EXTENDICARE®

... helping people live better

INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES

Q1 Three Months Ended March 31, 2019 and 2018

Extendicare Inc.
Dated: May 14, 2019

Extendicare Inc.

Interim Condensed Consolidated Statements of Financial Position

(unaudited)

(in thousands of Canadian dollars)	*notes*	**March 31, 2019**	**December 31, 2018**
Assets			
Current assets			
Cash and short-term investments		**70,500**	65,893
Restricted cash		**2,443**	2,290
Accounts receivable		**44,603**	50,570
Income taxes recoverable		**17,495**	17,316
Other assets	*5*	**20,469**	21,465
Total current assets		**155,510**	157,534
Non-current assets			
Property and equipment	*3, 4*	**518,425**	514,849
Goodwill and other intangible assets		**94,165**	95,200
Other assets	*5*	**107,261**	118,996
Deferred tax assets		**13,273**	9,745
Total non-current assets		**733,124**	738,790
Total assets		**888,634**	896,324
Liabilities and Equity			
Current liabilities			
Accounts payable and accrued liabilities		**138,979**	133,654
Income taxes payable		**75**	1,073
Long-term debt	*3, 7*	**81,303**	74,626
Provisions	*6*	**10,347**	17,621
Total current liabilities		**230,704**	226,974
Non-current liabilities			
Long-term debt	*3, 7*	**451,493**	454,344
Provisions	*6*	**37,643**	42,595
Other long-term liabilities	*8*	**37,275**	35,077
Deferred tax liabilities		**13,619**	11,343
Total non-current liabilities		**540,030**	543,359
Total liabilities		**770,734**	770,333
Share capital	*10*	**493,335**	492,064
Equity portion of convertible debentures		**7,085**	7,085
Contributed surplus		**2,924**	2,706
Accumulated deficit		**(375,823)**	(368,147)
Accumulated other comprehensive loss		**(9,621)**	(7,717)
Shareholders' equity		**117,900**	125,991
Total liabilities and equity		**888,634**	896,324

See accompanying notes to unaudited interim condensed consolidated financial statements.

Commitments and contingencies (note 16).

Subsequent event (note 7).

Extendicare Inc.

Interim Condensed Consolidated Statements of Earnings

(unaudited)

(in thousands of Canadian dollars except for per share amounts)	*notes*	Three months ended March 31, 2019	2018
CONTINUING OPERATIONS			
Revenue	*18*	**274,269**	271,424
Operating expenses		**243,883**	242,102
Administrative costs	*3*	**10,834**	9,345
Total expenses	*11*	**254,717**	251,447
Earnings before depreciation, amortization, and other expense		**19,552**	19,977
Depreciation and amortization	*3*	**9,427**	7,837
Other expense	*12*	**1,429**	180
Earnings before net finance costs and income taxes		**8,696**	11,960
Interest expense	*3*	**6,882**	7,081
Interest revenue		**(864)**	(1,035)
Accretion		**536**	664
Foreign exchange and fair value adjustments	*13*	**329**	(130)
Net finance costs		**6,883**	6,580
Earnings before income taxes		**1,813**	5,380
Income tax expense (recovery)			
Current		**1,524**	583
Deferred		**(768)**	1,231
Total income tax expense		**756**	1,814
Earnings from continuing operations		**1,057**	3,566
DISCONTINUED OPERATIONS			
Earnings from discontinued operations, net of income taxes	*15*	**1,901**	1,265
Net earnings		**2,958**	4,831
Basic and Diluted Earnings per Share			
Earnings from continuing operations	*14*	**0.01**	0.04
Net earnings	*14*	**0.03**	0.05

See accompanying notes to unaudited interim condensed consolidated financial statements.

Extendicare Inc.

Interim Condensed Consolidated Statements of Comprehensive Income

(unaudited)

(in thousands of Canadian dollars)	Three months ended March 31, 2019	2018
Net earnings	**2,958**	4,831
Other comprehensive income (loss), net of income taxes		
Items that will not be reclassified to profit or loss:		
Defined benefit plan actuarial losses	**(1,739)**	(576)
Tax recovery on defined benefit plan actuarial losses	**461**	152
Defined benefit plan actuarial losses, net of taxes	**(1,278)**	(424)
Items that are or may be reclassified subsequently to profit or loss:		
Net change in foreign currency translation adjustment	**(626)**	684
Other comprehensive income (loss), net of tax	**(1,904)**	260
Total comprehensive income	**1,054**	5,091

See accompanying notes to unaudited interim condensed consolidated financial statements.

Extendicare Inc.
Interim Condensed Consolidated Statements of Changes in Equity
(unaudited)

(in thousands of Canadian dollars)	*notes*	*Number of Shares*	Share capital	Equity portion of convertible debentures	Contributed surplus	Accumulated deficit	Accumulated other comprehensive income (loss)	Shareholders' equity
Balance at January 1, 2019		***88,489,984***	**492,064**	**7,085**	**2,706**	**(368,147)**	**(7,717)**	**125,991**
DRIP		***183,762***	**1,271**	**–**	**–**	**–**	**–**	**1,271**
Share-based compensation	*9*	**–**	**–**	**–**	**218**	**–**	**–**	**218**
Net earnings		**–**	**–**	**–**	**–**	**2,958**	**–**	**2,958**
Dividends declared		**–**	**–**	**–**	**–**	**(10,634)**	**–**	**(10,634)**
Other comprehensive loss		**–**	**–**	**–**	**–**	**–**	**(1,904)**	**(1,904)**
Balance at March 31, 2019		***88,673,746***	**493,335**	**7,085**	**2,924**	**(375,823)**	**(9,621)**	**117,900**

