Q1 04

quarterly report first quarter ended June 30, 2004

HÉROUX DEVTEK

message to shareholders

On behalf of the Board of Directors, I would like to take this opportunity to present the financial results for Héroux-Devtek's first quarter ended June 30, 2004.

The Company posted a net loss of $1.3 million or $0.05 per share for the period compared to a net loss of $818,000 or $0.03 per share for the first quarter last year. Sales during the first three months grew by 7.6% to $56.4 million from $52.4 million last year, due to the April 1, 2004 acquisition of Progressive Inc.

While we are indeed pleased that the acquisition of Progressive is providing the anticipated positive results, delays in deliveries are affecting our performance, mainly at the Landing Gear and Gas Turbine Components Divisions. This situation created a sales shortfall of $7 million in the first three months of the year. We are confident that the situation will improve through the balance of the year.

I invite you to read the enclosed Management Discussion & Analysis, but for your convenience, we also provide the following first quarter highlights.

- The $12.7 million in sales generated by Progressive was offset by a stronger Canadian dollar, which had an unfavourable impact of $2.3 million, as well as the sales shortfall mentioned above.
- The Company's Gas Turbine Components Division was awarded a $10.9 million order to produce components for use in the U.S. Air Force's F100 engine. Final delivery of all units is planned for February 2006.

Sector Results

Sales in the **Aerospace & Defence** segment increased 10.4% to $51.5 million compared to $46.7 million for the first period of fiscal 2004, due mainly to the acquisition of Progressive.

Sales for the Landing Gear military sector were down when compared to the last two years. Commercial Landing Gear sales slipped 5.4%, reflecting the ongoing slowdown in the commercial aerospace market. Aerostructure sales increased substantially on the strength of the Progressive acquisition. Growth in the Aircraft Engine Component sector, which represented an increase of 15.2%, was primarily due to last year's gain in market share. The 21.7% decline in the Defence sector sales arose from low demand in other defence products, with small arms product sales remaining stable year-over-year.

First quarter sales for the **Industrial** segment totalled $4.9 million, down 15.1% from $5.7 million in fiscal 2004. Industrial Gas Turbine sales remained low and were down 38.2%, reflecting the persistently weak market, while new parts manufacturing for a recently-added customer resulted in a significant increase in Other Industrial sales for the quarter.

Outlook

During the first quarter Héroux-Devtek continued to be affected by the economic and industry factors influencing our markets, as discussed at year-end. A recovery is still expected in the commercial aerospace market beginning in 2005, impacting on Héroux-Devtek's sales for fiscal 2006. The military aerospace market remains generally strong, with continued interest in unmanned aircraft vehicles ("UAV") and unmanned combat aircraft vehicles ("UCAV"), as well as other potential opportunities that could have an impact on the Company's fiscal 2006 sales. On the industrial side, the downturn in the power generation market continues and is expected to reach its low this year, with renewed growth beginning in 2005. The strength of the Canadian dollar continues to have a significant negative impact on Héroux-Devtek's results.

Our results for the first half of this year will remain under pressure, but we expect that our own initiatives and market conditions will lead to positive improvements through the balance of the year. As well, the Company continues to enjoy a strong balance sheet, which puts it in an excellent position to benefit from the current economic challenges.

I thank our shareholders for their continuing confidence and support. The management of Héroux-Devtek remains focused on the Company's growth and profitability objectives.

Gilles Labbé
President and Chief Executive Officer
July 29, 2004

Consolidated balance sheets

As at June 30, 2004 and March 31, 2004 (In thousands of dollars)

	June 2004 (Unaudited)	March 2004 (Unaudited) (Restated) (Note 2)
Assets		
Current assets		
Cash and temporary investments	$ 27,324	$ 58,560
Accounts receivable	32,523	31,532
Income taxes receivable	1,816	1,552
Other receivables (Note 2)	3,129	3,158
Inventories	77,332	55,782
Prepaid expenses	2,224	2,219
Future income taxes (Note 2)	5,961	5,570
	150,309	158,373
Capital assets, net (Note 2)	120,217	93,769
Other assets (Note 2)	1,323	2,890
Future income taxes	9,681	5,866
Backlog, net (Note 3)	9,435	–
Goodwill, net (Note 3)	43,507	22,060
	$ 334,472	$ 282,958
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (Note 2)	$ 69,115	$ 69,951
Customers' advances	5,788	9,991
Income taxes payable	10,224	229
Future income taxes	2,631	292
Current portion of long-term debt (Note 8)	3,632	4,049
	91,390	84,512
Long-term debt (Note 8)	88,632	59,464
Other liabilities	7,633	7,542
Future income taxes	10,675	10,938
	198,330	162,456
Shareholders' Equity		
Capital stock (Note 4)	87,150	70,883
Contributed surplus (Note 4)	270	227
Cumulative translation adjustment	499	(147)
Retained earnings	48,223	49,539
	136,142	120,502
	$ 334,472	$ 282,958

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statements of income

For the periods ended June 30, 2004 and 2003
(In thousands of dollars, except per share data) (Unaudited)

	2004	2003 (Restated) (Note 2)
Sales	$ 56,368	$ 52,385
Cost of sales	47,889	43,111
Amortization	4,496	3,507
Gross profit	3,983	5,767
Selling and administrative expenses	5,330	5,991
Operating loss	(1,347)	(224)
Financial expenses (Note 2 and 5)	441	563
Loss before restructuring charges and income taxes	(1,788)	(787)
Restructuring charges	–	374
Loss before income taxes	(1,788)	(1,161)
Income taxes recovery	(472)	(343)
Net loss	$ (1,316)	$ (818)
Loss per share	$ (0.05)	$ (0.03)
Loss per share - fully diluted	$ (0.05)	$ (0.03)
Weighted-average number of shares outstanding during the period	26,864,361	23,479,314

