeco for an amount of \$409 million, compared with no redemptions in the corresponding period of 2011.

Cash flows from investing activities resulted in a net outflow of \$4,872 million in the twelve-month period ended December 31, 2012, compared with a net outflow of \$3,106 million in the corresponding period of 2011.

Investing activities during the twelve-month period ended December 31, 2012, compared to the same period in 2011, included:

- > Investing activities at Lifeco resulted in a net outflow of \$3,838 million, compared with a net outflow of \$3,407 million in the corresponding period of 2011.
- > Investing activities at IGM resulted in a net outflow of \$839 million, compared with a net inflow of \$229 million in the corresponding period of 2011.
- > In addition, the Corporation increased its level of fixed income securities with maturities of more than 90 days, resulting in a net outflow of \$195 million, compared with a reduction in the corresponding period of 2011 for a net inflow of \$40 million.

CASH FLOWS – EQUITY BASIS

FOR THE YEARS ENDED DECEMBER 31	2012	2011
CASH FLOW FROM OPERATING ACTIVITIES		
Net earnings before dividends on perpetual preferred shares	1,743	1,826
Earnings from subsidiaries and Parjointco not received in cash	(634)	(776)
Other	10	4
	1,119	1,054
CASH FLOW FROM FINANCING ACTIVITIES		
Dividends paid on common and preferred shares	(1,105)	(1,095)
Issuance of perpetual preferred shares	250	–
Issuance of common shares	20	3
Other	(7)	–
	(842)	(1,092)
CASH FLOW FROM INVESTING ACTIVITIES		
Repayment of advance to Parjointco	–	32
	–	32
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	277	(6)
Cash and cash equivalents, beginning of period	707	713
Cash and cash equivalents, end of period	984	707

Power Financial is a holding company. As such, corporate cash flows from operations, before payment of dividends on common shares and on preferred shares, are principally made up of dividends received from its subsidiaries and Parjointco and income from investments, less operating expenses, financing charges, and income taxes. The ability of Lifeco and IGM, which are also holding companies, to generally meet their obligations and pay dividends depends in particular upon receipt of sufficient funds from their subsidiaries. The payment of interest and dividends by Lifeco's principal subsidiaries is subject to restrictions set out in relevant corporate and insurance laws and regulations, which require that solvency and capital standards be maintained. As well, the capitalization of Lifeco's principal subsidiaries takes into account the views expressed by the various credit rating agencies that provide ratings related to financial strength and other measures relating to those companies. The payment of dividends by IGM's principal subsidiaries is subject to corporate laws and regulations which require that solvency standards be maintained. In addition, certain subsidiaries of IGM must also comply with capital and liquidity requirements established by regulatory authorities.

Dividends declared by Lifeco and IGM during the twelve-month period ended December 31, 2012 on their common shares amounted to \$1.23 and \$2.15 per share, respectively, compared with \$1.23 and \$2.10 per share, respectively, in the corresponding period in 2011. In the twelve-month period ended December 31, 2012, the Corporation recorded dividends from Lifeco and IGM of \$1,115 million, compared with \$1,108 million in the corresponding period of 2011.

Pargesa pays its annual dividends in the second quarter. The dividend paid by Pargesa to Parjointco in 2012 amounted to SF2.57 per bearer share (SF123 million), compared with SF2.72 (SF125 million) in 2011. The Corporation received from Parjointco dividends of SF60 million (\$65 million) in 2012 (nil in 2011). In 2011, Parjointco reimbursed an advance from the Corporation of \$32 million.

In the twelve-month period ended December 31, 2012, dividends declared on the Corporation's common shares amounted to \$1.40 per share, the same as in the corresponding period of 2011.

SUMMARY OF CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires management to adopt accounting policies and to make estimates and assumptions that affect amounts reported in the Corporation's 2012 Consolidated Financial Statements. The major accounting policies and related critical accounting estimates underlying the Corporation's 2012 Consolidated Financial Statements are summarized below. In applying these policies, management makes subjective and complex judgments that frequently require estimates about matters that are inherently uncertain. Many of these policies are common in the insurance and other financial services industries; others are specific to the Corporation's businesses and operations. The significant accounting estimates and judgments are as follows:

INSURANCE AND INVESTMENT CONTRACT LIABILITIES

Insurance and investment contract liabilities represent the amounts required, in addition to future premiums and investment income, to provide for future benefit payments, policyholder dividends, commission and policy administrative expenses for all insurance and annuity policies in force with Lifeco. The Appointed Actuaries of Lifeco's subsidiary companies are responsible for determining the amount of the liabilities to make appropriate provisions for Lifeco's obligations to policyholders. The Appointed Actuaries determine the liabilities for insurance and investment contracts using generally accepted actuarial practices, according to the standards established by the Canadian Institute of Actuaries. The valuation uses the Canadian Asset Liability Method. This method involves the projection of future events in order to determine the amount of assets that must be set aside currently to provide for all future obligations and involves a significant amount of judgment.