(in thousands of Canadian dollars)	*notes*	*Number of Shares*	Share capital	Equity portion of convertible debentures	Contributed surplus	Accumulated deficit	Accumulated other comprehensive income (loss)	Shareholders' equity
Balance at January 1, 2018, previously		*88,523,290*	490,881	5,573	2,437	(365,084)	(4,851)	128,956
Adoption of new standard (1)		–	–	–	–	4,334	(4,334)	–
Balance at January 1, 2018		*88,523,290*	490,881	5,573	2,437	(360,750)	(9,185)	128,956
DRIP		*143,581*	1,212	–	–	–	–	1,212
Purchase of shares for cancellation	*10*	*(703,585)*	(3,903)	–	–	(2,358)	–	(6,261)
Share-based compensation	*9*	*5,032*	44	–	386	–	–	430
Net earnings		–	–	–	–	4,831	–	4,831
Dividends declared		–	–	–	–	(10,578)	–	(10,578)
Other comprehensive income		–	–	–	–	–	260	260
Balance at March 31, 2018		*87,968,318*	488,234	5,573	2,823	(368,855)	(8,925)	118,850

See accompanying notes to unaudited interim condensed consolidated financial statements.

(1) Adoption of new standard on financial instruments – IFRS 9.

Extendicare Inc.

Interim Condensed Consolidated Statements of Cash Flows

(unaudited)

		Three months ended March 31,	
(in thousands of Canadian dollars)	*notes*	**2019**	**2018**
Operating Activities			
Net earnings		**2,958**	4,831
Adjustments for:			
Depreciation and amortization	*3*	**9,427**	7,837
Share-based compensation		**218**	434
Deferred taxes		**(825)**	958
Current taxes		**1,581**	856
Net finance costs	*3*	**6,554**	6,710
Other expense (income)		**(472)**	(1,085)
Foreign exchange and fair value adjustments		**329**	(130)
		19,770	20,411
Net change in operating assets and liabilities			
Accounts receivable		**5,963**	2,415
Other assets		**984**	107
Accounts payable and accrued liabilities		**1,785**	5,597
		28,502	28,530
Payments for self-insured liabilities		**(8,894)**	(4,189)
Interest paid		**(4,948)**	(9,071)
Interest received		**867**	1,040
Income taxes paid		**(3,015)**	(5,871)
Net cash from operating activities	*3*	**12,512**	10,439
Investing Activities			
Purchase of property, equipment and other intangible assets		**(6,038)**	(6,713)
Decrease in investments held for self-insured liabilities		**9,266**	2,779
Decrease in other assets		**1,370**	1,300
Net cash from (used in) investing activities		**4,598**	(2,634)
Financing Activities			
Issuance of long-term debt		**5,183**	2,514
Repayment of long-term debt	*3*	**(7,741)**	(5,534)
Increase in restricted cash		**(153)**	(130)
Purchase of securities for cancellation		**–**	(6,258)
Dividends paid		**(9,355)**	(9,388)
Net cash used in financing activities		**(12,066)**	(18,796)
Increase (decrease) in cash and short-term investments		**5,044**	(10,991)
Cash and short-term investments at beginning of period		**65,893**	128,156
Foreign exchange gain (loss) on cash held in foreign currency		**(437)**	873
Cash and short-term investments at end of period		**70,500**	118,038

See accompanying notes to unaudited interim condensed consolidated financial statements.

Notes to Unaudited Interim Condensed Consolidated Financial Statements

THREE MONTHS ENDED MARCH 31, 2019 AND 2018

(Amounts in thousands of Canadian dollars, unless otherwise noted)

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1. GENERAL INFORMATION AND NATURE OF THE BUSINESS

The common shares (the "Common Shares") of Extendicare Inc. ("Extendicare" or the "Company") are listed on the Toronto Stock Exchange (TSX) under the symbol "EXE". Extendicare and its predecessors have been operating since 1968, providing care and services to seniors throughout Canada. Following the sale of its U.S. business in 2015, the Company has repositioned itself as a leading provider of care and services across Canada, committed to delivering quality care throughout the health continuum to meet the needs of a growing seniors population.

References to "Extendicare", the "Company", "we", "us" and "our" or similar terms refer to Extendicare Inc., either alone, or together with its subsidiaries. The registered office of Extendicare is located at 3000 Steeles Avenue East, Suite 700, Markham, Ontario, Canada, L3R 9W2.

2. BASIS OF PREPARATION

a) Statement of Compliance

The interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standards (IAS) 34 "Interim Financial Reporting", as issued by the International Accounting Standards Board (IASB), and were approved by the board of directors of Extendicare Inc. (the "Board") on May 14, 2019.

The interim condensed consolidated financial statements do not include all of the information required for full annual financial statements, and should be read in conjunction with Extendicare Inc.'s 2018 annual consolidated financial statements prepared in accordance with International Financial Reporting Standards (IFRS). These interim condensed consolidated financial statements follow the same accounting policies and methods of application as the consolidated financial statements as at and for the year ended December 31, 2018, except for those identified in *note 3*. Certain comparative information has been reclassified to conform to the current year presentation.

b) Basis of Measurement

The interim condensed consolidated financial statements have been prepared on the historical cost basis except for financial assets and liabilities classified at fair value through profit or loss.

The interim condensed consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. All financial information presented in dollars has been rounded to the nearest thousand, unless otherwise noted.

c) Use of Estimates and Judgement

The preparation of consolidated financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Estimates and underlying assumptions are reviewed on an ongoing basis.

Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

The more subjective of such estimates are:

- determination of the lease term for leases that include renewal options and the appropriate discount rate used to recognize lease liability (*note 3*);
- valuation of indemnification provisions (*note 6*);
- valuation of self-insured liabilities (*note 6*);
- valuation of equity portion of convertible debentures;
- valuation of financial assets and liabilities (*note 17(b)*);
- valuation of share-based compensation (*note 9*);
- determination of the recoverable amount of cash generating units (CGUs) subject to an impairment test; and
- accounting for tax uncertainties and the tax rates used for valuation of deferred taxes.