Consolidated statements of retained earnings

For the periods ended June 30, 2004 and 2003
(In thousands of dollars) (Unaudited)

	2004	2003 (Restated) (Note 2)
Balance at beginning of period – as previously reported	$ 49,361	$ 51,718
Change in accounting policy (Note 2)	178	301
Restated balance at beginning of period	49,539	52,019
Repurchase of common shares (Note 4)	–	(29)
Net loss	(1,316)	(818)
Balance at end of year	$ 48,223	$ 51,172

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statements of cash flows

For the periods ended June 30, 2004 and 2003
(In thousands of dollars) (Unaudited)

	2004	2003 (Restated) (Note 2)
Cash and cash equivalents provided by (used for):		
Operating activities		
Net loss	$ (1,316)	$ (818)
Items not requiring an outlay of cash		
Amortization	4,572	3,556
Future income taxes	(590)	(891)
Loss (gain) on sale of capital assets	7	(26)
Gain on financial derivative instrument - net (Notes 2 and 5)	(487)	–
Accretion expense of asset retirement obligation	50	48
Stock-based compensation (Note 4)	43	27
Cash flow from operations	2,279	1,896
Net change in non-cash items related to operations (Note 6)	(10,679)	(3,308)
Cash and cash equivalents used for operating activities	**(8,400)**	(1,412)
Investing activities		
Net change in temporary investments	(4,972)	2,232
Purchase of capital assets	(4,366)	(1,599)
Proceeds on disposal of capital assets	793	74
Business acquisition (Note 3)	(63,554)	–
Cash and cash equivalents provided by (used for) investing activities	**(72,099)**	707
Financing activities		
Increase in long-term debt (Note 3)	36,598	108
Repayment of long-term debt	(8,746)	(1,491)
Repurchase of common shares (Note 4)	–	(299)
Issuance of common shares (Notes 3 and 4)	16,267	–
Other	(80)	(192)
Cash and cash equivalents provided by (used for) financing activities	**44,039**	(1,874)
Effect of changes in exchange rates on cash and cash equivalents	**252**	(224)
Change in cash and cash equivalents	**(36,208)**	(2,803)
Cash and cash equivalents at beginning of period	**58,560**	7,781
Cash and cash equivalents at end of period	**$ 22,352**	$ 4,978
Cash and temporary investments are comprised of:		
Cash and cash equivalents	**$ 22,352**	$ 4,978
Temporary investments	**4,972**	42,959
	$ 27,324	$ 47,937
Interest paid	**$ 822**	$ 626
Income taxes paid	**$ 367**	$ 2,778

The accompanying notes are an integral part of these consolidated financial statements.

Notes to consolidated financial statements

For the periods ended June 30, 2004 and 2003
(All dollar amounts in thousands, except per share data) (Unaudited)

NOTE 1. CONSOLIDATED INTERIM FINANCIAL STATEMENTS

The consolidated interim financial statements include the accounts of Héroux-Devtek Inc. and its subsidiaries, all of which are wholly-owned.

The consolidated interim financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles applicable to interim financial statements and follow the same accounting policies and methods in their application as the most recent annual financial statements, except for the changes in accounting policies for Hedging relationships and Asset retirement obligations described in note 2. In the opinion of Management, all adjustments necessary for a fair presentation are reflected in the interim financial statements. Such adjustments are of a normal and recurring nature. The results of operations for the interim periods are not necessarily indicative of the operating results for the full year. The interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report for the fiscal year ended March 31, 2004.

NOTE 2. CHANGES IN ACCOUNTING POLICIES

Hedging Relationships

On April 1, 2004, the Company has adopted Accounting Guideline 13 (AcG-13) on Hedging relationships which applies to all existing and new hedging relationships and provides additional documentation and designation requirements for hedge accounting and requires regular, periodic assessment of effectiveness. Derivatives that are economic hedges, but do not qualify for hedge accounting, are recognized at fair value on the balance sheet with changes in fair value recorded in earnings until they are designated and then qualify for hedge accounting.

As at April 1, 2004, derivative instruments used by the Company and that previously qualified for hedge accounting continue to qualify under the accounting guideline except for the interest rate swap agreement of US$ 10,000.

Interest Rate Swap Agreement

As at April 1, 2004, the Company recorded a deferred loss amounting to $ 727 regarding the interest rate swap agreement.

On May 20, 2004, the interest rate swap agreement was designated for hedge accounting purposes and the change in its fair value since April 1, 2004 representing a gain of $ 487, net of the amortization of the deferred loss recorded as at April 1, 2004, and is included in the Company's financial expenses.

As at June 30, 2004, the net deferred loss for an amount of $ 481 is included in the Company's other assets and will be amortized over the remaining life of the interest rate swap agreement which matures on August 2, 2007.

Forward Foreign Exchange Contract

As part of its adoption of guideline AcG-13 as at April 1, 2004, the Company has revised its accounting policies regarding foreign currency transactions. Monetary items in foreign currencies included in current assets and liabilities are translated into Canadian dollars at the exchange rate prevailing at year-end. For accounts receivable which qualify for hedge accounting, unrealized gains and losses are included in the Company's balance sheet under "other receivables" or "accounts payable and accrued liabilities". As at June 30, 2004, the Company's other receivables included $ 419 for accounts receivable which qualify for hedge accounting. Revenues and expenses in foreign currencies not designated as hedged items are translated using the average exchange rates prevailing during each month of the year. Translation gains and losses are included in the statement of income. Foreign exchange translation gains and losses on foreign currency denominated derivative financial instruments used to hedge anticipated US dollar denominated sales are recognized as an adjustment of the revenues (sales) when the sale is recorded.