In the computation of insurance contract liabilities, valuation assumptions have been made regarding rates of mortality/morbidity, investment returns, levels of operating expenses, rates of policy termination and rates of utilization of elective policy options or provisions. The valuation assumptions use best estimates of future experience together with a margin for adverse deviation. These margins are necessary to provide for possibilities of misestimation and/or future deterioration in the best estimate assumptions and provide reasonable assurance that insurance contract liabilities cover a range of possible outcomes. Margins are reviewed periodically for continued appropriateness.

Additional detail regarding these estimates can be found in Note 2 to the Corporation's 2012 Consolidated Financial Statements.

FAIR VALUE MEASUREMENT

Financial and other instruments held by the Corporation and its subsidiaries include portfolio investments, various derivative financial instruments, and debentures and debt instruments.

Financial instrument carrying values reflect the prevailing market liquidity and the liquidity premiums embedded in the market pricing methods the Corporation relies upon.

In accordance with IFRS 7, *Financial Instruments—Disclosure*, the Corporation's assets and liabilities recorded at fair value have been categorized based upon the following fair value hierarchy:

- > Level 1 inputs utilize observable, quoted prices (unadjusted) in active markets for identical assets or liabilities that the Corporation has the ability to access.
- > Level 2 inputs utilize other-than-quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

- > Level 3 inputs utilize one or more significant inputs that are not based on observable market inputs and include situations where there is little, if any, market activity for the asset or liability.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Corporation's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

Refer to Note 26 to the Corporation's 2012 Consolidated Financial Statements for disclosure of the Corporation's financial instruments fair value measurement as at December 31, 2012.

Fair values for bonds classified as fair value through profit or loss or available for sale are determined using quoted market prices. Where prices are not quoted in a normally active market, fair values are determined by valuation models primarily using observable market data inputs. Fair values for bonds and mortgages and other loans, classified as loans and receivables, are determined by discounting expected future cash flows using current market rates.

Fair values for public stocks are generally determined by the last bid price for the security from the exchange where it is principally traded. Fair values for stocks for which there is no active market are determined by discounting expected future cash flows based on expected dividends and where market value cannot be measured reliably, fair value is estimated to be equal to cost. Fair values for investment properties are determined using independent appraisal services and include management adjustments for material changes in property cash flows, capital expenditures or general market conditions in the interim period between appraisals.

IMPAIRMENT OF INVESTMENTS

Investments are reviewed regularly on an individual basis to determine impairment status. The Corporation considers various factors in the impairment evaluation process, including, but not limited to, the financial condition of the issuer, specific adverse conditions affecting an industry or region, decline in fair value not related to interest rates, bankruptcy or defaults and delinquency in payments of interest or principal. Impairment losses on available-for-sale shares are recorded if the loss is significant or prolonged and subsequent losses are recorded in net earnings. Investments are deemed to be impaired when there is no longer reasonable assurance of timely collection of the full amount of the principal and interest due. The fair value of an investment is not a definitive indicator of impairment, as it may be significantly influenced by other factors, including the remaining term to maturity and liquidity of the asset. However, market price must be taken into consideration when evaluating impairment.

For impaired mortgages and other loans, and bonds classified as loans and receivables, provisions are established or impairments recorded to adjust the carrying value to the net realizable amount. Wherever possible, the fair value of collateral underlying the loans or observable market price is used to establish net realizable value. For impaired available-for-sale bonds, recorded at fair value, the accumulated loss recorded in investment revaluation reserves is reclassified to net investment income. Impairments on available-for-sale debt instruments are reversed if there is objective evidence that a permanent recovery has occurred. All gains and losses on bonds classified or designated as fair value through profit or loss are already recorded in earnings, therefore a reduction due to impairment of assets will be recorded in earnings. As well, when determined to be impaired, contractual interest is no longer accrued and previous interest accruals are reversed.

