Operator: This is Conference # 80797245

Our first question coming from the line is from Steve Arthur with RBC Capital Markets. Please proceed with your question.

Steve Arthur: Great, thank you. I guess I'll just start up with Civil margins in the quarter, revenue is quite strong obviously, but 13.7 percent is a little bit below anything we've seen for a while. I do understand that's similar to the normalized rate of last year, but I guess, was there anything specific that happened in the quarter that weighed on these margins or is that just kind of what we should expect on Q2-type utilization levels?

(Marc): I mean I'll start it off, Steve. It's (Marc). I think we stick with, you know, the four-year outlook that we've given the higher average margins that we saw last year at Civil. I think there are a number of factors that occurred in the quarter itself, maybe just go through those factors, (Stéphane,) for Steve.

(Stéphane): Yes. So I think we saw some good and interesting increase in revenue and that it came from both the service and the product businesses that we have. You've seen the factors for the increase in revenue from our service business. We've got more utilization and the number of (ACUs) is also up and that typically generates good margins.

There was also quite a significant increase in our product business, but dilutive to our margins for a number of reasons. The first thing is when I look at the composition of the backlog that we've executed in the quarter, Steve, the
mix was not as favorable as it was in the same quarter last year. So we have a few development programs that require some more R&D effort. I think you can see as well on the P&L there's an increase in the R&D. It doesn't all come from the Civil business but there was quite an increase in R&D and Civil which are typically development costs for certain programs.

The other thing that I'll mention is that we've continued to progress our process improvement program, but it's been quite disruptive to the operations during the second quarter, especially last – this summer where we've changed the layout of our shop floor here in the facility in Montreal, so we lost some productivity there. So it puts some pressure on the margins on the product side of our business.

But so overall, I think hopefully people will recall last year in the same quarter, we've had a one-time tax gain in one of our joint ventures. So, we generated 14 percent normalized margins last year. So we're at similar margins, but on higher (revenue). And I think with what (Marc) said, we're subtracting for our margin guidance for the year.

So, is it fair to assume that these are all short-term things and no change for the year and trending towards the upper teens over the next number of years, I would say.

Well, I guess we haven't gone that far, I think, Steve. But I think what we've said that's management outlook is that there's really no change to what we've said, maybe a little bit more precision, will be higher than the average. I think we're about 16.3 for the full year as a whole in Civil and certainly what we see is like – what we saw this quarter when you normalize it, therefore, the one-time last year, double-digit (SOI) growth for Civil for the year for sure.

OK. Thanks a lot for the color.

Thank you. Our next question coming from the line of Cameron Doerksen with National Bank Financial, please proceed with your question.

Yes, thanks. Good afternoon. I just want to just follow up on the Civil business, I'm just wondering if you can talk a bit about the competitive
environment there and specifically overseeing from pricing in the full-flight simulator business especially with a couple of the sort of newcomers to that market being fairly aggressive in the past couple of years.

(Marc): Well I think Cameron, to your question, I think the environment is pretty much the same as it has been. I think it's pretty much of a status quo. I mean these are neither worse nor substantially better. It's per the expectations or the assumptions we've had.

I mean as (Stéphane) said, if you look at the quarter, there's a number of factors that affect our margins and one of them is price competition. It is not unexpected, so we look at year-over-year. I think that we're seeing some of that in products. But I think it's fairly stable and again that's factored in to the outlook that we've given.

Cameron Doerksen: OK, thanks very much.

Operator: Thank you. Our next question coming from the line of Turan Quettawala with Scotiabank. Please proceed with your question.

Turan Quettawala: Yes, good afternoon. Sticking to the Civil side, I guess, (Marc), if you look at some of the recent order flow for the OEM, I think there's a bit of a slowdown on that front. I know your products, there's more to delivery here, but obviously that will have an impact as well on that over time. I'm just wondering how confident are you about your order flow on the success side over the next two years? You obviously have about two years of peak overflow here.

(Marc): Well as you know, Turan, we don't ever go given the outlook beyond this, the full year. We're certainly confident with the full year. You saw that 16 simulator (orders) in the quarter is, I think, the highest we've ever seen in Q2. That certainly looks well for our outlook that we've set for simulator sell as a whole.

From a macro going out a few years, not to give you guidance, but as you've said, it's the function of deliveries out of the major manufacturer which of course, we know who they are.
And the ratios haven't really changed and the fact of the matter is, I mean, as the thing in my remarks, I mean, you look at certainly the OEMs themselves are speaking with their delivery rates and their production rates, the AirBus announced that they're going up to 60 aircraft a month on the A320.