NOTE 2. CHANGES IN ACCOUNTING POLICIES *(cont'd)*

Asset Retirement Obligations

In March 2003, the CICA issued a new section in the CICA Handbook, Section 3110, Asset Retirement Obligations. This standard focuses on the recognition and measurement of liabilities related to legal obligations associated with the retirement of property, plant and equipment. Under this standard, these obligations are initially measured at fair value and subsequently adjusted for the accretion of discount and any changes in the underlying cash flows. The asset retirement cost is to be capitalized to the related asset and amortized into earnings over its useful life.

Effective April 1, 2004, the Company has adopted retroactively this change in accounting policy to account for asset retirement obligations.

The Company's asset retirement obligations represent essentially environmental rehabilitation costs related to the Company's manufacturing plant in Longueuil that were estimated at $ 4,700 and provided for in prior years, and are included in the Company's accounts payable and accrued liabilities at March 31, 2004.

The impact of this new accounting policy on the Company's balance sheet at March 31, 2004, using a discount rate of 4.5 %, was as follows:

• Increase in capital assets	$ 1,582
• (Increase) in accumulated amortization of capital assets	$ (1,582)
• Increase in retained earnings	$ (178)
• (Decrease) in future income taxes included in the current assets	$ (96)
• Decrease in accounts payable and accrued liabilities	$ 274

The impact of this change in accounting policy on the consolidated statements of income for the periods ended June 30, is as follows:

	2004	2003
Increase in Financial expenses	$ 50	$ 48
(Increase) in Income tax recovery	(17)	(17)
Increase of net loss	**$ 33**	$ 31

The estimated $ 4,700 rehabilitation costs are expected to be paid in the next three fiscal years.

NOTE 3. BUSINESS ACQUISITION

Description of Business

On April 1, 2004, the Company concluded the asset purchase agreement and plan for merger signed on February 24, 2004 and acquired all outstanding common shares of Progressive Incorporated (along with the net assets of Promilling LP), ("Progressive"), a Texas-based manufacturer of large structural components in the military sector with annual current sales of approximately $ 50,000. This acquisition was accounted for using the purchase method. Therefore the earnings of Progressive have been accounted for in the Company's Consolidated Statement of Income since the acquisition date and are included in the Aerospace & Defence activity segment. The total purchase price represented $ 74,193 (US$ 56,356), and can be detailed as follows:

Basic purchase price	$ 59,499
Tax impacts	7,767
Acquisition of a large specialized manufacturing equipment	4,246
Transaction costs and other	2,681
	$ 74,193

Additional payments of up to $15,798 (US $12,000) in total over the next two fiscal years could also be made based on additional profitability performance. At June 30, 2004, additional payments of $658 (US $500) were made.

NOTE 3. BUSINESS ACQUISITION *(cont'd)*

Financing of the Acquisition

In order to finance this acquisition, the Company drew $ 36,409 on its existing Secured Syndicated Evergreen Revolving Credit Facilities, issued 3,500,000 common shares through private placements for a total net cash consideration of $ 16,180 and used $ 21,604 of its available cash at March 31, 2004. The financing and the total outlay of cash and cash equivalents can be broken down as follows:

Secured Syndicated Evergreen Revolving Credit Facilities		$ 36,409
Issuance of common shares		16,180
Cash	14,363	
Sale balance in escrow	7,241	21,604
		74,193
Less: cash and cash equivalent acquired		2,498
		$ 71,695

As at June 30, 2004, the Company had paid $ 63,554 for the basic purchase price, the large specialized manufacturing equipment and some of the transactions costs.

Purchase Price Allocation

The identifiable intangible asset related to the acquisition of Progressive which amounted to $ 9,601 was attributed to the backlog. The underlying value of the backlog which relates to specific sales contracts will be amortized on a pro-rata basis over the life of the related sales contracts. The excess of the purchase price over the fair value of the net tangible assets acquired and the backlog value amounted to $ 21,168 and represented the allocated value to goodwill. Backlog and goodwill acquired are tax deductible, and the initial purchase price allocation was broken down as follows:

Cash	$ 2,498
Tangible assets	44,936
Backlog	9,601
Goodwill	21,168
Accounts payable and accrued liabilities	(4,010)
	$ 74,193

NOTE 4. CAPITAL STOCK

Authorized Capital Stock

The authorized capital stock of the Company consists of the following:

An unlimited number of common shares

An unlimited number of first preferred shares, issuable in series

An unlimited number of second preferred shares, issuable in series.

The rights, privileges, restrictions and conditions related to the preferred shares may be established by the Board of Directors.

The issued and outstanding capital stock of the Company consists of the following:

	June 30, 2004	March 31, 2004
26,924,059 common shares (23,401,559 at March 31, 2004)	$ 87,150	$ 70,883

NOTE 4. CAPITAL STOCK *(cont'd)*

Stock-based Compensation

Stock Option Plan

The Company has a stock option plan where options to purchase common shares are issued to directors, officers and key employees. The Company expenses all granting of stock options based on their earned period, using the Black & Scholes model to determine their fair value. The expense related to stock options recorded in the quarter ended June 30, 2004 amounted to $43 ($27 for the quarter ended June 30, 2003).

During the quarter ended June 30, 2004, 22,500 stock options were exercised at an average granted price of $3.89 for a total cash consideration of $87. No stock options were granted or cancelled during the period.

Stock Appreciation Rights

The Company has a Stock Appreciation Right plan (SAR) where rights are issued to its non-employee directors. The SAR enables the participants to receive by way of bonus, on the exercise date of a SAR, a cash amount equal to the excess of the market price of a common share over the granted price of the SAR. The SARs are expensed on an earned basis and their costs are determined based on the Company's common shares quoted market value over their granted price. No expense was recorded for SAR during the quarters ended June 30, 2004 and 2003.

