

**ANDREW ARNOVITZ (Vice President, Investor Relations and Strategy, CAE Inc.):** Operator, before we open the lines, I'd like to ask that in the interest of fairness that participants limit themselves to a single question. Thank you.

**OPERATOR:** Thank you. The first question is from Ben Cherniavsky from Raymond James. Please go ahead.

**BEN CHERNIAVSKY:** Hello. Andrew, I'll respect your request and just ask if there can be any more colour added to the foreign currency impact in the hedging, in particular? Is there way to – of indicating how much your hedge has helped you in the third quarter, or sorry, the second quarter to support it and potentially giving us maybe where – some indication of where you would be hedged going forward on future contracts?

**ANDREW ARNOVITZ:** I think, Ben, the way that we would respond, I think that there's some information in the MD&A that you can look at on amounts but essentially, you know, our hedges carry us out a year or slightly more than a year, something like that and this is the same as we've had over the last couple of years. And basically what, you know, I think the judgment has to be made is, are we going to be able to realize productivity gains related to cost cutting, related to the way we work and also related to the increased volumes that we have now that are going to allow us to offset any of the benefits for the hedging that, you know, that we've had. And if we had been reporting this during the period of the restructuring – I guess the reporting we're, you know, requirements are different now – we would have been in exactly the same – or the exact same kind of position.

So all I can tell you is that, from our point of view, we feel, you know, quite confident about the initiatives that we have in place. And, you know, the huge cultural change we've made in the organization to be able to allow us to, you know, to make the changes that are necessary to make sure we can deliver results in the future to shareholders. And I would also add that, you know, the diversity of our business now, the diversification we have is very different than we were a couple of years ago. So, you know, as we look about – we look at all of this, clearly the rate of change, the velocity of change is a challenge and will we be able to exactly match the change? I'm – quite frankly, I'm not sure. I'm not that good at predicting it, but are we going to be able to work through this in the way that we worked through the restructuring? I think we'll be able to do that.

**BEN CHERNIAVSKY:** Andrew, can I just ask if that, as a follow-up, if – in terms of the – it's the timing I think that concerns everyone and you guys do deserve credit for

what you've already done. But if you are able to adjust, as you are confident you will, how quickly can you do that? And how much of a near term challenge do you see the currency running to \$1.10 being as we close off the calendar year?

**ANDREW ARNOVITZ:** You know, I don't really think that the – I don't really think that the problem is short term. I think more of the challenge is, can we get our – continue to keep our act together and deliver, you know, out, sort of a year from now? We have time, is what I'm saying because we're hedged in the way that we've done it and because of the nature of the contracts that we've got and also because of the big increase in volume that we've got this year relative to previous years. So it's a mix of all of these things, you know, how you view the – where the OEMs are going to go, the – with the production and delivery of aircraft, how the business aircraft producers are going to come with deliveries of aircraft in the next period. What's going to be the benefit of our – the global reach we've got, the penetrations we're making in India and China and other emerging markets.

So it's really a mixture of all of those facts and, you know, where we – when we started the restructuring, as I mentioned, at \$0.80 and I think if you looked at over a two-year period, it went to about \$0.95, so we've got a similar kind of challenge. It's a little shorter period and that we've got to make sure that we put all of our initiatives that we have in place right now and accelerate a few of them to adapt to those conditions. That's essentially what we're doing.

**DAN CHERNIAVSKY:** Okay. Thanks very much.

**ANDREW ARNOVITZ:** You're welcome.

**OPERATOR:** Thank you. Your next question is from Daniel Kim from Paradigm Capital. Please go ahead.

**DANIEL KIM:** Good afternoon. Thank you. A question perhaps for Alain. Alain, could you give us a sense or remind us again, please, how many – what your exposure in terms of U.S. dollar inflows and other currencies? And could you disclose, at least, what percentage of those cash flows are hedged and if you can give us the actual amount that you've hedged in terms of what exchange rate, please?

**ALAIN RAQUEPAS (Vice President, Finance and Chief Financial Officer, CAE):** Yes. I do not have all of these numbers at the – at my fingertips, but what I would (inaudible) for you too, Daniel, is there is good information in the annual report in terms of the sensitivity at page 48, section 3.6, which is still accurate. So it's

going to help you to figure out the flow that was hedged in terms of sensitivity and also in the new statement that is published since the beginning of the year, the comprehensive income statement. I think you'll see there's a lot of information there to help you to understand that impact.