GOODWILL AND INTANGIBLES IMPAIRMENT TESTING

Goodwill and intangible assets are tested for impairment annually or more frequently if events indicate that impairment may have occurred. Intangible assets that were previously impaired are reviewed at each reporting date for evidence of reversal. In the event that certain conditions have been met, the Corporation would be required to reverse the impairment charge or a portion thereof.

Goodwill has been allocated to cash generating units (CGU), representing the lowest level in which goodwill is monitored for internal reporting purposes. Goodwill is tested for impairment by comparing the carrying value of the CGU groups to the recoverable amount to which the goodwill has been allocated. Intangible assets are tested for impairment by comparing the asset's carrying amount to its recoverable amount.

An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the asset's fair value less cost to sell and value in use, which is calculated using the present value of estimated future cash flows expected to be generated.

INCOME TAXES

The Corporation is subject to income tax laws in various jurisdictions. The Corporation's and its subsidiaries' operations are complex and related tax interpretations, regulations and legislation that pertain to its activities are subject to continual change. Lifeco's primary Canadian operating subsidiaries are subject to a regime of specialized rules prescribed under the *Income Tax Act* (Canada) for purposes of determining the amount of the companies' income that will be subject to tax in Canada. Accordingly, the provision for income taxes represents the applicable corporation's management's interpretation of the relevant tax laws and its estimate of current and future income tax implications of the transactions and events during the period. Deferred tax assets and liabilities are recorded based on expected future tax rates and management's assumptions regarding the expected timing of the reversal of temporary differences. The Corporation has substantial deferred income tax assets. The recognition of deferred tax assets depends on management's assumption that future earnings will be sufficient to realize the deferred benefit. The amount of the asset recorded is based on management's best estimate of the timing of the reversal of the asset.

The audit and review activities of the Canada Revenue Agency and other jurisdictions' tax authorities affect the ultimate determination of the amounts of income taxes payable or receivable, future income tax assets

or liabilities and income tax expense. Therefore, there can be no assurance that taxes will be payable as anticipated and/or the amount and timing of receipt or use of the tax-related assets will be as currently expected. Management's experience indicates the taxation authorities are more aggressively pursuing perceived tax issues and have increased the resources they put to these efforts.

PENSION PLANS AND OTHER POST-EMPLOYMENT BENEFITS

The Corporation and its subsidiaries maintain defined benefit pension plans as well as defined contribution pension plans for eligible employees and advisors. The plans provide pensions based on length of service and final average earnings. Certain pension payments are indexed either on an ad hoc basis or a guaranteed basis. The defined contribution pension plans provide pension benefits based on accumulated employee and Corporation contributions. The Corporation and its subsidiaries also provide certain post-employment healthcare, dental and life insurance benefits to eligible retirees, employees and advisors. For further information on the Corporation's pension plans and other post-employment benefits refer to Note 24 to the Corporation's 2012 Consolidated Financial Statements.

Accounting for pension and other post-employment benefits requires estimates of future returns on plan assets, expected increases in compensation levels, trends in healthcare costs, and the period of time over which benefits will be paid, as well as the appropriate discount rate for accrued benefit obligations. These assumptions are determined by management using actuarial methods and are reviewed and approved annually. Emerging experience, which may differ from the assumptions, will be revealed in future valuations and will affect the future financial position of the plans and net periodic benefit costs.

DEFERRED SELLING COMMISSIONS

Commissions paid on the sale of certain mutual fund products are deferred and amortized over their useful lives, not exceeding a period of five years. IGM regularly reviews the carrying value of deferred selling commissions with respect to any events or circumstances that indicate impairment. Among the tests performed by IGM to assess recoverability is the comparison of the future economic benefits derived from the deferred selling commission asset in relation to its carrying value. At December 31, 2012, there were no indications of impairment to deferred selling commissions.

FUTURE ACCOUNTING CHANGES

The Corporation continuously monitors the potential changes proposed by the International Accounting Standards Board (IASB) and analyzes the effect that changes in the standards may have on the Corporation's consolidated financial statements when they become effective:

EFFECTIVE FOR THE CORPORATION IN 2013

IAS 19—Employee Benefits Effective on January 1, 2013, the Corporation adopted the amended IAS 19, *Employee Benefits*. The amended IAS 19 includes requirements for the measurement, presentation and disclosure for defined benefit plans. Amendments include:

- > The elimination of the deferral and amortization approach (corridor approach) for recognizing actuarial gains and losses in net earnings. Actuarial gains and losses will be recognized in other comprehensive income. Actuarial gains and losses recognized in other comprehensive income will not be reclassified to net earnings in subsequent periods.