Issuance of Common Shares

On April 1, 2004, in conjunction with the closing of the acquisition of Progressive, the Company issued 3,500,000 common shares for a total net cash consideration of $16,180 (net of $970 fees and expenses). 22,500 common shares were also issued following the exercise of stock options for a total cash consideration of $87, bringing the total common shares issued for the quarter to 3,522,500 for a total net proceed of $16,267.

Repurchase of Common Shares

On August 21, 2002, the Company obtained approval from the Toronto Stock Exchange (TSX) to proceed with its normal course issuer bid allowing the Company to purchase up to 1,222,195 of its common shares during the twelve-month period ending August 20, 2003. In April 2003, the Company obtained TSX approval to increase the number of common shares to be repurchased at 1,585,700. Last year, during the quarter ended June 30, 2003, the Company repurchased for cancellation 89,200 common shares for a total cash consideration of $299. The excess ($29) of the cost of the common shares repurchased over their average book value ($270) was accounted for in reduction of the Company's retained earnings.

Diluted Earnings per share

The use of the treasury method, for the diluted earnings per share calculations had no impact on the average number of common shares for the quarters ended June 30, 2004 and 2003.

NOTE 5. FINANCIAL EXPENSES

The financial expenses for the quarters ended June 30 are as follows:

	2004	2003 (Restated) (Note 2)
Interest expense	$ 1,056	$ 899
Interest revenue	(128)	(336)
Gain on financial derivative instrument – net	(487)	–
	$ 441	$ 563

NOTE 6. NET CHANGE IN NON-CASH ITEMS RELATED TO OPERATIONS

The net change in non-cash items related to operations for the quarters ended June 30 represents the following:

	2004	2003
Accounts receivable	$ 2,612	$ 9,471
Income taxes receivable	(264)	614
Other receivables	339	986
Inventories	(2,892)	(2,720)
Prepaid	119	442
Accounts payable and accrued liabilities and other liabilities	(7,447)	(8,026)
Customers' advance	(4,203)	(2,139)
Income taxes payable	960	(605)
Effect of changes in exchange rate	97	(1,331)
	$ (10,679)	$ (3,308)

NOTE 7. PENSION AND OTHER POST-RETIREMENT BENEFIT PLANS

The Company has funded and unfunded defined benefit pension plans as well as defined contribution pension plans that provide pension benefits to its employees. Retirement benefits provided by the defined benefit pension plans are either based on years of service and flat amount, years of service and final average salary or set out by individual agreements.

Benefits provided by the post-retirement benefit plans are set out by individual agreements, which mostly provide for life insurance coverage and health care benefits. Since their amounts are not significant, they are not included in figures below.

Defined pension plan obligations are impacted by factors including interest rate, adjustments arising from plan amendments, changes in assumptions and experience gains or losses. The 2004 costs are based on a measurement of the pension benefit plan obligations and the funds' assets at March 31, 2004. The total pension plan expense is as follows:

	2004	2003
Defined benefit plans	$ 506	$ 523
Defined contribution plans	300	255
	$ 806	$ 778

NOTE 8. LONG-TERM DEBT

	June 30, 2004	March 31, 2004
Secured Syndicated Evergreen Revolving Credit Facilities of up to $ 100,000 (either in Canadian or U.S. currency equivalent) having revolving periods of two (2) years extendible annually, bearing interest at Bankers' acceptance plus 1.5 % for the Canadian term facility, at U.S. base rate plus 0.5 % for the U.S. operating facility, and at Libor plus 1.5 % for the U.S. term facility.	$ 64,639	$ 34,322
Loans bearing no interest, repayable in variable annual instalments, with various expiry dates until 2013.	14,343	15,509
Obligations under capital leases bearing interest between 5.4 % and 8.1 % maturing between June 2005 and September 2009, with amortization periods varying between five (5) to eight (8) years, secured by the related capital assets.	13,282	13,682
	92,264	63,513
Less: current portion	3,632	4,049
	$ 88,632	$ 59,464

NOTE 9. SEGMENTED INFORMATION

For the periods ended June 30

Activity Segments

	2004			2003		
	Products related to Aerospace & Defence	Industrial Products	Total	Products related to Aerospace & Defence (Restated) (Note 2)	Industrial Products (Restated) (Note 2)	Total (Restated) (Note 2)
Sales	$ 51,518	$ 4,850	$ 56,368	$ 46,674	$ 5,711	$ 52,385
Operating income (loss)	(388)	(959)	(1,347)	1,805	(2,029)	(224)
Financial expenses			441			563
Restructuring charges			–			374
Loss before income taxes			(1,788)			(1,161)
Assets	312,859	21,613	334,472	234,745	37,002	271,747
Blacklog, net	9,435	–	9,435	–	–	–
Goodwill	43,507	–	43,507	22,060	–	22,060
Purchase of capital assets	2,429	1,937	4,366	1,295	304	1,599
Amortization	4,049	523	4,572	2,789	767	3,556

NOTE 9. SEGMENTED INFORMATION *(cont'd)*

Geographic Segments

	2004			2003		
	Canada	Outside Canada	Total	Canada (Restated) (Note 2)	Outside Canada (Restated) (Note 2)	Total (Restated) (Note 2)
Sales	$ 33,663	$ 22,705	$ 56,368	$ 42,221	$ 10,164	$ 52,385
Operating income (loss)	(2,137)	790	(1,347)	1,787	(2,011)	(224)
Financial expenses			441			563
Restructuring charges			–			374
Loss before income taxes			(1,788)			(1,161)
Assets	184,707	149,765	334,472	219,689	52,058	271,747
Backlog, net	–	9,435	9,435	–	–	–
Goodwill	20,977	22,530	43,507	20,977	1,083	22,060
Purchase of capital assets	742	3,624	4,366	1,280	319	1,599
Amortization	2,663	1,909	4,572	2,539	1,017	3,556

NOTE 10. RECLASSIFICATION

Comparative figures for the financial statements as at June 30, 2003 have been reclassified to comply with the June 30, 2004 presentation.

