

**EGI FINANCIAL HOLDINGS INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION**  
**AND RESULTS OF OPERATIONS**  
**For the period ending September 30, 2009**

*References to "EGI" or "Company", "we" or "our" in this Management's Discussion and Analysis refer to EGI Financial Holdings Inc. on a consolidated basis, both now and in its predecessor forms.*

The following discussion should be read in conjunction with EGI's unaudited interim consolidated financial statements for the third quarter of fiscal 2009 and 2008, with the notes to the interim unaudited consolidated financial statements for the third quarter of fiscal 2009, with management's discussion and analysis (MD&A) set out on pages 4 to 48 of the Company's 2008 Annual Report and with the notes to the audited consolidated financial statements for fiscal 2008 set out on pages 55 to 75 of the Company's 2008 Annual Report. The following commentary is current as of November 4, 2009. Additional information relating to EGI is available on SEDAR at [www.sedar.com](http://www.sedar.com). Certain totals, subtotals and percentages may not reconcile due to rounding.

EGI uses both Canadian generally accepted accounting principles (GAAP) and certain non-GAAP measures to assess performance. Securities regulators require that companies caution readers about non-GAAP measures that do not have a standardized meaning under GAAP and may not be comparable to similar measures used by other companies. EGI analyzes performance based on operating income and underwriting ratios such as combined, expense and loss ratios.

The following discussion contains forward-looking information that involves risk and uncertainties based on current expectations. This information includes, but is not limited to, statements about the operations, business, financial condition, priorities, targets, ongoing objectives, strategies and outlook of EGI for 2009 and subsequent periods.

This information is based upon certain material factors or assumptions that were applied in drawing a conclusion or making a projection as reflected in the forward-looking information. By its nature, this information is subject to inherent risks and uncertainties that may be general or specific. A variety of material factors, many of which are beyond EGI's control, affect the operations, performance and results of EGI and its business, and could cause actual results to differ materially from the expectations expressed in any of this forward-looking information.

EGI's actual results could differ materially from those anticipated in this forward-looking information as a result of various factors, including those discussed in this MD&A. Additional information about the general risks and uncertainties regarding EGI's business is provided in its disclosure materials, including its annual information form, filed with the securities regulatory authorities in Canada, available at [www.sedar.com](http://www.sedar.com). EGI does not undertake to update any forward-looking information.

## Overview

EGI operates in the property and casualty (P&C) insurance industry in Canada and, commencing in 2007, in the United States, primarily focusing on non-standard automobile insurance and other niche and specialty general insurance products. Founded in 1997 as an insurance and reinsurance broker and marketer, EGI has since developed its business to focus on underwriting opportunities not served by many of the larger, standard insurers. EGI operates through two Strategic Business Units (SBUs) in Canada, the Personal Lines division and the Niche Products division. The Personal Lines division was created in 2006 to transition the Automobile division into a multi-product, multi-line SBU. Currently, the Personal Lines division continues to focus on the underwriting of non-standard automobile insurance and motorcycle business but has expanded into other non-standard products and specialty lines of business. Through its Niche Products division, EGI designs and underwrites specialized producer-initiated insurance programs, such as higher premium property, primary and excess liability, legal expense and accident and health insurance for a variety of businesses and consumers and extended warranty coverage for homes and consumer products.

In addition to the two SBUs in Canada, EGI also formed the International division in 2008 to leverage its strategy to expand into the United States. Currently, this division is focused on personal lines business, predominantly non-standard automobile insurance. As an interim step to execute this strategy, EGI entered the U.S. non-standard auto insurance market under reinsurance agreements with three arms-length insurance companies. These companies provide property and casualty insurance to the non-standard private passenger automobile segment of the industry and operate in several states in the southeastern U.S. Being dissatisfied with the results of these arrangements, EGI terminated the reinsurance agreements. EGI now intends to pursue its U.S. expansion exclusively as an insurer in its own right, through its wholly-owned U.S. subsidiary, Echelon Insurance Company of America (EICA), through which the Company can exercise greater underwriting control.

By pursuing its focused niche strategy, EGI's objective is to produce an ROE superior to the Canadian P&C insurance industry average. A key factor for EGI's ROE to outperform the industry is for its loss ratio to be below the industry average.

## Overall Performance

The operating environment remained challenging for insurance companies during the third quarter of 2009, as loss ratios continued to outpace rate increases and demand was suppressed in the wake of the recent financial crisis. Net operating income declined by 66.7% during the quarter.

Our Canadian divisions both reported underwriting profits during the quarter with combined underwriting income of \$1.2 million, while the International division reported a loss of \$0.7 million. Much of the loss in the International division was related to start-up costs for our U.S. subsidiary, EICA, which is expected to commence operations in the State of Florida during the fourth quarter of 2009.

In our Personal Lines division volumes increased 18.1% during the quarter, the non-standard auto line being the main contributor with a 23.6% increase. Management believes that this could be an early indication of a hardening Ontario auto insurance market, preceded by rate tightening on the part of standard insurance companies. Historically, EGI has benefited from increased business flows

when the insurance industry faces challenging market conditions.

## Financial Overview

The summary of financial data set forth in the following tables has been prepared in accordance with Canadian GAAP and has been derived from the unaudited interim consolidated financial statements for the three and nine months ended September 30, 2009 and 2008.

### *Restatement of financial results for the nine and three months ended September 30, 2008*

As described in note 2 of the interim consolidated financial statements for the nine months ended September 30, 2009 and 2008, the Company changed its accounting policy as at January 1, 2009, for determining the incurred but not reported reserve (IBNR) on its motorcycle business. The change in policy has been accounted for retrospectively, and the comparative statements for the three months ended September 30, 2008, have been restated. The change in accounting policy has no impact on the financial results for the nine-month period ended September 30, 2008, or the year ended December 31, 2008. The 2007 quarterly results presented in the MD&A have not been restated as the adjustment is immaterial.

For the three months ended September 30, 2008, the effect of the change is a decrease in incurred claims of \$1.4 million and an increase in income tax expense of \$0.5 million, resulting in an increase in net income for the period of \$0.9 million.

