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Management's Report on Internal Control over Financial Reporting

Management of CAE is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f), 15d-15(f) under the Securities Exchange Act of 1934). CAE's internal control over financial reporting is a process designed under the supervision of CAE's President and Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external reporting purposes in accordance with Canadian generally accepted accounting principles.

As of March 31, 2008, Management conducted an assessment of the effectiveness of the Company's internal control over financial reporting based on the framework and criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organization of the Treadway Commission. Based on this assessment, Management concluded that the Company's internal control over financial reporting as of March 31, 2008 was effective.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of March 31, 2008 has been audited by PricewaterhouseCoopers LLP, an independent auditor.



R.E. Brown
President and Chief Executive Officer



A. Raquepas
Vice-president Chief Financial Officer

Montreal (Canada)
May 14, 2008

Independent Auditors' Report

To the Shareholders of CAE Inc.

We have completed integrated audits of the consolidated financial statements and internal control over financial reporting of CAE Inc. (the "Company") as at March 31, 2008 and 2007 and audit of its 2006 consolidated financial statements. Our opinions, based on our audits, are presented below.

CONSOLIDATED FINANCIAL STATEMENTS

We have audited the accompanying consolidated balance sheets of the Company as at March 31, 2008 and 2007, and the related consolidated statement of earnings, retained earnings, comprehensive income, accumulated other comprehensive loss and cash flows for each of the three years in the period ended March 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits of the Company's financial statements as at March 31, 2008 and 2007 and for each of the years in the two year period then ended in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). We conducted our audit of the Company's financial statements for the year ended March 31, 2006 in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as at March 31, 2008 and 2007 and the results of its operations and its cash flows for each of the three years in the period ended March 31, 2008 in accordance with Canadian generally accepted accounting principles.

As described in note 2 to the consolidated financial statements, the Company has changed its accounting for financial instruments and hedging relationships.

INTERNAL CONTROL OVER FINANCIAL REPORTING

We have also audited the Company's internal control over financial reporting as at March 31, 2008, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as at March 31, 2008 based on criteria established in *Internal Control – Integrated Framework* issued by the COSO.

PricewaterhouseCoopers LLP

Chartered Accountants

May 13, 2008

Montreal, Quebec, Canada

Consolidated Balance Sheets

As at March 31

(amounts in millions of Canadian dollars)

	2008	2007
Assets		
<i>Current assets</i>		
Cash and cash equivalents	\$ 255.7	\$ 150.2
Accounts receivable (Note 6)	255.0	219.8
Inventories (Note 7)	229.9	203.8
Prepaid expenses	32.7	23.5
Income taxes recoverable	39.0	24.7
Future income taxes (Note 14)	14.1	3.7
	826.4	625.7
Property, plant and equipment, net (Note 8)	1,046.8	986.6
Future income taxes (Note 14)	64.3	81.5
Intangible assets (Note 9)	62.0	36.0
Goodwill (Note 10)	115.5	96.9
Other assets (Note 11)	138.2	129.5
	\$2,253.2	\$1,956.2
Liabilities and Shareholders' Equity		
<i>Current liabilities</i>		
Accounts payable and accrued liabilities	\$ 482.7	\$ 403.9
Deposits on contracts	209.3	184.8
Current portion of long-term debt (Note 12)	27.3	27.2
Future income taxes (Note 14)	16.8	4.9
	736.1	620.8
Long-term debt (Note 12)	352.5	256.0
Deferred gains and other long-term liabilities (Note 13)	184.9	232.7
Future income taxes (Note 14)	31.2	16.8
	1,304.7	1,126.3
Shareholders' Equity		
Capital stock (Note 15)	418.9	401.7
Contributed surplus (Note 15)	8.3	5.7
Retained earnings	644.5	510.2
Accumulated other comprehensive loss	(123.2)	(87.7)
	948.5	829.9
	\$2,253.2	\$1,956.2

Contingencies and commitments (Notes 19 and 20)

The accompanying notes form an integral part of these Consolidated Financial Statements.

Approved by the Board:



R. E. Brown
Director



L. R. Wilson
Director

Consolidated Statements of Earnings

Years ended March 31

(amounts in millions of Canadian dollars, except per share amounts)

	2008	2007	2006
Revenue	\$ 1,423.6	\$ 1,250.7	\$ 1,107.2
Earnings before interest and income taxes (Note 25)	\$ 251.5	\$ 189.4	\$ 104.0
Interest expense, net (Note 12)	17.5	10.6	16.2
Earnings before income taxes	\$ 234.0	\$ 178.8	\$ 87.8
Income tax expense (Note 14)	69.2	49.7	18.2
Earnings from continuing operations	\$ 164.8	\$ 129.1	\$ 69.6
Results of discontinued operations (Note 5)	(12.1)	(1.7)	(6.0)
Net earnings	\$ 152.7	\$ 127.4	\$ 63.6
Basic and diluted earnings per share from continuing operations	\$ 0.65	\$ 0.51	\$ 0.28
Basic earnings per share	\$ 0.60	\$ 0.51	\$ 0.25
Diluted earnings per share	\$ 0.60	\$ 0.50	\$ 0.25
Weighted average number of shares outstanding (basic) (Note 15)	253.4	251.1	249.8
Weighted average number of shares outstanding (diluted) (Note 15)	254.6	253.0	252.1

The accompanying notes form an integral part of these Consolidated Financial Statements.