Management Discussion and Analysis of Financial Position and Operating Results

This management discussion and analysis (MD&A) is intended to provide an overview of how the financial position of Héroux-Devtek Inc. ("Héroux-Devtek" or "the Company") changed between March 31, 2004 and June 30, 2004. It also compares the operating results and cash flows for the first quarter ended June 30, 2004 to those for the same period the previous year. It should be read in conjunction with the audited consolidated financial statements dated March 31, 2004 and the related MD&A, both available on the Company's website at www.herouxdevtek.com, and with the interim financial statements to June 30, 2004. Héroux-Devtek's financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The Company reports its results in Canadian dollars. All amounts in this MD&A are in Canadian dollars unless otherwise indicated.

Forward-Looking Statements

In the interest of providing shareholders and potential investors with information regarding Héroux-Devtek, including management's assessment of future plans and operations, certain statements in this MD&A are forward-looking statements subject to risks, uncertainties and other important factors that could cause the Company's actual performance to differ materially from those expressed in or implied by such statements.

Such factors include, but are not limited to: the impact of general economic conditions in Canada and the United States; industry conditions including changes in laws and regulations; increased competition; the lack of availability of qualified personnel or management; fluctuations in commodity prices; foreign exchange or interest rates; stock market volatility; and the impact of accounting policies issued by Canadian and US standard setters. Some of these factors are further discussed under Risks and Uncertainties in the Company's MD&A for the year ended March 31, 2004.

Although the Company believes that the expectations conveyed by the forward-looking statements are based on information available to it on the date such statements were made, there can be no assurance that such expectations will prove to be correct. All subsequent forward-looking statements, whether written or orally attributable to the Company or persons acting on its behalf, are expressly qualified in their entirety by these cautionary statements.

OVERVIEW

Héroux-Devtek designs, develops, manufactures and repairs systems and components for two main market segments: Aerospace & Defence, and Industrial. The Aerospace & Defence segment comprises the following:

Aerospace:
- landing gear products
- aerostructure products
- aircraft engine components

Defence:
- small arms and accessories
- other defence products

The Industrial segment includes:
- industrial gas turbine products
- other industrial products.

On April 1, 2004, the Company acquired Progressive Incorporated ("Progressive"), a privately-held Texas-based manufacturer of large structural components for military aircraft. This new business unit has a strong reputation in the industry, and will give the Company's aerostructure sector more depth by providing:

- a better military/commercial product mix (diversification of the customer base);
- increased knowledge of complex manufacturing of structural aircraft components; and
- greater penetration of the US military market.

The Company evolves in two (2) main sectors of activities (Aerospace & Defence and Industrial). However, in the past, the Company has also presented and discussed its results and financial position mainly by its four (4) divisions in its MD&A. Following the acquisition of Progressive, the Company decided to modify its MD&A structure to better reflect its activities, henceforth presenting its results by segment rather than by division. Results for last year's first quarter are presented on the same basis for comparison purposes.

During the first quarter ended June 30, 2004, the economic and industry factors influencing Héroux-Devtek's business remained essentially unchanged from those discussed at year-end 2004. A recovery is still expected in the commercial aerospace market beginning in 2005, impacting on Héroux-Devtek's sales for fiscal 2006. The military aerospace market remains generally strong, with continued interest in unmanned aircraft vehicles ("UAV") and unmanned combat aircraft vehicles ("UCAV"), as well as other potential opportunities that could have an impact on the Company's sales for fiscal 2006. On the industrial side, the downturn in the power generation market continues and is expected to reach its low in calendar year 2004, with renewed growth beginning in 2005. Finally, the strength of the Canadian dollar continues to have a significant negative impact on Héroux-Devtek's results.

RESULTS OF OPERATIONS

Consolidated Sales

Consolidated sales for the quarter ended June 30, 2004 grew by 7.6% to $56.4 million from $52.4 million last year, due to the acquisition of Progressive. The $12.7 million in new sales generated by this new business unit was offset by a stronger Canadian dollar, which had an unfavourable impact of $2.3 million, as well as a sales shortfall of $7.1 million arising primarily at the Landing Gear and Gas Turbine Components divisions. These factors are discussed in more detail below.

The Company's sales by segment were as follows:

First quarter ended June 30 Segment	2004 ($'000)	2003 ($'000)	% Change
Aerospace & Defence	**51,518**	46,674	10.4
Industrial	**4,850**	5,711	(15.1)
Total	**56,368**	52,385	7.6

Aerospace & Defence Segment

Sales for the Aerospace & Defence segment were as follows:

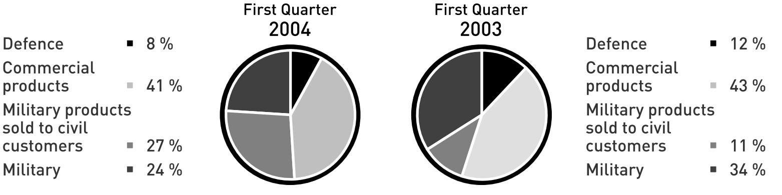
First quarter ended June 30 Sector	2004 ($'000)	2003 ($'000)	% Change
Landing Gear	**24,434**	31,129	(21.5)
Aerostructure	**17,683**	5,642	213.4
Aircraft engine component	**5,131**	4,453	15.2
Defence product	**4,270**	5,450	(21.7)
Total	**51,518**	46,674	10.4

Sales for the Aerospace & Defence segment were up 10.4 % in the first three months of fiscal 2005 to $ 51.5 million compared to $ 46.7 million for the same period of fiscal 2004. This increase was mainly due to the acquisition of Progressive, which contributed sales of $ 12.7 million.

