OPERATOR: Good day, ladies and gentlemen, and welcome to the CAE third quarter conference call.

Please be advised that this call is being recorded.

I would now like to turn the meeting over to Mr. Andrew Arnovitz. You may now proceed, Mr. Arnovitz.

ANDREW ARNOVITZ (Vice President, Strategy and Investor Relations, CAE Inc.): Good afternoon, everyone, and thank you for joining us today.

Before we begin I need to read the following: Certain statements made during this conference, including but not limited to statements that are not historical facts are forward-looking and are subject to important risks, uncertainties and assumptions. The results or events predicted in these forward-looking statements may differ materially from actual results or events. These statements do not reflect the potential impact of any non-recurring or other special items or events that are announced or completed after the date of this conference, including mergers, acquisitions or other business combinations and divestitures.

You’ll find more information about the risks and uncertainties associated with our business in our third quarter fiscal 2014 MD&A, and in
our annual information form for the year ended March 31st, 2013. These
documents have been filed with the Canadian Securities Commission and
are available on our website at CAE.com and on SEDAR. They have also
been filed with the U.S. Securities and Exchange Commission under Form
40F and are available on EDGAR.

Forward-looking statements in this conference represent our
expectations as of today, February the 11th, 2014, and accordingly are
subject to change after this date.

On the call with me this afternoon are Marc Parent, CAE’s
President and Chief Executive Officer, and Stéphane Lefebvre, our Chief
Financial Officer. After comments from Marc and Stéphane we will take
questions from financial analysts and institutional investors. Following the
conclusion of that Q&A period we’ll open the lines to members of the media.

Let me now turn the call over to Marc.

MARC PARENT (President and Chief Executive Officer, CAE
Inc.): Thank you, Andrew, and good afternoon to everyone joining us on the
call.

As per our usual practice, I'll first review some highlights of the
quarter, and then Stéphane will provide a detailed look at our results. I'll
conclude the formal portion of the call by commenting on the way forward.
I’m pleased with the results we’ve achieved in the third quarter. We saw an across the board improvement in our performance with sequentially higher operating margins and a stronger order intake. For the company overall, order backlog stood at $4.1 billion, and we had an additional $421 million in backlog related to our joint ventures.

In Civil, we expected the combined operating margin to improve to the high teens in the second half of the fiscal year, and the 16-per-cent margin reached in the quarter puts us right on track. We’ve now completed the majority of the simulator relocations, and the higher margins owes mainly to the operational improvements we’ve made, higher volume, and higher utilization in Training, which reached 69 per cent in the quarter. The increased profitability we achieved since the start of the year underscores the operating leverage that exists in the business.

In Civil Products, we sold 12 simulators in the quarter, and 43 year to date, which is a new record, giving us good backlog visibility. Our strong sales this year are a testament to our market leadership, and more specifically our ability to deliver what matters to our customers. That being said, we don’t take our success lightly, and we constantly evaluate CAE’s winning formula. Our customers tell us they value CAE’s brand and the long-standing relationships that they’ve held with the company. They enjoy the seamless end-to-end experience they get by choosing us as their
partner of choice, and they value the technology and capability underlying our products, as well as the broad portfolio we offer.

In Training and Services, we signed long-term agreements with airlines and operators, including Japan Airlines, Virgin, Australia Regional Airlines, Air Transat, and JetFlight. In Business Aviation, CAE was selected since the end of the quarter as the exclusive Dassault-approved training provider for the newly launched Falcon 5X long-range business jet. This adds to our broad relationship with Dassault involving a full range of Falcon business jets. In all, we received $329 million in combined civil segment orders this quarter for a book-to-sales ratio of 1.17 times. And our civil backlog reached a record $2.1 billion.

In Military, our business remained resilient this quarter. Revenue was up 2 per cent over last year, and up 6 per cent over last quarter. The combined Military margin got up above 15 per cent, driven by our restructuring in Europe and a strong program mix in the quarter. In terms of new business, we booked orders during the quarter for simulators, upgrades and services on enduring aircraft platforms, including the MH-60R Seahawk helicopter for the Royal Danish Navy, the P-8 Poseidon aircraft for the U.S. Navy, and the C-130 aircraft for the U.S. Air Force.

We had success getting orders on new aircraft programs for CAE with contracts for a comprehensive ground-based training system for the T-
6C aircraft for the Mexican Air Force, an Unmanned Aerial System Mission Trainer for the General Atomics Predator for the Italian Air Force, and an air crew training services contract for the T-44C Pegasus for the U.S. Navy.