Consolidated Statements of Retained Earnings

Years ended March 31

(amounts in millions of Canadian dollars)

	2008	2007	2006
Retained earnings at beginning of year	\$ 510.2	\$ 392.8	\$ 339.2
Transition adjustments – Financial instruments (Note 2)	(8.3)	–	–
Net earnings	152.7	127.4	63.6
Dividends	(10.1)	(10.0)	(10.0)
Retained earnings at end of year	\$ 644.5	\$ 510.2	\$ 392.8

The accompanying notes form an integral part of these Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income

Years ended March 31

(amounts in millions of Canadian dollars, except per share amounts)

	2008	2007	2006
Net earnings	\$ 152.7	\$ 127.4	\$ 63.6
Other comprehensive (loss) income, net of income taxes:			
Foreign Currency Translation Adjustment			
Net foreign exchange (losses) gains on translation of financial statements of self-sustaining foreign operations	(50.2)	26.1	(49.2)
Net change in gains on certain long-term debt denominated in foreign currency and designated as hedges on net investments of self-sustaining foreign operations	15.7	1.5	4.6
Reclassifications to income	–	–	(5.3)
Income tax adjustment	(0.6)	(0.1)	1.0
	(35.1)	27.5	(48.9)
Net Changes in Cash Flow Hedge			
Net change in gains on derivative items designated as hedges of cash flows	29.7	–	–
Reclassifications to income or to the related non-financial assets or liabilities	(25.2)	–	–
Income tax adjustment	(1.4)	–	–
	3.1	–	–
Total other comprehensive (loss) income	(32.0)	27.5	(48.9)
Comprehensive income	\$ 120.7	\$ 154.9	\$ 14.7

The accompanying notes form an integral part of these Consolidated Financial Statements.

Consolidated Statement of Accumulated Other Comprehensive Loss

	Foreign Currency Translation Adjustment	Cash Flow Hedge	Accumulated Other Comprehensive Loss
<i>As at and for the year ended March 31, 2008</i> (amounts in millions of Canadian dollars)			
Foreign currency translation adjustment reclassification	\$ (87.7)	\$ –	\$ (87.7)
Transition adjustments – Financial instruments (Note 2)	–	(3.5)	(3.5)
Balance in accumulated other comprehensive loss on April 1, 2007	\$ (87.7)	\$ (3.5)	\$ (91.2)
Details of other comprehensive loss:			
Net change in (losses) gains	(34.5)	29.7	(4.8)
Reclassifications to income or to the related non financial assets or liabilities	–	(25.2)	(25.2)
Income tax adjustment	(0.6)	(1.4)	(2.0)
Total other comprehensive loss for year	\$ (35.1)	\$ 3.1	\$ (32.0)
Balance in accumulated other comprehensive loss	\$ (122.8)	\$ (0.4)	\$ (123.2)

The accompanying notes form an integral part of these Consolidated Financial Statements.

Consolidated Statements of Cash Flows

Years ended March 31

(amounts in millions of Canadian dollars)

	2008	2007	2006
Operating Activities			
Net earnings	\$ 152.7	\$ 127.4	\$ 63.6
Results of discontinued operations (Note 5)	12.1	1.7	6.0
Earnings from continuing operations	164.8	129.1	69.6
Adjustments to reconcile earnings to cash flows from operating activities:			
Depreciation	60.6	55.0	52.5
Financing cost amortization	0.8	0.8	2.2
Amortization and write down of intangible and other assets	16.9	15.8	22.9
Future income taxes (Note 14)	26.4	(14.2)	5.1
Investment tax credits	15.4	19.3	(11.8)
Stock-based compensation plans (Note 16)	(0.8)	24.6	12.2
Employee future benefits, net	0.1	(0.9)	(2.0)
Other	(7.6)	(10.4)	(3.9)
Changes in non-cash working capital (Note 18)	(15.7)	20.2	79.1
Net cash provided by continuing operating activities	260.9	239.3	225.9
Net cash provided by discontinued operating activities	–	–	2.1
Net cash provided by operating activities	260.9	239.3	228.0
Investing Activities			
Business acquisitions (net of cash and cash equivalents acquired) (Note 3)	(41.8)	(4.4)	2.6
Proceeds from disposal of discontinued operations (net of cash and cash equivalents disposed) (Note 5)	–	(3.8)	(4.9)
Capital expenditures	(189.5)	(158.1)	(130.1)
Deferred development costs	(16.5)	(3.0)	(1.8)
Deferred pre-operating costs	(3.9)	(5.9)	(0.7)
Other	(5.5)	(2.9)	(9.9)
Net cash used in continuing investing activities	(257.2)	(178.1)	(144.8)
Net cash used in discontinued investing activities	–	–	(2.3)
Net cash used in investing activities	(257.2)	(178.1)	(147.1)
Financing Activities			
Net borrowing under revolving unsecured credit facilities (Note 12)	–	(0.6)	(30.7)
Proceeds from long-term debt, net of transaction costs and debt basis adjustment (Note 12)	141.1	45.8	32.1
Reimbursement of long-term debt (Note 12)	(37.4)	(39.8)	(65.7)
Dividends paid	(9.8)	(9.8)	(9.7)
Common stock issuance (Note 15)	13.9	10.0	8.0
Other	(5.9)	(2.1)	11.6
Net cash provided by (used in) continuing financing activities	101.9	3.5	(54.4)
Net cash provided by discontinued financing activities	–	–	1.2
Net cash provided by (used in) financing activities	101.9	3.5	(53.2)
Effect of foreign exchange rate changes on cash and cash equivalents	(0.1)	4.4	(8.1)
Net increase in cash and cash equivalents	105.5	69.1	19.6
Cash and cash equivalents at beginning of year	150.2	81.1	61.5
Cash and cash equivalents at end of year	\$ 255.7	\$ 150.2	\$ 81.1

Supplementary Cash Flows Information (Note 18)

The accompanying notes form an integral part of these Consolidated Financial Statements.