(\$ THOUSANDS except per share amounts)	Quarter to September 30		9 months to September 30	
	2009	(Restated) 2008	2009	2008
Direct written and assumed premiums	44,455	46,062	124,558	130,783
Net earned premiums	35,881	36,150	112,940	117,708
Underwriting income	284	2,894	115	651
Interest expense	306	305	910	913
Investment income	3,403	3,186	11,294	12,491
Net income	2,261	3,958	6,862	8,302
Net income per share				
Basic	0.19	0.36	0.58	0.82
Diluted	0.18	0.33	0.54	0.76
Net operating income <sup>(1)</sup>	1,328	3,990	4,805	6,181
Net operating income per share – diluted	0.10	0.34	0.38	0.55
Return on equity (ROE) <sup>(2)</sup>			1.8%	11.0%

(1) Net operating income is defined as net income excluding after-tax realized losses or gains on sale of investments.

(2) Represents EGI's net income for the twelve months ended on the date indicated, divided by the average shareholders' equity over the same twelve-month period.

	Quarter to September 30		9 months to September 30	
	2009	(Restated) 2008	2009	2008
Loss ratio	63.6%	60.2%	66.1%	66.8%
Expense ratio	35.6%	31.7%	33.8%	32.6%
Combined ratio	99.2%	91.9%	99.9%	99.4%

(\$ THOUSANDS except per share amounts)	As at September 30, 2009	As at December 31, 2008
Investments (excluding premium finance receivables)	278,348	259,774
Premium finance receivables	26,971	20,615
Total assets	440,994	402,780
Total shareholders' equity	137,867	118,604
Book value per share <sup>(1)</sup>	11.62	10.16

(1) Shareholders' equity divided by the number of shares issued and outstanding.

#### *Quarter ended September 30, 2009*

Net income of \$2.3 million for the three months ended September 30, 2009, represents a decrease of \$1.7 million, or 42.5% compared to net income of \$4.0 million in the third quarter of 2008. Underwriting income of \$0.3 million was recorded in the third quarter of 2009 compared to \$2.9 million in 2008. In our Canadian operations, both divisions recorded underwriting profits in the third quarter, with the Personal Lines division earning underwriting income of \$0.8 million compared to income of \$2.6 million in the same period of 2008; and the Niche Products division earning underwriting income of \$0.4 million compared to income of \$1.0 million in 2008. Our International division incurred an underwriting loss of \$0.7 million in the three months ended September 30, 2009, compared to a loss of \$0.3 million for the same period last year. As described below, a significant portion of the International division loss is attributable to the start-up costs of EGI's new U.S. insurance company, which is expected to commence underwriting business prior to this year end. There was \$0.3 million of corporate and other expenses in the third quarter of 2009 and \$0.5 million in 2008, which have not been allocated by division.

On a total Company basis, the loss ratio for the quarter ended September 30, 2009, was 63.6% compared to 60.2% for the same period last year. Although not as significant as in Q3 2008, favourable prior year loss development continued in the third quarter of 2009 resulting in the release of \$0.1 million in prior year claims reserves, compared to \$1.9 million in the third quarter of 2008.

The decrease in underwriting income in the Personal Lines division compared to 2008 was primarily due to an increase in the loss ratio to 67.1% compared to 63.6% in the third quarter of 2008. The year-over-year change was mainly due to the decrease, noted above, in favourable development of prior year claims in 2009 compared to last year.

Similarly, the year-over-year decrease in the Niche Products division underwriting income was

primarily the result of an increase in the loss ratio to 48.7% compared to 40.6% for the same period in 2008. Although higher than the excellent result achieved in the third quarter of 2008, the loss ratio experienced in this division for the third quarter of 2009 is in line with management's expectations.

The \$0.7 million underwriting loss incurred in the International division was the result of adverse claims development, with limited earned premiums relating to the run-off of assumed reinsurance treaties with U.S. non-standard auto insurers, the largest of which was cancelled effective December 31, 2008. The remaining contract was cancelled effective March 31, 2009. As this discontinued business runs off, management expects that these contracts will have a significantly reduced impact on EGI's financial results. The International division's expense ratio reflects the start-up costs (primarily salaries) incurred to prepare for the launch of EGI's Florida-based subsidiary, Echelon Insurance Company of America (EICA).

Investment income increased to \$3.4 million in the third quarter of 2009 compared to \$3.2 million in the same period in 2008. The increase in investment income was due to the realization of gains on the sale of investments of \$1.4 million in the third quarter of 2009 compared to net losses of \$0.1 million in the same period last year. Partially offset by foreign exchange losses of \$1.0 million incurred in the third quarter of 2009, compared to foreign exchange gains of \$0.1 million in the same period in 2008. These losses were experienced due to the weakening of the U.S. dollar compared to the Canadian dollar in the period. The Company holds U.S. denominated currency to support claims liabilities payable in U.S. dollars, as well as holding U.S. denominated investments comprising the initial capitalization of \$10 million (U.S) provided to EICA in July 2009. No impairment provisions were recorded in the third quarter of 2009 or 2008.

The basic net income per share for the quarter was \$0.19, compared to income per share of \$0.36 for the same period in 2008. The fully diluted net income per share was \$0.18 in the third quarter of 2009, compared to \$0.33 in 2008.

Net operating income, defined as net income excluding after-tax realized losses or gains on the sale of investments was \$1.3 million or \$0.10 per share on a diluted basis. This compares to net operating income of \$4.0 million, or \$0.34 per share, for the same period in 2008.

#### *Nine months ended September 30, 2009*

For the nine-month period ended September 30, 2009, net income was \$6.9 million, a decrease of 16.9% compared to net income of \$8.3 million in the same period last year. An underwriting gain of \$0.1 million was earned in the first nine months of 2009, compared to underwriting income of \$0.6 million earned in 2008. The Personal Lines division recorded underwriting income of \$3.8 million compared to \$6.6 million in 2008. An underwriting gain of \$0.2 million was earned by the Niche Products division, which represented a significant improvement over the loss of \$3.4 million incurred in the first nine months of 2008. The improvement is primarily the result of the reduced exposure to the Emergency Travel Health (ETH) line of business compared to 2008.

The loss ratio for the Personal Lines division was 66.2%, slightly higher than the 63.9% for the same period in 2008. The Niche Products division experienced a loss ratio of 58.1% for the first nine months of 2009, compared to 68.7% in the same period last year. The International division continued to experience adverse loss experience from assumed reinsurance treaties, which are now in run-off. This resulted in a loss ratio for this division of 113.1% for the first nine months of 2009 compared to 83.7% in the same period in 2008.

For the nine months ended September 30, 2009, EGI recorded total positive development of \$2.3 million related to prior year claims reserves compared to \$5.3 million in 2008.