In addition, the assessment of contingencies (*note 16*) is subject to judgement. The recorded amounts for such items are based on management's best available information and are subject to assumptions and judgement, which may change as time progresses; accordingly, actual results could differ from estimates.

3. NEW ACCOUNTING POLICIES ADOPTED

Leases

Effective January 1, 2019, the Company adopted IFRS 16 "Leases", which supersedes IAS 17 "Leases" and related interpretations. This new standard requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value, using a single accounting model, thereby eliminating the distinction between operating and finance leases. The nature and timing of the related expense has changed as IFRS 16 replaces the straight-line lease costs with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

Lease costs for the prior year have been reclassified under administrative costs to conform with the current year presentation. The impact of adopting this standard on net earnings and overall cash flow is neutral; however, the principal payment of the lease liabilities is presented in financing activities (previously reflected as operating activities).

The Company has applied IFRS 16 using the modified retrospective approach, under which the comparative information presented has not been restated. Certain practical expedients were selected on transition. The transition did not result in any retrospective adjustment to opening retained earnings on January 1, 2019.

TRANSITION

At transition, for leases classified as operating leases under IAS 17, lease liabilities were measured at the present value of the remaining lease payments, discounted at the Company's incremental weighted average borrowing rate as at January 1, 2019, of 4.86%. Right-of-use assets were measured at an amount equal to the lease liability. For leases that were classified as finance leases under IAS 17, the carrying amount of the right-of-use assets and the lease liability as at January 1, 2019, was the carrying amount of the lease assets and lease liability immediately before the date of initial application. These are accounted for using IFRS 16 from that date.

The Company used the following practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17:

- applied the exemption not to recognize right-of-use assets and liabilities for leases with less than 12 months of lease term;
- applied the exemption not to recognize right-of-use assets and liabilities for leases that are of low value;
- excluded initial direct costs from measuring the right-of-use asset as at January 1, 2019; and
- used hindsight as at January 1, 2019, when determining the lease term if the contract contains options to extend or terminate the lease.

IMPACTS ON FINANCIAL STATEMENTS

i. Impacts on transition

On transition to IFRS 16, the Company recognized additional right-of-use assets and lease liabilities of $5.8 million.

ii. Impacts for the period

For the three months ended March 31, 2019, the Company recognized $0.7 million of depreciation expense and $0.1 million of interest expense related to the leases impacted by the adoption of IFRS 16.

Income Taxes

On June 7, 2017, the IASB issued IFRIC Interpretation 23 "Uncertainty over Income Tax Treatments". The interpretation provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. Effective January 1, 2019, the Company adopted the IFRIC Interpretation 23, with no material impact on the interim condensed consolidated financial statements.

4. PROPERTY AND EQUIPMENT

	March 31, 2019	December 31, 2018
Land and land improvements	**57,918**	58,280
Buildings	**594,524**	587,161
Furniture and equipment	**61,787**	63,047
Leasehold improvements	**1,143**	1,927
Construction in progress	**34,006**	30,851
	749,378	741,266
less: accumulated depreciation	**(230,953)**	(226,417)
	518,425	514,849

The right-of-use assets included in buildings were $86.8 million (December 31, 2018 ─ $81.0 million) with accumulated depreciation of $33.5 million (December 31, 2018 ─ $32.2 million).

For the three months ended March 31, 2019, the Company capitalized $0.2 million of borrowing costs related to development projects under construction at an average capitalization rate of 4.5% (2018 ─ $0.3 million at 5.6%).

5. OTHER ASSETS

	March 31, 2019	December 31, 2018
Investments held for self-insured liabilities	**58,705**	67,938
Amounts receivable and other assets	**67,525**	69,967
Interest rate swaps	**1,500**	2,556
	127,730	140,461
less: current portion	**20,469**	21,465
	107,261	118,996

Investments Held for Self-insured Liabilities

After the sale of our U.S. business in 2015 (the "U.S. Sale Transaction"), as part of its continuing operations, Extendicare retained its wholly owned Bermuda-based captive insurance company, Laurier Indemnity Company, Ltd. (the "Captive"), which, along with third-party insurers, insured Extendicare's U.S. general and professional liability risks up to the date of the U.S. Sale Transaction.

Extendicare holds U.S. dollar-denominated investments within the Captive for settlements of the self-insured liabilities that are subject to insurance regulatory requirements (*note 6*).

As at March 31, 2019, the investment portfolio comprises cash of $3.2 million (December 31, 2018 – $5.8 million), money market funds of $55.5 million (December 31, 2018 – $53.8 million), and no investment-grade corporate securities (December 31, 2018 – $8.3 million). Certain of these investments in the amount of $24.0 million (December 31, 2018 – $35.1 million), have been pledged as collateral for letters of credit issued by the banker of the Captive in favour of ceding companies. As at March 31, 2019, all investments were carried at fair value, with changes in fair value reflected in earnings (*note 13*).

Amounts Receivable and Other Assets

Amounts receivable and other assets include discounted amounts receivable due from the government of Ontario with respect to construction funding subsidies for long-term care centres, totalling $52.0 million (December 31, 2018 – $53.3 million) of which $5.6 million (December 31, 2018 – $5.5 million) is current. These subsidies represent funding for a portion of long-term care centre construction costs over a 20-year or 25-year period. The weighted average remaining term of this funding is 15 years.

Also included in amounts receivable and other assets is a $1.4 million receivable as at March 31, 2019 (December 31, 2018 – $2.0 million), resulting from the U.S. Sale Transaction, as well as prepaid expenses and deposits.

Interest Rate Swaps

The interest rate swaps include swap contracts relating to mortgages, totalling $84.2 million, to lock in the rates between 3.11% and 5.04% for the full term of the loans being five to ten years (*note 7*).

