# Management Discussion and Analysis
# of Financial Position and Operating Results

The purpose of this management discussion and analysis ("MD&A") is to provide the reader with an overview of how the financial position of Héroux-Devtek Inc. ("Héroux-Devtek" or "the Company") changed between March 31, 2005 and March 31, 2006. It also compares the operating results and cash flows for the year ended March 31, 2006 to those for the previous year.

This analysis should be read in conjunction with the consolidated financial statements dated March 31, 2006. Héroux-Devtek's consolidated 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; availability of commodities and fluctuations in commodity prices; foreign exchange or interest rates; stock market volatility; and the impact of accounting policies issued by Canadian and U.S. standard setters. Some of these factors are further discussed under Risks and Uncertainties in this MD&A.

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 Inc. and its subsidiaries (the «Company») specialize in the design, development, manufacture, repair and overhaul of systems and components used principally in the aerospace and industrial sectors. As such, a significant portion of the Company's sales are made to a limited number of customers mainly located in the United States.

The Company was founded in 1942 as Héroux Machine Parts Limited, and later changed its name to Héroux Inc. The Company became public in 1986. In 2000, it acquired Devtek Corporation and the two entities were merged to form Héroux-Devtek Inc., one of the largest second-tier manufacturers in the Canadian aerospace industry.

On April 1, 2004, the Company acquired Progressive Incorporated ("Progressive"), a privately-held Texas-based manufacturer of large structural components for military aircraft, thereby boosting its aerostructure capability and opening access to the important aerostructure military sector.

Héroux-Devtek serves two main segments: Aerospace and Industrial. The former Aerospace & Defence segment became the Aerospace segment as of March 31, 2005, following the sale of Diemaco, which formed the Company's Logistics and Defence Division. This Division is shown as discontinued operation. The Company supplies both the commercial and military sectors of the Aerospace market with landing gear (including spare parts and repair and overhaul services), airframe structural components including kits, and aircraft engine components. In the commercial sector, the Company is active in the business jet, regional jet and large commercial jet markets. On the military side, the Company provides parts and services for all major military aircraft mainly in the United States.

Héroux-Devtek's main product for the Industrial segment is large components for electricity-generating gas turbines, with its largest customer being The General Electric Company (GE). It also sells precision components for other industrial applications including products for the wind energy market.

The Company's sales by segment are as follows:

| | **2006** | **2005** |
|---|---|---|
| Aerospace | 91% | 91% |
| Industrial | 9% | 9% |
| | 100% | 100% |

Héroux-Devtek sells mainly to original equipment manufacturers (OEMs) such as GE, Lockheed Martin, Bombardier and Boeing, and into the aftermarket, where its main customers are the U.S. Air Force (USAF) and U.S. Navy. In fiscal 2006, sales to these customers represented approximately 64% of total sales.

Héroux-Devtek is structured around two segments: Aerospace and Industrial. The Aerospace segment is comprised of the Landing Gear and Aerostructure Divisions and of the Aircraft Engine Components of the Gas Turbine Components Division. The Industrial segment is comprised of the large components for the power generation and other industrial products. The Landing Gear Division designs, manufactures, repairs and overhauls landing gears and has built a strong, well-recognized design engineering team. The Aerostructure Division manufactures airframe components ranging in size from small to very large, for the commercial and military aerospace markets. The Gas Turbine Components Division manufactures aircraft engine components and large components for the power generation and other industrial markets.

Each division is assigned responsibility for its own market development and operating results in order to foster entrepreneurship and employee involvement. The Company's corporate head office provides support to the divisions and retains responsibility for such areas as global strategic development, financing, legal counsel, human resources, public relations and the Company's public financial reporting and disclosure requirements.

## Business Strategy

Héroux-Devtek's business strategy is to position itself as a key supplier for its customers in the three pillars of its business: landing gear, aerostructure and gas turbines. For the Company, being a key supplier means providing not only manufactured components but also other services such as design, assembly and program management in order to become a complete service provider and allow customers to focus on their core business. In order to achieve this, the Company aims to develop management and technical expertise so as to add value to products at competitive costs. It also seeks to grow to attain a critical mass in each of its market segments, while maintaining a solid financial position.

In practice, this translates into:

- A focused factory approach, with each plant specializing in a specific type of component;
- Standard, compatible information systems across the Company;
- Migration of technical and managerial know-how between divisions;
- A lean manufacturing approach in all its plants;
- Revenue stability through long-term agreements with its customers;
- Maintain a balanced sales mix between civil and military aerospace markets and, industrial sales; and
- Maintain and build on a culture of entrepreneurship through the participation, dedication and commitment of its employees.

Héroux-Devtek seeks growth externally through acquisitions that can be easily integrated into its existing operations or that bring complementary technology, leading to greater added value. Internally, the Company aims to:

- Develop valued-added, proprietary products through design engineering;
- Establish or enhance its presence in certain product markets, such as the after-market repair and overhaul of commercial and military landing gear, design and manufacturing of small landing gear, and large structural assemblies for commercial and military aircraft OEMs; and
- Diversify the customer base for its existing product lines, which generally means finding new OEM customers for its landing gear, airframe structural components and industrial products.

## Key Performance Indicators

Héroux-Devtek measures its performance on a company-wide basis through key financial indicators that include sales, gross profit, EBITDA, operating income, working capital, long-term-debt-to-equity ratio, and earnings per share. These items are discussed in the appropriate sections below.

Management also tracks the performance through certain indicators related to operations. These include Return On Net utilized Assets ("RONA"), backlog, value-added as a percentage of sales, percentage of on-time deliveries, non-quality costs, attainment of cost reduction targets, and capacity utilization.

## Market Trends

In the aerospace industry, there is a broad trend toward OEMs outsourcing manufacturing activities. OEMs are buying more components from increasingly fewer suppliers. They are tending to buy kits for assembly and large sub-assemblies, and to reduce their manufacturing activities in order to concentrate on design and marketing. OEMs are also sourcing components for their products on the global market, in order to benefit from the best cost-quality-delivery parameters, wherever they can. This is expected to be an ongoing trend.

The commercial aerospace market, which started a turnaround last year, showed a steady growth this year with, Boeing[1] and Airbus[2] deliveries increasing by 10%.

As indicated last year, the regional jet market is shrinking, with reduced demand for 50-seaters[3]. However, the outlook for 70- to 90-seaters looks promising for the next three years should the financial situation of the airlines improve[4].

Deliveries of business jets are up 20%, with 754 units[5] delivered in calendar 2005 compared to 591 units in 2004. The outlook for the next four to five years is positive.

