REMARKS FOR CAE'S FIRST QUARTER FISCAL YEAR 2023

August 10, 2022

Time: 1:30 p.m.

Speakers:

Mr. Marc Parent, President and Chief Executive Officer

Ms. Sonya Branco, Executive Vice President, Finance, and Chief Financial Officer

Mr. Andrew Arnovitz, Senior Vice President, Investor Relations and Enterprise Risk Management

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Good afternoon, everyone, and thank you for joining us today.

Before we begin, I'd like to remind you that today's remarks, including management's outlook and answers to questions, contain forward-looking statements. These forward-looking statements represent our expectations as of today, August 10, 2022, and accordingly are subject to change. Such statements are based on assumptions that may not materialize and are subject to risks and uncertainties. Actual results may differ materially, and listeners are cautioned not to place undue reliance on these forward-looking statements. A description of the risks, factors, and assumptions that may affect future results is contained in CAE's Annual MD&A available on our corporate website and in our filings with the Canadian Securities Administrators on SEDAR at www.sedar.com and the U.S. Securities and Exchange Commission on EDGAR at www.sec.gov.

On the call with me this afternoon are Marc Parent, CAE's President and Chief Executive Officer, and Sonya Branco, our Chief Financial Officer.

After remarks from Marc and Sonya, we will take questions from financial analysts and institutional investors. Following the conclusion of that Q&A period, we will open the call to questions from members of the media.

Let me now turn the call over to Marc…

Marc Parent, President and Chief Executive Officer

Thank you, Andrew, and good afternoon to everyone joining us on the call.

We had a mixed performance in the first quarter, with Civil delivering results in line with our view for strong annual growth and increased market share momentum. Defense results were disappointing; however, coming in well short of our expectations. The shortfall was mainly due to unanticipated discrete charges on two of our legacy programs, and the increased intensity of the defence-sector-wide headwinds we're facing in this early stage of our multi-year growth journey. We'd already factored into our prior outlook that the second half of the fiscal year would be stronger than the first, mainly because we're still working our way through the lag effects of a protracted period of less than one book to sales -- and it takes time for new program awards to ramp up. We also expected some of the additional headwinds in the first half, but they were significantly more acute than we thought they'd be.

Order activity is the best indicator of our future growth, and despite a challenging global environment, for CAE overall, we secured over $1 billion in orders for a record $10 billion backlog and 1.12 times book-to-sales ratio.

In **Civil**, we made excellent progress converting our large opportunities pipeline into $522 million of orders for a 1.09 times book-to-sales ratio. These include long-term training agreements with airlines and business aircraft operators, and 11 full-flight simulator sales. Notable training contracts for the quarter involve several exclusive training agreements in the Americas, which add to a long list of exclusive training agreements Civil has signed in the last year-and-a-half with the vast majority of major airlines in

the region. This quarter, they include a three-year extension to a long-term exclusive aviation training agreement with Mesa Airlines, a five-year exclusive training agreement with United Airlines, a five-year exclusive training agreement with JetBlue, and a ten-year exclusive training agreement with another major North American airline. In the U.K., Civil expanded its existing 12-year exclusive commercial aviation training agreement with Virgin Atlantic to include the Boeing 787 platform, now covering all their existing aircraft platforms under the training exclusivity. In business aviation, Civil concluded a pair of three-year training agreements with Tag Aviation Holdings, and the NATO Support and Procurement Agency.

Civil's year-over-year financial and operational performance was also strong in the quarter with double-digit growth in training revenue and adjusted segment operating income. We delivered ten full-flight simulators and first quarter average training centre utilization was 71%, up from 56% last year. Training demand in the Americas continued to be strongest, followed by a much-improved Europe, and a still lagging Asia Pacific, which remained at a much lower level due to travel restrictions. In business aviation, training demand continued to be robust, reflecting a sustained high level of business aircraft flight activity.

Now turning to **Defense**, we booked orders for training and mission support solutions valued at $488 million for 1.18 times book-to-sales. Although we were expecting some key orders that pushed rightward this quarter, this represents a record-level order intake for Defense in a first quarter. We normally see some variability in quarterly Defense results and so performance is best evaluated on an annual basis. To that point, our trailing twelve-month book-to-sales ratio of 1.31 times is a good indication of the trend in order momentum.