- > The elimination of the concept of an expected return on assets (EROA). Amended IAS 19 requires the use of the discount rate in the place of EROA in the determination of the net interest component of the pension expense. This discount rate is determined by reference to market yields at the end of the reporting period on high-quality corporate bonds.
- > Changes in the recognition of past service costs. Past service costs resulting from plan amendments or curtailments will be recognized in net earnings in the period in which the plan amendments or curtailments occur, without regard to vesting.

In accordance with the transitional provisions in IAS 19, this change in IFRS will be applied retroactively and is anticipated to decrease equity by approximately \$470 million at January 1, 2012 (decrease of \$330 million in shareholders' equity, and \$140 million in non-controlling interests) with an additional decrease to equity of approximately \$240 million at January 1, 2013 (decrease of \$165 million in shareholders' equity and \$75 million

in non-controlling interests). Furthermore, the effect of applying this standard retroactively will decrease earnings before tax by approximately \$12 million for the year ended December 31, 2012.

IFRS 10—Consolidated Financial Statements Effective for the Corporation on January 1, 2013, IFRS 10, *Consolidated Financial Statements* uses consolidation principles based on a revised definition of control. The definition of control is dependent on the power of the investor to direct the activities of the investee, the ability of the investor to derive variable returns from its holdings in the investee, and a direct link between the power to direct activities and receive benefits.

The IASB issued amendments to IFRS 10 and IFRS 12 in October 2012 that introduced an exception from consolidation for the controlled entities of investment entities. Lifeco continues to review the financial reporting of the segregated funds for the risk of policyholders presented within Lifeco's financial statements to determine whether it would be different than the current reporting under IFRS.

IFRS 11—Joint Arrangements Effective for the Corporation on January 1, 2013, IFRS 11, *Joint Arrangements* separates jointly controlled entities between joint operations and joint ventures. The standard eliminates the option of using proportionate consolidation in accounting for interests in joint ventures, requiring an entity to use the equity method of accounting. The standard is not expected to have a significant impact on the Corporation's financial position or results of operations.

IFRS 12—Disclosure of Interest in Other Entities Effective for the Corporation on January 1, 2013, IFRS 12, *Disclosure of Interest in Other Entities* provides new disclosure requirements for the interest an entity has in subsidiaries, joint arrangements, associates, and structured entities. The standard requires enhanced disclosure, including how control was determined and any restrictions that might exist on consolidated assets and liabilities presented within the financial statements. The standard is expected to result in additional disclosures.

IFRS 13—Fair Value Measurement Effective for the Corporation on January 1, 2013, IFRS 13, *Fair Value Measurement* provides guidance to increase consistency and comparability in fair value measurements and related disclosures through a "fair value hierarchy". The hierarchy categorizes the inputs used in valuation techniques into three levels. The hierarchy gives the highest priority to (unadjusted) quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

The standard relates primarily to disclosure and will not impact the financial results of the Corporation.

IAS 1—Presentation of Financial Statements Effective for the Corporation on January 1, 2013, IAS 1, *Presentation of Financial Statements* includes requirements that other comprehensive income be classified by nature and grouped between those items that will be classified subsequently to profit or loss (when specific conditions are met) and those that will not be reclassified.

This revised standard relates only to presentation and will not impact the financial results of the Corporation.

IFRS 7—Financial Instruments: Disclosure Effective for the Corporation on January 1, 2013, the IASB issued amendments to IFRS 7 regarding disclosure of offsetting financial assets and financial liabilities. The amendments allow users of financial statements to improve their understanding of transfer transactions of financial assets (for example, securitizations), including understanding the possible effects of any risks that may remain with the entity that transferred the assets. The amendments also require additional disclosures if a disproportionate amount of transfer transactions are undertaken near the end of a reporting period.

This revised standard relates only to disclosure and will not impact the financial results of the Corporation.