The military market remains solid again this year. This market is adapting to unconventional war with helicopters and small weapons. This opens new possibilities in this market. Furthermore, there is continued interest in unmanned aircraft vehicles ("UAV").

After a major decline in the last couple of years, the power generation market has stabilized somewhat and is expected to experience slight growth in fiscal 2007[6].

In fiscal 2006, the Company made inroads into the new and promising wind energy market. This source of "green" energy is very promising, with growth expected for the next 10 years[7].

Finally, the continued strength of the Canadian dollar has had a significant negative impact on Héroux-Devtek in the past few years, given that a substantial portion of the Company's sales is in U.S. dollars while it reports in Canadian currency.

## Major Achievements of Fiscal 2006

- **Closing of the sale of the Logistics and Defence Division, Diemaco**

  The Company entered into an agreement with Colt Defence LLC, a U.S. company, for the sale of its Logistics and Defence Division, Diemaco, in February 2005. The sale transaction closed on May 20, 2005 (see Note 4 to the consolidated financial statements).

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[1] Source : Boeing press releases
[2] Source : Airbus press releases
[3] Source : Forecast International
[4] Source : Forecast International
[5] Source : GAMA (General Aviation Manufacturer Association)
[6] Source : GEPS (General Electric Power System)
[7] Source : EWEA (European Wind Energy Association)

- **Successful public offering**
  In November 2005, 4.5 million common shares were sold at a price of $3.75 per share for gross proceeds of $16,875,000.

- **Extension of credit facilities**
  The Company's credit facilities, allowing it to borrow up to $80 million, were extended to March 21, 2007.

- **Financial turnaround**
  The Company posted profits in the last two quarters of fiscal 2006.

- **Major contracts awarded or renewed in fiscal 2006**
  - $125 million contract with Goodrich to supply landing gear components for the Boeings' B-777 aircraft over the next 10 years;
  - $62.6 million contracts for the provision of the following:
    - Major structural machined components and assemblies for the F-35 Joint Strike Fighter (JSF) Short-Take-Off / Vertical Landing (STOVL) aircraft currently in the development phase. Deliveries will run through fiscal 2008;
    - Major components for the B-777 aircraft to Boeing. The work will be performed over 3 years and commenced in fiscal 2006;
    - Landing Gear components and complete assemblies for the F-15 and F-16 fighter aircraft, and B-1B aircraft to be delivered over 3 years and commenced in fiscal 2006;
  - Additional contracts for over $20 million with the USAF and the U.S. Navy for the production of landing gear components for the KC135R, C-130, B1B aircraft and the P-3, to be delivered over the next four years;
  - $12 million in new contracts with Lockheed Martin for work on the Conventional Take-Off and Landing (CTOL) versions of the F-35 Joint Strike Fighter (JSF), currently in the development phase.

- **Kitchener plant expansion**

  Work began on expanding the Kitchener landing gear plant by 27,000 square feet to accommodate new work on the B-777. The $12 million expansion should be completed by December 2006.

- **Progressive plant expansion**

  The Company announced a 12,500 square feet extension to its main plant in Arlington, Texas, to support work on the JSF and other aircraft programs.

### Selected Annual Financial Information

The following table presents selected financial information for the past three financial years:

| **Years ended March 31** **($'000, except per share data)** | **2006** | **2005** | **2004 restated[1]** |
|---|---|---|---|
| Sales | 256,197 | 232,998 | 192,678 |
| Restructuring charges, net of income tax recovery | - | - | (694) |
| EBITDA | 20,907 | 14,623 | 9,249 |
| Net loss from continuing operations | (406) | (4,291) | (3,972) |
| Net income from discontinued operations | 8,661 | 2,162 | 1,637 |
| Net income (loss) | 8,255 | (2,129) | (2,335) |
| Loss per share from continuing operations ($) – basic and diluted | (0.01) | (0.16) | (0.17) |
| Earnings (loss) per share ($) – basic and diluted | 0.29 | (0.08) | (0.10) |
| Total assets from continuing operations | 315,673 | 295,197 | 262,948 |
| Long-term debt | 50,637 | 65,660 | 59,464 |
| Cash and cash equivalents | 20,863 | 9,550 | 53,599 |

The Company's EBITDA from continuing operations is calculated as follows:

| **Years ended March 31** **($'000)** | **2006** | **2005** | **2004 restated[1]** |
|---|---|---|---|
| Net loss from continuing operations | (406) | (4,291) | (3,972) |
| Income tax recovery | (425) | (2,043) | (3,041) |
| Restructuring charges | - | – | 1,052 |
| Financial expenses | 4,221 | 4,009 | 1,920 |
| Amortization | 17,517 | 16,948 | 13,290 |
| EBITDA | 20,907 | 14,623 | 9,249 |

Due mainly to the acquisition of Progressive in April 2004, sales and EBITDA rose in fiscal 2005. Progressive's good performance was partially offset by further reductions in sales and profitability at the Landing Gear Division in fiscal 2005 arising from reduced business activity and an unfavourable sales mix. The Company's fiscal 2005 results were also negatively affected by continued marginal capacity utilization at its plants, mainly attributable to sluggish business activity in its key markets. The sustained strength of the Canadian dollar, sharp raw materials

[1] Due to the change in accounting policy on asset retirement obligations – see Note 2 to the consolidated financial statements.

price increases and lengthening raw materials delivery times also had a significant negative impact on the Company's fiscal 2005 results.

The Company's results improved in fiscal 2006 due to an improved performance by the Landing Gear Division. Sales and EBITDA continued to increase, and the net loss from continuing operations was significantly reduced. These improved results were somewhat tempered by a low production volume at the Gas Turbine Components Division and the even stronger Canadian dollar.

## RESULTS OF OPERATIONS

Following the February 2005 announcement of an agreement for the sale of its Logistics & Defence Division (Diemaco), all Diemaco's operations were reclassified as discontinued operations (see Discontinued Operations below and Note 4 to the consolidated financial statements). The Diemaco sales transaction was completed on May 20, 2005, with total proceeds amounting to $19.0 million.

### Consolidated Sales

Consolidated sales for the year ended March 31, 2006 rose 10.0% to $256.2 million from $233.0 million last year, essentially due to the increase in landing gear sales for large civil aircraft and business jets. However, sales were negatively affected by the strength of the Canadian dollar relative to the U.S. dollar, which reduced sales figures by $15.7 million or 6.7%.