All interest rate swap contracts are measured at fair value through profit or loss, and hedge accounting has not been applied. Changes in fair value are recorded in the statements of earnings (*note 13)*. As at March 31, 2019, the interest rate swaps were valued as a net asset of $0.7 million, including a liability of $0.8 million (*notes 7 and 8*) (December 31, 2018 – net asset of $2.0 million, including a liability of $0.5 million).

6. PROVISIONS

	March 31, 2019	**December 31, 2018**
Accrual for self-insured liabilities	**25,752**	37,138
Indemnification provisions	**12,831**	13,713
Decommissioning provisions	**9,407**	9,365
Total provisions	**47,990**	60,216
Less: current portion	**(10,347)**	(17,621)
	37,643	42,595

Accrual for Self-Insured Liabilities

The obligation to settle U.S. self-insured general and professional liability claims relating to the period prior to the closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, remains with Extendicare, which it intends to fund through the Captive. Consequently, the balance of the accrual for self-insured liabilities and the related investments held for self-insured liabilities (*note 5*) remain on the consolidated statement of financial position. However, any expense incurred or release of reserves for U.S. self-insured liabilities are presented as discontinued operations; while the Captive's costs to administer and manage the settlement of the remaining claims are reported as continuing operations within the U.S. segment.

The accrual for self-insured liabilities is based on management's best estimate of the ultimate cost to resolve general and professional liability claims. Actual results can differ materially from the estimates made due to a number of factors including the assumptions used by management and other market forces.

As at March 31, 2019, the accrual for self-insured general and professional liabilities was $25.7 million (US$19.3 million) compared to $37.1 million (US$27.2 million) as at December 31, 2018. The decline represented mainly claim payments and the release of reserves (*note 15*).

Indemnification Provisions

As a result of the U.S. Sale Transaction, the Company agreed to indemnify certain obligations of the U.S. operations related to tax, a corporate integrity agreement (the "CIA"), and other items. Any revisions to these estimates are reflected as part of other expense in discontinued operations (*note 15*). As at March 31, 2019, the remaining provisions totalled $12.8 million (US$9.6 million) (2018 – $13.7 million or US$10.1 million). Actual results can differ materially from the estimates made due to a number of factors including the assumptions used by management and other market forces.

Decommissioning Provisions

The decommissioning provisions relate to possible asbestos remediation of Extendicare's pre-1980 constructed centres. An estimated undiscounted cash flow amount of approximately $11.0 million was discounted using a rate of 1.98% over an estimated time to settle of 7 years. This represents management's best estimate and actual amounts may differ.

7. LONG-TERM DEBT

	Interest Rate	Year of Maturity	March 31, 2019	December 31, 2018
Convertible unsecured subordinated debentures	5.0%	2025	**119,995**	119,775
CMHC mortgages	2.93% - 7.7%	2020 - 2037	**111,539**	114,083
Non-CMHC mortgages	3.11% - 5.637%	2020 - 2038	**168,352**	169,670
Construction loans	variable	on demand	**58,049**	52,866
Lease obligations	2.28% - 7.19%	2019 - 2028	**82,892**	80,992
			540,827	537,386
Deferred financing costs			**(8,031)**	(8,416)
Total debt, net of deferred financing costs			**532,796**	528,970
Less: current portion			**81,303**	74,626
Long-term debt, net of deferred financing costs			**451,493**	454,344

A summary of significant changes in long-term debt since December 31, 2018, is provided below.

CMHC Mortgages

Subsequent to March 31, 2019, the Company secured a CMHC-insured mortgage of $16.0 million, inclusive of fees, on the Lynde Creek Manor retirement living community, that matures in September 2029, with a fixed rate of 2.81% per annum.

Construction Loans

Construction financings totalling $87.6 million for four retirement development projects in Simcoe, Bolton, Uxbridge, and Barrie are available and provide for additional letter of credit facilities of $0.5 million, $0.8 million, $0.8 million, and $1.0 million respectively, at rates ranging from 2.25% to 2.5% if utilized. Loan payments are interest-only based on a variable rate of 30-day banker's acceptance (BA) plus 2.25% to 2.5%, with no standby fee.

The construction loans are repayable on demand and, in any event, are to be fully repaid: by the earlier of achieving stabilized occupancy as defined by the agreements and specified dates between late 2019 and 2022 for Simcoe, Bolton and Uxbridge; and by the earlier of September 2023 and three months following stabilized occupancy as defined by the agreement for Barrie.

All these financings have been reflected as current. Permanent financing for each of the communities will be sought upon maturity of the construction financing.

As at March 31, 2019, an aggregate of $58.0 million was drawn on the construction loans, leaving $29.6 million available; in addition, letters of credit totalling $1.2 million were issued under credit facilities, leaving $1.8 million undrawn.

Lease Obligations

Lease obligations outstanding as at March 31, 2019 include leases on long-term care centres, customized cloud-based software, and the liability related to office leases (*note 3*). The Company operates nine Ontario long-term care centres, which were built between 2001 and 2003, under 25-year lease arrangements. The software balance will be amortized over the contract term of five years. The liability associated with the office lease obligation will be amortized over the remaining lease terms ranging up to five years.

Credit Facilities

The Company has two demand credit facilities totalling $112.3 million, secured by either 13 Class C long-term care centres in Ontario or the assets of the home health care business. Neither of these facilities has financial covenants, but do contain normal and customary terms. As at March 31, 2019, $38.0 million of the facilities secure the Company's defined benefit pension plan obligations, $7.0 million was issued in connection with obligations relating to centres that were recently acquired and under development, leaving $67.3 million undrawn.

Deferred Financing Costs

Deferred financing costs are deducted against long-term debt and are amortized using the effective interest rate method over the term of the debt.