Investment income decreased to \$11.3 million compared to \$12.5 million in the same period in 2008. Net realized gains from the sale of investments were \$3.1 million in the first nine months of 2009, compared to \$3.2 million in the same period in 2008. The decrease in investment income was due primarily to foreign exchange losses incurred in 2009 of \$0.9 million compared to a foreign exchange gain of \$0.4 in the same period in 2008, due to the deteriorating U.S. dollar and the significant portion of total assets held in cash and short-term investments during the third quarter of 2009.

The basic net income per share for the first nine months of 2009 was \$0.58 compared to income per share of \$0.82 for the same period in 2008. The fully diluted income per share was \$0.54, compared to \$0.76 in the first nine months of 2008.

Net operating income, defined as net income excluding after-tax realized losses and gains, including impairments, on the sale of investments, was \$4.8 million or \$0.38 per share on a diluted basis. This compares to net operating income of \$6.2 million, or \$0.55 per share, for the same period in 2008.

Year-to-date shareholders' equity grew to \$137.9 million, an increase of \$19.3 million from December 31, 2008. The contributing elements consisted of net income of \$6.9 million in the period, the issuance of common shares of \$1.0 million and other comprehensive income of \$12.3 million resulting from an increase in the fair value of investments held. These increases were partially offset by the payment of dividends of \$0.9 million to common shareholders in the first quarter of 2009.

## Segmented Financial Information

### Three months ended September 30

(\$ THOUSANDS)	2009				(Restated) 2008			
	Canada			International	Canada			International
	Personal Lines	Niche Products	Total		Personal Lines	Niche Products	Total	
Net earned premiums	26,965	8,474	35,439	442	25,579	7,374	32,953	3,198
Underwriting income (loss)	805	429	1,234	(677)	2,653	1,045	3,698	(323)
Loss ratio	67.1%	48.7%	62.7%	133.8%	63.6%	40.6%	58.5%	78.2%
Expense ratio	29.9%	46.3%	33.8%	119.2%	26.0%	45.3%	30.3%	31.8%
Combined ratio	97.0%	95.0%	96.5%	253.0%	89.6%	85.9%	88.8%	110.0%

Note: The underwriting income per division noted above excludes corporate and other expenses of \$0.3 million and \$0.5 million for the third quarters of 2009 and 2008 respectively.

The segmented information, for the third quarter of 2009, shows that Personal Lines contributed an underwriting income of \$0.8 million and the Niche Products division recorded an underwriting gain of \$0.4 million, resulting in an underwriting income of \$1.2 million for the Canadian business segments combined.

The International division, with business currently consisting of assumed reinsurance from U.S. insurers, recorded an underwriting loss of \$0.7 million due to continued adverse development of claims activity related to reinsurance treaties that were cancelled earlier this year. The International division's high expense ratio reflects the start-up costs (primarily salaries) incurred to prepare for the launch of EICA, with no corresponding earned premiums at this time. The third quarter loss ratio in Personal Lines was 67.1%, compared to 63.6% for the same period in 2008. Favourable prior year loss development related to Personal Lines claims reserves continued in the third quarter of 2009, totaling \$0.2 million, compared to positive development of \$1.8 million in the same period in 2008.

The loss ratio for the Niche Products division was 48.7%, compared to 40.6% for the same period in 2008. As noted above, although this result was higher than last year, the loss ratio experienced in the third quarter of 2009 was in line with management's expectations for this division.

### Nine months ended September 30

(\$ THOUSANDS)	2009				2008			
	Canada		International		Canada		International	
	Personal Lines	Niche Products	Total		Personal Lines	Niche Products	Total	
Net earned premiums	77,221	30,719	107,940	5,000	73,165	35,774	108,939	8,769
Underwriting income (loss)	3,799	160	3,959	(2,862)	6,592	(3,368)	3,224	(1,405)
Loss ratio	66.2%	58.1%	63.9%	113.1%	63.9%	68.7%	65.5%	83.7%
Expense ratio	28.8%	41.3%	32.4%	44.1%	27.1%	40.8%	31.6%	32.4%
Combined ratio	95.0%	99.4%	96.3%	157.2%	91.0%	109.5%	97.1%	116.1%

Note: The underwriting income per division noted above excludes corporate and other expenses of \$1.0 million and \$1.2 million for the first nine months of 2009 and 2008 respectively.

The segmented information, for the first nine months of 2009, shows that Personal Lines contributed an underwriting income of \$3.8 million while the Niche Products division earned an underwriting gain of \$0.2 million, resulting in combined underwriting income of \$4.0 million for the Canadian business segments. The International division, currently consisting of assumed business from U.S. insurers, recorded an underwriting loss of \$2.9 million. As noted previously, these contracts were cancelled effective December 31, 2008, and March 31, 2009, and are currently in run off, as premiums from policies issued prior to cancellation are earned.

The loss ratio in Personal Lines was 66.2% for the nine-month period ended September 30, 2009, compared to 63.9% in 2008. Positive development of prior year claims in the first nine months of 2009 was \$3.9 million, a reduction of \$0.7 million, compared to positive development of \$4.6 million last year.

The Niche Products division loss ratio was 58.1% for the nine-month period compared to 68.7% for the same period in 2008. As noted earlier, the significant decrease was the result of limited exposure to the ETH line of business in the first nine months of 2009 compared to the same period in 2008. All other programs in the Niche Products division experienced a loss ratio of 54.8% in the nine-month period compared to a loss ratio of 43.3% in 2008. The increase resulted from higher than expected

losses incurred in the liability line of business during the second quarter of 2009.

The International division incurred a loss ratio of 113.1% in the first nine months of 2009 compared to 83.7% in 2008. As noted above, this result pertains to claims experience related to the run-off of cancelled assumed reinsurance contracts effective December 31, 2008, and March 31, 2009.

The expense ratio for Personal Lines increased to 28.8% compared to 27.1% for the same period in 2008. The Niche Products division expense ratio also increased slightly to 41.3% in 2009 compared to 40.8% for the first nine months of 2008. As noted earlier, the International division's expense ratio reflects the start-up costs (primarily salaries) incurred to prepare for the launch of EICA.

## **Critical Accounting Estimates and Assumptions**

For a description of EGI's accounting policies, refer to notes 2 and 3 in the 2008 audited financial statements as set out on pages 55 to 58 of the Company's 2008 Annual Report. A further description of EGI's critical accounting estimates and assumptions is also detailed on pages 19 to 21 of the 2008 Annual Report.