**DANIEL KIM:** Can you, at least briefly, explain your hedging strategy in terms of how far you are hedged?

**ALAIN RAQUEPAS:** Yes. In fact, all my backlog in Sim Products/Civil is hedged so as I'm getting an order or as I got orders in the last 12 months or 14 months, I have hedged my total top line in some products civil as per the policy. So – and, you know, we've continued to do that in the last six months so you can assume that the civil backlog is hedged.

**DANIEL KIM:** Great. Thank you very much.

**ALAIN RAQUEPAS:** You're welcome.

**OPERATOR:** Thank you. Your next question is from Claude Proulx from BMO Capital Markets. Please go ahead.

**CLAUDE PROULX:** Thank you. Good afternoon. First question is, I guess it's about the margins in civil in the quarter. They were obviously very impressive and I was reading the paragraph in your MD&A; I'm not sure I understand. I mean are you talking about concentrated number of deliveries for which some key performance risks have been mitigated? And then you've got – talk about cost savings partly due to the stronger Canadian dollar against the U.S. dollar. Can you give more colour, explain more what these means?

**ROBERT BROWN (President and Chief Executive Officer, CAE):** Yes. I think, you know, it all depends on the mix of products that you have in the quarter and your ability to deliver. I think, you know, the other thing that we've done is, because of the very strong market and the short-term demand, we some – we will build on a very limited basis, maybe an A320 or a 737, and if a customer arrives and we get the, we get the contract, we can accelerate the revenue and the income related to that. So there is a bit of that but that's sort of an ongoing thing we're doing because we're in a strong market position right now.

And the other point that related to benefiting the Company through procurement, you know, if you take a simulator, what you've basically got is about, say 20 percent is profit. You've got about 40 percent that relates to labour and then you've got about 40 percent that relates to your bill of material, and you can assume

that, you know, maybe two thirds or whatever of your bill of material is U.S. dollars. And so that you can – you're now paying with Canadian dollars that are worth, and you know, worth a lot more so you're paying less than you had planned to pay, and that's likely something that's going to go on into the future.

So when you take the mix of all of those things, you know, going forward we're saying we did about 23 percent of margin there. I said at the start of the year, and I stick with it, you know, that our goal is to try and get to around 20 percent, so you're going to see some ups and downs, basically related to the mix of the products that come through for the year. But I hope that, I hope that explains the approach and answers your question.

**CLAUDE PROULX:** Just to follow-up on, that means that from a material standpoint, when you hedge your revenue, you're hedging more than your true exposure to the U.S. dollar. You're not – you're exposing your hedging more than your true cash flow exposure –?

**ROBERT BROWN:** No, because you have to, you have to pay in U.S. dollars at the end – sorry, you have to pay Canadian dollars for U.S. dollars, you know, and not what you anticipate that you were going to pay when you won the contract.

**CLAUDE PROULX:** Okay.

**ROBERT BROWN:** Okay.

**CLAUDE PROULX:** Thank you.

**OPERATOR:** Thank you. Your next question is from Nick Morton from RBC Capital Markets. Please go ahead.

**NICK MORTON:** Good day. I just wanted to ask you about project Phoenix and what kind of contribution you got in the period and how that affected your earnings?

**ROBERT BROWN:** Yes, I think it's laid out. I'll ask Alain to answer that; it's less than I think we had fourth quarter (inaudible).

**ALAIN RAQUEPAS:** Yes, for sure.

**ROBERT BROWN:** You'll find it moves up and down but –.

**ALAIN RAQUEPAS:** Contribution to income of Phoenix this quarter was 8.6 million. You can see that in the note 9 of the financial statement.

**NICK MORTON:** Okay. And how did that compare to the prior period?

**ALAIN RAQUEPAS:** Year-over-year –

**ROBERT BROWN:** Last quarter was the –

**ALAIN RAQUEPAS:** Last quarter I don't have the data in front of me, but last – year-over-year 13.7 was booked to income at the end of same quarter last year, so it went down.

**NICK MORTON:** And what division does that impact?

**ALAIN RAQUEPAS:** Same products, civil; same products, military. When we do build the simulator and which we carried some development that – similar to that goes to the network so a portion of the Phoenix contribution goes to training services also.