The Company's sales by segment were as follows:

| | 2006 ($'000) | 2005 ($'000) | % Change |
|---|---|---|---|
| Aerospace | 233,752 | 211,689 | 10.4 |
| Industrial | 22,445 | 21,309 | 5.3 |
| **Total** | **256,197** | **232,998** | 10.0 |

*Aerospace Segment*

Sales for the Aerospace segment were as follows:

| | 2006 ($'000) | 2005 ($'000) | % Change |
|---|---|---|---|
| Landing Gear | 143,476 | 116,864 | 22.8 |
| Aerostructure | 75,129 | 75,913 | (1.0) |
| Aircraft Engine Components | 15,147 | 18,912 | (19.9) |
| **Total** | **233,752** | **211,689** | **10.4** |

Aerospace sales rose by 10.4% to $233.7 million from $211.7 million last year. The increase was primarily due to the improved results at our Landing Gear Division. This improved performance comes from the continued growth in large civil and business jet sales and, military sales to civil customers, along with the impact in the last two quarters of the year of the supply of materials under the USAF repair and overhaul contract, which started last August.

Aerostructure sales were almost flat, year-over-year, with an increased built rate on business jet and turbo prop (commuter) contracts offset by reduced regional jets sales following the suspension of the Bombardier RJ200 program.

Aircraft engine components sales declined almost 20% to $15.1 million. These sales were impacted this year by the completion of a military contract and by certain delivery and quality issues at our Gas Turbine Division, which caused a customer to terminate the manufacturing of certain commercial parts. Aircraft Engine Component sales totalled $1.9 million in the last quarter of fiscal 2006.

*Industrial Segment*

Sales for the Industrial segment were as follows:

| | 2006 ($'000) | 2005 ($'000) | % Change |
|---|---|---|---|
| Gas Turbine | 11,117 | 13,206 | (15.8) |
| Other Industrial | 11,328 | 8,103 | 39.8 |
| **Total** | **22,445** | **21,309** | **5.3** |

Industrial sales increased by 5.3% to $22.4 million from $21.3 million last year, driven by the wind energy market, which added $1.7 million to other industrial sales.

*Sales by Destination*

With the Company's improved commercial sales to Canadian customers, sales by destination changed as shown below:

| | **2006 (%)** | **2005 (%)** |
|---|---|---|
| Canada | 27 | 24 |
| U.S. | 71 | 74 |
| International | 2 | 2 |
| **Total** | **100** | **100** |

**Gross Profit**

Consolidated gross profit improved from 5.8% to 7.5% of sales in fiscal 2006 in spite of a 1.4% negative impact attributable to the continued strength of the Canadian dollar relative to the US currency. The increase reflects the overall increase in sales, which contributed to a better absorption of manufacturing overhead costs, as well as improved pricing on certain civil aerospace contracts.

Gross profit was also impacted during the fiscal year 2006 by an insurance recovery of $1.8 million, which was partially offset by a $1.0 million provision for non-quality and certain terminated aircraft engine component parts referred to above. The net impact of the two above-mentioned items, which were recorded as a reduction of cost of sales in fiscal year 2006, increased the gross profit by $0.8 million or 0.3% expressed as a percentage of sales.

**Selling and Administrative Expenses**

Selling and administrative expenses were as follows:

| | **2006** | **2005** |
|---|---|---|
| Selling and administrative expenses ($'000) | 15,847 | 15,746 |
| % of sales | 6.2% | 6.8% |

Selling and administrative expenses were almost flat in dollars but were actually 0.6% lower as a percentage of sales. The increased variable costs associated with the Company's higher sales were substantially offset by the favourable impact of the stronger Canadian dollar on these expenses.

Selling and administrative expenses include a gain on currency translation of $646,000 this year compared to $916,000 last year.

**Operating Income (Loss)**

*Aerospace Segment*

Aerospace operating income was $6.2 million or 2.7% of sales this year, compared to $1.0 million or 0.1% of sales last year, reflecting higher sales and the improved performance of the Landing Gear Division.

*Industrial Segment*

The operating loss of $2.9 million or (12.7)% of sales in the industrial segment, compares to last year's figures of $3.3 million or (15.5)% of sales, and reflects the slight increase in industrial segment sales. The negative operating margins for the industrial segment are essentially caused by the overall low business volume and the related high unabsorbed manufacturing overhead costs.

| **Financial Expenses** | **2006 ($'000)** | **2005 ($'000)** |
|---|---|---|
| Interest | 3,707 | 4,112 |
| Amortization of deferred financing costs | 388 | 307 |
| Standby fees | 261 | 181 |
| Gain on financial derivative instrument | - | (528) |
| Amortization of net deferred loss related to a financial derivative instrument | 138 | 148 |
| Interest revenue | (273) | (211) |
| Financial expenses | **4,221** | **4,009** |

The increase in financial expenses can be explained by the $528,000 gain on financial derivative instrument recorded in fiscal 2005 and the general increase in interest rates this year, mainly in the US. The reduction in interest expenses is mainly due to the $22.7 million in net capital repayments on the Company's long-term debt since the beginning of the current fiscal year following the sale of Diemaco in the first quarter and the closing of the 4.5 million common shares offering in November.

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 $528,000, representing the change in the fair value of the interest rate swap agreement between April 1, 2004 and May 20, 2004.

## Discontinued Operations

On May 20, 2005, the Company concluded the sale of its Logistics & Defence Division (Diemaco) to Colt Defense LLC. The final total sale price was $19.0 million. All assets and liabilities related to Diemaco were reclassified as discontinued assets and liabilities on the consolidated balance sheets. Diemaco's revenues, expenses and net income are shown under discontinued operations in the consolidated statements of income (loss) and, the impact of Diemaco's operations on the Company's cash and cash equivalents is presented under discontinued operations in the consolidated statements of cash flows (see Note 4 to the consolidated financial statements).

A significant portion of the net proceeds from the sale of Diemaco was used to repay $15.3 million on the Company's Secured Syndicated Revolving Credit Facilities.

## Income Tax Recovery, Income Tax Receivable and Future Income Tax Assets

*Income Tax Recovery*

The income tax recovery for fiscal 2006 amounted to $0.4 million compared to $2.0 million for the previous year. Although the reduced recovery amount is primarily a function of the significant reduction in the loss from continued operations on a year-over-year basis, certain items particular to fiscal 2006 had a direct impact on the income tax recovery for the year.