And we also had success broadening our core market, with a 10-year agreement with the Brunei Ministry of Home Affairs to establish a training centre and conduct emergency management training. This is our first major contract, leveraging modelling, simulation and training in an adjacency such as public safety.

In total, we received $240 million in combined Military segment orders this quarter, representing a book-to-sales ratio of 1.19 times. This quarter marks the first time in the last four quarters that we’ve seen book to sales above 1 time for both products and services.

Contract options were also significant, and not included in the order intake is another $97 million in options. Third quarter Military backlog was $2 billion, and in addition to that we had another $435 million of unfunded backlog.

Looking now at new core markets, in CAE Healthcare we made further inroads in the defence market with the sale of a record 44 Caesar Trauma Patient Simulators for the U.S. Navy Expeditionary Combat Command. We also sold our centre management, ultrasound simulators,
and patient simulators for a range of teaching institutions in the United States.

Since the end of the quarter we unveiled CAE’s Fidelis Maternal Fetal Simulator at IMSH, which is the world’s largest healthcare simulation conference. Our R&D efforts are bearing fruit, and we’re already seeing strong interest in this new simulator ahead of its official release. We at CAE are particularly proud of this solution, which will be used by healthcare structures to improve training for the serious complications that can arise during childbirth. Our vision for healthcare involves using simulation to help to improve the quality of patient outcomes, much in the same way we’ve made air travel safer with our simulation-based solutions in aviation.

In CAE Mining, we released a major update to our flagship resource modelling software. And in terms of business activity, we sold our resource modelling open pit and underground mine planning solutions and engineering services to customers globally.

With that I’ll now turn the call over to Stéphane.

STÉPHANE LEFEBVRE (Chief Financial Officer, CAE Inc.): Thank you, Marc, and good afternoon, everyone.

Consolidated revenue for the quarter was up 3 per cent year over year at $513.6 million, and net income attributable to equity holders was $46.1 million or $0.18 per share. We’ve had very good cash performance on
a year-to-date basis with $96 million of free cash flow generated to the end of December. This is $117 million higher than the first nine months of last year. The improvement came mainly from favourable changes in non-cash working capital, and an increase in cash provided by our operating activities.

Free cash flow was negative $12.7 million in the third quarter. As we look to the fourth quarter we expect to see some improvement and be able to sustain a sizeable improvement in free cash flow for the year as a whole.

Third quarter capital expenditures totalled $37.2 million this quarter with $22.8 million for growth. This brings our year-to-date growth capex to $60.7 million. Maintenance capex was $14.4 million this quarter and $31 million for the year to date.

Net debt was $886.5 million as at December 31st, 2013, compared to $810.4 million as at September 30th, 2013, and our net debt-to-total capital ratio remains stable at 39 per cent.

Now looking at our segmented financial performance. For Combined Civil, third quarter revenue increased 3 per cent year over year, reaching $282.1 million. Operating income was relatively stable year over year at $45.2 million for an operating margin of 16 per cent.
In our Combined Military segment, third quarter revenue was up 2 per cent year over year at $201.8 million, and we generated 15.4 per cent operating margin.

And finally, new core markets, revenue was $29.7 million for the quarter compared to $28.7 million in the third quarter last year. Operating income was $1.4 million compared to $1.7 million last year. We continue to invest in SG&A and new products to develop a larger business.

With that I’ll turn the call back to you, Marc.

MARC PARENT: Thanks, Stéphane.

Our discipline is continuing to drive positive results, and we’re meeting the objectives we established for operational improvements and greater financial performance. In Civil, we expect to continue to lead the market and to see a higher combined segment margin in the fourth quarter as we continue to ramp up utilization in our training centres, grow our training network, and work through our record volume and products.

Our business in commercial aviation customers expect CAE to continue offering the widest and most capable range of product and service solutions in the industry with the broadest global reach. Taken together, this puts us in a prime position to continue to lead within a large and growing civil aviation market.
In Military, the U.S. Bipartisan Budget Act has given greater clarity to immediate spending priorities. In recent weeks we’ve seen investment commitments in the U.S. and internationally to purchase enduring aircraft platforms where CAE has a strong position. In terms of our order outlook, we’re continuing to build our bid pipeline with more bids submitted fiscal year to date than all of last year. The increased level of orders booked in this quarter is the product of our increased bid pipeline and our global footprint, and we expect this trend to continue.