**NICK MORTON:** Okay. Great. Well I guess that's my one question, so thank you very much.

**ROBERT BROWN:** Thanks, Nick.

**OPERATOR:** Thank you. Your next question is from Richard Stoneman from Dundee Securities. Please go ahead.

**RICHARD STONEMAN:** Morning, Bob.

**ROBERT BROWN** (President and Chief Executive Officer, CAE): Morning.

**RICHARD STONEMAN:** I have a question on the Multi-Crew Pilot license training program that ICAO is putting forward. You mentioned that in your MD&A. How do you think will affect your business? And when do you think you'll see some impact from the new requirements?

**ROBERT BROWN:** Boy, I don't know precisely. I think on that one, Richard, that essentially – normally it takes a little while to get these things into place. I think we're going to be very well situated with our global network to play in this. I would not expect anything to be coming till some time next year.

**RICHARD STONEMAN:** Thank you.

**OPERATOR:** Thank you. Your next question is from Tim James from CIBC World Markets. Please go ahead.

**TIM JAMES:** Thank you. Could you discuss a little bit further within the training and services civil segment of your business the strength of the different markets? We

know both commercial and the business jet market are very strong. Can you talk a little bit about each specifically and whether one is contributing more to the strength than the other?

**ROBERT BROWN:** Yes. I think both of the areas are doing very well. However, you know, I would say that on the business aircraft side, because we have more value added by the provision of instructors and the courseware that we do, that, you know, you'd see that more of the margin coming from that particular area. So, you know, and I think it will continue to grow and you've seen in what we've talked about and the comments I just made that we're moving very quickly to make sure that we can cover all of the in-service aircraft are there to make sure that we can capitalize on the new models that are coming into the business aircraft segment and also, you know, the increased volumes.

There's, in fact, I think over in the five-year period there's more business aircraft being delivered than commercial aircraft, so we've got to make sure that we stay concentrated on that and a – now for the first time a greater percentage of these airplanes are being delivered outside of North America, which also plays well to our global network.

**TIM JAMES:** Thank you.

**ROBERT BROWN:** You're welcome.

**OPERATOR:** Thank you. The following question is from Marko Pencak from GMP Securities. Please go ahead.

**MARKO PENCAK:** Good afternoon. Bob, could you talk about competitive dynamics and the focus particularly on pricing in both the civil equipment and the civil training side?

**ROBERT BROWN:** Yes. I think, you know, if you look at the big simulator sales business, third parties, Thales is a strong competitor. You know, they're basically in the same situation as we are as it relates to exchange, so they're having some adjustments and challenges that have to be made. But, you know, the – I can tell you the activity level on third party sales is very good and we see the sales going well for the two major OEMs as well, so I think all of that is encouraging.

As I look at the training side, really not much of a change in the dynamic here. You know, I think we continue to compete against the airlines that are selling some third party work; we compete against Altheon, you know, that is primarily supporting their own customers; we compete against FSI in the business segment. But, you know, I

think everybody there – I mean there's more work available than people can handle with the increased volume of aircraft going into the market.

So, you know, I think that, say pricing is stable in all of those, in all of those particular markets, and we see the utilization factor is a high 70s, 80 percent. So I think it's – all of that I think or reflects what's happening in the marketplace right now as it relates to where we are in the cycle and the greater diversity we have right now outside of North America, in Europe, Asia, the emerging markets, in China and India.

**MARKO PENCAK:** So if there's more work than people can handle, I mean – and particularly on the equipment side, if it's as effective duopoly, why aren't you guys taking pricing up?

**ROBERT BROWN:** Well I think, you know, that you have to look at the fragility of a – the customers that – remember the customers are still not entirely out of the woods. And I think if it isn't – it is a competitive environment and it takes two to tango and, you know, so – and as we've always said going along that our advantage is not necessarily in jacking up prices; it's related to having a better technology, a better product support and having a continual culture of reducing our costs and listening very carefully to the customer in terms of what they want to have. And we don't think changing that formula now is a – is the thing to do.