We continued to build on that momentum in the quarter, winning orders across all five domains. In the air domain, we entered a contract with the Netherlands Ministry of Defence to provide a training system in support of the Joint NH90 Training Program. In Land, the US Army Synthetic Training Environment Cross Functional Team (STE CFT) awarded CAE a task order to develop a Soldier Virtual Trainer Prototype with immersive capabilities that empower Soldier-led training at the Point-of-Need. In the sea domain, in partnership with Lockheed Martin, we were awarded a design support contract on the Royal Canadian Navy's next generation frigates. In space, we were awarded a contract from US Air Force Research Lab, as part of the STAR-FISH initiative, to develop prototype software that enables simulation of current and future capabilities operating across a multi-domain environment. And in the cyber domain, as part of a larger team, we secured a position on the approximately $1 billion ACT 3 - ID/IQ contract vehicle.

While Defense's order activity was generally positive in the quarter, financial performance was clearly not. The loss incurred of $21.2 million was driven mainly by unanticipated charges on a legacy CAE training program with the U.S. Navy and a legacy L3H MT classified U.S. program. These discrete charges totaled $28.9 million and result from our reassessment of cost estimates, following discussions with our customers this past June. The reassessments are due in part from, delays and meeting customer requirements on scope and timing, as well as a change in expectations for the expansion of the program requirements. In the case of the US Navy contract, customer utilization trends have exceeded our estimates, resulting in cost growth on a firm-fixed-price contract — and our expectations for contract adjustments and extensions, at more favourable terms, have changed. The program in question is the Chief of Naval Air Training (CNATRA) with Contract Instruction Services (CIS). CAE provides classroom and simulator instructors at five Naval Air Stations (NAS) to support primary, intermediate, and advanced pilot training for the U.S. Navy.

The second charge stems from a classified U.S. program that's also structured on a firm-fixed-price basis and involves the initial phases of a large, long-term opportunity. The program is a complex national defence priority, and our current work positions us well to capture significant future opportunities on the program. Given the nature of the work, which is performed in close quarters, COVID-19-related staff shortages of cleared professionals has been highly disruptive to the program's schedule. In addition, logistics and shipping costs, which are significant for this contract, increased our estimated cost to complete. After a re-baseline review of the program's critical schedule elements and deliverables with the customer in June, the costs to complete were revised upwards. Due to the critical nature of the program and the strategic long-term value it holds for CAE, we are working toward meeting our commitment to the customer and positioning Defense for future work. I'd add that while we're hopeful that the customer will work with us in the future for equitable adjustments that can help to offset some of the charges taken this quarter, at the moment, we haven't included any of those in our expectations. I'd also add that we have a clear understanding of the specific issues that resulted in the charges taken on both programs. After thorough analysis we consider that these provisions capture adequately the expected cost overruns and I'm confident there are no more negative surprises like this in our backlog.

Beyond the two program charges, Defense performance was still well below our expectations for the quarter. Across the company we've been managing through labour and supply chain challenges that have been consistent with what we observe in the broader economy. However, in Defense these challenges were more acute, as sector-wide staffing shortages led to less billable work on cost-plus contracts and inefficiencies on other work. Supply chain challenges were also more severe than anticipated, which pressured schedules. We also experienced delays on a few key orders we were expecting to commence work on in the quarter. Excluding the charges and the impact of these additional

challenges, Defense performance would have been more consistent with our expectations and the full year plan, which also considers a more elevated level of bid-and-proposal costs, as we pursue several large awards that are in our pipeline.

Finally, in **Healthcare**, we continued to drive double-digit revenue growth with our innovative solutions. Healthcare's leadership transitioned from Heidi Wood during the quarter. We're grateful for her contribution and wish her well in her future endeavors. Healthcare is now being led on an interim basis by Jeff Evans, who was formerly head of sales and has been instrumental in driving the business's extended period of double-digit growth.