In new core markets, our research and development initiatives are translating into unique new products, and expanding interest in the kinds of solutions that CAE is bringing to market.

To conclude, we’re working from a solid base with a well-diversified business, a record order backlog, and a strong financial position. The commercial aerospace market is robust with unprecedented aircraft orders and deliveries, giving us good visibility. This, together with a clearer picture for defence, bolster our confidence for the way forward and position us well for growth.

Thank you for your attention, and we’re now ready to take your questions. Andrew?

ANDREW ARNOVITZ: Operator, we’d now be pleased to take questions from analysts and institutional investors. As we usually ask,
before we open the lines, in the interest of fairness I would ask that please limit themselves to a single, one-part question, and if you have additional questions after that and time permits, please feel free to re-enter the queue.

OPERATOR: Certainly. Thank you. And ladies and gentlemen, once again as a reminder, to register a question just press the 1 followed by the 4 on your telephone. You’ll hear a three-tone prompt to acknowledge your request. If your question has been asked or if you’d like to withdraw your registration, press the 1 followed by the 3. If using a speakerphone just lift the handset before entering your request.

One moment, please, for the first question.

And we’ll proceed with our first question from the line of Steve Arthur with RBC Capital Markets. Go right ahead.

STEVE ARTHUR: Great. Thank you very much. Just wondering, as part of your margin improvement programs, if you can elaborate just a little more on the status of some of the simulator moves across your training network? Just a recap perhaps if some... any were being moved, how many have yet to land in their new spot? And then some sense on what the target utilization might look like for these relocated simulators. Is it any different from what’s more broadly in your base?

MARC PARENT: Lots to that question, Steve. Let me try to... I mean, overall...
STEVE ARTHUR: I'm only allowed one part.

MARC PARENT: Yeah, exactly. You're cheating. But look, I'll try to (inaudible) Well I think we're... I think I'll let Stéphane, he has the exact numbers, but I think the majority of our relocations are going to be complete by the end of... we've done a lot in Q3. Why don't you just go over the numbers? That'll be easier.

STÉPHANE LEFEBVRE: Well you may remember, we started the year with about, in the first quarter, having 20 sims being in a state of flux and we've relocated some of that in the second quarter, as well as in the third quarter. At the end of the third quarter we still had about 16 sims either in the process of being moved or having been relocated, but ramping up. And as we completed the year we really see the bulk of the relocations being done. At the end of Q4 there may... will be a little one, a few more in Q1, but in the near term we're planning to have the bulk of the relocation pretty much completed.

And so in the... that will definitely play in the increase in utilization rate. I think Marc said that in his remarks. In Q3 our utilization rate was at 69 per cent. And as we continue in Q4, as we continue ramping up some sims that have been relocated and complete some relocations, we expect to see some increase in our utilization rate going forward.
STEVE ARTHUR: Okay. I guess just to clarify my question, just with the simulators that have been moved to these new locations, is there unusually high demand in those areas that the utilization rates on those particular sims should be higher? Or will it just kind of average out where the network is generally?

ANDREW ARNOVITZ: Steve, it’s Andrew. They’d certainly be higher than where they’ve left their original locations, but I think on balance, when you put it all together, at 69 per cent we’re still operating at a fairly low level of utilization. So you should expect that to continue to go higher as these simulators moving around are bedded down.

But also remember in the first quarter we launched three new training centres. So those are ramping up as well, plus there’s business aviation, which, in the small- and mid-sized segment, really hasn’t picked up from the ’08-’09 period. So a lot of different factors that drive toward a higher utilization rate.

STEVE ARTHUR: Okay, that’s great. Thank you. I’ll pass the line.

OPERATOR: Thank you very much. We’ll proceed to our next question from the line of Cameron Doerksen with National Bank Financial. Go right ahead.

CAMERON DOERKSEN: Good afternoon.

ANDREW ARNOVITZ: Hi, Cameron.
CAMERON DOERKSEN: A question on the sim products civil margins. Given that you’ve had a record backlog there, which presumably means that the volumes or deliveries will remain pretty high, and the Canadian dollar is working in your favour, do you think that these margins that you reported in Q3, which are pretty solid, do you think those are sustainable or could even go higher in future quarters?

MARC PARENT: Well let me give it to Stéphane to go in detail. I think that in terms of… there’s one thing maybe I should answer in your… part of your question there. In terms of the revenue, I think that these orders are translating through. So we’ll be seeing a revenue pickup – I don’t think we’ve seen a lot of it yet, but – as these orders take time to go through our revenue. I think you’ll be seeing some increased revenue steadily in the next few quarters. But as a result, the margin specifically, maybe you want to take that one, Stéphane.