EFFECTIVE FOR THE CORPORATION SUBSEQUENT TO 2013

IFRS 4—Insurance Contracts The IASB issued an exposure draft proposing changes to the accounting standard for insurance contracts in July 2010. The proposal would require an insurer to measure insurance liabilities using a model focusing on the amount, timing, and uncertainty of future cash flows associated with fulfilling its insurance contracts. This is vastly different from the connection between insurance assets and liabilities considered under the Canadian Asset Liability Method (CALM) and may cause significant volatility in the results of Lifeco. The exposure draft also proposes changes to the presentation and disclosure within the financial statements.

Since the release of the exposure draft, there have been discussions within the insurance industry and between accounting standards setters globally recommending significant changes to the 2010 exposure draft. At this time no new standard has been either re-exposed or released.

Lifeco will continue to measure insurance contract liabilities using CALM until such time when a new IFRS for insurance contract measurement is issued. A final standard is not expected to be implemented for several years; Lifeco continues to actively monitor developments in this area.

IFRS 9—Financial Instruments Effective for the Corporation on January 1, 2015, IFRS 9, *Financial Instruments* requires all financial assets to be classified on initial recognition at amortized cost or fair value while eliminating the existing categories of available for sale, held to maturity, and loans and receivables.

The new standard will also require:

- > embedded derivatives to be assessed for classification together with their financial asset host;
- > an expected loss impairment method be used for financial assets; and
- > amendments to the criteria for hedge accounting and measuring effectiveness.

The full impact of IFRS 9 on the Corporation will be evaluated after the remaining stages of the IASB's project to replace IAS 39, *Financial Instruments: Recognition and Measurement*—impairment methodology, hedge accounting, and asset and liability offsetting—are finalized. The current timetable for adoption of IFRS 9, *Financial Instruments* is for the annual period beginning January 1, 2015; however, the Corporation continues to monitor this standard in conjunction with developments to IFRS 4.

IAS 32—Financial Instruments: Presentation Effective for the Corporation on January 1, 2014, IAS 32, *Financial Instruments: Presentation* clarifies the existing requirements for offsetting financial assets and financial liabilities.

The Corporation is evaluating the impact this standard will have on the presentation of its financial statements.

EXPOSURE DRAFTS NOT YET EFFECTIVE

IAS 17—Leases The IASB issued an exposure draft proposing a new accounting model for leases where both lessees and lessors would record the assets and liabilities on the balance sheet at the present value of the lease payments arising from all lease contracts. The new classification would be the right-of-use model, replacing the operating and finance lease accounting models that currently exist.

The full impact of adoption of the proposed changes will be determined once the final leases standard is issued.

IAS 18—Revenue The IASB issued a second exposure draft in November 2011 which proposed a single revenue recognition standard to align the financial reporting of revenue from contracts with customers and related costs. A company would recognize revenue when it transfers goods or services to a customer in the amount of the consideration the company expects to receive from the customer.

The full impact of adoption of the proposed changes will be determined once the final revenue recognition standard is issued, which is targeted for release in 2013.

RISK FACTORS

There are certain risks inherent in an investment in the securities of the Corporation and in the activities of the Corporation, including the following and others disclosed elsewhere in this document, which investors should carefully consider before investing in securities of the Corporation. This description of risks does not include all possible risks, and there may be other risks of which the Corporation is not currently aware.

Power Financial is a holding company that holds substantial interests in the financial services sector through its controlling interest in each of Lifeco and IGM. As a result, investors in Power Financial are subject to the risks attributable to its status as a shareholder of its subsidiaries, including those that Power Financial has as the principal shareholder of each of Lifeco and IGM.

As a holding company, Power Financial's ability to pay interest and other operating expenses and dividends, to meet its obligations and to complete current or desirable future enhancement opportunities or acquisitions generally depends upon receipt of sufficient dividends from its principal subsidiaries and other investments and its ability to raise additional capital. The likelihood that shareholders of Power Financial will receive dividends will be dependent upon the operating performance, profitability, financial position and creditworthiness of the principal subsidiaries of Power Financial and on their ability to pay dividends to Power Financial. The payment of interest and dividends by certain of these principal subsidiaries to Power Financial is also subject to restrictions set forth in insurance, securities and corporate laws and regulations which require that solvency and capital standards be maintained by such companies. If required, the ability of Power Financial to arrange additional financing in the future will depend in part upon prevailing market conditions as well as the business

performance of Power Financial and its subsidiaries. In recent years, global financial conditions and market events have experienced increased volatility and resulted in the tightening of credit that has reduced available liquidity and overall economic activity. There can be no assurance that debt or equity financing will be available, or, together with internally generated funds, will be sufficient to meet or satisfy Power Financial's objectives or requirements or, if the foregoing are available to Power Financial, that they will be on terms acceptable to Power Financial. The inability of Power Financial to access sufficient capital on acceptable terms could have a material adverse effect on Power Financial's business, prospects, dividend paying capability and financial condition, and further enhancement opportunities or acquisitions.