There have been no changes to the Company's accounting policies or assumptions made in critical accounting estimates in this quarter, except as described in Note 2 of the interim financial statements for the quarter ended September 30, 2009, included in this report.

## **Future Changes in Accounting Policies and Disclosure**

### *Transition to International Financial Reporting Standards (IFRS)*

The CICA has announced that Canadian generally accepted accounting principles (GAAP) for publicly accountable enterprise companies will be replaced with IFRS effective January 2011. EGI will begin reporting its financial statements in accordance with IFRS on January 1, 2011. EGI is planning its transition to IFRS. The Company has formed an IFRS implementation project plan, assigned responsibilities to appropriate committees consisting of senior management, and identified specific tasks and timeframes to be achieved such that the Company is successful in meeting the financial reporting objectives of the IFRS implementation requirements.

Currently management is undergoing a detailed evaluation of each component of the financial statements to evaluate the nature and extent of the financial impact of the transition to IFRS.

The impact on its consolidated financial position and results of operations has not yet been determined.

## **Controls and Procedures**

### *Disclosure Controls and Procedures*

Our disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by EGI is recorded, processed, summarized and reported in a timely manner. This includes controls and procedures that are designed to ensure that information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

As of September 30, 2009, an evaluation was carried out, under the supervision of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as defined under Multilateral Instrument 52-109. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of these disclosure controls and procedures was effective.

#### *Internal Controls over Financial Reporting*

As at the quarter ended September 30, 2009, the Chief Executive Officer and the Chief Financial Officer evaluated the design of the Company's internal controls over financial reporting. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of internal controls was effective as at September 30, 2009, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

There have been no changes in the Company's internal controls over financial reporting during the quarter ended September 30, 2009, that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

#### **Summary of Quarterly Results**

A summary of the Company's last eight quarters is as follows:

	2009			2008				2007
					(Restated)			
(\$ THOUSANDS EXCEPT PER SHARE DATA)	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Direct written and assumed premiums	44,455	48,487	31,616	39,948	46,062	49,784	34,936	43,098
Total revenues (excluding investment income)	35,881	35,486	41,573	39,547	36,150	35,999	45,559	34,161
Underwriting income (loss)	284	1,703	(1,872)	(489)	2,894	22	(2,265)	868
Income (loss) before income taxes	3,381	7,415	(297)	(3,272)	5,776	4,434	2,020	5,658
Net income (loss)	2,261	4,831	(230)	(2,322)	3,958	3,019	1,325	3,727
Earnings per adjusted share								
– Basic	\$0.19	\$0.41	\$(0.02)	\$(0.20)	\$0.36	\$0.31	\$0.14	\$0.39
– Diluted	\$0.18	\$0.38	\$(0.02)	\$(0.19)	\$0.33	\$0.28	\$0.13	\$0.35
Selected financial ratios (%)								
Loss ratio	63.6	61.8	71.9	68.7	60.2	66.3	72.5	65.1
Expense ratio	35.6	33.4	32.6	32.5	31.7	33.6	32.4	33.1
Combined	99.2	95.2	104.5	101.2	91.9	99.9	104.9	98.2

## Quarter Ended September 30, 2009, Compared to Quarter Ended September 30, 2008

The following financial information compares the third quarter 2009 results with the third quarter of 2008.

(\$ THOUSANDS)	3rd Quarter 2009	(Restated) 3rd Quarter 2008	Variance \$	Variance %
Direct written and assumed premiums	44,455	46,062	(1,607)	(3.5)
Net written and assumed premiums	40,753	43,062	(2,309)	(5.4)
Net earned premiums	35,881	36,150	(269)	(0.7)
Claims incurred	22,821	21,764	1,057	4.9
Acquisition costs	8,197	7,896	301	3.8
Operating expenses	4,578	3,596	982	27.3
Underwriting income	284	2,894	(2,610)	(90.2)
Investment income	3,403	3,186	217	6.8
Interest expense	306	305	1	-
Net income before income taxes	3,381	5,775	(2,394)	(41.5)
Income taxes	1,120	1,817	(697)	(38.4)
Net income	2,261	3,958	(1,697)	(42.9)

### *Written and Assumed Premiums*

Overall direct written and assumed premiums decreased 3.5%, to \$44.5 million for the three months ended September 30, 2009, compared to \$46.1 million for the third quarter of 2008, despite the significant growth in non-standard auto premiums. The increase in premium volume from the non-standard auto line of business was offset by the impact of the cancellation of U.S. assumed reinsurance contracts effective December 31, 2008, and March 31, 2009. Premiums continue to be earned pursuant to U.S. assumed reinsurance arrangements in 2009, from policies issued prior to cancellation; however, no further premiums will be written in 2009. As a result, assumed premiums in the International division declined by \$3.7 million compared to the third quarter of 2008.

Personal Lines premiums increased by \$4.8 million to \$31.4 million in 2009 compared to \$26.6 million in the third quarter of 2008. Despite ongoing competitive conditions in the market, non-standard auto premiums increased significantly to \$27.1 million, an increase of \$5.2 million or 23.7% compared to \$21.9 million in the same period of 2008. Motorcycle direct written premiums decreased slightly to \$3.5 million compared to \$3.6 million in 2008. This reflects a reduction in the number of policies written as the result of rate increases implemented to improve the underwriting performance of this product. Direct written premiums for the Niche Products division decreased to \$13.1 million for the three months ended September 30, 2009, compared to \$15.7 million in the same period in 2008 due to the reduction in ETH premiums. Excluding the ETH line of business, premiums written from core Niche programs increased 18.7% to \$12.7 million in the third quarter of 2009, compared to \$10.7 million in the same period last year.

Net written and assumed premiums decreased \$2.3 million, or 5.4%, to \$40.7 million compared to \$43.0 in the same period last year. This decrease is slightly higher than the decrease in direct written premium, due to a change in the mix of business in 2009.

### *Earned Premiums*

Net earned premiums for the three months ended September 30, 2009 totaled \$35.9 million, a decrease of \$0.3 million, or 0.7%, compared to \$36.2 million in 2008. The decrease is primarily attributable to the previously noted cancellation of U.S. assumed reinsurance contracts, which are in run-off in 2009. Minimal premiums will be earned from this business in 2010.

Net earned premiums from the Canadian divisions (Personal Lines and Niche Products) increased to \$35.4 million in the third quarter of 2009, or 7.5%, compared to \$32.9 earned in the same period in 2008.

