Management's Discussion and Analysis

CONSOLIDATED FINANCIAL STATEMENTS

The following discussion and analysis should be read in conjunction with the audited consolidated financial statements and accompanying notes of Elexicon Corporation ("Elexicon" or the "Corporation") for the year ended December 31, 2020. The consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") and in effect at December 31, 2020.

BUSINESS OF ELEXICON

Elexicon Corporation is 100% municipally owned by five municipal shareholders: the Town of Whitby (32.0%), the City of Pickering (27.88%), the Town of Ajax (21.828%), the Municipality of Clarington (9.248%) and the City of Belleville (9.044%). Elexicon Corporation provides, through two wholly owned subsidiaries, energy-related services in east-central Ontario. Elexicon Energy Inc., its regulated electricity distribution company serves approximately 171,000 customers in 10 municipalities – 8 of which are in Durham Region. Durham Region is one of the fastest growing regions in Ontario. Its residential customer growth is expected to grow on average by 2.55% annually over the next five years. The City of Belleville and Town of Gravenhurst are also expected to see significant growth over the next five years. Elexicon Group Inc., its unregulated energy service subsidiary provides management and innovative energy solutions to help businesses better manage their energy cost and infrastructure needs. The company is actively expanding its product offerings and client base as it enters into new markets as we witness transformational change in the energy sector.

2020 A YEAR IN REVIEW

Significant Developments – COVID-19 Pandemic

The World Health Organization declared the outbreak of a strain of novel coronavirus disease, COVID-19, a global pandemic on March 11, 2020. The impact of the COVID-19 pandemic on the economy has continued to evolve with disruptive effects throughout Canada and in the province of Ontario and the regions in which Elexicon Energy operates. In an attempt to contain the spread of COVID-19, measures including business closures, social distancing protocols, travel and gathering restrictions, school closures, and lockdowns have been imposed and continue to be in effect.

Although staged and full reopening plans vary and are fluid across Ontario and its regions, these measures are continuing to have extensive implications for the economy and continue to contribute to the uncertainty about the timing and extent of an economic and social recovery. The development and distribution of an effective vaccine also continues to raise uncertainty as the addition of new variants of the virus continue to surface. As a result, the COVID-19 pandemic has continued to affect our employees, our customers and the communities we service, with resultant impacts on our operations, financial results and present and future risks to our organization.

During the COVID-19 pandemic, governments and regulatory bodies have provided unprecedented relief programs and temporary measures to facilitate the continued operation of the global economy and financial system, all of which are intended to provide support to individuals and businesses. For further details on these measures and their impact on us, refer to the Relief Program sections outlined below as well as the Regulatory Environment, Shareholders' Equity and Returns for Shareholders, and Liquidity and Financing sections of this Report.

Given the uncertainty of the extent and duration of the COVID-19 pandemic and its impacts on the economy and society, as well as the timeline of the transition to a fully reopened economy, the future impact on our businesses and our financial results and condition remains uncertain.

Commencing in the first quarter of 2020, in line with Provincial Government edicts, we instituted various measures and programs to protect and support our employees, customers and communities, while also striving to ensure continued safety and reliability of our local electrical distribution systems. We have and will continue to review the effectiveness of these measures and programs and adapt them accordingly.

Impact of pandemic risk factor

We are closely monitoring the potential continued effects and impacts of the COVID-19 pandemic, however much will depend on future developments that are highly uncertain and cannot be predicted, including the scope, severity, duration and additional subsequent waves of the COVID-19 pandemic, as well as the effectiveness of actions and measures taken by government and regulatory authorities.

The COVID-19 pandemic has and may continue to result in disruptions to our customers and the way in which we conduct our business, including prolonged duration of staff working from home, and changes to our operations due to higher volumes of customer requests. To date, we have taken proactive measures through our business continuity plans and our pandemic response plans to adapt to the ongoing work from home arrangements, carefully planning the return to premise for some of our employees, if appropriate, ensuring the continuation of critical projects while also preserving the well-being of our employees and our ability to serve customers. We are also communicating with partners, suppliers and selective customers to continuously assess impacts to our current work in progress, and making adjustments as necessary.

Relief programs

In response to the COVID-19 pandemic, several government programs have been and continue to be developed to provide financial aid to individuals and businesses, which include interest free loans, rate relief programs and energy assistance programs for individuals and small businesses.

Elexicon Energy has also instituted an outreach campaign to assist customers who are facing hardship as a result of the pandemic including the offer of extended bill payment options.

FEDERAL AND PROVINCIAL GOVERNMENT

Commencing in the first quarter of 2020, the Federal and Provincial Government announced new programs and revisions to existing programs to help support individuals and businesses, in light of the impact of the COVID-19 pandemic.