The market price for Power Financial's securities may be volatile and subject to wide fluctuations in response to numerous factors, many of which are beyond Power Financial's control. Economic conditions may adversely affect Power Financial, including fluctuations in foreign exchange, inflation and interest rates, as well as monetary policies, business investment and the health of capital markets in Canada, the United States and Europe. In recent years, financial markets have experienced significant price and volume fluctuations that have affected the market prices of equity securities held by the Corporation and its subsidiaries and that have often been unrelated to the operating performance, underlying asset values or prospects of such companies. Additionally, these factors, as well as other related factors, may cause decreases in asset values that are deemed to be significant or prolonged, which may result in impairment losses. In periods of increased levels of volatility and related market turmoil, Power Financial's subsidiaries' operations could be adversely impacted and the trading price of Power Financial's securities may be adversely affected.

OFF-BALANCE SHEET ARRANGEMENTS

GUARANTEES

In the normal course of their businesses, the Corporation and its subsidiaries may enter into certain agreements, the nature of which precludes the possibility of making a reasonable estimate of the maximum potential amount the Corporation or subsidiary could be required to pay third parties, as some of these agreements do not specify a maximum amount and the amounts are dependent on the outcome of future contingent events, the nature and likelihood of which cannot be determined.

LETTERS OF CREDIT

In the normal course of their reinsurance business, Lifeco's subsidiaries provide letters of credit to other parties or beneficiaries. A beneficiary will typically hold a letter of credit as collateral in order to secure statutory credit for reserves ceded to or amounts due from Lifeco's subsidiaries. A letter of credit may be drawn upon demand. If an amount is drawn on a letter of credit by a beneficiary, the bank issuing the letter of credit will make a payment to the beneficiary for the amount drawn, and Lifeco's subsidiaries will become obligated to repay this amount to the bank.

Lifeco, through certain of its operating subsidiaries, has provided letters of credit to both external and internal parties, which are described in Note 30 to the Corporation's 2012 Consolidated Financial Statements.

CONTINGENT LIABILITIES

The Corporation and its subsidiaries are from time to time subject to legal actions, including arbitrations and class actions, arising in the normal course of business. It is inherently difficult to predict the outcome of any of these proceedings with certainty, and it is possible that an adverse resolution could have a material adverse effect on the consolidated financial position of the Corporation. However, based on information presently known, it is not expected that any of the existing legal actions, either individually or in the aggregate, will have a material adverse effect on the consolidated financial position of the Corporation.

A subsidiary of Lifeco has declared a partial windup in respect of an Ontario defined benefit pension plan which will not likely be completed for some time. The partial windup could involve the distribution of the amount of actuarial surplus, if any, attributable to the wound-up portion of the plan. In addition to the regulatory proceedings involving this partial windup, a related class action proceeding has been commenced in Ontario related to the partial windup and three potential partial windups under the plan. The class action also challenges the validity of charging expenses to the plan. The provisions for certain Canadian retirement plans in the amounts of \$97 million after tax established by Lifeco's subsidiaries in the third quarter of 2007 have been reduced to \$34 million. Actual results could differ from these estimates.

The Court of Appeal for Ontario released a decision on November 3, 2011 in regard to the involvement of the participating accounts of Lifeco subsidiaries London Life and Great-West Life in the financing of the acquisition of London Insurance Group Inc. in 1997 (the Appeal Decision).

The Appeal Decision ruled Lifeco subsidiaries achieved substantial success and required that there be adjustments to the original trial judgment regarding amounts which were to be reallocated to the participating accounts going forward. Any monies to be reallocated to the participating accounts will be dealt with in accordance with Lifeco subsidiaries' participating policyholder dividend policies in the ordinary course of business. No awards are to be paid out to individual class members. On May 24, 2012, the Supreme Court of Canada dismissed the plaintiff's application for leave to appeal the Appeal Decision. The Appeal Decision directed the parties back to the trial judge to work out the remaining issues. On January 24, 2013 the Ontario Superior Court of Justice released a decision ordering that \$285 million be reallocated to the participating account surplus. Lifeco will be appealing that decision.