The combined Canadian federal and provincial income tax rate, given the mix by jurisdiction as well as the combination of profitable and unprofitable business units, was 28.6% for fiscal 2006 compared to 32.6% last year. The aforementioned mix caused a reduction of the combined income tax rate from 32.5% to 28.6% for fiscal 2006. When applied to the consolidated loss before income tax recovery and discontinued operations for the fiscal year 2006, this rate resulted in an income tax recovery of $0.2 million. The actual recovery was increased by $1.2 million due to favorable permanent differences ($1.5 million last year) and by $0.5 million as a result of re-evaluating the relevant net future tax assets in line with Quebec provincial income tax rate increases from 8.9% to 11.9% over a three-year period, enacted during the year. The main offset to the foregoing is the valuation allowance of $0.5 million this year ($1.5 million last year) taken by means of non-recognition of certain income tax benefits in relation to the pre-tax loss of a Canadian subsidiary (see Note 17 to the consolidated financial statements).

*Income Tax Receivable*

Prior to March 31, 2006, Héroux-Devtek Aérostructure inc., a wholly owned Canadian subsidiary, was wound-up into the Company. This resulted in an increase of approximately $4.2 million in income tax receivable at March 31, 2006, through the availability of certain tax attributes due to the winding-up. Since the materialization of these tax attributes is primarily related to tax depreciation, the ensuing counterpart was mainly reflected in an increase in long-term future income tax liabilities.

*Future Income Tax Assets*

The current future income tax assets amounted to $8.9 million at March 31, 2006, in comparison to $7.2 million a year ago. The main difference is the $0.8 million increase in tax benefits related to certain non deductible inventory provisions this year.

Long-term future income tax assets amounted to $6.5 million at March 31, 2006, a reduction of $1.1 million in comparison to last year. This reduction is mainly attributable to the use of previously recorded tax loss benefits in the amount of $1.6 million this year (see Note 17 to the consolidated financial statements).

**Net Loss**

For fiscal year 2006, the Company posted a net loss from continuing operations of $0.4 million compared to a net loss of $4.3 million last year, as shown below:

| | **2006** | **2005** |
|---|---|---|
| Net loss from continuing operations ($'000) | (406) | (4,291) |
| Net income from discontinued operations ($'000) | 8,661 | 2,162 |
| Net income (loss) ($'000) | 8,255 | (2,129) |
| Loss per share from continuing operations ($) | (0.01) | (0.16) |
| Earnings (loss) per share ($) | 0.29 | (0.08) |

Earnings (loss) per share figures are based on weighted-averages of 28,727,386 common shares outstanding for fiscal 2006 and 26,932,650 for the previous year. The increase is essentially due to the 4.5 million common share offering completed last November, and the issuance of 34,047 common shares pursuant to the Company's stock purchase and ownership incentive plan (see Note 15 to the consolidated financial statements).

On May 31, 2006, the date of this MD&A, the Company had 31,493.546 common shares and 873,021 stock options outstanding.

## LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2006, the Company had cash and equivalents amounting to $20.9 million, compared to $9.6 million a year earlier.

*Operating Activities*

The Company generated cash flows from continuing operations and used cash and cash equivalents for its operating activities as follows:

| | 2006 ($'000) | 2005 ($'000) |
|---|---|---|
| Cash flows from continuing operations | 20,007 | 11,934 |
| Net change in non-cash items related to operations | (3,130) | (17,908) |
| Cash and cash equivalents provided by (used for) operating activities | **16,877** | (5,974) |

The $8.1 million increase in cash flows from continuing operations for fiscal 2006 was mainly due to the reduction of $3.9 million in the net loss, a $0.6 million increase in amortization and a $3.0 million net increase in future income taxes, mainly due to the winding-up of a subsidiary into the Company in the last quarter of fiscal 2006. The net change of $3.1 million in non-cash items was mainly caused by an $8.0 million increase in accounts receivable due the higher sales, and a $3.4 million increase in income tax receivables, offset by a $9.7 million increase in accounts payable. The increase in accounts payable reflects the increase in purchase of raw materials in the last quarter of fiscal 2006, for which progress billings were made and received before the March 31, 2006 year-end. Amounts related to the progress billings are shown as a reduction of the related inventories on the Company's balance sheets.

For fiscal 2005, the net change in non-cash items reduced cash flows from continuing operations by $17.9 million. The main reasons for this were the following: accounts receivable increased by $4.1 million due to higher fourth quarter sales; other receivables rose by $3.3 million, reflecting mainly tooling costs invoiced to customers; inventories grew by $3.6 million, primarily on the strength of higher business volume at the Landing Gear Division at fiscal year-end 2005; other current assets were up $2.3 million because of deposits for the purchase of machinery and equipment included in this item; and finally, customer advances at the Landing Gear Division declined by $5.0 million during the course of fiscal 2005 since they were liquidated as deliveries were made on the related sales contracts. All these net uses of cash flows were somewhat offset by a $2.8 million increase in accounts payable and accrued liabilities at March 31, 2005 (see Note 18 to the consolidated financial statements).

*Investing Activities*

The Company's investing activities were as follows:

| | 2006 ($'000) | 2005 ($'000) |
|---|---|---|
| Purchase of property, plant and equipment and finite-life intangible assets | (13,391) | (13,370) |
| Proceeds on disposal of property, plant and equipment | 305 | 1,388 |
| Business acquisition, net of cash acquired | (3,425) | (67,349) |
| Proceeds from the sale of Logistics and Defence Division, Diemaco | 19,035 | - |
| Cash and cash equivalents provided by (used for) investing activities | **2,524** | **(79,331)** |

The Company's investing activities provided cash and cash equivalents of $2.5 million, having used $79.3 million last year.

In fiscal 2006, the Company invested $13.4 million in property, plant and equipment, which included investments for its Kitchener plant expansion and the first phase of the modernization of its plating department at the Longueuil plant.

Investments in business acquisition represent essentially the acquisition of Progressive on April 1, 2004 and additional payments of $3.4 million made in 2006 related to profitability performance at Progressive for fiscal 2005. The last additional payment to be made related to profitability performance for fiscal 2006 was estimated at US $1 million ($1.2 million) and was accrued for at March 31, 2006 (see Note 3 to the consolidated financial statements).

In fiscal 2005, the Company invested $13.4 million in property, plant and equipment, including $3.3 million invested to expand the assembly and machining section at the Laval plant and add a new landing gear test facility for business and regional jet landing gear. A further $3.9 million was invested at the Gas Turbine Components Division, representing essentially the exercise of a purchase options for equipment under operating leases.

Investments in capital expenditures for fiscal 2007 are expected to be close to $25 million.

On May 20, 2005, the Company concluded the sale of its Logistics and Defence Division, Diemaco. The final sale price amounted to $19.0 million (see Note 4 to the consolidated financial statements).