Notable during the quarter, Healthcare expanded its strategic relationship with the Mayo Clinic College of Medicine and Science, finalizing a partnership for its LearningSpace centre management solution for its simulation centre in Rochester, Minnesota. Healthcare also increased its presence and visibility in the U.S. through efforts supported by CARES Act funding and Mon Health hospital system, to address West Virginia's increased demand for nurses with the deployment of mobile training units.

With that, I'll now turn the call over to Sonya who will provide additional details about our financial performance. I'll return at the end of the call to comment on our outlook. Sonya?

Ms. Sonya Branco, Executive Vice President, Finance, and Chief Financial Officer

Thank you, Marc, and good afternoon, everyone.

Consolidated revenue of $933.3 million was 24% higher compared to the first quarter last year. **Adjusted segment operating income** was $60.9 million, compared to $98.4 million last year. And, quarterly **adjusted net income** was $17.6 million, or 6 cents per share, compared to 19 cents in the first quarter last year. This quarter's results include $28.9 million in unfavourable contract profit adjustments in Defense, which equates to a 7 cent negative EPS impact. We incurred restructuring, integration and acquisition costs of $21.5 million during the quarter, including $16 million related to the L3H MT and AirCentre acquisitions.

Net cash provided by operating activities this quarter was negative $162.6 million, compared to negative $129.1 million in the first quarter of fiscal 2022. **Free cash flow** was negative $182.4 million compared to negative $147.6 million in the first quarter last year. The decrease was mainly due to lower cash provided by operating activities. The decrease was partially offset by a lower investment in non-cash working capital. We usually see a higher level of investment in non-cash working capital accounts during the first half of the fiscal year and tend to see a portion of these investments reverse in the second half.

Growth and maintenance capital expenditures totaled $73.9 million this quarter, mainly for growth, and specifically to add capacity to our global training network to deliver on the long-term exclusive training contracts in our backlog.

Income tax recovery this quarter was $0.5 million, for a negative effective tax rate of 16%, compared to a positive effective tax rate of 18% for the first quarter last year. The income tax rate was impacted by restructuring, integration and acquisition costs this quarter, and excluding these costs the income tax rate this quarter was 21%, which is the rate we used to determine adjusted net income of $17.6 million and adjusted EPS of $0.06.

Our **Net debt** position at the end of the quarter was approximately $3.0 billion, for a net debt-to-adjusted EBITDA of 4.15 times at the end of the quarter. The more elevated debt ratio this quarter reflects the impact of the two non-cash charges in Defense. We continue to expect net debt-to-adjusted EBITDA of below 3 times within the next 15 months.

Now turning to our segmented performance...

In Civil, first quarter revenue was $480.4 million vs. $432.9 million in the first quarter last year and adjusted segment operating income was up $16.9 million over the first quarter last year to $86.6 million, for a margin of 18.0%. Our Civil performance reflects a mix of higher training revenue in the quarter, offset by lower revenue from simulator deliveries, lifecycle support services, and a less favourable program mix. We also incurred higher R&D investments to support our innovation pipeline.

In **Defense**, first quarter revenue of $413.3 million was up 43% over Q1 last year due to the integration of L3H MT in our financials. Adjusted segment operating loss was $21.2 million for the quarter compared to an adjusted segment operating income of $23.7 million in the first quarter last year. The loss

this quarter was driven mainly by the aforementioned contract profit adjustments and more acute challenges than we expected, stemming from staffing shortages, supply chain pressures, and slower order awards. These additional challenges had an approximately $20 million impact on adjusted segment operating income. We also had higher SG&A costs for bids and proposals that were approximately $6 million greater than what we had in Q1 last year. The higher bid costs were expected, as they're linked to our pursuit of a larger opportunities pipeline, but they were more impactful given the other Defense headwinds.

And in **Healthcare**, first quarter revenue was $39.6 million, up from $31.6 million in Q1 last year. Adjusted segment operating loss was $4.5 million in the quarter compared to an income of $5.0 million in Q1 of last year. Last year's results included a higher level of investment tax credits, while this year we had a higher level of selling, general and administrative expenses to support growth.

With that, I will ask Marc to discuss the way forward.

Marc Parent, President and Chief Executive Officer

Thanks, Sonya.

As we look to the period ahead, despite the prevailing macroeconomic headwinds and added defence sector-related challenges, we continue to see a clear multi-year path to becoming a larger, more resilient, and more profitable CAE.

