MANAGEMENT'S DISCUSSION AND ANALYSIS

Third quarter ended December 31, 2019

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OVERVIEW

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. and its subsidiaries (''Héroux-Devtek'', the ''Corporation'' or "Management") evolved between March 31, 2019 and December 31, 2019. It also compares the operating results and cash flows for the quarter and nine-month period ended December 31, 2019 to those of the same periods of the prior fiscal year.

This MD&A is based on the unaudited interim condensed consolidated financial statements for the quarter ended December 31, 2019, and should be read in conjunction with them as well as with the audited consolidated financial statements and MD&A for the fiscal year ended March 31, 2019, all of which are available on the Corporation's website at www.herouxdevtek.com and on SEDAR at www.sedar.com. All amounts in this MD&A are in thousands of Canadian dollars unless otherwise indicated. This MD&A was approved by the Audit Committee and Board of Directors of the Corporation on February 5, 2020.

IFRS and non-IFRS financial measures

This MD&A contains both IFRS and non-IFRS financial measures. Non-IFRS financial measures are defined and reconciled to the most comparable IFRS measures in the *Non-IFRS Financial Measures* section under *Operating Results*.

Materiality for disclosures

Management determines whether information is material based on whether they believe a reasonable investor's decision to buy, sell or hold securities of the Corporation would likely be influenced or changed should the information be omitted or misstated, and discloses material information accordingly.

FORWARD-LOOKING STATEMENTS

Certain statements in this MD&A, including those presented in the Guidance section, are forward-looking statements subject to risks, uncertainties and other important factors that could cause the Corporation's actual performance to differ materially from those expressed in or implied by such statements. These statements are provided for the purpose of assisting the reader in understanding the Corporation's financial performance and prospects and to present management's assessment of future plans and operations. The reader is cautioned that such statements may not be appropriate for other purposes.

They may be impacted by factors including, but not limited to: the impact of worldwide general economic conditions; 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; financial and operational performance of suppliers and customers; foreign exchange or interest rate fluctuations; and the impact of accounting policies issued by international standard setters. For further details, please see the Risk Management section of the Corporation's MD&A for the fiscal year ended March 31, 2019. Readers are cautioned that the foregoing list of factors that may affect future growth, results and performance is not exhaustive, and undue reliance should not be placed on forward-looking statements.

Although management believes the expectations conveyed by these statements, and while they are based on information available on the date such statements were made, there can be no assurance that such expectations will prove to be correct and readers are advised that actual results may differ from expected results. All subsequent forward-looking statements, whether written or orally attributable to the Corporation or persons acting on its behalf, are expressly qualified in their entirety by these cautionary statements. Unless otherwise required by applicable securities laws, the Corporation expressly disclaims any intention, and assumes no obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise.

HIGHLIGHTS

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Sales	$ 157,253	$ 144,528	$ 446,196	$ 325,963
Operating income	13,466	11,904	34,356	22,050
Adjusted operating income(1)	13,466	13,973	34,971	25,355
Adjusted EBITDA(1)	24,563	22,883	67,582	48,303
Net income	8,705	7,390	21,455	14,236
Adjusted net income(1)	8,705	9,367	21,971	17,558
Cash flows related to operating activities	9,664	12,651	25,863	32,788
Free cash flow(1)	7,939	11,901	13,599	26,421
In dollars per share				
EPS - basic and diluted	$ 0.24	$ 0.20	$ 0.60	$ 0.39
Adjusted EPS(1)	0.24	0.26	0.61	0.48
As at			December 31, 2019	September 30, 2019
Funded backlog(2)			$ 839,000	$ 769,000

(1) Non-IFRS financial measure. Refer to the Non-IFRS financial measures section under Operating Results for definitions and reconciliations to the most comparable IFRS measures.
(2) Represents firm orders

- Backlog increased to $839 million, compared to $769 million as at September 30, 2019, mainly due to increased demand for defence products under long term contracts.
- During the quarter ended December 31, 2019, the Corporation achieved consolidated sales of $157.3 million, operating income of $13.5 million and adjusted EBITDA of $24.6 million, compared to $144.5 million, $11.9 million and $22.9 million during the same period last fiscal year.
- On January 25, 2020, The Boeing Company completed the first flight of the Boeing 777X for which the Corporation provides complete landing gear systems.
- During the quarter, the Corporation reached an agreement to extend the term of its Revolving Facility from May 2022 to December 2024.

Guidance

- In February 2020, Management increased its fiscal 2020 sales guidance from between $580-$600 million to $600 to $610 million in order to reflect stronger than expected growth.

OPERATING RESULTS

	Three months ended December 31,			Nine months ended December 31,		
	2019	2018	*Variance*	2019	2018	*Variance*
Sales	$157,253	$144,528	*$ 12,725*	$446,196	$325,963	*$120,233*
Gross profit	26,829	24,927	*1,902*	73,268	53,466	*19,802*
Selling and administrative expenses	13,363	10,954	*2,409*	38,297	28,111	*10,186*
Adjusted operating income[(1)]	13,466	13,973	*(507)*	34,971	25,355	*9,616*
Non-recurring items	—	2,069	*(2,069)*	615	3,305	*(2,690)*
Operating income	13,466	11,904	*1,562*	34,356	22,050	*12,306*
Net financial expenses	2,906	2,764	*142*	8,379	5,409	*2,970*
Income tax expense	1,855	1,750	*105*	4,522	2,405	*2,117*
Net income	$ 8,705	$ 7,390	*$ 1,315*	$ 21,455	$ 14,236	*$ 7,219*
Adjusted net income[(1)]	$ 8,705	$ 9,367	*$ (662)*	$ 21,971	$ 17,558	*$ 4,413*
As a percentage of sales						
Gross profit	17.1%	17.2%	*-10 bps*	16.4%	16.4%	*0 bps*
Selling and administrative expenses	8.5%	7.6%	*90 bps*	8.6%	8.6%	*0 bps*
Operating income	8.6%	8.2%	*40 bps*	7.7%	6.8%	*90 bps*
Adjusted operating income[(1)]	8.6%	9.7%	*-110 bps*	7.8%	7.8%	*0 bps*
In dollars per share						
EPS - basic and diluted	$ 0.24	$ 0.20	*$ 0.04*	$ 0.60	$ 0.39	*$ 0.21*
Adjusted EPS[(1)]	$ 0.24	$ 0.26	*$ (0.02)*	$ 0.61	$ 0.48	*$ 0.13*

[(1)] Non-IFRS financial measure. Refer to the Non-IFRS financial measures section for definitions and reconciliations to the most comparable IFRS measures.