*Financing Activities*

The Company's financing activities were as follows:

| | 2006 ($'000) | 2005 ($'000) |
|---|---|---|
| Increase in long-term debt | 17,590 | 51,488 |
| Repayment of long-term debt | (40,287) | (24,335) |
| Issuance of common shares | 15,790 | 16,386 |
| Other | (210) | (530) |
| Cash and cash equivalents provided by (used for) financing activities | **(7,117)** | **43,009** |

During the first quarter of fiscal year 2006, subsequent to the sale of the Logistics and Defence Division, Diemaco, the Company repaid $15.3 million on its Secured Syndicated Revolving Term Credit Facilities.

On November 10, 2005, the Company closed a public offering of 4.5 million common shares priced at $3.75 per share for net proceeds of $15.7 million (net of $1.2 million in fees and expenses) (see Note 15 to the consolidated financial statements). The Company also applied the net proceeds from the sale of common shares to the reduction of its lines of credit under its credit facilities but not as a permanent reduction thereof. On a year-to-date basis, net capital repayments on the credit facilities totalled $24.7 million (see Note 13 to the consolidated financial statements).

In fiscal 2005, in order to finance the acquisition of Progressive, the Company used $36.4 million from its Secured Syndicated Revolving Credit Facilities and issued 3.5 million common shares for proceeds of $16.2 million. The Company also drew an additional $15.1 million and repaid a total of $20.6 million on its credit facilities.

At the end of the third quarter ended December 31, 2005, the Company concluded the annual extension of its credit facilities from March 21, 2006 to March 21, 2007.

The Company was in compliance with all its restrictive debt covenants at March 31, 2006, and expects to continue to comply with these restrictive financial covenants in fiscal 2007.

**Pension Plans**

Some of the Company's employees are covered by defined benefit pension plans. The funded status of these plans is as follows:

| | 2006 ($'000) | 2005 ($'000) |
|---|---|---|
| Deficit | 14,662 | 14,285 |
| Accrued liabilities (included in other liabilities) | 6,716 | 6,949 |

The pension plan deficit of $14.7 million at March 31, 2006 includes $9.5 million in pension plan obligations related to unregistered pension plans, primarily for ex-executives of Devtek Corporation which was acquired by the Company in June 2000, that do not require funding of the deficit. Funding occurs as pension benefits are paid to the retired executives.

**Capital Stock, Stock Option Plan and Stock Purchase and Ownership Incentive Plan (Stock Purchase Plan)**

At March 31, 2006, the Company had 31,488,599 common shares outstanding (26,954,552 in 2005).

In fiscal 2006, the Company issued 4.53 million common shares at a weighted-average price of $3.75 for a total net cash consideration of $15.8 million. This includes the 4.5 million common shares issued pursuant to the November 2005 public offering and 34,047 common shares issued under the Stock Purchase Plan.

In fiscal 2005, the Company issued 3.55 million common shares for a total net cash consideration of $16.4 million. Of these, 3.5 million common shares were issued at a price of $4.90 for a net cash consideration of $16.2 million in conjunction with the financing and closing of the Progressive acquisition. The remaining 52,993 common shares were issued under the Stock Purchase Plan (17,993 common shares) and pursuant to the exercise of stock options (35,000 common shares) for a total cash consideration of $0.2 million.

As of March 31, 2006, 873,021 stock options were issued and outstanding with weighted-average maturity of 4.2 years and a weighted-average exercise price of $5.72 (see Note 15 to the consolidated financial statements).

*Changes to the Company's Stock Option Plan*

On February 1, 2006, the Human Resources and Corporate Governance Committee recommended to the Board of Directors (the "Board") the approval of certain changes to the Company's stock option plan, which were approved the same day by the Board. The purpose of these changes is to increase the number of common shares that may be issued under the stock option plan and under the stock purchase plan from an aggregate of 2,277,118 common shares (of which 300,319 common shares remain available for future grants at March 31, 2006 and of which 90,000 are reserved for the stock purchase and ownership incentive plan) to 3,148,257 common shares (representing about 10% of the common shares outstanding at March 31, 2006 and of which 340,000 will be reserved for the stock purchase and ownership incentive plan).

These changes are subject to the approval of the Toronto Stock Exchange and by the shareholders of the Company at the next annual general meeting on August 3, 2006.

**Foreign Exchange**

The Company is subject to foreign currency fluctuations from the translation of revenues (sales), expenses, assets and liabilities of its self-sustaining foreign operations and from transactions denominated in foreign currency. The year-end and average exchange rates were as follows at March 31, 2006 and 2005 and for the fiscal years then ended:

| Canada / US Exchange Rates | | 2006 | 2005 |
|---|---|---|---|
| Year-end exchange rates used to translate assets and liabilities | 1$ Canadian/ US $ equivalent | 1.1680 | 1.2096 |
| | US $ equivalent | 0.856 | 0.827 |
| Average exchange rates used to translate revenues (sales) and expenses | 1$ Canadian/ US $ equivalent | 1.1982 | 1.3079 |
| | US $ equivalent | 0.835 | 0.765 |

The Company makes use of derivative contracts to hedge foreign currency fluctuation exposure or risks in an effort to mitigate these risks. At March 31, 2006, the Company had forward foreign exchange contracts totalling US $146.5 million at an average exchange rate of 1.2617 maturing over the next four fiscal years, the majority of which mature over the next two fiscal years. See off-balance sheet items and commitments below.

**Consolidated Balance Sheets**

The following table itemizes and explains the significant changes in the consolidated balance sheets between March 31, 2005 and March 31, 2006:

| Item | Change ($ Million) | Explanation |
|---|---|---|
| Cash and cash equivalents | 11.3 | See consolidated statements of cash flows |
| Accounts receivable | 8.0 | Increase consistent with the higher year-over-year fourth quarter sales |
| Income tax receivable | 3.4 | Increase due primarily to the realization of certain income tax attributes of a Canadian subsidiary wound-up into the Company prior to year-end |
| Property, plant and equipment, net | (4.3) | Due to:<br>– Purchase of capital assets ($12.5 million)<br>Net of:<br>– Amortization ($15.1 million)<br>– Net proceeds ($0.3 million)<br>– A lower US exchange rate used to convert the net assets of self-sustaining US subsidiaries ($1.4 million) |