- Canada Emergency Business Account ("CEBA") – The Government of Canada created the CEBA to provide qualified businesses with interest free loans (subject to some terms and conditions) of up to $60,000 to help defray operating costs during a period where revenues have been temporarily reduced.
- To support Ontarians staying home during the rapidly evolving COVID-19 pandemic, the Government of Ontario implemented an emergency rate relief program for households, farms, and small businesses who pay time of use (TOU) electricity rates to off-peak rates 24 hours a day, seven days a week. The program ended on May 31, 2020 and was replaced with the COVID-19 Recovery Rate that saw households, farms, and small businesses pay 12.8 cents per kWh. The program ran from June 1, 2020 – October 31, 2020. It was subsequently replaced with a new program, which held the price of electricity at 8.5 ¢/kWh for electricity used from January 1, 2021 until February 22, 2021. The fixed price was equal to the off-peak price set by the Ontario Energy Board for January 1, 2021.
- Summer and Winter Disconnection Ban - To help support Ontarians a temporary moratorium on disconnections for residential and small general service customers was implemented by the Ontario Energy Board. The summer moratorium, which ended on July 31, 2021, was then extended into the winter from November 15, 2020 – April 30, 2021.
- Ontario Small Business Support Grant, which provides a minimum of $10,000 to a maximum of $20,000, to eligible small businesses who have had to restrict their operations due to the province-wide shut down. All small businesses that are eligible for the grant are also eligible for the property tax and energy bill rebates.
- COVID-19 Energy Assistance Program (CEAP) and COVID-19 Energy Assistance Program for Small Business (CEAP-SB), which provide one time, on-bill credits to eligible customers to help them catch up on their energy bills and resume regular payments. As at January 20, 2021, we have facilitated the administration of CEAP to more than 614 residential customers and 54 small business customers who have enrolled in these programs.

Corporate Overview

On April 1, 2019, the former Veridian Corporation ("Veridian") amalgamated with the former Whitby Hydro Energy Corporation ("Whitby Hydro") to form Elexicon Corporation.

To date, the merger has created some increased efficiency in the electricity distribution sector through the creation of economies of scale and/or contiguity. It is expected that benefits to customers through lower costs and equal or better service levels and increased shareholder value will also result. Under the current regulatory regime, shareholders of Elexicon will retain the benefit of operating synergies following the merger for up to ten years. Thereafter, the cost savings will be passed on to customers in the form of lower distribution rates. The total forecasted net operating, maintenance and administration ("OM&A") savings from the merger over the ten-year rebasing deferral period approximates $42.1 million. OM&A cost savings have already occurred and will continue to be realized largely from labour cost reductions through staff attrition. The expectation is for reduced controllable costs per customer as economies of scale within the larger, merged entity and labor and non-labor synergies are realized. The longer-term exercise is to focus on identifying new opportunities for potential synergy savings in all aspects of the operations over the next several years.

Elexicon Corporation's ("EC") core business is distribution of electricity and is provided through EC's wholly owned regulated subsidiary, Elexicon Energy Inc. ("EE"). Additionally, separate and apart from the regulated business, a small business focused on renewable energy generation is also operated through EE. EE holds a distribution licence issued by the Ontario Energy Board ("OEB" or "the Board") that provides the local distribution company ("LDC") the exclusive right to distribute electricity to all customers within its prescribed service territories. EE distributes electricity to residential and business customers throughout a non-contiguous service area in southern Ontario.

EE’s geographic service area is over 750.9 square kilometres with an asset base of $621 million. The company delivered approximately 3,478 gigawatt hours of electricity to customers for the year ended December 31, 2020.

EE earns its revenues through charges to its customers for delivery of electricity through its electricity distribution network. EE has two distinct rate zones for the former Veridian and Whitby Hydro service areas.

In its Incentive Rate Mechanism rate application filed during 2020, EE requested and received approval to harmonize the rate year for its two rate zones to January 1. Distribution charges have two components; a fixed monthly service charge and a volumetric charge based on electricity consumption or demand. Residential customers, however, are billed only fixed monthly distribution charges. EE’s rates are regulated and approved by the OEB.

EC also operates a non-regulated energy service business through its wholly owned subsidiary, Elexicon Group Inc. (“EG”). EG’s ambition is to deliver strong growth in revenue and returns for shareholders by providing services to clients that are designed to reduce energy operating costs, carbon footprint and improve energy efficiencies. The growth focus will be on both i) organic growth and ii) expanding the business through merger and acquisition opportunities, with the goal of diversifying EG’s portfolio and expanding its product offerings, all from within its entrepreneurial culture.