And I know, you know, having in the early part of my career, 20 years, you don't increase production rates unless you're pretty darn sure that you'll be able to maintain them because it's extremely costly to go the other way. So, I mean to me, that's a strong testimony and certainly the OEMs themselves think that this backlog and supporting delivery rates will last for quite a long time which, of course, supports our business.

Turan Quettawala: Great. Thanks, helpful. Thank you.

(Marc): Thank you.

Operator: Thank you. Our next question coming from the line of Benoit Poirier with Desjardins Securities. Please proceed with your question.

Benoit Poirier: Yes. Just with respect to your backlog, it’s up (70) percent. I was wondering if you could provide more color, how much is driven by the FX and especially on the military side what is the split between – is there a big change in the mix between equipment and services. Thank you.

(Stéphane): Yes. Benoit, I think, it's (Stéphane), I'm just looking at this because we do disclose in the MD&A the adjustment that we put in, in defense for the FX.

I think one reason why you are asking is we've also included the adjustment for the (BMAT) acquisition and so I'll just pull out the assessment for FX and I will get back to that in a second.

Benoit Poirier: OK, thank you.

Operator: Thank you. Our next question coming from the line of Kunal Gupta with Macquarie. Please proceed with your question.
Kunal Gupta: Hi. Good afternoon. My question is on – sorry, actually a clarification before the question, on the Civil margin. So, the no change in guidance for the full year basically implies pretty solid margins in the second half of this year versus last year, right? So, and that's not driven by any sort of one time impact so that you could potentially have.

(Marc): No, no. I mean if you look at our seasonal pattern on a full-year basis, we tend to have a stronger second half, driven – a couple of reasons. One, I think the biggest one is that fact that you tend to have a higher training in the second half because it's typically the winter months and that's where airlines specifically train the most and also, you know, as the fourth quarter is also a big quarter for business aviation training where they attend the training in the early part of or late part of the winter, in the February, March. And that explains why you have, you know, more training and therefore when you have more training of existing assets, well that translates into better margins, obviously, a better bottom line.

So the other thing that plays into that sort of extent is what we've just experienced is we have our summer shutdown that affects manufacturing which is sort of products business. So all in all, that's why per – what we've seen in previous year, we see a stronger half not driven by anything else, but the normal business and the higher – the higher product and the product sales that we've had and the higher sales that we have in the service business.

Kunal Gupta: OK, thanks. So on the Defence side, (Marc), I was just wondering, the book-to-bill ratio or the book-to-sales has been improving quite a lot and obviously you are now above (one) trading 12-month basis. So what's exactly happening on that side and what are you hearing from the US Defence guys given the 2016 fiscal year is underway now?

(Marc): Well, I think it's better than it was. I mean, with these – I don't think the government – I don't think nobody wants to make this on either part of the floor in the US, to make this defense and election issue.
I don't think – hopefully, we're not going to be hearing sequestration again for a little while. We have continuous resolution. So it's pretty much of a quasi-normal kind of environment.

So what we're starting – what you're seeing is. I think, the fruit of all the bidding activity that we've done over the past few years. You know, we've been talking for, I think more, closer to three years now. But this backlog, this bow wave of proposals that we've been writing and really what – and in those backing up the step, we don't typically write proposals on the military side unless we feel pretty good about our chances of winning because it's extremely costly and time – both in terms of the time and money to bid on military contracts because of the very detailed requirements.

So the fact that we've had this bow wave, this large bow wave now reach up to 2.8 billion of proposals out there, what we did not control and which is affected by government vagaries here that we've been talking about is when they actually get attributed.

So now we're seeing a little more regularity about these contracts being attributed and we're seeing it come through. And that's why you see this order intake coming through and you also see some larger contracts, which is testimony to our strategy of going after big training services integration contract.

These are the factors we're seeing and as I said in my outlook, I mean that's factoring for our outlook for modest growth this year. You know, you start to see the book-to-bill above one on a 12-month basis which is the better way of looking at it because you know quarter-to-quarters can vary.

And our – the bidding activity continues. It's this largest – we have a large proposal, you know, quantum as we've ever had, so I feel pretty good as I've said for quite a while here that Defence is a (growth) business for CAE, but we don't control when things get attributed, so we'll continue to watch what the government does.

Kunal Gupta: Perfect. Thank you very much.
(Marc): Sorry, before we take the next question, (Stéphane), you want to respond to your earlier comment on that?

(Stéphane): Yes. Benoit had a question on the impact of the section, the backlog for the Defence business. The FX is about 77 million of the 460 million adjustment that we see in our Defence backlog, so the rest is really the acquisition of the BMAT backlog that we close in the quarter, so 77 million of FX.