| Item | Change ($ Million) | Explanation |
|---|---|---|
| Finite-life intangible assets, net | (1.8) | Represents mainly the amortization of the underlying value of the net backlog acquired as part of the acquisition of Progressive |
| Goodwill | 2.6 | Due to the variation in additional payments to the sellers related to the profitability performance of Progressive ($3.1 million), net of the lower US exchange rate used to convert the net assets of self-sustaining US subsidiaries ($0.5 million) |
| Accounts payable and accrued liabilities | 10.9 | Consistent with the higher level of activity and to the increase in raw material purchases in the fourth quarter |
| Income tax payable | 1.9 | Due mainly to the tax impact related to the gain on sale of the Logistics and Defence Division, Diemaco |
| Long-term debt (including current portion) | (24.1) | Mainly due to:<br>– Increase in non-interest bearing loans ($3.1 million)<br>Net of:<br>– Net capital repayments of long-term debt ($25.8 million) mainly on the Secured Syndicated Revolving Credit Facilities; and<br>– A lower US exchange rate used to convert the net assets of self-sustaining US subsidiaries ($1.4 million) |
| Future income taxes (long-term liabilities) | 3.6 | Increase represents mainly the counter-part of the realization of the income tax attributes explained above. |
| Capital stock | 16.2 | Due to:<br>– Net proceeds from the 4.5 million common share issue ($15.7 million)<br>– Future income tax impact relating to common share issue fees and expenses ($0.4 million)<br>– The Company’s stock purchase and ownership incentive plan ($0.1 million) |
| Cumulative translation adjustment | (2.0) | Represents the counterpart of the impact of foreign exchange rate fluctuations on the net assets of self-sustaining US subsidiaries |
| Retained earnings | 8.3 | See consolidated statements of retained earnings |

The Company's working capital ratio was 1.76:1 on March 31, 2006 compared to 1.48:1 on March 31, 2005, while the long-term debt-to-equity ratio was 0.33:1 on March 31, 2006 compared to 0.51:1 on March 31, 2005. At March 31, 2006, the balance sheet included cash and cash equivalents of $20.9 million. At March 31, 2005, cash and cash equivalents stood at $9.6 million.

The summary of the Company’s contractual obligations, including payments due over the next five years and thereafter, is as follows:

| | | Payments due by period | | | |
|---|---|---|---|---|---|
| **Contractual Obligations ($’000)** | **Total** | **Less than 1 year** | **1-3 years** | **4-5 years** | **After 5 years** |
| Non-interest-bearing loans | 17,268 | 2,638 | 5,126 | 3,395 | 6,109 |
| Capital leases (including interest expenses) | 9,595 | 3,079 | 5,922 | 594 | - |
| Operating leases – Machinery and equipment | 10,688 | 2,955 | 3,936 | 2,165 | 1,632 |
| Operating leases - Buildings | 1,003 | 451 | 499 | 53 | - |
| Sub-total, contractual obligations | 38,554 | 9,123 | 15,483 | 6,207 | 7,741 |
| Secured Syndicated Revolving Credit Facilities, if not extended next year | | | | | |
| − Operating credit facilities | 5,840 | 5,840 | - | - | - |
| − Term credit facilities | 29,966 | - | 11,988 | 17,978 | |
| Total contractual obligations | 74,360 | 14,963 | 27,471 | 24,185 | 7,741 |

**Off-Balance Sheet Items and Commitments**

The Company had entered into operating leases amounting to $11.7 million as at March 31, 2006, mainly for machinery and equipment. All these amounts are repayable over the next seven years (see Note 20 to the consolidated financial statements). At March 31, 2006, the Company also had machinery and equipment purchase commitments totalling $7.4 million (see Note 20 to the consolidated financial statements).

At March 31, 2006, the Company had forward foreign exchange contracts with Canadian chartered banks totalling US $146.5 million at an average exchange rate of 1.2617. These contracts relate mainly to its export sales, and mature at various dates between April 2006 and December 2009 (see Note 5 to the consolidated financial statements). This compares to US $128.0 million in forward foreign exchange contracts held at March 31, 2005 at an average exchange rate of 1.3308.

## Critical Accounting Estimates

- *Design-to-manufacture contracts and major assembly manufacturing contracts*

  The Company's management uses estimates to value inventory and cost of sales related to design-to-manufacture contracts and major assembly manufacturing contracts. In fact, non-recurring costs (development, pre-production and tooling costs) and the excess over production costs (production costs incurred in the early stage of a contract in excess of the average estimated production unit cost for the entire contract) are included in inventory. Recovery of these costs is expected from related contract sales as production costs decline to below the average production unit cost.

  Two major assumptions are made when capitalizing non-recurring costs and the excess over production costs in inventory:
  - Estimated average production unit cost; and
  - Production accounting quantities.

  The estimated average production unit cost includes raw materials, direct labour and manufacturing overhead cost, and is based on the learning curve concept. This anticipates a predictable decrease in direct labour costs as tasks and production techniques become more efficient through repetition. To evaluate the average production unit cost, management bases its analysis mainly on historical performance, economic trends, labour agreements and information provided by customers and suppliers. It also takes into consideration inflation rates, foreign exchange rates, labour productivity, employment levels and salaries.

  Production accounting quantities for a particular contract are essentially established at the inception of the contract or contract date, and are based on management's assessments of the anticipated demand for the related aircraft or product, taking into account mainly firm order and committed order backlog and options, as well as prevailing market and economic conditions.

  Management reviews the major assumptions on a quarterly basis, and a more detailed review is made at fiscal year-end. The effect of any revision to the assumptions is accounted for by way of a cumulative catch-up adjustment in the period or year in which the revision takes place.

  A 1% change in the estimated future costs to produce the remaining quantities on all design-to-manufacture contracts and all major assembly manufacturing contracts would have an impact of approximately \$0.7 million on the Company's cost of sales, including \$0.4 million relating to cumulative catch-up adjustments for prior years.

- *Goodwill*

  Goodwill is tested for impairment annually or more frequently if events or circumstances indicate that the asset might be impaired. The Company selected its fourth quarter as its annual testing period for its goodwill. A goodwill impairment charge is recorded when the discounted value of the expected future cash flows of the entire related reporting unit is less than its carrying value. Future cash flows are forecast based on the management's best estimates of revenues, production costs, manufacturing overhead and other costs. These estimates are made by reviewing existing contracts, expected future orders, current cost structure, anticipated cost variations, labour agreements and general market conditions, and are subject to review and approval by Company's senior management. The future cash flows are discounted using an estimated weighted-average cost of capital rate.

- *Pension plans and other employee post-retirement benefits*

  Certain critical assumptions are used in the determination of pension plan and other employee post-retirement benefit costs and obligations. In particular, the discount rate and the expected long-term rate of return on plan assets are important assumptions used to measure these costs and obligations. Other assumptions include the rate of increase in employee compensation, as well as demographic factors such as employee retirement ages, mortality rates and turnover. These assumptions are reviewed annually.

  A lower discount rate increases benefit costs and obligations. A 1% change in the discount rate would have an impact of approximately $0.2 million and $4.0 million, respectively, on the Company's pension plan expense and accrued benefit obligation.