### *Incurred Claims Expense*

Net incurred claims expense increased 4.9%, to \$22.8 million for the quarter ended September 30, 2009, compared to \$21.7 million for the same period in 2008. The total Company loss ratio was 63.6% in the third quarter of 2009 compared to 60.2% for the three months ended September 30, 2008, primarily due to the much higher than expected loss ratio on the U.S. assumed reinsurance business and a decrease in the positive development of prior year claims compared to the third quarter of 2008. The loss ratio in 2009 also reflects the generally higher claims costs, which have been experienced across the industry.

The loss ratio in Personal Lines was 67.1% for the quarter ended September 30, 2009, compared to 63.6% in 2008. The increase in the loss ratio compared to 2008 reflects the decrease in positive development of prior year claims compared to last year. Positive development of prior year claims in the third quarter of 2009 was \$0.2 million compared to \$1.4 million last year.

The non-standard auto loss ratio was 62.4% in the third quarter of 2009 compared to 56.3% in 2008. The loss ratio from the motorcycle line of business was 96.1% in the third quarter, which compares to a restated loss ratio of 101.1% in the same period in 2008.

For the quarter ended September 30, 2009, our external actuary changed his estimate for the current full-year loss ratio for motorcycles from 71% to 73%. The loss ratio for the quarter reflects the application of the higher loss ratio to the premiums earned in the first three quarters of 2009. The lower loss ratio, as compared to the third quarter of 2008, reflects a premium rate increase implemented in 2009.

As noted earlier, the Company changed the methodology of determining IBNR on motorcycle business in the first quarter of 2009. The new method is based on an annualized loss ratio and is intended to reduce the seasonal variation of results that were experienced with the previous methodology. Financial results for the third quarter of 2008 have been restated to reflect the new methodology.

The Niche Products division recorded a loss ratio of 48.7% in the third quarter of 2009 compared to 40.6% for the same period in 2008. Although higher than the prior year loss ratio, which benefitted from positive development of ETH claims in the period, the loss ratio for the third quarter of 2009 was in line with management's expectations for this division.

The International division incurred a loss ratio of 133.8% in the third quarter of 2009 compared to 78.2% in 2008. As noted above, this result pertains to claims experience related to the run-off of cancelled assumed reinsurance contracts effective December 31, 2008. The reinsured underwriter has advised that the adverse claims experience reported in 2009 partially pertains to changes in

claims personnel and adoption of a more conservative reserving philosophy in late 2008 and early 2009, which, if accurate, may result in a reduction of EGI's carried IBNR reserve over time.

#### *Acquisition Costs*

Net acquisition costs, which mainly consist of commissions and premium taxes, increased 3.8%, to \$8.2 million for the three months ended September 30, 2009, compared to \$7.9 million in the same period in 2008. The increase reflects the increase in net earned premiums from the Canadian divisions offset by the decline in earned premiums from the International division. As a percentage of net earned premiums, acquisition expenses increased to 22.8% in the third quarter of 2009 compared to 21.8% last year.

#### *Operating Expenses*

Operating expenses increased \$1.0 million, or 27.3%, to \$4.6 million for the third quarter compared to \$3.6 million in the same period of 2008. The increase is related to general increases in salaries, system amortization and occupancy costs. During the quarter a revaluation of intangible assets was also performed which resulted in the write-down of \$0.4 million in system development costs related to termination of a systems project.

#### *Underwriting Income*

Underwriting results reflect revenues from net earned premiums less incurred claims and acquisition and operating expenses. In the quarter ended September 30, 2009, total underwriting contribution decreased by \$2.6 million to an underwriting gain of \$0.3 million, compared to an underwriting gain of \$2.9 million for the comparable period in 2008. The underwriting results for 2009 and 2008 include \$0.3 million and \$0.5 million of corporate and other expenses, respectively, which have not been allocated to the operating divisions.

Underwriting income from the Personal Lines division for the three months ended September 30, 2009, was \$0.8 million, a decrease of \$1.9 million, compared to a gain of \$2.7 million for the same period in 2008. This decrease was primarily due to the increase in the loss ratio experienced in the Personal Lines division compared to the same period of 2008.

The underwriting gain from Niche Products was \$0.4 million, compared to an underwriting gain of \$1.0 million in the third quarter of 2008. This result is also primarily due to the increase in the loss ratio incurred by this division in the quarter compared to last year.

The International division experienced an underwriting loss of \$0.7 million in the third quarter of 2009, compared to a loss of \$0.3 million in the same period in 2008. This was due to adverse claims development of prior year claims related to cancelled, assumed reinsurance contracts from third party U.S. insurers, and to the ongoing costs (primarily salaries) incurred to prepare for the launch of EICA.

#### *Investment Income*

Investment income for the three months ended September 30, 2009, was \$3.4 million compared to \$3.2 million for the same period in 2008. Income from interest and dividends decreased slightly to \$3.0 million compared to \$3.1 million last year. As noted earlier, net realized gains on the sale of investments were \$1.4 million in the third quarter of 2009 compared to a net loss of \$0.1 million in the prior year. No investment impairments were recorded in the third quarters of 2009 or 2008. Also, as

noted earlier, the increase in net realized gains in the period compared to last year was offset by a foreign exchange loss of \$1.0 million in the third quarter of 2009 compared to a foreign exchange gain of \$1.0 million in the same period in 2008.

EGL's investment portfolio, including finance receivables, based on fair values, increased to \$305.3 million, or 8.1%, compared to total fair values of \$282.3 million as at September 30, 2008.

#### *Interest Expense*

During this quarter, interest expense related to bank indebtedness of \$0.3 million was incurred. The same amount of interest expense was incurred in the corresponding period of 2008.

#### *Net Income before Income Taxes*

Net income before income taxes for the three months ended September 30, 2009, was \$3.4 million, compared to income before income taxes of \$5.8 million in 2008.

For the three months ended September 30, 2009, the net income before income taxes of \$3.4 million reflects an underwriting gain of \$0.3 million plus investment income of \$3.4 million, less interest expense on bank indebtedness of \$0.3 million. This compares to an underwriting gain of \$2.9 million, plus investment income of \$3.2 million, reduced by interest expense of \$0.3 million, in the same period of 2008.

#### *Income Taxes*

Income tax expenses were \$1.1 million in the third quarter of 2009 compared to an income tax expense of \$1.8 million in 2008. The effective tax rate was 33% in 2009 compared to 31% the previous year. The increase in the effective tax rate is the result of EGL's conservative decision to only record a portion of the entire future tax benefit related to taxable losses incurred in the International division in 2009 and 2008. The balance of this benefit, being \$0.3 million, may be recorded in subsequent periods based on EGL's assessment of recoverability.