Below is a summary of the deferred financing costs:

	March 31, 2019	December 31, 2018
Convertible unsecured subordinated debentures	**4,581**	4,774
CMHC mortgages	**1,922**	2,017
Non-CMHC mortgages	**1,330**	1,419
Lease obligations	**198**	206
Total deferred financing costs	**8,031**	8,416
Less: current portion	**1,399**	1,404
	6,632	7,012

Interest Rates

The weighted average interest rate of all long-term debt as at March 31, 2019, was approximately 4.8% (December 31, 2018 – 4.9%). As at March 31, 2019, 89.3% of the long-term debt, including interest rate swaps, was at fixed rates (December 31, 2018 – 90.2%).

8. OTHER LONG-TERM LIABILITIES

	March 31, 2019	December 31, 2018
Accrued pension plan obligation	**34,978**	33,486
Interest rate swaps (*notes 5 and 7*)	**827**	523
Other	**1,470**	1,068
	37,275	35,077

9. SHARE-BASED COMPENSATION

The Company's share-based compensation, which includes deferred share units (DSUs) and performance share units (PSUs), and prior to 2019, share appreciation rights (SARs) was an expense of $0.2 million for 2019 (2018 – $0.4 million).

The carrying amounts of the Company's share-based compensation arrangements are recorded in the consolidated statements of financial position as follows:

	March 31, 2019	December 31, 2018
Contributed surplus – DSUs	**2,065**	1,914
Contributed surplus – PSUs	**859**	792

Equity-settled Long-term Incentive Plan

The Company's long-term incentive plan (the "LTIP") provides for a share-based component of executive and director compensation designed to encourage a greater alignment of the interests of the Company's executives and directors with its shareholders, in the form of PSUs for employees and DSUs for non-employee directors.

PSUs and DSUs granted under the LTIP do not carry any voting rights. DSUs vest immediately upon grant and PSUs vest three years from the date of grant. An aggregate of 4,387,974 Common Shares are reserved and available for issuance pursuant to the LTIP.

A summary of the Company's DSU and PSU activity is as follows:

	Deferred Share Units		Performance Share Units	
	Three months ended March 31, 2019	**Twelve months ended December 31, 2018**	**Three months ended March 31, 2019**	**Twelve months ended December 31, 2018**
Units outstanding, beginning of period	**239,725**	134,369	**188,909**	342,944
Granted	**19,987**	109,744	**–**	192,116
Reinvested dividend equivalents	**4,063**	10,498	**3,009**	26,007
Forfeited	**–**	–	**(34,900)**	(367,126)
Settled	**–**	(14,886)	**–**	(5,032)
Units outstanding, end of period	**263,775**	239,725	**157,018**	188,909
Weighted average fair value of units granted during the period at grant date	**$7.54**	$7.36	**–**	$9.33

The grant date values of PSUs awarded were based on the fair values of one award comprised of two equal components being the adjusted funds from operations (AFFO) and total shareholder return (TSR). The fair values of the AFFO component were measured using the previous day's closing trading price of the Common Shares. The fair values of the TSR component were measured using the Monte Carlo simulation method.

A summary of PSUs granted and the assumptions used to determine the grant date values are as follows:

	Twelve months ended December 31, 2018
Grant date	March 15, 2018
Vesting date	March 15, 2021
PSUs granted	192,116
Fair value of AFFO component	$4.36
Fair value of TSR component	4.97
Grant date fair value	$9.33
Expected volatility of Extendicare's Common Shares	23.66%
Expected volatility of the Index	12.20%
Risk-free rate	1.84%
Dividend yield	nil

10. SHARE CAPITAL

Dividend Reinvestment Plan

The Company has a Dividend Reinvestment Plan (DRIP) pursuant to which shareholders who are Canadian residents may elect to reinvest their cash distributions in additional Common Shares. During the three months ended March 31, 2019, the Company issued 183,762 Common Shares at a value of $1.3 million in connection with the DRIP (2018 – 143,581 Common Shares at a value of $1.2 million).

Normal Course Issuer Bid

In January 2019, Extendicare received the approval of the TSX to renew its normal course issuer bid (the "Bid") to purchase for cancellation up to 8,830,000 Common Shares (approximately 10% of the public float) through the facilities of the TSX, and on alternative Canadian trading platforms. The Bid commenced on January 15, 2019, and provides Extendicare with flexibility to purchase Common Shares for cancellation until January 14, 2020, or on such earlier date as the Bid is complete. Subject to the TSX's block purchase exception, on any trading day, purchases under the Bid will not exceed 54,852 Common Shares. The price that Extendicare will pay for any Common Shares purchased under the Bid will be the prevailing market price at the time of purchase and any Common Shares purchased will be cancelled.

During the three months ended March 31, 2019, the Company did not purchase any Common Shares under the Bid. During the three months ended March 31, 2018, under the normal course issuer bid that commenced on January 15, 2018 and ended on January 14, 2019, the Company acquired and cancelled 703,585 Common Shares at an average price of $8.89 per share, for a total cost of $6.3 million.

11. EXPENSES BY NATURE

	Three months ended March 31,	
	2019	**2018**
Employee wages and benefits	**215,256**	214,209
Food, drugs, supplies and other variable costs	**12,271**	11,817
Property based and other	**26,177**	23,794
Lease costs (*note 3*)	**1,013**	1,627
Total operating expenses and administrative costs	**254,717**	251,447

12. OTHER EXPENSE

	Three months ended March 31,	
	2019	**2018**
Acquisition costs	**–**	180
Termination of B.C. market home health care contracts	**1,429**	–
	1,429	180

On March 13, 2019, the Company received notice from Fraser Health and Vancouver Coastal Health, both regional health authorities in British Columbia (the "Health Authorities"), that the Health Authorities will be bringing their home support services in-house, and as a result will not be renewing contracts with private sector home support agencies, including ParaMed Inc. (ParaMed), the Company's home health care operations. Consequently, ParaMed's contracts with the B.C. Health Authorities will expire in March 2020. The Company recognized a $1.4 million provision in the first quarter of 2019 for costs to be incurred in connection with the contract expiration.