STÉPHANE LEFEBVRE: Yeah. So I mean the margins in SPC specifically, at 20.7 per cent, was high in Q3. You look at TSC, TSC’s margin was at 13.1, so it averages out at 16 per cent combined. So we’ve seen some improvement on both sides of our business in terms of margin.

What I find though is the numbers don’t necessarily do justice to all the improvements that we made in TSC specific to the increase in utilization from the prior quarter as well as the actual operational
improvements that we've made. And that’s… I don’t want to be too technical here, Cameron, but that’s highly as a result of the way we account for our joint ventures. Every time that we sell a product to a joint venture it’s a plus on the product side, but it’s a minus on the service side, so we get all the profit in the product segment, but we eliminate the part of the profit that doesn’t belong to us in service. And therefore that’s what I mean by I find that the results don’t necessarily do justice to the improvements that we actually could see in operational performance in TSC.

Just some numbers; if I exclude the impact of the elimination of the inter-company profit there could be around 150 to 200 basis points of margin impact on TSC. So that’s just on the operational performance itself.

CAMERON DOERKSEN: Okay. But is it fair to say though, just thinking about the products business, that the weakness in the Canadian dollar we’ve seen should be positive for margins? Obviously you have hedging in place, but should we expect that over time that we’ll see the benefit of that?

STÉPHANE LEFEBVRE: Well I think over time… over time we will, but I think you pointed at the right thing, Cameron in terms of our hedging policy because as we win contracts, we do hedge, not 100 per cent, but the large portion of our contracts to match our cost structure that’s in Canadian dollars.
I was looking at in Q3 the exchange rate at which we converted our backlog into revenue. And it was running at 1.03. If I look at the Canadian dollar today it's at 1.10. So as we execute our backlog and as we flush out the hedges that we have at lower FX rate we'll see a pickup, and my guess is probably in the later part of next year.

CAMERON DOERKSEN: Okay. Thanks very much.

MARC PARENT: I think the other help(?) of this, Cameron, is that clearly it helps us be more competitive as we bid.

CAMERON DOERKSEN: Right. Right. Thanks.

OPERATOR: Thank you very much. We’ll proceed to our next question, the line of Turan Quettawala from Scotiabank. Go right ahead.

TURAN QUETTAWALA: Yes, good afternoon. I guess maybe I’ll talk a little bit about the military business. Marc, you mentioned the Bipartisan deal here, and I think overall in your comments, probably been a little bit more optimistic this time around than you’ve been in the past few quarters here for sure. Just wondering if you’re seeing any opening up here of the spending side? And maybe some comments there specifically on the military business and how the revenue environment looks there?

MARC PARENT: Well, I think what you’re sensing from me on optimism is it’s really more clarity, which actually is good clarity. I mean, in the past close to a couple of years now, we’ve been in a bit of a murk in
terms of being able to understand what is going to be budgeted. What is going to come out and we had most recently this whole sequestration affair. But now with this new agreement they have, now we have clarity.

I mean, there’s still going to be cuts. There’s still going to be significant cuts. Now the cuts have been delayed. And I’m talking about the United States in particular. The cuts are going to be delayed to what was anticipated before. And now we know which programs are going to be funded, and how likely that is to translate into CAE’s business.

And we’ve talked about in the past these what we called enduring aircraft platforms, meaning platforms that have been around for a long time or will be around for a long time in the U.S. inventory, where we have a very strong platform. And we talked about some of those in our remarks, but the C-130, the P-8, the MH-50R, the Predator, all of which CAE has a very strong franchise in in terms of… in a lot of those cases we’re the only ones that have done simulators for those platforms. And so that gives us some clarity with regards to what we would expect some of the orders that are in our bid pipeline to come out as realized orders. So that’s where my increased confidence comes from.

TURAN QUETTAWALA: So I guess, can we expect sort of maybe this low single-digit kind of growth going forward now or this is sort of more of a one quarter kind of phenomenon for now?
MARC PARENT: Well I don’t think it’s one quarter. I think it’s a bit too early to tell in terms of... I think I would maintain what I’ve said in the past that we’re going to continue to be resilient in this business, and I think so far this year I think we’ve done pretty well on that. And longer term I think this is a growth business. But it’s a bit too early for me to be able to say much more at this point.

TURAN QUETTAWALA: Okay. Thank you very much.