#### *Other Comprehensive Income*

Other comprehensive income was \$5.7 million in the third quarter of 2009 compared to an other comprehensive loss of \$7.6 million for the same period in 2008.

The income in 2009 was derived from a significant increase in the fair value of investments designated as "available for sale" of \$6.5 million, after income tax, offset by the reclassification of net realized gains to net income of \$0.9 million in the period, plus a small unrealized gain on the translation of financial statements of foreign operations of \$0.1 million.

The significant other comprehensive loss in the third quarter of 2008 resulted from the steep decline in equity markets during the third quarter of 2008.

## **Nine Months Ended September 30, 2009, Compared to Nine Months Ended September 30, 2008**

### *Written and Assumed Premiums*

Direct written premiums decreased \$6.2 million, or 4.7%, to \$124.6 million for the nine months ended September 30, 2009, compared to \$130.8 million in 2008. However, the combined Canadian divisions delivered premium growth for the first nine months of 2009. Direct written premiums from Personal Lines totaled \$90.2 million in the first nine months of 2009, which represents a 5.9% increase compared to \$85.2 million in 2008. Non-standard auto recorded growth of 9.5% to \$74.0 million, offset by a decline in the motorcycle line of 8.7% compared to the same period in 2008. The decline in the motorcycle line was due to premium rate increases implemented in the first half of 2009 and the prevailing economic conditions, resulting in a reduction in the number of policies written. The Niche Products division recorded written premiums of \$35.0 million in the first nine months of 2009 compared to \$35.7 million for the same period of 2008. The slight decline resulted from the planned decrease in ETH premium in 2009. Excluding the ETH line of business, premiums written from core Niche programs totaled \$33.6 million in 2009 compared to \$27.6 million in the first nine months of 2008, an increase of 21.7%.

In the International division, as noted earlier, assumed reinsurance contracts in place in 2008 have been cancelled resulting in negative premiums written of \$0.7 million, from the cancellation of policies written in 2008, in the first nine months of 2009 compared to \$9.8 million for the same period in 2008.

Net written and assumed premiums decreased \$7.5 million, or 6.2%, to \$113.9 million compared to \$121.4 million in the same period last year. This decrease is slightly higher than the decrease in direct written premiums, due to a change in the mix of business in 2009.

### *Earned Premiums*

Net earned premiums for the nine months ended September 30, 2009, totaled \$112.9 million, a decrease of \$4.8 million, or 4.1%, compared to \$117.7 million in the first nine months of 2008. As noted above, in the third quarter analysis, the decrease is primarily attributable to the previously noted cancellation of U.S. assumed reinsurance contracts.

Net earned premiums from the Canadian divisions decreased by 0.9% to \$107.9 million in the nine-month period ended September 30, 2009, compared to \$108.9 earned in the same period in 2008. This decrease occurred despite the growth in written premiums from the Canadian division due to the lag in earned premiums from the non-standard auto line and a decrease in premiums earned from the ETH line of business compared to 2008, which experienced significant premiums written from this line of business in 2007.

### *Incurred Claims Expense*

Net incurred claims expense decreased \$4.0 million, or 5.1%, to \$74.7 million for the first nine months of 2009, compared to \$78.7 million for the same period in 2008. This represents a greater decrease than the decline in net earned premiums, primarily due to the significant improvement in the loss ratio in the Emergency Travel Health line of business. The loss ratio incurred in the ETH line of business was 68.2% in the first nine months of the year compared to 95.6% for the previous year. The loss

ratio for the entire Niche Products division was 58.1% compared to 68.7% for the first nine months of 2008.

The Personal Lines loss ratio for the nine month period in 2009 was 66.2% compared to 63.9% in 2008. Generally rising claims in the industry impacted this result. Positive prior year loss development resulted in the release of \$3.9 million of reserves in the period compared to a release of \$4.6 million in the first nine months of 2008. Non-standard auto recorded a loss ratio of 65.7% in the first nine months of 2009 compared to 61.1% in the same period last year. The motorcycle line of business incurred a year-to-date 2009 loss ratio of 69.2% compared to 78.8% in 2008.

The International division recorded a loss ratio of 113.1% in the first nine months, compared to 83.7% in 2008, from business assumed pursuant to quota share treaties which have been cancelled. The higher than expected loss ratio is the result of continued adverse loss development on prior year claims on this business with limited earned premiums.

For all lines of business combined, positive loss development on prior years' claim reserves was \$2.2 million year-to-date compared to \$5.1 million in the same period of 2008.

#### *Acquisition Costs*

Net acquisition costs, which mainly consist of commissions and premium taxes, decreased \$1.8 million, or 6.5%, to \$26.2 million, compared to \$28.0 million in the same period in 2008. This relatively large decrease is due to lower earned premiums and a change to the mix of business.

#### *Operating Expenses*

Operating expenses increased \$1.6 million, or 15.5%, to \$11.9 million, compared to \$10.3 million for the first three quarters of 2008. The increase is primarily the result of increases in salaries, IT amortization and occupancy costs associated with the new office location in Canada, and start-up costs associated with the U.S. operation and EICA launch.

#### *Underwriting Income (Loss)*

Underwriting results reflect revenues from net earned premiums less claims, acquisition and operating expenses. In the first nine months of 2009 total underwriting contribution decreased \$0.5 million to an underwriting gain of \$0.1 million, compared to an underwriting gain of \$0.6 million for the comparable period in 2008. The underwriting results for 2009 and 2008 include \$0.9 million and \$1.2 million of corporate and other expenses, respectively, which have not been allocated to the operating divisions.

Underwriting income from the Personal Lines division was \$3.8 million, a decrease of \$2.8 million, compared to income of \$6.6 million for the same period of 2008. This result was caused by the higher loss ratio in Personal Lines in the first nine months of 2009 compared to 2008.

The underwriting gain in Niche Products for the first nine months of 2009 was \$0.2 million, a significant improvement of \$3.6 million compared to an underwriting loss of \$3.4 million in 2008. As noted earlier, this improvement was primarily the result of the positive turnaround in the ETH line of business.

The International division experienced an underwriting loss of \$2.9 million in 2009 compared to an underwriting loss of \$1.4 million in the same period in 2008. Included in the loss for this division are \$0.7 million of operating costs attributable to the start up of EICA.