Longueuil and Dorval plants did not make the expected sales level due to delays in deliveries and to the implementation of new customers' requirements. This caused sales shortfalls of $3.5 million and $1.5 million respectively, for a total of $5.0 million.

Sales for the Landing Gear military sector were down due to reduced demand and the completion of the KC-135 and P-3 contracts. Commercial Landing Gear sales slipped 5.4 %, reflecting the ongoing slowdown in the commercial aerospace market. Growth in the Aircraft Engine Component sector, which represented an increase of 22.9 % in constant US dollars, was mainly due to last year's gain in market share. Finally, the decline in the Defence sector sales arose from low demand in other defence products, with small arms product sales remaining stable year-over-year.

Aerospace & Defence Sales



Industrial Segment

Sales for the Industrial segment were as follows:

First quarter ended June 30 Segment	2004 ($'000)	2003 ($'000)	% Change
Industrial Gas Turbine	3,056	4,944	(38.2)
Other Industrial	1,794	767	133.9
Total	**4,850**	5,711	(15.1)

First quarter sales for the Industrial segment totalled $ 4.9 million for fiscal 2005, down 15.1 % from $ 5.7 million in fiscal 2004. Industrial Gas Turbine sales remained low, reflecting the persistently weak market, while new parts manufacturing for a new customer resulted in a substantial increase in Other Industrial sales for the quarter. Nonetheless, sales shortfall of $ 2.1 million was experienced in the first quarter, due in part to manufacturing problems related to the introduction of this new business, as well as to material shortages.

Sales by Destination

The Company's sales by destination were as follows:

First quarter ended June 30 Destination	2004	2003
Canada	23%	29%
US	72%	63%
International	5%	8%
	100%	100%

The proportion of US sales rose due to the acquisition of Progressive, which generates all of its sales in the United States.

Gross Profit

Expressed as a percentage of sales, consolidated gross profit decreased 3.9 % in the first quarter to 7.1 % from 11.0 % last year. The Canadian dollar accounted for 0.7 % of this decline. The sales shortfalls discussed above translated into a negative impact of 3.3 % on gross profit.

Selling and Administrative Expenses

First quarter selling and administrative expenses were down from last year, as shown below:

First quarter ended June 30	2004	2003
Selling and administrative expenses ($'000)	**5,330**	5,991
% of sales	**9.5**	11.4

The decrease was due to lower royalties on military product sales at the Landing Gear Division, and a $ 391,000 loss on foreign exchange booked in the first quarter of last year.

Operating Income (Loss)

Aerospace & Defence Segment

Expressed as a percentage of sales, operating income for the Aerospace & Defence sector decreased by 4.7 % compared to last year. This was mainly due to the low business volume generated by the Longueuil and Dorval plants and to the operational challenges experienced during the quarter, although pricing pressures resulting from the reduced aerospace activity in recent years also contributed to the decrease. These factors were offset by the good performance of Progressive.

Industrial Segment

The Gas Turbine Components Division decreased its operating loss by 15.7% in the first quarter of fiscal 2005, due to the fact that the division incurred significant unabsorbed overhead costs last year during the months preceding the closure of the Tampa operation on June 30, 2003. Last year's consolidation of the division has not yet produced the expected level of productivity improvements and manufacturing efficiencies. An unfavourable product sales mix (a higher ratio of aircraft engine parts to industrial gas turbine sales) also impacted this year's first quarter operating results.

Financial Expenses

Net financial expenses for the first quarter declined slightly from last year, as shown below :

First quarter ended June 30	2004 ($'000)	2003 ($'000)
Interest expense	**1,056**	899
Interest revenue	**(128)**	(336)
Gain on financial derivative instrument - net	**(487)**	–
Financial expenses	**441**	563

On May 20, 2004, the Company designated its interest rate swap agreement as a hedging instrument to be recorded under the hedge accounting rules. This resulted in a gain of $ 487,000, representing the change in the fair value of the interest rate swap agreement between April 1, 2004 and May 20, 2004, net of the amortization of the related deferred loss recorded on April 1, 2004 (see under Hedging Relationships in Changes in Accounting Policy, below).

Net Loss

For the first quarter of fiscal 2005, the Company posted a net loss of $1.3 million, as shown below:

First quarter ended June 30	2004	2003
Net loss ($'000)	1,316	818
Net loss per share ($)	0.05	0.03

The increase in the net loss resulted from the various factors discussed above. Net loss per share figures are based on weighted averages of 26,864,361 common shares outstanding for the first quarter of this year and 23,479,314 for last year. The increase is due to the issuance of 3.5 million common shares pursuant to the acquisition of Progressive (see Notes 3 and 4 to the consolidated financial statements).

Last year's first quarter loss was restated and increased by $31,000 to $818,000 due to the change in accounting policy on asset retirement obligations (see Note 2 to the consolidated financial statements).

On July 29, 2004, the date of this MD&A, the Company had 26,924,059 common shares outstanding.

LIQUIDITY AND CAPITAL RESOURCES

Operating Activities

Internally, the Company generated cash flow from operations and cash flow provided by operating activities as follows:

First quarter ended June 30	2004 ($'000)	2003 ($'000)
Cash flow from operations	2,279	1,896
Net change in non-cash items related to operations	(10,679)	(3,308)
Cash and cash equivalents used for in operating activities	**(8,400)**	(1,412)

In the first quarter of fiscal 2005, the net change in non-cash items included a $7.4 million reduction in accounts payable and accrued liabilities and other liabilities, a $4.2 million decrease in customers' advances, and a $2.9 million increase in inventories. These items were offset by a $2.6 million reduction in accounts receivable and a $1.0 million increase in income tax payable during the quarter.