**MARKO PENCAK:** And then, just finally on pricing, I just want to go back to the comment you made about the sort of short-term order intake and delivery on the civil equipment side where you say you might build an extra 320 or 737 simulator. So, just to understand the impact on margins, are you saying that because you may sort of build one "on spec" and you can deliver it quickly, that you're getting the volume benefit that helps the margins? Or are you actually able to preferentially price such a short-term delivery and that helps your margins?

**ROBERT BROWN:** No. It's a – it's basically – relates to the mix of products that we can put out there. And, you know, it – it's just not going to happen every quarter; it just – and you may get it in one quarter and not the next; it all depends on an opportunistic basis if somebody comes along and you're able to do it.

**MARKO PENCAK:** Okay. Thanks very much.

**OPERATOR:** Thank you. Your next question is from Robert Fay from Canaccord Adams. Please go ahead.

**ROBERT FAY:** Good. A couple of questions actually. In that comment that you made about the – this is for

Alain – the Civil Sim Products, can you quantify the hedge gain or the hedging on revenues that you got from the hedging? And can you also quantify the fact that you were able to purchase in Canadian dollars the goods on the other side? Can you actually get a number for those two items so we can get an idea on the impact on the margins?

**ALAIN RAQUEPAS:** Yes. Well in fact, it's a, you know, FX is all over the place in the system so it would be very difficult, Robert, to give you a very precise number.

**ROBERT FAY:** Can you give it to us in a general sense over all of the business?

**ALAIN RAQUEPAS:** Well, the general sense is what we've published in the annual report in terms of sensitivity with the basket (phon) we add at that point in time. And the future earnings – the impact on earnings of \$0.01 of the USD that was hedged was 1.4 million. That's what is published in the annual report so that's the best data that we have.

**ROBERT FAY:** Okay. In terms of the quarter, what was the hedge number in the revenues?

**ALAIN RAQUEPAS:** What do you mean by that?

**ROBERT FAY:** The overall. The hedge that you had, how much did it help revenues in the quarter? Just the hedging.

**ALAIN RAQUEPAS:** Why, we don't know that; that's what I'm saying. As I'm getting a contract in a dominant – in U.S. or in Euros, for instance, we hedged that at the specific rate, at this port (phon) rate at that point in time, and I do bring the – my revenue on the top line in Canadian dollars after that date. So it's difficult for me to monitor it exactly how much more revenue I have because I have hedged these contracts at that point in time, my accounting system is not allowing me to monitor that, unfortunately.

**ROBERT FAY:** Okay. In the military side, you recorded some milestone payments in the quarter on a year-over-year basis. What was the impact of those milestone payments? Just so that we can sort of smooth out what to expect in terms of revenues and operating income in Sim Products military.

**ALAIN RAQUEPAS:** (Inaudible) sorry, you have a (inaudible). What was your question, Robert, again?

**ROBERT FAY:** Well I guess the commentary that you made in the Sim Products business, military, you said that revenues were up resulting from the achievement of

some milestones on U.S. programs. And then you said that the operating income was there because of the achievement of some significant milestones on U.S. and UK programs.

**ALAIN RAQUEPAS:** Yes.

**ROBERT FAY:** For which key performance risks had been mitigated and cost integration savings realized.

**ALAIN RAQUEPAS:** Yes. Okay. So the milestone, when we do on military program, when we hit a milestone in which we have a significant subcontractor, we accrue the costs for these subcontractors that gives us the top line. And in regard of the bottom line, what we said there was, because we were toward the end of the program, so when you are toward the end of the program, you know, you de-risk your program and that helps to explain the margin.

**ROBERT FAY:** Well I'm just trying to get some quantification of those milestone impacts on revenue and on the operating earnings, just from the milestones?

**ALAIN RAQUEPAS:** And we're not revealing that, Robert.

**ROBERT FAY:** Okay. Thank you.

**ALAIN RAQUEPAS:** You're welcome.

**OPERATOR:** Thank you. The following question is from Benoit Poirier from Desjardins Securities. Please go ahead.

**BENOIT POIRIER:** Yes. Good afternoon, gentlemen. With the current Canadian dollar, I'm just wondering if it's changing your overall growth strategy? And do you intend to benefit from the Canadian dollar to maybe look at making some acquisition in the U.S.?