In April 2018, the Company acquired the Lynde Creek Retirement Community, and incurred transaction costs of $0.2 million during the three months ended March 31, 2018.

13. FOREIGN EXCHANGE AND FAIR VALUE ADJUSTMENTS

Foreign exchange and fair value adjustments for the three months ended March 31, 2019, was a loss of $0.3 million for 2019 (2018 – gain of $0.1 million). These include: (1) foreign exchange gains or losses related to balances in connection with the U.S. Sale Transaction that are denominated in U.S. dollars; (2) fair value adjustments to interest rate swap contracts that lock in the interest rates for certain mortgages (*notes 5 and 8*); and (3) fair value adjustments on investments held for self-insured liabilities (*note 5*).

14. EARNINGS PER SHARE

Basic earnings per share (EPS) is calculated by dividing the net earnings for the period by the weighted average number of shares outstanding during the period, including vested DSUs awarded that have not settled. Diluted EPS is calculated by adjusting the net earnings and the weighted average number of shares outstanding for the effects of all dilutive instruments. The Company's potentially dilutive instruments include the convertible debentures and equity-settled compensation arrangements. The number of shares included with respect to the PSUs is computed using the treasury stock method. The convertible debentures and equity-settled compensation arrangements would be antidilutive and as such, these are not included in the calculation of diluted EPS.

The following table reconciles the numerator and denominator of the basic and diluted earnings per share computation.

	Three months ended March 31,	
	2019	**2018**
Numerator for Basic and Diluted Earnings per Share		
Earnings from continuing operations		
Net earnings for basic earnings per share	**2,958**	4,831
Less: earnings from discontinued operations, net of tax	**1,901**	1,265
Earnings from continuing operations for basic earnings per share	**1,057**	3,566
Add: after-tax interest on convertible debt	**1,524**	1,821
Earnings from continuing operations for diluted earnings per share	**2,581**	5,387
Net earnings		
Net earnings for basic earnings per share	**2,958**	4,831
Add: after-tax interest on convertible debt	**1,524**	1,821
Net earnings for diluted earnings per share	**4,482**	6,652
Denominator for Basic and Diluted Earnings per Share		
Actual weighted average number of shares	**88,583,070**	88,243,066
Vested equity-settled compensation	**242,007**	135,540
Weighted average number of shares for basic earnings per share	**88,825,077**	88,378,606
Shares issued if all convertible debt was converted	**10,326,531**	11,244,444
Dilutive effect of equity-settled compensation	**34,313**	65,200
Total for diluted earnings per share	**99,185,921**	99,688,250

	Three months ended March 31,	
	2019	2018
Basic and Diluted Earnings per Share *(in dollars)*		
Earnings from continuing operations	**0.01**	0.04
Earnings from discontinued operations	**0.02**	0.01
Net earnings	**0.03**	0.05

15. DISCONTINUED OPERATIONS

Earnings from discontinued operations for the three months ended March 31, 2019, included the release of a portion of the accrual for self-insured liabilities of $1.9 million (US$1.4 million). For the three months ended March 31, 2018, an adjustment of $1.3 million (US$1.0 million) related to the discount rate applied, reducing the accrual for self-insured liabilities.

16. COMMITMENTS AND CONTINGENCIES

Property and Equipment Commitments

The Company has outstanding commitments of $12.4 million at March 31, 2019, in connection with private-pay retirement communities under development in Ontario, which will be substantially financed with a combination of construction financing and cash on hand. These are expected to be incurred over the next year.

Legal Proceedings and Regulatory Actions

Extendicare and its consolidated subsidiaries are defendants in various actions and proceedings that are brought against them from time to time in connection with their operations.

As previously disclosed, in April 2018, the Company was served with a statement of claim alleging negligence by the Company in the operation of its long-term care centres and its provision of care to residents and seeking $150.0 million in damages. The claim sought an order certifying the claim as a class action pursuant to the *Class Proceedings Act* (Ontario). By order of the Ontario Superior Court of Justice, a request from the plaintiff for discontinuance of the class proceeding was approved on October 25, 2018. Following the discontinuance, the plaintiff who commenced the class proceeding still has the option to pursue a claim on her own behalf while others may also do so separately on their own behalf. The Company intends to defend itself against any and all such individual claims and does not believe the outcome on any or all such claims would have a material adverse impact on its business, results of operations or financial condition and in any event believes that any potential liability would be resolved within the limits of its insurance coverage.

On September 19, 2018, the Company was served with a statement of claim that seeks an order certifying the claim as a class action pursuant to the *Class Proceedings Act* (Ontario). The claim alleges that the Company failed to properly apply certain required medical equipment sterilization protocols at one or more of its home health care clinics and seeks $20.0 million in damages. The Company does not believe that the lawsuit or the damages sought have merit. The Company intends to vigorously defend itself against the claim and does not believe the outcome will have a material adverse impact on its business, results of operations or financial condition and in any event believes that any potential liability would be resolved within the limits of its insurance coverage.

The provision of health care services is subject to complex government regulations. Every effort is made by the Company to prevent deficiencies in the quality of patient care through quality assurance strategies and to remedy any such deficiencies cited by government inspections within any applicable prescribed time period. Extendicare accrues for costs that may result from investigations (or any possible related litigation) to the extent that an outflow of funds is probable and a reliable estimate of the amount of the associated costs can be made.

17. MANAGEMENT OF RISKS AND FINANCIAL INSTRUMENTS

(a) Management of Risks

LIQUIDITY RISK

Liquidity risk is the risk that the Company will encounter difficulty in meeting its contractual obligations. We manage our liquidity risk through the use of budgets and forecasts. Cash requirements are monitored regularly based on actual financial results and actual cash flows to ensure that there are sufficient resources to meet operational requirements. In addition, since there is a risk that current borrowings and long-term debt may not be refinanced or may not be refinanced on as favourable terms or with interest rates as favourable as those of the existing debt, we attempt to appropriately structure the timing of contractual long-term debt renewal obligations and exposures. In April 2018, the Company successfully refinanced the 2019 Debentures by issuing a new series of 2025 debentures.