Investing Activities

The Company's first quarter investing activities were as follows:

First quarter ended June 30	2004 ($'000)	2003 ($'000)
Net change in temporary investments	(4,972)	2,232
Purchase of capital assets	(4,366)	(1,599)
Proceeds on disposal of capital assets	793	74
Business acquisition	(63,554)	–
Cash and cash equivalents provided by (used for) investing activities	**(72,099)**	707

Héroux-Devtek acquired Progressive on April 1, 2004, for a total purchase price of $74.2 million (US $56.4 million). During the first quarter, the Company paid $63.6 million (US $48.3 million), representing payment of the basic purchase price, the acquisition of a new piece of specialized equipment and a portion of the transaction costs. An amount of $7.8 million (US $5.9 million) representing the tax impacts of the transaction will be paid in the second quarter.

Purchase of capital assets totalled $ 4.4 million in the first quarter and included $ 3.6 million for the Gas Turbine Components Division pursuant to the exercise of a purchase option for machinery and equipment under operating leases. The Company's contractual obligations (off-balance-sheet financing) related to machinery and equipment under operating leases have been reduced accordingly.

Capital assets include $ 3.2 million of assets for resale related mainly to the closure of the Tampa and Metro operations last year.

Financing Activities

The Company's first quarter financing activities were as follows:

First quarter ended June 30	2004 ($'000)	2003 ($'000)
Increase in long-term debt	36,598	108
Repayment of long-term debt	(8,746)	(1,491)
Repurchase of common capital stock	–	(299)
Issuance of common shares	16,267	–
Other	(80)	(192)
Cash and cash equivalents provided by (used for) financing activities	**44,039**	(1,874)

On April 1, 2004, the Company drew $ 36.4 million (US $ 27.7 million) on its US Syndicated Evergreen Revolving Term Credit Facility to finance the acquisition of Progressive.

During the first quarter, the Company repaid $ 7.0 million on its Canadian Syndicated Evergreen Revolving Term Credit Facility. The outstanding remaining balance of $ 7.0 million due on this Term Credit Facility at June 30, 2004, will be repaid in the second quarter.

On February 24, 2004, the Company entered into a bought deal private placement, to finance the acquisition of Progressive. Pursuant to this private placement and in conjunction with the closing of the acquisition of Progressive, the Company, on April 1, 2004, issued 2,975,000 common shares for a cash consideration of $ 13.6 million, net of $ 1.0 million in fees and expenses. In addition, the Company's President and Chief Executive Officer and principal shareholder purchased 525,000 common shares for a total net cash consideration of $ 2.6 million through a concurrent private placement, on the same terms and conditions as the underwritten bought deal (see Note 21 to the consolidated financial statements for the year ended March 31, 2004).

Consolidated Balance Sheets

The following table itemizes and explains the significant changes in the consolidated balance sheets between March 31, 2004 and June 30, 2004:

Item	Change ($ million)	Explanation
Cash and temporary investments	(31.2)	See statement of cash flows
Accounts receivable	1.0	Due to the acquisition of Progressive, offset by a low business volume in the first quarter
Inventories	21.6	Due to the acquisition of Progressive ($ 14.7 million), and, to a lesser degree, to late deliveries at the Landing Gear Division
Capital assets	26.4	Due to: • Acquisition of Progressive ($ 26.5 million) • Purchase of capital assets ($ 4.4 million) • A higher U.S. exchange rate used to convert the net assets of self-sustaining U.S. subsidiaries ($ 0.6 million) Net of: • Amortization ($ 4.2 million) • Disposal of capital assets ($ 0.9 million)
Other assets	(1.6)	Due to: • Capitalization of $ 2.0 million in transaction costs at March 31, 2004 related to the Progressive acquisition Partially offset by: • The net deferred loss on the interest rate swap agreement, recorded on April 1, 2004 pursuant to the implementation of AcG-13 (see under Changes in Accounting Policy, below)
Backlog, net	9.4	Represents the underlying value of the net backlog acquired following the acquisition of Progressive (see Note 3 of the consolidated financial statements)
Goodwill	21.4	Mainly related to the acquisition of Progressive
Accounts payable and accrued liabilities	(0.8)	Reduction due to payment of transaction costs capitalized at March 31, 2004, to lower business volume offset by the acquisition of Progressive
Customers' advance	(4.2)	Represents unearned amounts received by the Landing Gear and Logistics & Defence division; these advances are liquidated based on units delivered to customers (see Note 10 to the consolidated financial statements dated March 31, 2004)
Income tax payable	10.0	Mainly due to the tax impacts related to the acquisition of Progressive

Item	Change ($ million)	Explanation
Long-term debt (including current portion)	28.8	Due to: • New long-term debt assumed to finance the acquisition of Progressive ($ 36.4 million) • Other new long-term debt ($ 0.2 million) • A higher U.S. exchange rate used to convert the net assets of self-sustaining U.S. subsidiaries ($ 0.9 million) Net of: • Repayment of long-term debt ($ 8.7 million)
Capital stock	16.3	Represents the issuance of 3,500,000 common shares to finance the acquisition of Progressive for a total net cash consideration of $ 16.2 million, and 22,500 common shares for a total cash consideration of $ 0.1 million related to the exercise of stock options
Cumulative translation adjustment	0.6	Represents the counterpart of the impact of foreign exchange rate fluctuations on the net assets of self-sustaining U.S. subsidiaries
Retained earnings	(1.3)	See consolidated statement of retained earnings

The Company continues to enjoy a strong balance sheet, which puts it in an excellent position to benefit from the current economic challenges.