During the fourth quarter of 2011, in response to the Appeal Decision, Lifeco re-evaluated and reduced the litigation provision established in the third quarter of 2010, which positively impacted common shareholder net earnings of Lifeco in 2011 by \$223 million after tax (Power Financial's share—\$158 million).

During the subsequent event period, in response to the Ontario Superior Court of Justice decision on January 24, 2013, Lifeco established an incremental provision of \$140 million after tax in the common shareholders account of Lifeco (Power Financial's share—\$99 million). Lifeco now holds \$290 million in after-tax provisions for these proceedings.

Regardless of the ultimate outcome of this case, there will not be any impact on the capital position of Lifeco or on participating policy contract terms and conditions. Based on information presently known, this matter is not expected to have a material adverse effect on the consolidated financial position of the Corporation.

In connection with the acquisition of its subsidiary Putnam, Lifeco has an indemnity from a third party against liabilities arising from certain litigation and regulatory actions involving Putnam. Putnam continues to have potential liability for these matters in the event the indemnity is not honoured. Lifeco expects the indemnity will continue to be honoured and that any liability of Putnam would not have a material adverse effect on its consolidated financial position.

On October 17, 2012, a subsidiary of Lifeco received an administrative complaint from the Massachusetts Securities Division in relation to that subsidiary's role as collateral manager of two collateralized debt obligations. The complaint is seeking certain remedies, including the disgorgement of fees, a civil administrative fine and a cease and desist order. In addition, that same subsidiary is a defendant in two civil litigation matters brought by institutions involved in those collateralized debt obligations. Based on information presently known, Lifeco believes these matters are without merit. The potential outcome of these matters is not yet determined.

Subsidiaries of Lifeco have an investment in a USA-based private equity partnership wherein a dispute arose over the terms of the partnership agreement. Lifeco established a provision in the fourth quarter of 2011 for \$99 million after tax. The dispute was resolved on January 10, 2012, and as a result, Lifeco no longer holds the provision.

COMMITMENTS AND CONTRACTUAL OBLIGATIONS

The following table provides a summary of future consolidated contractual obligations.

PAYMENTS DUE BY PERIOD	TOTAL	LESS THAN 1 YEAR	1-5 YEARS	MORE THAN 5 YEARS
Long-term debt ^[1]	5,858	296	302	5,260
Deposits and certificates	163	145	13	5
Obligations to securitization entities	4,701	789	3,877	35
Operating leases ^[2]	733	153	422	158
Purchase obligations ^[3]	83	58	25	
Contractual commitments ^[4]	516	470	46	
Total	12,054	1,911	4,685	5,458
Letters of credit ^[5]				

[1] Please refer to Note 13 to the Corporation's 2012 Consolidated Financial Statements for further information.

[2] Includes office space and certain equipment used in the normal course of business. Lease payments are charged to operations in the period of use.

[3] Purchase obligations are commitments of Lifeco to acquire goods and services, essentially related to information services.

[4] Represents commitments by Lifeco. These contractual commitments are essentially commitments of investment transactions made in the normal course of operations, in accordance with its policies and guidelines, which are to be disbursed upon fulfilment of certain contract conditions.

[5] Please refer to Note 30 to the Corporation's 2012 Consolidated Financial Statements.

FINANCIAL INSTRUMENTS

FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table presents the fair value of the Corporation's financial instruments. Fair value represents the amount that would be exchanged in an arm's-length transaction between willing parties and is best evidenced by a quoted market price, if one exists. Fair values are management's estimates

and are generally calculated using market conditions at a specific point in time and may not reflect future fair values. The calculations are subjective in nature, involve uncertainties and matters of significant judgment (please refer to Note 26 to the Corporation's 2012 Consolidated Financial Statements).