In **Civil**, our outlook is as bright as ever. We're in the early stages of an upcycle with near-record margins with plenty of room to grow beyond that. We've invested both organically and inorganically to expand our training network globally, leveraging our position as the world's largest Civil Aviation Training company. A greater desire by airlines to entrust CAE with their critical training and digital operational support and crew management needs, acute pilot demand, and strong business jet travel demand are enduring positives underpinning a secular growth market. The unevenness of the global recovery is likely to continue for some time, but we're ultimately in an excellent position to benefit from the multi-year cyclical market recovery underway. We continue to expect strong growth in Civil this fiscal year, driven by high demand for pilot training, as evidenced by robust full-flight simulator sales and the exclusive long-term training agreements we've secured in recent quarters with virtually all major airlines in the Americas. We're poised to continue growing market share from an expanded pipeline of Civil training opportunities, and I believe these successes provide a compelling blueprint for what a broader global market recovery holds for CAE.

In **Defense**, despite the additional challenges we encountered in the quarter, the positive long-term outlook we shared at our investor day in June is unchanged. We're on a multi-year journey to becoming bigger and more profitable, and the first and most critical link in that chain involves winning

orders. Our record order intake last year and for the first quarter, confirm that we are indeed on the right path to growth. And critically, the orders that we won over the last year-and-a-half bear a profitability profile that's consistent with our long-term view to returning to a low double-digit margin in Defense. Furthermore, our record $9 billion of Defense bids and proposals is the result of bidding *more* and bidding *larger*. An important element of our strategy involves strengthening our strategic relationships with OEMs and the Memorandum of Understanding we signed last month with Boeing is a great example of how the major OEMs recognize CAE's unique expertise in training. We agreed to expand our international teaming and supplier networks to provide solutions that support both customer and regional development.

The external environment for Defense remains largely favourable, with some near-term headwinds having become more acute, but we believe temporary. Current geopolitical events have galvanized national defence priorities in the U.S. and across NATO, and we expect increased spending and specific prioritization on defence readiness to translate into additional avenues for CAE to support our defence customers in the years ahead. Although somewhat counterintuitive, the immediate priority on operational needs is actually contributing to training program award delays in the short-term. Taking all these factors into consideration, we're lowering our expectations for Defense for the current fiscal year to account for the two U.S. program charges we just incurred, and to reflect the more acute, sector-wide headwinds we're now experiencing, namely supply chain pressures, labour shortages, and a slower defence contracting environment. We had previously indicated our expectation of a back-half-weighted performance in Defense this fiscal year, as we manage through the effects of a protracted period of less than one book-to-sales and begin to ramp up new orders in the second half. The additional Defense headwinds have made this weighting even more pronounced, and we expect them to largely continue into the next quarter and then gradually abate through the course of the fiscal year. As the year

progresses, we expect to be able to partially offset these impacts through new internal cost reductions and efficiency initiatives, currently underway.

And lastly in **Healthcare**, the long-term potential continues for it to become a more material and profitable business within CAE as it gains share in the healthcare simulation and training market and continues to build on its double-digit revenue growth momentum.

For **CAE overall**, we're reducing our outlook for the current fiscal year to mid-twenty percent consolidated adjusted segment operating income growth, from the mid-30s previously, which largely reflects our revised expectations for Defense.

We greatly enhanced our position and expanded our addressable market over the last couple of years, and I have complete confidence in our team's ability to maintain a strong order momentum and drive superior and sustainable growth and profits over the long-term. Broadly speaking, the underlying trendlines of our multi-year progress are very much intact, and my conviction in CAE's long-term growth outlook is resolute. As such, we continue to target a three-year EPS compound growth rate in the mid-twenty percent range.

With that, I thank you for your attention. We're now ready to answer your questions.

Andrew Arnovitz, Senior Vice President, Investor Relations and Enterprise Risk Management

Operator, we would now be pleased to take questions from analysts and institutional investors.

Before we open the lines, let me first ask in the interest of fairness that you please limit yourselves to a single, one-part question. If you have additional questions after that, and if time permits, please feel free to re-enter the queue.