OPERATOR: Thank you. And we’ll proceed with our next question. It is from the line of David Newman with Cormark Securities. Go right ahead.

DAVID NEWMAN: Good afternoon, gentlemen.

MARC PARENT: Good afternoon, David.

DAVID NEWMAN: If I look at year to date you sold 42 sims, and then your utilization is starting to turn a corner as you bed down the simulators in your training network. What does a high-teens margin in Civil imply for your production rates I guess going forward, and your training asset utilization? Because it would seem to me that if you’re hitting the high teens by the end of the year, and your utilization is just beginning to ramp up, and you’ve won a significant amount of orders here, a record level, where directionally do you think these margins could go to in the Civil?
MARC PARENT: Well, I think they’re going higher. I mean, that’s I think what we’ve implied. I mean, we’ve said high teens, so I think you could argue that we’re there now. So I think that it’s going to be higher teens. How about that?

DAVID NEWMAN: But Marc, let’s say you did like 80 per cent utilization, and what is your production rate at right now? Probably 35-36, somewhere around there?

MARC PARENT: It’s hard to look at it that way, to be very frank with you. We have a high number going through the plant right now, which is good from absorption of overhead, things like that. That’s why you’re seeing the margins... part of the reason why you’re seeing the margins relatively higher in Civil products. I mean, the benefit we get of the factors you mentioned on utilization is mainly affecting Training Service Civil.

DAVID NEWMAN: Right.

MARC PARENT: I think, continuing to look at this thing from a combined Civil margin, Stéphane talked about some of the problems by looking at margins and products alone versus margins and services alone, just because of the way we account for joint ventures. So when we look at combined civil margins, and also the fact that that’s the way we’ve run the business. I mean, we really go out there trying to sell a complete solution, whether simulators or products. And if I look at increased volume on one
side and increased utilization based on more activity in our business and commercial centres, and the fact that we, as you said, pretty much completed bedding down these new... these simulators moving around, and opening up three new centres, all translates into... will have caused higher teen...

DAVID NEWMAN: Okay.

MARC PARENT: ... margins as we get into that back half of the year or the last quarter.

DAVID NEWMAN: And the currency looks like it could have been on the margin side, Stéphane, around $3 million benefit, around there in the quarter on the EBIT margin?

STÉPHANE LEFEBVRE: Not really. Actually you look at...

DAVID NEWMAN: You gave the top line, you gave the bottom line, but I'm just kind of looking at the EBIT margin, what that might have been helpful.

STÉPHANE LEFEBVRE: Right. Well, as a matter of fact we've, in the quarter, in Q3, we've actually had $1 million loss as a result of FX, as a result of translation of some non-cash working capital accounts, our accounts payable that are denominated in U.S. dollars. So in fact in Q3 alone, looking at just the quarter, we've actually had to absorb $1 million hit.
DAVID NEWMAN: Oh. Because, I mean, the top line you had a benefit and the bottom line you had a benefit, so why were you being negative on the EBIT side?

STÉPHANE LEFEBVRE: No, there’s... well it depends against which quarter you compare. If you compare it to just sequentially, I look at the second quarter, although the Canadian dollar went down, we continued to turn revenue at an hedged – I'm thinking about the product side of our business – at our hedging rates that haven’t moved that much from Q2 to Q3.

On the other hand in Q2 we had not a huge gain, but a small FX gain. I think it was close to $0.5 million in Q2. I think Q3, we actually had, as I said, a hit in the translation of our non-cash working capital account. So one quarter over the other sequentially we’ve had a $1.3 million hit.

DAVID NEWMAN: Okay, very good. Understood. Thank you.

OPERATOR: Thank you very much. And our next question is from the line of Benoît Poirier with Desjardins Capital Markets. Go right ahead.

BENOÎT POIRIER: Yeah, good afternoon. My question is more about the margin for simulation product military. So it stood at 18.3 per cent in the quarter, so up obviously sequentially, but also year over year. Could you please give more colour on the reason and also highlight whether it’s sustainable or we should see a little softness in the next quarter?
MARC PARENT: Again, Benoît, as we said in the Civil, I would try to look at it the way we look at is a more combined military business because there’s things that move over from training to products that we do to gain advantage in contracts that underlie. But I think, and to specifically this quarter, I think that a lot of that has to do with program mix. In a quarter, in military sometimes we execute contracts that are run at a higher relative margin, and I think that’s what you’re seeing in the quarter, coupled with the benefits that we’ve had from the restructuring in the military business that we completed last year and this year. So I think those are the things that you’re looking at specifically in this quarter.