In 2020, the government announced an additional $150 million in funding for its zero-emission vehicle infrastructure program, providing incentives for Electric Vehicle charges to workplaces, light duty fleet and multi-unit residential buildings. EG is poised to capitalize on this opportunity and EG sees an opportunity in the area of providing power solutions where existing grid restraints are preventing large scale charging and on providing cheaper EV energy solutions.

Regulatory Environment

ELECTRICITY REGULATION

In Ontario, the OEB has powers and oversight responsibilities for regulation of the energy industry, including all electricity distributors such as EE. These include approving or fixing distribution rates, setting service standards, ensuring that distribution companies fulfill obligations to connect and service customers and prescribing conditions of license requirements.

These conditions can include specific programs and investments such as record keeping and filing requirements, establishing the new-tiered customer class, connecting and enabling renewable generation facilities and specific requirements for rate setting.

IMPACT OF COVID-19 PANDEMIC

In 2020, the OEB and the Government of Ontario directed LDCs to implement several COVID-19 emergency measures. These included a flat rate for electricity over numerous periods; programs to help offset costs for residential and small business customers; a moratorium on disconnections, and various other customer-benefiting programs. The OEB has also issued accounting guidelines for LDCs to keep track of the costs associated with these programs.

On March 25, 2020, the OEB issued an accounting order that established a deferral account for utilities to track any incremental costs and lost revenues associated with the COVID-19 pandemic. In the accounting order, the OEB also stated that it will assess any claimed costs and/or lost revenues associated with the deferral account when they are requested for disposition.

On May 14, 2020 the OEB initiated a consultation process regarding the use and recoverability and disposition of deferral accounts by utilities. The ongoing consultation process considers the development of new accounting guidance and filing requirements for these deferral accounts with regard to bill impacts on customers. As this consultation is still underway, recovery is uncertain at this time, and the OEB anticipates that formal guidelines will not be available until the spring of 2021.

RATE SETTING

EE's distribution rates and other regulated charges are determined to allow shareholders the opportunity to earn a regulated Return on Equity on deemed shareholder equity as determined by regulation. Periodically EE makes applications to the OEB for rate setting under various mechanisms. Currently, EE annually processes applications for both its rates zones.

RATE APPLICATIONS

In April 2020, the OEB approved a Price Cap Incentive Rate setting application for the Veridian rate zone for changes to distribution rates effective May 1, 2020. Due to the uncertainty regarding the severity and duration of the COVID-19 emergency, EE elected to postpone the implementation of its new rates to January 1, 2021, to minimize the impact to customers, and provide it with the opportunity to align its rate years.

In December 2020, the OEB approved Annual Incentive Rate-setting Index applications for Whitby and Veridian rate zones for changes to distribution rates effective January 1, 2021. On a total bill basis, the distribution rates for the Whitby rate zone result in a net 1.33% reduction for the average residential customer and a net 1.20% reduction for the average small commercial customer. For the Whitby rate zone, regulatory balances that accumulated prior to 2021, were approved to be refunded to customers in 2021. In the Veridian rate zone the bill impact is a 0.25% increase for the average residential customer and a net 0.32% increase for the average small commercial customer.

CONSERVATION AND DEMAND MANAGEMENT ("CDM")

On March 21, 2019, the Ontario government issued a directive to the IESO giving the IESO responsibility for delivering the CDM programs instead of local distribution companies. As part of implementing its new mandate, the IESO terminated the Energy Conservation Agreement (ECA) effective June 20, 2019. EE was required to cease marketing and business development for all CDM programs immediately and wind down the delivery of programs.

CDM participation agreements with customers for many of the CDM programs in effect before April 1, 2019 remain in effect and EE will remain responsible for its obligations under such agreements. Participants have until June 30, 2021 to complete the projects. Amounts received from the IESO for the funding of projects under the participant agreements but not spent, are presented on the Consolidated Balance Sheets under current liabilities as deferred revenue. Settlement with the IESO will continue until all projects are completed and a compliance audit will be completed thereafter.

The 2020 financial statements includes a reversal of a $675,000 provision from the prior year, associated with a potential liability involving customer incentive payments. This issue has now been resolved and as a result, EE no longer believes a provision is necessary.

The OEB has established a mechanism to compensate distributors for revenue losses related to the reduction of load or energy usage associated with the distributors' CDM activities. During rate setting, a forecasted impact on revenues due to CDM activities is included within rates and any variance from that forecast is recorded in a variance account (LRAMVA) to be settled in the future. The recovery risk associated with LRAMVA claims is low and these claims have historically been approved by the OEB.

While CDM will no longer be a program administered by EE in 2021, it is anticipated that any future benefits from the program will be offset by the future focus on growth and innovation from both EE and EG alongside any government funding mechanism to support its strategic imperatives.