AS AT DECEMBER 31	2012		2011	
	CARRYING VALUE	FAIR VALUE	CARRYING VALUE	FAIR VALUE
ASSETS				
Cash and cash equivalents	3,313	3,313	3,385	3,385
Investments (excluding investment properties)	120,062	122,805	113,841	116,170
Funds held by ceding insurers	10,537	10,537	9,923	9,923
Derivative financial instruments	1,060	1,060	1,056	1,056
Other financial assets	4,212	4,212	3,539	3,539
Total financial assets	139,184	141,927	131,744	134,073
LIABILITIES				
Obligation to securitization entities	4,701	4,787	3,827	3,930
Debentures and debt instruments	5,858	6,830	5,888	6,502
Capital trust securities	119	171	533	577
Derivative financial instruments	413	413	427	427
Other financial liabilities	4,923	4,925	4,509	4,510
Total financial liabilities	16,014	17,126	15,184	15,946

DERIVATIVE FINANCIAL INSTRUMENTS

In the course of their activities, the Corporation and its subsidiaries use derivative financial instruments. When using such derivatives, they only act as limited end-users and not as market-makers in such derivatives.

The use of derivatives is monitored and reviewed on a regular basis by senior management of the companies. The Corporation and its subsidiaries have each established operating policies and processes relating to the use of derivative financial instruments, which in particular aim at:

- > prohibiting the use of derivative instruments for speculative purposes;
- > documenting transactions and ensuring their consistency with risk management policies;
- > demonstrating the effectiveness of the hedging relationships; and
- > monitoring the hedging relationship.

There were no major changes to the Corporation's and its subsidiaries' policies and procedures with respect to the use of derivative instruments in the twelve-month period ended December 31, 2012. There has been an increase in the notional amount outstanding (\$16,888 million at December 31, 2012, compared with \$14,948 million at December 31, 2011) and an increase in the exposure to credit risk (\$1,060 million at December 31, 2012, compared with \$1,056 million at December 31, 2011) that represents the market value of those instruments, which are in a gain position. During the third quarter of 2012, Lifeco purchased equity put options with a notional amount of \$849 million as a macro balance sheet credit hedge against a decline in European equity market levels. See Note 25 to the Corporation's 2012 Consolidated Financial Statements for more information on the type of derivative financial instruments used by the Corporation and its subsidiaries.

DISCLOSURE CONTROLS AND PROCEDURES

Based on their evaluations as of December 31, 2012, the Chief Executive Officer and the Chief Financial Officer have concluded that the Corporation's disclosure controls and procedures were effective as at December 31, 2012.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Based on their evaluations as of December 31, 2012, the Chief Executive Officer and the Chief Financial Officer have concluded that the Corporation's internal controls over financial reporting were effective as at December 31, 2012. During the fourth quarter of 2012, there have been no changes in the Corporation's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

SELECTED ANNUAL INFORMATION

FOR THE YEARS ENDED DECEMBER 31	2012	2011	2010
Total revenue including discontinued operations	32,412	32,433	32,559
Operating earnings attributable to common shareholders ^[1]	1,686	1,729	1,625
per share—basic	2.38	2.44	2.30
Net earnings attributable to common shareholders	1,626	1,722	1,468
per share—basic	2.30	2.43	2.08
per share—diluted	2.28	2.41	2.06
Earnings from discontinued operations attributable to common shareholders	—	38	1
per share—basic	—	0.05	—
per share—diluted	—	0.05	—
Earnings from continuing operations attributable to common shareholders	1,626	1,684	1,467
per share—basic	2.30	2.38	2.08
per share—diluted	2.28	2.36	2.06
Consolidated assets	268,593	252,678	244,644
Total financial liabilities	16,014	15,184	17,748
Debt and debt instruments	5,858	5,888	6,313
Shareholders' equity	14,029	13,521	12,811
Book value per share	16.60	16.26	15.26
Number of common shares outstanding [millions]	709.1	708.2	708.0
Dividends per share [declared]			
Common shares	1.4000	1.4000	1.4000
First preferred shares			
Series A	0.5250	0.5250	0.45238
Series C ^[2]			0.9750
Series D	1.3750	1.3750	1.3750
Series E	1.3125	1.3125	1.3125
Series F	1.4750	1.4750	1.4750
Series H	1.4375	1.4375	1.4375
Series I	1.5000	1.5000	1.5000
Series J ^[3]			0.5875
Series K	1.2375	1.2375	1.2375
Series L	1.2750	1.2750	1.2750
Series M	1.5000	1.5000	1.5000
Series O	1.4500	1.4500	1.4500
Series P ^[4]	1.1000	1.1000	0.6487
Series R ^[5]	1.2837		

[1] Operating earnings and operating earnings per share are non-IFRS financial measures.

[2] Redeemed in October 2010.

[3] Redeemed in July 2010.

[4] Issued in June 2010.

[5] Issued in February 2012.