## Investment Income

Investment income for the nine-month period was \$11.3 million compared to \$12.5 million in 2008. Income from interest and dividends increased to \$9.9 million compared to \$9.8 million in the same period last year, due to the growth in the investment portfolio. Net realized gains on the sale of investments decreased slightly to \$3.1 million compared to realized gains of \$3.2 million in the first nine months of 2008. Foreign exchange losses of \$0.9 million were incurred in 2009 compared to foreign exchange gains of \$0.4 million in 2008, resulting from the decline in the U.S. dollar in 2009.

EGL's investment portfolio, including finance receivables, based on fair values, increased to \$305.3 million, or 8.1%, compared to total fair values of \$282.3 million as at September 30, 2008.

## *Interest Expense*

During the first nine months of 2009 and 2008, interest expense of \$0.9 million was incurred on bank indebtedness of \$19.55 million.

## *Net Income before Income Taxes*

Income before income taxes for the nine months ended September 30, 2009, was \$10.5 million, a decrease of \$1.7 million compared to income of \$12.2 million for the same period in 2008.

For the nine months ended September 30, 2009, an underwriting gain of \$0.1 million plus investment income of \$11.3 million, reduced by interest expense on bank indebtedness of \$0.9 million, comprised net income before income taxes of \$10.5 million. This compares to an underwriting gain of \$0.6 million, plus investment income of \$12.5 million, reduced by interest expense of \$0.9 million, in the same period of 2008.

## *Income Taxes*

The provision for income taxes was \$3.6 million compared to \$3.9 million for the same period in 2008. The effective tax rate was 34% for the first nine months of 2009 compared to 32% in 2008. The increase in the effective tax rate is the result of EGL's conservative decision to only record a portion of the entire future tax benefit related to taxable losses incurred in the International division in 2009 and 2008. The balance of this benefit may be recorded in subsequent periods based on EGL's assessment of recoverability.

## *Other Comprehensive Income*

Other comprehensive income was \$12.3 million in the first nine months of 2009 compared to an other comprehensive loss of \$10.4 million for the same period in 2008.

The income in 2009 was derived from a significant increase in the fair value of investments designated as "available for sale" of \$14.0 million, after income tax, offset by the reclassification of net realized gains to net income of \$1.8 million in the period, plus a small unrealized gain on the translation of financial statements of foreign operations of \$0.1 million.

The significant other comprehensive loss in the same period in 2008 resulted from the steep decline in equity markets during the third quarter of 2008.

## BALANCE SHEET ANALYSIS

The Balance Sheet analysis that follows should be read in conjunction with the unaudited interim consolidated third quarter 2009 financial statements and notes therein, which include additional disclosures related to balance sheet risk management.

### Investments

The following table sets forth EGI's invested assets as at September 30, 2009, and December 31, 2008.

	September 30, 2009	December 31, 2008
(\$ THOUSANDS)	Fair value	Fair value
Bonds		
Canadian		
Federal	75,255	82,078
Provincial	43,285	45,162
Municipal	6,322	6,935
Corporate	85,064	86,570
	209,926	220,745
United States		
Corporate	7,982	2,717
Total Bonds	217,908	223,462
Preferred shares	6,738	4,042
Common shares		
Canadian	50,014	29,049
United States	1,039	1,178
	51,053	30,227
Investment income due and accrued	2,649	2,043
	278,348	259,774

Due to the improvement in the third quarter of 2009, particularly in equity markets, Accumulated Other Comprehensive Income (AOCI) was \$6.8 million as at September 30, 2009, compared to a loss of \$5.5 million as at December 31, 2008. This balance represents the total net unrealized gains or losses in the Company's investment portfolio (the difference between adjusted cost and fair value), net of income taxes.

The Board of Directors has established a policy to write down or make a provision for any investment with "other than temporary" impairment.

Management has reviewed currently available information regarding those investments whose estimated fair values are less than carrying values. For those securities whose decline in fair value was other than temporary, the Company has recorded the difference between the cost of the investment and its fair value as an impairment charge which reduces investment income in the year recorded.

The Company considers an impairment to be other than temporary if it is unlikely the Company will recover an investment's amortized cost in a reasonable period of time. Factors considered by the Company include but are not limited to the impact of issuer-specific events, industry-specific events, current and expected future market and economic conditions, the nature of the investment and the severity and duration of the fair value deficiency.

An impairment loss of \$2.0 million, related to common shares, was recognized in net income in the first quarter of 2009. The investments in question were disposed of in the second quarter of 2009. No provisions for impairment were recorded in the second or third quarter of 2009.

### **Recoverable from Reinsurers**

As at September 30, 2009, the recoverable from reinsurers decreased to \$44.4 million compared to \$45.6 million as at December 31, 2008. This decrease represents recoveries of amounts for claims which were reinsured pursuant to quota share arrangements related to policy years 2002 through 2005.

### **Accounts Receivable**

Premium financing receivables were the largest component of this asset as at September 30, 2009, and represented approximately 80% of the \$33.6 million of total receivables. During the first nine months of 2009 premium financing receivables increased to \$27.0 million from \$20.6 million at December 31, 2008. These premiums are primarily billed directly to policyholders who are provided with a monthly payment financing option.

### **Provision for Unpaid Claims**

EGL establishes loss reserves to provide for future amounts required to pay claims related to insured events, that have occurred and been reported but have not yet been settled, and related to events that have occurred but have not yet been reported to EGL. Claims provisions (i.e., reserves for claims liability) are established at the individual file level by the "case method" as claims are reported. Provision for unpaid claims consists of the aggregate amount of individual case reserves established and management's estimate of claims incurred but not reported based on the volume of business currently in force and historical claims experience. In order to ensure as far as possible that EGL's provision for unpaid claims (often called "reserves") is adequate, management has retained the services of an independent actuary. EGL strives to establish adequate provisions at each quarter end.

The table below shows the development of the provision for claims reserves for Echelon General Insurance Company (EGI's primary insurance subsidiary), including loss adjustment expenses as at December 31 in each of the five years and for the nine months ended September 30, 2009.