Financial Highlights

REVENUES AND NET INCOME

Distribution revenues for the year ended December 31, 2020 were $79.4 million. Customer growth was 1,838 customers, or 1.1%, since December 31, 2019. At the request of the provincial government, due to COVID-19, EE postponed the implementation of its new rates for the Veridian rate to January 1, 2021, resulting in lower than expected distribution revenues.

Elexicon's adjusted net income after net movements in regulatory balances (of $12.5 million), and further adjusted to exclude unrealized gains or losses on interest rate swap derivatives (addback of $3.5 million) and deferred tax impacts (reduced by $0.9 million) for the year ended December 31, 2020 was $15.1 million.

OM&A COSTS AND COSTS PER CUSTOMER

Within its regulated electricity distribution company, EE, the standard industry measure of controllable cost per customer is tracked at least annually. In 2020, the EE controllable cost per customer, calculated on an annualized basis, after adjustment for merger related costs, was $254.

CAPITAL EXPENDITURES

Total net capital expenditures for 2020 were $35.09 million.

Capital Expenditures (millions)	2020	(nine months) 2019
Distribution System Assets	27.21	26.85
Intangible Assets	4.07	2.30
Other Assets	3.81	3.73

Of these capital investments, 77.5% or $27.2 million was expended on distribution system assets. These assets include poles, wires and cables, transformers, substations and meters.

These reflect investments for expanding, replacing and refurbishing distribution infrastructure to ensure safe and reliable distribution of electricity to customers and ensure compliance with statutes and regulations.

Intangible assets acquired in the reporting period include computer software and intellectual property. Other asset investments are in facilities, furniture and office equipment, computer hardware, fleet vehicles and system control equipment and tools.

SHAREHOLDERS’ EQUITY AND RETURNS FOR SHAREHOLDERS

	Balance 31-Dec-19	Net Income	Other comp. loss	Dividends paid/ accrued	Balance 31-Dec-20
Share Capital	$ 97,692				$ 97,692
Contributed Capital	25				25
Contributed Surplus	79,301				79,301
Accum. other comprehensive loss	(816)		(999)		(1,815)
Retained Earnings	75,585	12,499			88,084
Dividends	(6,988)			(11,294)	(18,282)
Total Equity	**$ 244,799**	**$ 12,499**	**$(999)**	**$(11,294)**	**$ 245,005**

In 2020, the shareholders’ equity position increased from $244.8 million to $245.0 million, an increase of $0.2 million.

Net income realized after net movements in regulatory balances was $12.5 million. This is offset by $1.0 million due to the re-measurement of employee future benefits liability that is recognized as part of the accumulated other comprehensive loss. This actuarial loss was due to a 0.50% decrease in the discount rate from 3.20% (2019) to 2.70% (2020) thereby increasing the present value of the employee future benefit

Municipal shareholders benefit from distributions of Elexicon’s earnings through annual dividends. As set out in the Shareholder Agreement, the Board of Directors of Elexicon Corporation reaffirmed a dividend policy for calendar 2020 with base dividends of $11.31 million for the fiscal year. For the year ended December 31, 2020, Elexicon recorded dividends paid or payable to shareholders of $11.29 million.

LIQUIDITY AND FINANCING

Elexicon's debt to capitalization ratio on December 31, 2020 was 48%. The Corporation's debt includes $89.1 million in shareholder promissory note debt, as well as an available committed reducing term credit facilities of $130.0 million held with a Canadian chartered bank. Elexicon also has access to a revolving demand facility of up to $40 million which was increased to $100 million on a short-term basis up to June 30, 2021, after which date the revised credit limit will be re-assessed. The facility may be renewed for the remainder of 2021. This $100 million credit facility is available for short-term working capital requirements and was temporarily increased to $100 million in light of the COVID-19 pandemic. If the business need for the temporary increase is determined to be no longer necessary, this demand facility will revert back to $40 million. These facilities carry covenants normally associated with long-term debt, including debt to capitalization and debt service coverage ratios. Elexicon complies with all bank covenants as at December 31, 2020.

On May 4, 2020, the Dominion Bond Rating Service ("DBRS") confirmed the Issuer Rating of Elexicon Corporation at "A" with a stable trend. The DBRS report noted that Elexicon's rating continues to be supported by its stable regulated operations, reasonable financial profile and supportive shareholders.

Elexicon's operating activities and these credit facilities are the primary sources of funds for liquidity and capital resource requirements. These resources are required for the following:

- capital expenditures to maintain, improve and modernize the electricity distribution system;
- servicing and repayment of debt;
- purchased power expense;
- prudential requirements;
- other investing activities; and
- dividends.

Management will continue to assess Elexicon's financial capital requirements and capacity as the capital needs evolve to meet all stated corporate strategic objectives.