**ROBERT BROWN:** The only thing I can say is, it hasn't changed our growth strategy. We still have an aggressive growth strategy, and, you know, it's clear that assets that we would buy would be – it would be less expensive at, where the dollar is now than where it was before. So we're, you know, we're continuing to, we're continuing to look and see what possibilities would make sense as we, you know, bolt on various capabilities to our business. We're not going to go out and, you know, buy something that is large; we think that the incremental strategy that we've had of bolting things on and growing incrementally makes sense, and I can only say with the dollar where it's at that may be easier than it's been in the past.

**BENOIT POIRIER:** Okay. And you talked about your competitiveness on the civil side, but could you maybe provide more details about your competitiveness on the military side?

**ROBERT BROWN:** I would say in the – on the military side, you know, it comes down very much to your technological capability. And, you know, we continue to work very, very hard to improve our technology offering. And I would say the second factor would be your ability to execute contracts in the way that you said you were going to do that, and I think our record here has been quite good and, of course, you know, price is important as well. But whether we're building into the U.S. market or into Europe, and we have operations there where we can have natural hedges and do the business and be quite competitive.

**BENOIT POIRIER:** Okay. Thank you very much.

**ROBERT BROWN:** You're welcome.

**OPERATOR:** Thank you. Your next question is from Brian Morrison from TD Newcrest. Please go ahead.

**BRIAN MORRISON:** Yes. Good morning, Alain. Just – with the purchase of the sims back in the network, I see the impact on the training margin and on the interest expense, but can you just elaborate a little bit more on why you've done this or what is the benefit from it? And then just lastly, can you provide the present value of your off-balance sheet debt now?

**ALAIN RAQUEPAS:** Yes. Well, Brian, I'm not too sure we mentioned how many cents we bought back in the MD&A, but in fact, it was three operating leases that were operated in Canada. So it's probably one tenth of systems that were off-balance sheet to put it in perspective. You've seen the balance sheet; we had a lot of cash. Having them on the balance sheet or being the owner gives us flexibility when we want to move these simulators and I was earning interest income and paying interest expense and there was a net saving in doing the transaction, so it simply made sense to bring them back on the balance sheet.

**BRIAN MORRISON:** Okay. So in terms of off-balance sheet debt, what would that be reduced to?

**ALAIN RAQUEPAS:** I do not have the data with me.

**ANDREW ARNOVITZ:** Brian, I'll circulate it.

**ALAIN RAQUEPAS:** And we can email that to you.

**BRIAN MORRISON:** Okay.

**ALAIN RAQUEPAS:** I might find it before the end of the call.

**BRIAN MORRISON:** Okay. With the reallocation of your fleet now complete though, you know, is the flexibility such a huge benefit at this point in time?

**ALAIN RAQUEPAS:** Yes.

**BRIAN MORRISON:** Okay.

**OPERATOR:** Thank you.

**ANDREW ARNOVITZ:** Operator, we'll take one more question from investors and then we'll open up the lines to the media.

**OPERATOR:** Thank you. The next question is from Cameron Jeffreys from Credit Suisse. Please go ahead.

**CAMERON JEFFREYS:** Thanks. Just housekeeping question. Most of mine have been asked and answered. On the interest expense line, is kind of 5.5 million of interest expense a good number to use as a run rate going forward through the end of the year and into next year?

**ALAIN RAQUEPAS:** Yes. It's a good number.

**CAMERON JEFFREYS:** Okay. Thanks.

**ALAIN RAQUEPAS:** Thank you.

**OPERATOR:** Thank you. We are now opening the question period for the media. Once again, if you have a question, please press star, one at this time.

The first question is from Kurt Epstein (phon) from Aviation International News. Please go ahead.

**KURT EPSTEIN:** Yes. Thank you. You mentioned that there is going to be 16 additional training programs that you're going to be starting up. Can you give me some of those type aircraft that you'll be concentrating on?

**ROBERT BROWN:** No. We basically don't announce these until we get closer to when they're actually going to be deployed. We do this for competitive reasons and they're basically being deployed in North America and in Europe.

**KURT EPSTEIN:** Okay. Thank you very much.

**ROBERT BROWN:** You're welcome.

**OPERATOR:** Thank you. Once again, please press star, one if you have any questions. So Mr. Arnovitz, there are no further questions registered at this time. I would now like to turn the meeting back over to you.

**ANDREW ARNOVITZ:** Thank you very much, Operator. I'd like to thank all of our participants this afternoon.