I think another second part of this question was on the service part, I just want to know the fact that the – most of the unfunded backlog in defense which is 755 million is service-based and we get a lot of new orders in service especially we've been approved from the training service integration strategy that we proposed. So we get more, a bigger share of training and services contract than we've had in the past. And most of the unfunded backlog is service-based.

(Marc): Operator, we'll take the next question.

Operator: Thank you. Our next question coming from the line of David Tyerman with Canaccord Genuity, please proceed with your question.

David Tyerman: Yes, good afternoon. My question is on Civil sale side, there was a pretty nice tick up in the sales in the quarter, quite a bit above my expectations and I think the consensus also. So I'm just wondering how much of that was foreign exchange and then whether there were any unusual things in there that might have caused the quarter to be a bit higher than normal?

(Stéphane): I mean, not so much on the – nothing unusual on the revenue side, David. For the company as a whole, the translation of our foreign operations into Canadian dollars gave us above 40 million of top line. And of course, it's spread across all the different business units. I think I did the math even stripping out the FX impact for Civil, we'd still get close to 10 percent revenue growth from Q2 of last year and so, pretty substantial.

David Tyerman: OK, thank you.
Operator: Thank you. Our next question coming from the line of Sami Hazboun with Investors Group, please proceed with your question.

Sami Hazboun: Good afternoon, gentlemen. I want to follow up on the R&D expenses having you see it ticked up year-over-year in this quarter. In actual fact, they're up 32 percent year-on-year for the year to date. Should we expect that pace to continue or should it abate as we go forward with the year?

(Stéphane): Well, there's been quite a lot more of R&D in the year. I mean part of it is the process improvement projects that we've undergone. A part of it is also some – I've talked about it in the first quarter results, from the Defence side, we're incurring more development cost than we've had in the past and the other part is really specific Civil programs that we've undertaken as well that require some R&D.

So in total and even if you include the deferred development cost and capitalized cost, you will see some increase in R&D over time going forward.

Sami Hazboun: And if I may, related to the process improvement as it would impact SG&A, it's not disordinately increased versus sales, but should we expect a benefit to SG&A as well as a result of the process improvement?

(Stéphane): You know, there will be. I think we've talked about it in the first quarter. The benefits really we'll start seeing it more in the second half of next year once the program is completed, but there will be some benefit on the G&A line as well.

Sami Hazboun: Thank you very much.

Operator: Thank you. Ladies and gentlemen, as a reminder, to register for a question, please press the one followed by the four.

Our next question is a follow-up question coming from Benoit Poirier with Desjardins Securities. Please proceed with your question.

Benoit Poirier: Yes. Just coming back on your free cash flow, there was a nice recovery in the working cap. I was just wondering what are your expectations for the
second half and also if you could elaborate on your cash deployment opportunities given your net debt to cap improved a lot in the quarter.

(Stéphane): Yes. We're pretty pleased with the performance in this quarter on cash, working cap, Benoit. I keep seeing some improvement in the day sales outstanding, so this is always a good sign. It seems that our collection is pretty good.

Inventory is down and the order – volume of order intake, it seems that we sold in the quarter where typically we get some down payments from customer also generated some good cash flow. So we're pleased with where we are for the first half of the year.

I think I've said in the past, we still see some investment in non-cash working cap needed for the year as a whole as we get more service-based business. What I see so far and I'll keep the same guidance as I have said in the past, I think we'll see an investment in non-cash working capital lower this fiscal year than what we have last year.

Benoit Poirier: OK, that's great color. And on the Healthcare side, you grew revenues by 5 percent year-over-year, you are still confident to grow double-digit this year. So, how much is in the backlog right now or what we should expect in the second half in order to meet the double digit, (Stéphane)?

(Stéphane): Yes, we still see some – I mean we're with the guidance that we've given for Healthcare as well, double-digit growth. Quite frankly, was expecting a little bit more revenue in this quarter. For Healthcare, we've got some orders that we were just not able to fulfill in September and that slipped through the third quarter. So you can expect a stronger H2 in healthcare and we really see double-digit growth as we guided since the beginning of the year.

Benoit Poirier: OK. And – yes.

(Marc): Sorry, Benoit, I was just going to come back on the thought – I was just going to come back to what you are saying for use of our cap, use of our capital there or free cash flow. Our capital allocation priorities haven't changed.
I mean we've always said and we'll continue to say that we're going to be – we'll continue to look for growth and we see growth opportunities, but in terms of our outlook for CapEx has changed. This is the one we've given 100 million for the year and we're tracking to that.