In addition to cash generated from its operations and cash on hand, the Company has available undrawn credit facilities totalling $67.3 million (*note 7*).

CURRENCY RISK

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Cross-border transactions are subject to exchange rate fluctuations that may result in realized gains or losses as and when payments are made.

As a result of the U.S. Sale Transaction, our exposure to foreign currency risk has been significantly reduced. The following table outlines the net asset exposure to both the U.S. continuing operations and other items retained from the U.S. Sale Transaction as at March 31, 2019.

		March 31, 2019
	US$	**C$**
Assets		
Current assets	*15,867*	**21,183**
Investments held for self-insured liabilities	*43,979*	**58,705**
Liabilities		
Current liabilities	*5,013*	**6,691**
Indemnification provisions	*9,610*	**12,831**
Non-current liabilities	*15,504*	**20,696**
Net asset exposure	*29,719*	**39,670**

INTEREST RATE RISK

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

To mitigate interest rate risk, the Company's long-term care debt portfolio includes fixed-rate debt and variable-rate debt with interest rate swaps in place. At March 31, 2019, construction loans of $58.0 million are variable-rate debt, which do not have interest rate swaps in place. The Company's credit facility, and future borrowings, may be at variable rates which would expose the Company to the risk of interest rate volatility (*note 7*).

Although the majority of the Company's long-term debt is effectively at fixed rates, there can be no assurance that as debt matures, renewal rates will not significantly impact future income and cash flow. The Company does not account for any fixed-rate liabilities at FVTPL; consequently, changes in interest rates have no impact on our fixed-rate debt and therefore, would not impact net earnings.

Below is the interest rate profile of our interest-bearing financial instruments, which reflects the impact of the interest rate swaps (*notes 5*, *8 and 13*):

	Carrying Amount	
	March 31, 2019	**December 31, 2018**
Fixed-rate instruments:		
Long-term debt [(1)]	**482,778**	484,520
Total liability in fixed-rate instruments	**482,778**	484,520
Variable-rate instruments:		
Long-term debt [(1)]	**58,049**	52,866
	58,049	52,866

[(1)] Includes current portion and excludes netting of deferred financing costs.

Fair Value Sensitivity Analysis for Variable-rate Instruments

All long-term debt with variable rates are classified as other financial liabilities, which are measured at amortized cost using the effective interest method of amortization; therefore, changes in interest rates would not affect OCI or net earnings with respect to variable-rate debt. As at March 31, 2019, long-term debt with variable rates represented 10.7% of total debt. The value of the interest rate swaps is subject to fluctuations in interest rates, changes in fair value of these swaps are recognized in net earnings (*notes 5 and 13*).

Cash Flow Sensitivity Analysis for Variable-rate Instruments

An increase of 100 basis points in interest rates would have decreased net earnings by $0.1 million and a decrease of 100 basis points in interest rates would have increased net earnings by $0.1 million. This analysis assumes that all other variables, in particular foreign currency rates, remains constant, and excludes variable interest rate debt that is locked in through interest rate swaps.

(b) Fair values of Financial Instruments

As at March 31, 2019	**Amortized Cost**	**Fair Value through Profit and Loss**	**Total Carrying Amount**	**Fair Value**	**Fair Value Hierarchy**
Financial assets:					
Cash and short-term investments	**70,500**	**–**	**70,500**	**70,514**	
Restricted cash	**2,443**	**–**	**2,443**	**2,443**	
Invested assets [1]	**442**	**–**	**442**	**442**	
Accounts receivable	**44,603**	**–**	**44,603**	**44,603**	
Interest rate swaps	**–**	**1,500**	**1,500**	**1,500**	Level 2
Amounts receivable and other assets [2] [3]	**51,971**	**–**	**51,971**	**54,390**	Level 2
Investments held for self-insured liabilities	**3,173**	**55,532**	**58,705**	**58,705**	Level 1
	173,132	**57,032**	**230,164**	**232,597**	
Financial liabilities:					
Accounts payable	**4,656**	**–**	**4,656**	**4,656**	
Interest rate swaps	**–**	**827**	**827**	**827**	
Long-term debt excluding convertible debentures [3] [4]	**420,832**	**–**	**420,832**	**443,843**	Level 2
Convertible debentures	**119,995**	**–**	**119,995**	**128,271**	Level 1
	545,483	**827**	**546,310**	**577,597**	

As at December 31, 2018	**Amortized Cost**	**Fair Value through Profit and Loss**	**Total Carrying Amount**	**Fair Value**	**Fair Value Hierarchy**
Financial assets:					
Cash and short-term investments	65,893	–	65,893	65,907	
Restricted cash	2,290	–	2,290	2,290	
Invested assets [1]	442	–	442	442	
Accounts receivable	50,570	–	50,570	50,570	
Interest rate swaps	–	2,556	2,556	2,556	Level 2
Amounts receivable and other assets [2] [3]	53,341	–	53,341	55,142	Level 2
Investments held for self-insured liabilities	5,834	62,104	67,938	67,938	Level 1
	178,370	64,660	243,030	244,845	
Financial liabilities:					
Accounts payable	6,239	–	6,239	6,239	
Interest rate swaps	–	523	523	523	
Long-term debt excluding convertible debentures [3] [4]	417,611	–	417,611	443,277	Level 2
Convertible debentures	119,775	–	119,775	125,551	Level 1
	543,625	523	544,148	575,590	

(1) Included in other assets.
(2) Includes primarily amounts receivable from government.
(3) Includes current portion.
(4) Excludes netting of deferred financing costs.