BENOIT POIRIER: Okay. That’s my one. Thanks.

OPERATOR: Thank you very much. We’ll get to our next question is from the line of David Tyerman with Canaccord Genuity. Go right ahead.

DAVID TYERMAN: Yes, my question’s on new core markets. The sales growth has been fairly slow and the margins have kind of stalled out in the mid-single digits. Could you give us some sense of where things are heading in that unit?

MARC PARENT: What I would anticipate that… that’s definitely not where we want to stay and that’s not where we will stay. I think we’ll have to indulge a little bit of patience here, but I think the new R&D that we’re putting in, we’ve rolled out two new products in the backend of the
year, one that’s just coming online now with this Maternal Fetal Simulator, which there’s nothing else out there in the market, which not only I think would be a good revenue driver for CAE, but it’s going to have a real, to me, societal benefit here of improving the way that people prepare to deal with abnormalities during birth. So we’re very proud of that.

But in terms of the bottom line I think let’s have a little patience here. I mean, that’s what I’ll ask you here. But I see this trending positive, and we’ll just… as these new products come out. Both bottom and top line.

DAVID TYERMAN: Okay. So if I’m interpreting this correctly, I should have patience, but eventually things get better on both top line and bottom line?

MARC PARENT: I guess, yeah, that’s what I’m saying. Yeah.

DAVID TYERMAN: Okay. Thank you.

OPERATOR: Thank you very much. We’ll get to our next question, the line of Tim James with TD Securities. Go right ahead.

TIM JAMES: Thank you. Just wondering if you could discuss the outlook for the pilot sourcing business in Oxford. I believe revenue was down slightly year over year there. And then not sure if it’s related at all, but the decision to initiate a loan program for aspiring pilots in France, and I’m just wondering if that’s something that could be rolled out to other regions as well?
MARC PARENT: I’ll start with the back one, Tim. The loan program is something that is very good. I mean, it allows us… the aspiring candidates to be able to get financing for their studies, which you’ll probably know that it’s very expensive to become an airline pilot. So I mean that’s a good thing. It’s something that we try. We’ve done in the U.K. Now it’s rolled out to France. It’s something that gives us competitive advantage. So that’s something we definitely want to continue. It’s not really related to pilot sourcing.

And I think the difference in the business in terms of top line revenue, I think there’s nothing really to point out specifically in this quarter. I think normal variations in business.

TIM JAMES: Is that sourcing business, I mean is it… so this is just an anomaly this quarter? I mean, generally speaking – and I realize the profitability of that business is not what it is in other areas of your training segment, but is it expected to be a growth business or more or less a relatively flat business in the future?

MARC PARENT: Well look, we’ve had it since the acquisition of Oxford, so ourselves we’re going to continue to grow and know this business. It’s a business… yeah, we would expect it to grow, as is the goal for all of our businesses. It is a business that has inherently low margin, which we’ve disclosed since the beginning there. And it’s remained that
way, but I would not expect to have any big surprises, negative or positive in the next few quarters.

TIM JAMES: Thank you.

OPERATOR: Thank you very much. And before we proceed, once again, as a reminder, it’s 1-4 on your telephone to register a question.

And our next question’s from the line of Ben Cherniavsky with Raymond James. Go right ahead with your question.

BEN CHERNIAVSKY: Good morning, guys. I guess you wouldn’t really see it in your stock price lately, but there have been some observations and concerns that I’ve heard over the last little while about the investments you’ve made, the capex, the general lack of free cash flow, and the declining returns on invested capital as you’ve gone up and gone out and done some major acquisitions and scaled out the training business. Is there any change in your strategic thinking of priorities towards these variables? I mean, are there… do you recognize that these issues have been a drag on your performance, and are you making any changes to how you’re going to allocate capital and set priorities going forward?

MARC PARENT: Let me take a couple of those, if I could, Ben. I think if I just go back to the acquisitions, if I take the biggest one, which arguably has the biggest impact, Oxford. I think one thing I think is worth saying now that the consolidation that’s happened in our industry has come
to light in the last few months there, the thing that was missed, and part of that is us not talking too much about it, was the fact that the Oxford acquisition, there was a defensive nature to it, which was strong... is a strong motivation to do that. What we did in that business, by acquiring Oxford, is we were able to acquire and gain a strong leadership position in training, and arguably consolidate the only remaining business in training of any size where somebody wanted to get in the business could have acquired. And at the same time because of our simulator training business and our flight schools, we could bring the most synergies to such a buy, by far.