(\$ THOUSANDS)	Years ended December 31				
	2008	2007	2006	2005	2004
Reserve Carried (actuarial present value basis) <sup>(1)</sup>	178,694	168,257	145,691	129,041	107,196
Reserve at December 31, 2005					70,620
Cumulative paid to December 31, 2005					24,922
Cumulative Redundancy (Deficiency)					11,654
Reserve at December 31, 2006				88,029	49,557
Cumulative paid to December 31, 2006				25,817	41,158
Cumulative Redundancy (Deficiency)				15,195	16,481
Reserve at December 31, 2007			107,992	67,408	36,129
Cumulative paid to December 31, 2007			30,432	46,413	55,306
Cumulative Redundancy (Deficiency)			7,267	15,220	15,761
Reserve at December 31, 2008		117,541	81,172	50,013	25,237
Cumulative paid to December 31, 2008		44,265	53,325	62,210	66,181
Cumulative Redundancy (Deficiency)		6,450	11,194	16,818	15,778
Reserve at September 30, 2009	140,475	95,714	66,079	36,581	19,236
Cumulative paid to September 30, 2009	37,359	64,854	68,265	74,005	72,115
Cumulative Redundancy	860	7,689	11,347	18,455	15,845

1) Amounts include Provision for Adverse Deviation (PfAD) of \$19,689 for 2008; \$17,401 for 2007; \$14,756 for 2006; \$12,473 for 2005; and \$8,613 for 2004.

The table above, which is reflected on a gross basis for all years, shows that for the first nine months of 2009 the total prior year reserve redundancies released pursuant to the September 30, 2009 (Echelon General) actuarial report were \$0.8 million.

The uncertainties regarding EGI's reserves could result in a liability exceeding the reserves by an amount that would be material to EGI's financial condition or results of operations in a future period. Future development could be significantly different from the past, due to many unknown factors.

## Reinsurance

EGI has reinsurance treaties with several unaffiliated reinsurers, all of whom are selected on the basis of their creditworthiness. EGI purchases reinsurance to reduce its exposure to the insurance risks that it assumes in writing business. For 2009 the maximum net retention on a single risk is \$1.5 million (2008 – \$1.5 million).

In accordance with industry practice, EGI's reinsurance recoverables with licensed Canadian reinsurers are generally unsecured, because Canadian regulations require these reinsurers to maintain minimum asset and capital balances in Canada to meet their Canadian obligations. Policy liabilities rank in priority to any subordinated creditors a reinsurer may have. For reinsurance recoverables with non-licensed reinsurers, EGI maintains security against reinsurance recoverables in the form of cash, letters of credit and/or assets held in trust accounts. At March 31, 2009, EGI was

the assigned beneficiary of such trust accounts totaling \$2.3 million (December 31, 2008 – \$2.4 million) in guarantees from unlicensed reinsurers.

EGL purchases renewable excess of loss and catastrophe reinsurance from third party reinsurers, covering its automobile and general liability business. In 2009, excess of loss coverage on a single occurrence is for a total of \$23.5 million and in 2008 it was for \$18.5 million. Total catastrophic coverage is \$23.0 million in 2009 and \$18.0 in 2008. Other than general and professional liability, coverages comprising the programs of the Niche Products division are reinsured on a program-by-program basis.

Using reinsurance, EGL's policy is to limit its loss exposure on any one claim to not more than 2% of its shareholders' equity.

## **Share Capital**

As of November 3, 2009, there were 11,864,582 common shares issued and outstanding. (See Note 7 to the unaudited interim consolidated third quarter 2009 financial statements.)

## **Liquidity and Capital Resources**

The purpose of liquidity management is to ensure there is sufficient cash to meet all of EGL's financial commitments and obligations as they come due. EGL believes that it has the flexibility to obtain, from internal sources, the funds needed to fulfill its cash requirements during the following financial year and to satisfy regulatory capital requirements. EGL's principal sources of funds are premiums collected, investment income and proceeds from investments that have been sold or have matured. However, such funds may not provide sufficient capital to enable EGL to pursue additional market opportunities.

In October 2007, EGL entered into a non-revolving term credit facility with a major Canadian bank in the amount of US\$20 million, converted to CDN\$19.55 million, the equivalent Canadian dollar amount as of the closing date. The facility bears interest of 6.2% which is payable monthly over the three-year term of the agreement. After three years EGL is obligated to repay the amounts drawn as at the termination of the agreement. Pursuant to the credit facility agreement EGL is required to comply with various financial covenants and financial information reporting requirements.

During the three year term, EGL has agreed to financial covenants which require EGL to maintain a minimum tangible net worth of \$80.0 million and a maximum debt to capital ratio of 0.30:1.00.

The initial drawdown of \$19.55 million was used to increase the capital of CIM Re, EGL's Barbados based reinsurance company, which is currently used to reinsure selected niche and specialty line business.

EGL's contractual obligations relating to operating leases are \$1.0 million due in less than a year and \$4.1 million due in the next five years.

## **Capital Resources**

Year-to-date shareholders' equity increased to \$137.9 million, an increase of \$19.3 million from December 31, 2008. The contributing elements consisted of net income of \$6.9 million in the period, the issuance of common shares of \$1.0 million and other comprehensive income of \$12.3 million which resulted from an increase in the fair value of investments held. The increases were partially offset by the payment of dividends of \$0.9 million to common shareholders in the first quarter of 2009.

As at September 30, 2009, Echelon's Minimum Capital Test margin was 314%, compared to 268% as at December 31, 2008, significantly exceeding the minimum regulatory capital level required by the Office of the Superintendent of Financial Institutions.

## **Outlook**

Though conditions for the insurance industry remain challenging in Ontario, we believe that recent rate increases will begin to have a positive impact on our results in the coming quarters. Hardening market conditions have historically driven increased business flows to EGI when standard insurers are forced to increase their rates in order to combat rising loss ratios stemming from earlier price cuts aimed at capturing market share.

Our conservative investment strategy has ensured that we remain on solid financial footing and in a stronger position than many of our competitors. We continue to monitor insurance company valuations in the U.S. and believe that attractive acquisition opportunities could emerge in 2010 as we work to advance our growth strategy.

We continue to work towards launching our wholly-owned U.S. subsidiary, EICA and expect to begin writing premiums in the State of Florida sometime during the fourth quarter of 2009. From there we intend to service the large south-eastern U.S. non-standard insurance market. Our entry into the \$36 billion U.S. market will be gradual and cautious and implemented using the same business model that has contributed to our success in Canada. We will maintain direct control over all underwriting and claims management processes in order to ensure that our standards and discipline are maintained at all times.

We believe that we are well positioned to capitalize on the opportunities that emerge in the quarters and years ahead. We have a committed management team, a focused growth strategy and the financial resources necessary to continue to profitably grow the Company.