  A lower expected rate of return on pension plan assets also increases benefit costs. A 1% change in the return assumption would have an impact of approximately $156,000 on the Company's pension plan expense.

- *Income taxes*

  The Company accounts for future income tax assets mainly from loss carry-forwards and deductible temporary differences. Company management assesses and reviews the realization of these future income tax assets at least annually, at year-end, to determine whether a valuation allowance is required. Based on that assessment, it is determined whether it is more likely than not that all or a portion of the future income tax assets will be realized. Factors taken into account include future income based on internal forecasts, losses in recent years and their expiry dates and a history of loss carry-forwards, as well as reasonable tax planning strategies.

## FUTURE CHANGES IN ACCOUNTING POLICIES

The following standards may, when adopted, have a material impact on the Company consolidated financial statements:
- Financial instruments – Recognition and measurement;
- Hedges; and
- Comprehensive income.

These standards will be effective for the Company for the first quarter of fiscal year 2008. The principal impacts of the standards are summarized below:

*Financial instruments – Recognition and measurement*
- All derivative financial instruments, including embedded derivatives that are not closely related to the host contract, must be recorded on the balance sheet and measured at fair value.
- All financial assets must be classified as held for trading, available for sale, held to maturity or as loans and receivables, and measured either at fair value, cost or amortized cost.

- Gains and losses on financial instruments measured at fair value must be recognized in the income statement or in their comprehensive income.

*Hedges*
Hedges can be designed as either fair value hedges, cash flow hedges or hedges of a net investment in a self-sustaining foreign operation. Gains and losses as a result of changes in the fair value of hedging instruments which quality for hedge accounting must be recognized to income, together with the offsetting gains or losses on the hedged risk in the change period or to other comprehensive income if certain criteria are met, with subsequent reclassification to income when the hedged item affects income.

*Comprehensive income*
Comprehensive income is the change in equity (net assets) of an enterprise during a period from transactions and other events and circumstances from non-owner sources. Comprehensive income and its components must be presented in the consolidated financial statements with the same prominence as other financial statements that constitute the complete set of consolidated financial statements.

The Company is currently assessing the impact of these recommendations on its consolidated financial statements.

## CERTIFICATION ON DISCLOSURE CONTROLS AND PROCEDURES, AND OTHER CORPORATE GOVERNANCE POLICIES

At March 31, 2006 and 2005, Company management proceeded with the certification on disclosure controls and procedures by its Chief Executive Officer (CEO) and Chief Financial Officer (CFO).

Disclosure controls and procedures have the general objective of seeking to ensure that information disclosable by the Company in its reports, regulatory statements, filings and other communications is recorded, processed, summarized and reported on a timely basis. This information also includes controls to ensure compliance with Canadian disclosure requirements beyond the Company's consolidated financial statements.

In that regard, in February 2005, the Company's Human Resources and Corporate Governance Committee and the Board approved the creation of a disclosure management committee. This committee has the responsibility to ensure that management has access to all information that must be disclosed in the Company's public reporting to provide accurate and complete information to security holders.

It also ensures that the Company's CEO and CFO can evaluate the effectiveness of the design and operation of the Company's disclosure controls and procedures for the purpose of improving them as necessary and disclosing the results of evaluation in the reports.

At March 31, 2006 an evaluation was carried out, under the supervision of the CEO and the CFO of the effectiveness of the Company's disclosure controls and procedures as definited in Multilateral Instruments 52-109. Based on this evaluation, the Company's CEO and CFO concluded that the design and operation of these disclosure controls and procedures were effective.

The required certification on disclosure controls and procedures and their effectiveness will be filed on SEDAR on or before June 29, 2006.

The Human Resources and Corporate Governance Committee and the Board also approved the Company's Code of Business Conduct in February 2005, which establishes a high standard for ethical behaviour throughout the Company, and the Company's Whistleblower Policy in September 2004, which encourages and enables employees to raise any serious concerns, particularly in relation to the violation of laws within the Company, without fear of reprisal or discrimination.

## RISKS AND UNCERTAINTIES

Héroux-Devtek operates in industry segments subject to various risks and uncertainties that could have a material adverse effect on the Company's business, financial condition and results of operations. These risks and uncertainties include, but are not limited to, those mentioned below.

*Reliance on Large Customers*

The Company has exposure due to its reliance on certain large contracts and customers. The Company's six largest customers account for approximately 64% of its sales. Any loss or delay in certain orders from any of these customers could have a negative impact on the Company's results.

*Availability and Cost of Raw Materials*

The main raw materials purchased by the Company are aluminium, steel and titanium. Supply and cost of these materials is somewhat outside the Company's control. Difficulty in procuring raw materials in sufficient quantities and in a timely fashion, along with cost increase for these materials, could also have a material adverse effect on the Company's operations and financial condition.

In the past two years, as this situation has escalated with the improvement of the global economy and the explosive growth of the Chinese economy in particular, the Company has begun to take steps to mitigate this risk. It now includes clauses in its contracts to share the risk of raw materials availability and cost with its customers. It also negotiates long-term supply agreements with its suppliers of raw materials, and has increased its monitoring of the supply chain to ensure timely deliveries.

*Operational Risk*

The activities conducted by the Company are subject to operational risks including competition from other businesses, performance of key suppliers, product performance warranties, regulatory risks, successful integration of new acquisitions, dependence on key personnel and reliance on information systems, all of which could affect the Company's ability to meet its obligations.

*General Economic Conditions*

Unfavourable economic conditions may adversely affect the Company's business. For example, the large civil aerospace industry has experienced considerable uncertainty in prior years, especially the market for planes with more than 100 seats. In fiscal 2006, the regional jet market was negatively impacted by lower demand. Furthermore, the industrial power generation market, which collapsed in 2002, is now recovering slowly. This could adversely affect the Company's financial condition and results of operation. Although long-term growth will likely eventually resume, the timing of that resumption is uncertain, and these sectors will remain cyclical. In addition, curtailment of production activities due to unfavourable economic conditions could result in the Company incurring significant costs associated with temporary layoffs or termination of employees.

*Military Spending*

Although significant increases in military budgets, particularly in the United States, were announced in recent years, these expenses are approved by government on a yearly basis and are subject to the political climate and changing priorities.

*Foreign Currency Fluctuations*

The Company is exposed to risks resulting from foreign currency fluctuations arising either from carrying on business in Canada in foreign currencies or through operations in the United States. In an effort to mitigate those risks, the Company makes use of derivative contracts to hedge this exposure.