That being said, I mean in the end of the day you got to make money, and I think as you see our margins in training, as we're saying, they've been improving sequentially every quarter in the... if I look at combined civil over the past, certainly this year, and it will continue to trend higher. And as we've looked about the capital intensity of the business, I mean, we have over the past few years invested to create the network that we have today, which is now the most globally diverse training network that exists. And that's important because inherently commercial aviation is... it's a local business. And that gives you competitive advantage. The same way we've invested price significantly to emerging markets, which has given us quite a nice position in those markets. So you just look at the amount of
simulators that we’re selling in those markets gives you an idea of the success we’ve had.

Coming back to our capital allocation… I think we’ve said our priorities, Stéphane has stated our capital allocation priorities, and they continue to be the same. They haven’t changed over the past… better part of a year now as that the capital is going to continue to sustain growth.

Now having said that, with all the capital that we’ve deployed and the leadership position we’ve established, if all things being equal, I would expect the business to be less capital intensive going forward, certainly the training business, which is the business which has the bulk of our capital. So going forward we should be less capital intensive. If you look at just this year, what we’ve pointed out – and we haven’t changed our outlook on that – is that our capital deployment will be similar to last year even though our revenue’s going up. So you can see some measure of capital intensity going down.

Our second priority was to increase for cash returns for shareholders, and again, I think you saw last quarter we’ve increased the dividend for the third time in the last three years.

And finally, our last priority has been to deleverage. And again, I think that we’re seeing our capital ratios trending in a right direction. We were at 50 per cent net debt to capital after Oxford. We’re now at what…
STÉPHANE LEFEBVRE: Thirty-nine per cent net debt to cap. So it’s decreased just slightly below the target that we had initially, the 40 per cent we had initially given ourselves actually in the last quarter, so a year after the acquisition of Oxford.

MARC PARENT: So in summary of all that, I think roundabout way, but I think the return on capital is a target, it’s part of the management incentive compensation in a big way, and that it’ll improve as we grow earnings and ramp up those new investments.

BEN CHERNIAVSKY: But I guess it’s… the short answer is no big changes to strategy? Is that a yes or a no? Like there’s no acknowledgement here that… Well let me ask it differently. Would you have done anything, looking back – recognizing hindsight is 20-20 of course – would you have done anything differently in the last five years?

MARC PARENT: Oh, there’s lots I would do differently and in no particular order, but as you say, hindsight is 20-20, and I’m only looking forward. And our strategy hasn’t changed in the light of how we run our overall business. And I talked to you about… we’re going to continue to invest in growth. Primary growth there is in support of our network. That’s not going to change. Investments in R&D. We still… nearly 10 per cent of our profits into R&D, which I think is important to maintain our technological edge. And I think that notwithstanding, clearly we’ve seen the Oxford
acquisition, to a large extent, has dragged our return on capital, plus the capital.

As I said, as we invest less capital, less capital intensive, and frankly, I don't think we've talked about acquisitions in any big way and it's because we're not focused on that. We're focused on getting the juice out of our business. So I think as we see the next few quarters, I would expect that our strategy will be paying off. I mean, we've been largely pre-funding growth for the last few years.

BEN CHERNIAVSKY: Yeah. And everyone's been sort of waiting for the returns. And I guess what you're saying is you're starting to see them now.

MARC PARENT: Yes.

BEN CHERNIAVSKY: Except in new core markets. I mean, that's another big... that was another big one in addition to Oxford, right, where you spent a lot of money.

MARC PARENT: Yeah, about $100 million. You're right. Yeah.

BEN CHERNIAVSKY: So no more acquisitions there, in that... in those (inaudible)?

MARC PARENT: Well, what we said is... what we've said is that we don't foresee any large acquisitions or any sizeable acquisitions in our radar scope right now. If we acquire some it would be probably to seek
particular niches in certain areas, products, and it could be in new core. But it’s not going to be…

As I said, largely acquisitions are not something we look at. And the only exception I would make there is always if opportunistically somebody in our space became available and it would help us as the industry consolidates, that’s something we would look at. Arguably you couldn’t do it in the civil side because civil side we have a strong leadership position and not much more we can do there. And you could do it on the military if something came up.

BEN CHERNIAVSKY: Okay. Thanks very much.

MARC PARENT: Thank you.