BASIS FOR DETERMINING FAIR VALUES

The following summarizes the significant methods and assumptions used in estimating the fair values of financial instruments reflected in the previous table.

Fair values for investments designated as FVTPL are based on quoted market prices. Accounts receivable are recorded at amortized cost. The carrying values of accounts receivable approximate fair values due to their short-term maturities, with the exception of the amounts receivable due from government of Ontario, which are valued at discounted future cash flows using current applicable rates for similar instruments of comparable maturity and credit quality (*note 5*). The fair values of convertible debentures are based on the closing price of the publicly traded convertible debentures on each reporting date, and the fair values of mortgages and other debt are estimated based on discounted future cash flows using discount rates that reflect current market conditions for instruments with similar terms and risks.

FAIR VALUE HIERARCHY

We use a fair value hierarchy to categorize the type of valuation techniques from which fair values are derived: Level 1 – use of quoted market prices; Level 2 – internal models using observable market information as inputs; and Level 3 – internal models without observable market information as inputs.

The fair value hierarchy for the fair values of financial instruments where carrying value is not a reasonable approximation of fair value, are indicated above.

18. SEGMENTED INFORMATION

The Company reports the following segments: i) long-term care; ii) retirement living; iii) home health care; iv) management, consulting and group purchasing as "other Canadian operations"; and v) the Canadian corporate functions and any intersegment eliminations as "corporate Canada". The continuing U.S. operations consist of the Captive.

The long-term care segment represents the 58 long-term care centres that the Company owns and operates in Canada. The retirement living segment includes seven acquired retirement communities, and three communities that were constructed. The retirement communities provide accommodation and services to private-pay residents at rates set by Extendicare based on the services provided and market conditions. Through our wholly owned subsidiary ParaMed, ParaMed's home health care operations provide complex nursing care, occupational, physical and speech therapy, and assistance with daily activities to accommodate those living at home.

The Company's other Canadian operations are composed of its contract operations management, consulting and group purchasing operations. Through our Extendicare Assist division, we provide management and consulting services to third-party owners; and through our SGP Purchasing Partner Network division, we offer cost-effective purchasing contracts to other senior care providers for food, capital equipment, furnishings, cleaning and nursing supplies, and office products.

The Company continues to group its former and remaining U.S. operations as one segment. The Captive's expense incurred for self-insured liabilities related to the Company's U.S. general and professional liability risks up to the date of the U.S. Sale Transaction as well as the disposed U.S. businesses are presented as discontinued operations; while the Captive's costs to administer and manage the settlement of the remaining claims are reported as continuing operations within the U.S. segment.

	Three months ended March 31, 2019							
(in thousands of Canadian dollars)	**Long-term Care**	**Retirement Living**	**Home Health Care**	**Other Canadian Operations**	**Corporate Canada**	**Total Canada**	**Total U.S.**	**Total**
CONTINUING OPERATIONS								
Revenue	**156,221**	**9,508**	**102,665**	**5,875**	**–**	**274,269**	**–**	**274,269**
Operating expenses	**139,383**	**6,929**	**95,112**	**2,459**	**–**	**243,883**	**–**	**243,883**
Net operating income	**16,838**	**2,579**	**7,553**	**3,416**	**–**	**30,386**	**–**	**30,386**
Administrative costs					**10,612**	**10,612**	**222**	**10,834**
Earnings (loss) before depreciation, amortization, and other expense						**19,774**	**(222)**	**19,552**
Depreciation and amortization					**9,427**	**9,427**	**–**	**9,427**
Other expense					**1,429**	**1,429**	**–**	**1,429**
Earnings (loss) before net finance costs and income taxes						**8,918**	**(222)**	**8,696**
Net interest costs					**6,320**	**6,320**	**234**	**6,554**
Foreign exchange and fair value adjustments					**1,829**	**1,829**	**(1,500)**	**329**
Net finance costs (income)					**8,149**	**8,149**	**(1,266)**	**6,883**
Earnings before income taxes						**769**	**1,044**	**1,813**
Income tax expense (recovery)								
Current					**1,524**	**1,524**	**–**	**1,524**
Deferred					**(768)**	**(768)**	**–**	**(768)**
Total income tax expense					**756**	**756**	**–**	**756**
Earnings from continuing operations						**13**	**1,044**	**1,057**
DISCONTINUED OPERATIONS								
Earnings from discontinued operations, net of income taxes					**–**	**–**	**1,901**	**1,901**
Net earnings						**13**	**2,945**	**2,958**

							Three months ended March 31, 2018	
(in thousands of Canadian dollars)	Long-term Care	Retirement Living	Home Health Care	Other Canadian Operations	Corporate Canada	Total Canada	Total U.S.	Total
CONTINUING OPERATIONS								
Revenue	152,805	6,971	106,464	5,142	3	271,385	39	271,424
Operating expenses	136,844	5,339	97,835	2,084	–	242,102	–	242,102
Net operating income	15,961	1,632	8,629	3,058	3	29,283	39	29,322
Administrative costs					9,062	9,062	283	9,345
Earnings (loss) before depreciation, amortization, and other expense						20,221	(244)	19,977
Depreciation and amortization					7,837	7,837	–	7,837
Other expense					180	180	–	180
Earnings (loss) before net finance costs and income taxes						12,204	(244)	11,960
Net interest costs					6,375	6,375	335	6,710
Foreign exchange and fair value adjustments					(879)	(879)	749	(130)
Net finance costs					5,496	5,496	1,084	6,580
Earnings (loss) before income taxes						6,708	(1,328)	5,380
Income tax expense								
Current					583	583	–	583
Deferred					1,231	1,231	–	1,231
Total income tax expense					1,814	1,814	–	1,814
Earnings (loss) from continuing						4,894	(1,328)	3,566
DISCONTINUED OPERATIONS								
Earnings from discontinued operations, net of income taxes					–	–	1,265	1,265
Net earnings (loss)						4,894	(63)	4,831