*Liquidity and Access to Capital Resources*

The Company requires continued access to capital markets to support its activities. To satisfy its financing needs, the Company relies on long-term and short-term debt and cash flow generated from operations. Any impediments to the Company's ability to access capital markets, including significant changes in market interest rates, general economic conditions or the perception in the capital markets of the Company's financial condition or prospects, could have a material adverse effect on the Company's financial condition and results of operation.

*Restrictive Debt Covenants*

The indentures governing certain of the Company's indebtedness and, in particular, syndicated credit facilities contain covenants that, among other things, restrict the Company's ability to:

- sell all or substantially all its assets;
- incur secured indebtedness;
- engage in mergers or consolidations;
- invest in capital expenditures over a certain amount per year; and
- engage in transactions with affiliates.

These restrictions could impair the Company's ability to finance its future operations or its capital needs, or to engage in other business activities that may be in its interest.

*Changing Interest Rates*

The Company's profitability may be directly affected by the level of and fluctuations in interest rates. The Company uses derivatives as an integral part of its asset/liability management program to mitigate or reduce its overall financial risk.

*External Business Environment*

The Company faces a number of external risk factors, more specifically, general economic conditions, government policies and changing priorities or possible spending cuts by governments.

*Warranty Casualty Claim Losses*

The products manufactured by the Company are complex and sophisticated and may contain defects that are difficult to detect and correct. Errors may be found in the Company's products after they are delivered to the customers. If so, the Company may not be able to correct such errors. The occurrence of errors and failures in the Company's products could result in warranty claims or the loss of customers. Any claims, errors or failures could have an adverse effect on the Company's operating results and business. In addition, due to the nature of the Company's business, the Company may be subject to liability claims involving its products or products for which it provides services. The Company cannot be certain that its insurance coverage will be sufficient to cover one or more substantial claims. Furthermore, there can be no assurance that the Company will be able to obtain insurance coverage at acceptable levels and cost in the future.

*Environmental Matters*

The Company's activities are subject to environmental laws and regulations associated with risks to human health and the environment. Changes to these laws and regulations could have a significant adverse effect on the Company's operations and financial situation. The Company monitors these risks through environmental management systems and policies.

*Collective Bargaining Agreements*

The Company is party to some collective bargaining agreements, which are subject to expiration at various times in the future. If the Company is unable to renew these agreements or others as they become subject to renegotiation from time to time, it could result in work stoppages and other labour disturbances, which could have a material adverse effect on the Company's business. The Company currently has collective agreements in place with all its unionized employees for the next two years.

*Skilled Labour*

Héroux-Devtek's ability to meet its future goals and objectives depends, in part, on its ability to attract and retain the necessary skilled labour. The skilled labour market in the aerospace industry is expected to be highly competitive in the future. The Company's inability to attract and retain skilled labour, particularly engineers, machinists and programmers, could adversely affect its financial condition and results of operations.

Héroux-Devtek does not anticipate a substantial increase in its manpower requirements over the next few years. The Company is therefore addressing this risk by developing its human resource strengths internally and by working to retain the skilled employees that it currently has and attract the best talent by fostering a strong sense of corporate culture. In 2006, management filled a senior position that includes responsibility for the Company's human resources.

## SELECTED QUARTERLY FINANCIAL INFORMATION

| ($'000 except per share data) | Total | First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|---|
| *For the fiscal year ended March 31, 2006* | | | | | |
| Sales | 256,197 | 53,917 | 62,303 | 66,853 | 73,124 |
| Net income (loss) from continuing operations | (406) | (2,432) | (256) | 743 | 1,539 |
| Net income from discontinued operations | 8,661 | 8,844 | - | - | (183) |
| Net income (loss) | 8,255 | 6,412 | (256) | 743 | 1,356 |
| Earnings (loss) per share from continuing operations ($) – basic and diluted | (0.01) | (0.09) | (0.01) | 0.03 | 0.05 |
| Earnings (loss) per share ($) – basic and diluted | 0.29 | 0.24 | (0.01) | 0.03 | 0.04 |
| *For the fiscal year ended March 31, 2005* | | | | | |
| Sales | 232,998 | 52,318 | 57,165 | 57,101 | 66,414 |
| Net income (loss) from continuing operations | (4,291) | (1,440) | (1,734) | (1,631) | 514 |
| Net income from discontinued operations | 2,162 | 124 | 173 | 744 | 1,121 |
| Net income (loss) | (2,129) | (1,316) | (1,561) | (887) | 1,635 |
| Earnings (loss) per share from continuing operations ($) – basic and diluted | (0.16) | (0.05) | (0.06) | (0.06) | 0.02 |
| Earnings (loss) per share ($) – basic and diluted | (0.08) | (0.05) | (0.06) | (0.03) | 0.06 |

After a slow start in the first half of the year, sales picked up in the last two quarters of fiscal 2006. The improved results of the Landing Gear Division helped generate positive figures in the last two quarters.

## Fourth Quarter 2006 Results

Traditionally a strong period, the fourth quarter of fiscal 2006 was yet again strong for the Company, with both Landing Gear and Aerostructure showing improved net earnings over last year's fourth quarter due to increased sales and performance.

The adjustment of $(0.2) million in the fourth quarter to the net income from discontinued operations represents the final adjustment at year-end to the provision for income taxes estimated at time of sale related to the gain on sale of Diemaco.

## OUTLOOK

The military aerospace market is expected to remain solid for the next three years. The Joint Strike Fighter (JSF) program, considered to be the largest on-going military program over the next 20 years, is still in the development phase, with the first aircraft set for an inaugural flight later this year. Through our Aerostructure Division, the Company is particularly well positioned to grow with the JSF program, scheduled to ramp-up over a seven-year period beginning in calendar 2008.

Aircraft engine component sales have been impacted by delivery and quality issues at the Gas Turbine Components Division, and while improvements have been made, these sales are expected to decline further in the current fiscal year.

With the exception of regional jets, there is good demand for all civil aircraft, particularly 100+ seaters. Repair and maintenance business for both civil and military aircraft is expected to increase.

The Gas Turbine Components Division has experienced low business volume which negatively impact on its overall results. However, modest sales growth is expected in industrial gas turbines while wind power represents a fast-growing sector where the Company is well positioned to benefit from in the coming years.

The Company continues to work on managing the negative impact of the low US/Canada exchange rate and high raw materials prices. Based on the actual backlog, the Company's management is expecting an internal sales growth of approximately 10% per year over the next 3 years and an increase in the Company's overall performance with a return to profit in the current fiscal year.

## Additional Information and Continuous Disclosure

This MD&A was approved by the Audit Committee on May 30, 2006 and by the Board of Directors on May 31, 2006. Updated information on the Company can be found on the SEDAR web site at www.sedar.com.