OPERATOR: Thank you. And we’ll get to our next question is from the line of Anthony Scilipoti from Veritas Investment Research. Go right ahead.

ANTHONY SCILIPOTI: Thanks very much. Maybe my question would be a follow-on from Ben’s somewhat. Maybe if we look forward, Marc, we can say what is it that… you’ve had great, I think, if you look at all the segments, the book to bill has been strong and improving and yet we haven’t seen sharp increases in revenue in general. So I’m wondering when is this – maybe that’s the key to answering your question there – is when is this backlog going to turn into revenue, over what sort of period, and what
margins can we expect? I mean, you know what you sold, and you know the price and you’ve probably hedged out the costs, so you have a good inclination of what the margin’s going to be. So maybe you can answer the question that way, if I can suggest, and that might give us some clarity on where the business goes going forward. Thanks.

MARC PARENT: Well I think a lot of where – thanks, Anthony. A lot of the revenue hike coming out of these record orders will come out of, clearly, the civil business and in terms of both products. And products, we put that… we see that in SPC. I mean, really what you’re seeing there is that the record order intakes that we’ve had has not really gone through our backlog. Part of that is because we’ve been executing over the last few years a number of programs, which are going to deliver not over one year but over… they were development programs, they were programs that were ordered now, but only going to be delivered in three, four years. So you’re not seeing the ramp up. You’ll start to see it. You’ll start to see it.

I would expect that you’re going to start see it in a more material way in Q4. And you’ll be seeing even more material as the next few years… sorry, next year, all the quarters next year will fold out. I mean, it’s for sure that you’ll see some consistently stronger quarters there, which is normal. Typically an order on the sim product side typically takes a month… a year
to 18 months to go through our... from backlog to revenue, typically. I mean, development programs take longer, and that’s what you’re seeing there.

On training side, well it’s really a question of higher utilization in our training centres, and bedding down all these simulators. That’s going to continue to rise in the Q4, and as I mentioned, my margin expectations in that area.

Military, harder to predict. I mean what we’ve shown I think is that this business is definitely not going off a cliff. It’s resilient. And we’re still going through a period of time where it’s been difficult in military getting clarity. We’re getting more clarity now.

Our bidding, as I said, our bidding year to date is higher than we’ve had all of last year. And it’s not that we’re enlarging our net that much in terms of what we’re bidding on. And as I’ve said before, we don’t bid on them in the military until we feel pretty confident that we can win because it costs so much to bid on the military. So I would expect that you will see a growth business in that area.

ANDREW ARNOVITZ: Operator, thanks very much to all participants on the investor portion of the call. In the interest of giving some time to members of the media, I would ask that you please now open the call to members of the media.
OPERATOR: Absolutely. And ladies and gentlemen, once again on the phones for the press and media, you’d like to register a question you can press the 1 followed by the 4 on your telephone keypad.

And we do have a question queued up from the media side is from the line of Ross Marowits with Canadian Press. Go right ahead.

ROSS MAROWITS: Yeah, just wanted a follow-up on the bidding in the military. Are you expecting a higher success rate or just that you’re bidding more and therefore you’ll get more as a result of that?

MARC PARENT: Mainly because we’d be bidding more. And we’re expecting that our win rate will be similar. I think between the combination of bidding, bidding more and... I think that’s the lion’s share that we would expect.

ROSS MAROWITS: And are you seeing... Sorry.

MARC PARENT: Yeah, go ahead?

ROSS MAROWITS: And are you seeing more competition in bidding?

MARC PARENT: Yes, we are. I think the fact that our business is simulation-based training, which is a nice solution in the time of budget cuts, where simulation... typically you could do simulation-based training for an aircraft at about 10 per cent of the cost of training on a real aircraft results from the fact that it’s very attractive as budgets are being cut. So this is an
attractive segment of the market, and if anything’s going to grow in this kind of environment, simulation-based training likely will. And inevitably that attracts more competition.

ROSS MAROWITS: Thank you.

OPERATOR: Thank you very much. And once again for the press and media you can press the 1-4 on your telephone if you can register a question.

ANDREW ARNOVITZ: Operator, if there are no other questions from members of the media, I wish to thank members of the investment community and the media for their participation on this afternoon’s call. And I’d like to remind you that a transcript of today’s call will be made available on CAE’s website at CAE.com.

Thanks again.

OPERATOR: Thank you very much. And ladies and gentlemen, that does conclude the conference call for today. We thank you for your participation and ask that you disconnect your lines. Have a good day, everyone.

* * * * *