But we keep our eyes open for investment opportunities that are accretive to returns in investment capital in a relatively rapid fashion that includes, you know, we could do some outsourcing of training centers, that kind of opportunity. So, we all constantly look for that. So that would be number one.

Plus we'll continue to invest and that's part of our CapEx guidance into simulators to grow our network, again business aircraft or, you know, supporting our joint ventures, things like that. Second priority is continue to leverage. And you've seen us do that, you know, I think quite handily in the quarter again. And finally, you know, continuing cash returns for shareholders and I think our dividend story continues to be coincident with that or a consequence of that, I would say.

Benoit Poirier: OK. That is very good color. And last one just in terms of product needs for Healthcare, it seems that it was the main reason for the margin. So could you elaborate a little bit on the product mix impacting margin in healthcare?

(Marc): I think two things I would say, really, we sell a whole host of kind of products in our healthcare division and depending on – and what I'm talking about there is you have a whole series of different types of mannequins not all run at the same margins. So depending on which ones you sell in that quarter will dictate the margin mix.

The same thing for other types of products like our intervention simulator which are essentially surgical simulators, services will do for OEM. So all of that is what you see. So you would expect – and I think you'll continue to expect some differences depending on the flow of product mix we have in the quarter. So I think that really explains the story.

Plus the other fact is that we continue – I mean, we're not at the end of this business. Clearly we want to get to a larger business here, so we'll continue to
invest in SG&A and R&D to make this a larger business. So I think that in itself contributes a little bit as well.

Benoit Poirier: OK, thank you very much for the time.

Male: Benoit before you go, I think (Stéphane) has a clarification on …

(Stéphane): Yes, I just want to clarify a response that I gave I think to one of the questions on the impact of FX on the Civil business on the top line, the increase over Q2 of last year FX neutral would have been 18 percent. I gave another number, but it's actually 18 percent, not 10 percent. Sorry for the confusion there.

Benoit Poirier: Right.

Operator: Thank you. Our next question is a follow-up question coming from the line Kunal Gupta with Macquarie, please proceed with your question.

Kunal Gupta: Hi, guys. It's a follow-up question. One is on the written on capital employed by colleague segment. I'm just kind of doing a quick math on the segment, Civil and Defence and using basically the EBIT or segment of an income and dividing that by the capital employed number that you kind of provide.

So to me, it sounds like the Civil return on capital is pretty stable this year versus last full year, but there seems to be some decline in the Defence return on capital. So, am I reading that correct or is there something else I should be factoring in?

(Stéphane): Yes. The way we look at it is we look at the return on capital employed pre-financing but after tax. And if I may, while we're talking about it, we've got – we've reported 11 percent (inaudible) for the quarter. And so it's improving compared to the 10.3 percent that we've had in the first quarter, so it's trending in the right direction.

As far as the trend for the Defence business along, I wonder if there isn't any temporary distortion from the (BMAT) acquisition, but I'd have to go back and check, you know, maybe the case, but there's nothing that comes to mind right now. Which specifically, which quarter are you looking at?
Kunal Gupta: No. I was just looking at the second quarter. I'm looking on the trailing 12-month basis basically, so I'm taking the trailing 12-month EBIT dividing that by average capital employed, so.

(Stéphane): Yes. One thing is we got a lot of our capital employed in defenses US based. So I'm sure that the fact that we translate in capital employed in Canadian dollars, I'm sure that it had a quite significant impact on the capital employed, so that's what I can think of.

Kunal Gupta: OK, that makes sense. OK, thank you.

(Stéphane): But there's nothing else, yes.

Kunal Gupta: OK, thank you. And quickly on the second question is on the Healthcare side. So, I understand and I can see how Healthcare can actually grow double digits year-over-year on the revenue side, but what are your thoughts on the margin profile for this year as well as next year? Should we expect a meaningful improvement in margin this year and similarly next year or will that be somewhat sort of muted?

(Marc): Well, we haven't given any for next year, but I think what we've said is certainly double-digit growth in revenue which I mean should translate into pretty good margin pick-up at the bottom line. I mean that's as far as I'll go for this year.

Kunal Gupta: OK, thank you.

Male: Operator, we do want to keep the last minutes of time allotted for members of the media, so we'll draw to a close the Q&A session for investors. I would remind the analysts and investors on the line, if you have any follow-up questions or we haven't responded to your questions, please do follow up with me after the call.

And if you would now please open the lines to members of the media.
Operator: Thank you. For the media, if you would like to register for a question, please press the one followed by the four on your telephone. Once again, it is one followed by the four. One moment, please.

There are no questions from the media at this time.

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