The Company's long-term debt-to-equity ratio was 0.65:1 on June 30, 2004 compared to 0.49:1 on March 31, 2004. At June 30, 2004, the balance sheet included cash and cash equivalents of $ 27.3 million compared to $ 58.6 million at March 31, 2004.

CHANGES IN ACCOUNTING POLICIES

Hedging Relationships

On April 1, 2004, the Company adopted Accounting Guideline 13, Hedging Relationships ("AcG-13"), which applies to all existing and new hedging relationships. AcG-13 provides additional documentation and designation requirements for hedge accounting and requires regular, periodic assessment of effectiveness. Derivatives that are economic hedges but that do not qualify for hedge accounting are recognized at fair value on the balance sheet, with changes in fair value recorded in earnings until they are designated as qualifying for hedge accounting.

As at April 1, 2004, derivative instruments used by the Company that previously qualified for hedge accounting continue to qualify for hedge accounting under AcG-13, except for the US $ 10.0 million interest rate swap agreement.

Interest Rate Swap Agreement

As at April 1, 2004, the Company recorded a deferred loss amounting to $ 727,000 for the interest rate swap agreement. Subsequent changes in the fair value of the interest rate swap agreement are recorded in earnings, and the deferred loss is amortized on an effective yield basis over the remaining life of the agreement.

On May 20, 2004, the interest rate swap agreement was designated for hedge accounting purposes and the change in its fair value since April 1, 2004 representing a gain of $ 487,000, net of the amortization of the deferred loss recorded as at April 1, 2004. This gain is included in the Company's financial expenses.

As at June 30, 2004, the net deferred loss for an amount of $ 481,000 is included in the Company's other assets and will be amortized over the remaining life of the interest rate swap agreement, which matures on August 2, 2007.

Forward Foreign Exchange Contract

As part of its adoption of AcG-13, the Company revised its accounting policies regarding foreign currency transactions. Monetary items in foreign currencies included in current assets and liabilities are translated into Canadian dollars at the exchange rate prevailing at year-end. For accounts receivable that qualify for hedge accounting, unrealized gains and losses are included in the Company's balance sheet under "other receivables" or "accounts payable and accrued liabilities". At June 30, 2004, the Company's other receivables included $ 419,000 for accounts receivable that qualified for hedge accounting. Revenues and expenses in foreign currencies not designated as hedged items are translated using the average exchange rates prevailing during each month of the year. Translation gains and losses are included in the statement of income. Foreign exchange translation gains and losses on foreign currency-denominated derivative financial instruments use to hedge anticipated US dollar-denominated sales are recognized as an adjustment of the revenues when the sale is recorded.

Asset Retirement Obligations

In March 2003, the CICA issued a new section in the CICA Handbook, Section 3110, *Asset Retirement Obligations*. This standard focuses on the recognition and measurement of liabilities related to legal obligations associated with the retirement of property, plant and equipment. Under this standard, these obligations are initially measured at fair value and subsequently adjusted for the accretion of discount and any changes in the underlying cash flows. The asset retirement cost is to be capitalized to the related asset and amortized into earnings over its useful life.

Effective April 1, 2004, the Company adopted this change in accounting policy retroactively. The Company's asset retirement obligations essentially represent environmental rehabilitation costs related to the Company's manufacturing plant in Longueuil. These costs were estimated at $ 4.7 million and provided for in prior years, and are included in the Company's accounts payable and accrued liabilities at March 31, 2004.

At June 30, 2004, the impact of this new accounting policy on the Company's balance sheet was as follows:

	($'000)
• Increase in capital assets	$ 1,582
• (Increase) in accumulated amortization of capital assets	$ (1,582)
• (Increase) in retained earnings	$ (178)
• (Decrease) in future income taxes included in current assets	$ (96)
• Decrease in accounts payable and accrued liabilities	$ 274

This new accounting policy will also have a negative impact of $ 200,000 on the Company's results for each of fiscal years 2005 and 2006, representing additional financial expenses (non-cash items) to be capitalized to the Company's assets retirement obligations.

First Certification of Disclosure by the Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO")

In early 2004, the Canadian Securities Administrators released its final rules for Audit Committees, CEO and CFO certifications and auditor oversight. The Company's management and Audit Committee are in the process of developing an implementation plan that can span up to the next nine months and more.

Pursuant to these new rules, the Company's CEO and CFO have released their first certification of disclosure in the Company's interim filings for the first quarter ended June 30, 2004.

Integration of Progressive

The Company has established a plan to integrate Progressive, its new business unit acquired on April 1, 2004. The plan includes the implementation of a complete computerized business information system, scheduled for completion by the end of the current fiscal year. There are risks and uncertainties related to this integration and implementation that could have a material adverse effect on the financial information reported during the transition period. The Company has taken steps to minimize such risks and uncertainties, including in particular an in-depth review of its financial reporting.

RISKS AND UNCERTAINTIES

Héroux-Devtek operates in industry segments that have a variety of risk factors and uncertainties that could have a material adverse effect on the Company's business, financial condition and results of operations. Such risks and uncertainties include, but are not limited to, those mentioned below, which are more fully described in the Company's MD&A for the year ended March 31, 2004.

- Reliance on large customers
- Operational risk
- General economic conditions
- Military spending
- Foreign currency fluctuations
- Liquidity and access to capital resources
- Restrictive debt covenants
- Changing interest rates
- External business environment
- Warranty casualty claim losses
- Environmental matters
- Collective bargaining agreements

Additional Information and Continuous Disclosure

This MD&A was prepared as of July 29, 2004. Updated information on the Company, including the annual information form, can be found on the SEDAR web site at www.sedar.com.

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