Sales

Sales by sector were as follows:

	Three months ended December 31,					
	2019	2018	Acquisitions	FX impact	Net variance	
Commercial	$ 73,203	$ 65,493	$ 9,848	$ 302	$ (2,440)	(3.7)%
Defence[(1)]	84,050	79,035	924	236	3,855	4.9 %
Total	$ 157,253	$ 144,528	$ 10,772	$ 538	$ 1,415	1.0 %

	Nine months ended December 31,					
	2019	2018	Acquisitions	FX impact	Net variance	
Commercial	$ 211,782	$ 158,279	$ 43,127	$ 1,597	$ 8,779	5.5 %
Defence[(1)]	234,414	167,684	48,393	1,768	16,569	9.9 %
Total	$ 446,196	$ 325,963	$ 91,520	$ 3,365	$ 25,348	7.8 %

[(1)] Includes defence sales to civil customers and governments.

Sales grew 8.8% to $157.3 million, up from $144.5 million for the quarter and grew 36.9% to $446.2 million, up from $326.0 million for the nine-month period compared to the same period last year. This increase is coming from recent acquisitions, which contributed $10.8 million for the quarter and $91.5 million for the nine-month period ended December 31, 2019. Foreign exchange fluctuations had a favorable net impact of $0.5 million during the quarter and $3.4 million for the nine-month period ended December 31, 2019.

The following explanations relate to sales variations by sector excluding acquisitions and the impact of foreign exchange fluctuations compared to last year :

Commercial

For the quarter, the $2.4 million net decrease in commercial sales was mainly driven by lower aftermarket requirements.

For the nine-month period ended December 31, 2019, the $8.8 million net increase in commercial sales was mainly driven by increased deliveries for the Boeing 777 and 777X programs.

Defence

The $3.9 million and $16.6 million net increases in defence sales for the quarter and nine-month period ended December 31, 2019 were mainly driven by:

- Increased aftermarket demand for the C-130 and KC-135 programs with AAR and Sikorsky H-60;
- The production rate increase of the Lockheed Martin F-35 program; and,
- Higher spares demand for the Northrop Grumman RQ-4 program.

These positive factors were partially offset by lower delivery of spares to the U.S. Government.

Gross Profit

Strong performances by Beaver and CESA, offset by the temporarily dilutive effect of the margin of more recently acquired businesses, led to relatively stable gross profit as a percentage of sales for the quarter as compared to the same last year.

The nine-month period was also negatively impacted by higher manufacturing costs at our Longueuil facility compared to last year.

The net impact of foreign exchange fluctuations was negligible for both the quarter and the nine-month period ended December 31, 2019.

Selling and Administrative Expenses

When excluding gains and losses on translation of net monetary items, selling and administrative expenses represented 8.1% and 8.4% of sales for the quarter and nine-month period, compared to 8.1% and 8.9% for the same periods last fiscal year. The decrease for the nine-month period is mainly explained by higher sales volume.

Non-recurring items

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Non-recurring items in operating income				
Acquisition-related costs	$ —	$ 2,069	$ 615	$ 3,305
	$ —	$ 2,069	$ 615	$ 3,305
Non-recurring items in financial expenses				
Net losses on certain derivative financial instruments	$ —	$ —	$ —	$ 391
	$ —	$ —	$ —	$ 391

Acquisition-related costs

These costs mainly pertain to professional fees and expenses related to the acquisition of Alta this fiscal year and the acquisitions of CESA and Beaver last fiscal year.

Net losses on certain derivative financial instruments

These losses relate to derivative financial instruments acquired in order to mitigate foreign currency and interest rate risks arising from the purchase price and financing related to the acquisition of CESA last year.

Operating Income

Operating income increased from 8.2% to 8.6% of sales (or decreased from 9.7% to 8.6% excluding non-recurring items) for the quarter and increased from 6.8% to 7.7% of sales (or remained at 7.8% excluding non-recurring items) for the nine-month period compared to the same periods last fiscal year, mainly as a result of the factors described above.

Year-over-year, foreign exchange fluctuations had an unfavorable net impact on operating income of $1.1 million and $1.5 million (representing 0.7% and 0.3% of sales), respectively, for the quarter and nine-month period.

Net Financial Expenses

	Three months ended December 31,			Nine months ended December 31,		
	2019	2018	*Variance*	2019	2018	*Variance*
Interest on long-term debt[(1)]	$ 1,613	$ 1,870	*$ (257)*	$ 4,996	$ 3,270	*$ 1,726*
Interest related to government loans	963	682	*281*	2,226	1,874	*352*
Interest income on cash and cash equivalents	(20)	(90)	*70*	(74)	(754)	*680*
Other interest expense	350	302	*48*	1,231	1,019	*212*
	$ 2,906	$ 2,764	*$ 142*	$ 8,379	$ 5,409	*$ 2,970*
						As at
	December 31, 2019	March 31, 2019	*Variance*	December 31, 2019	March 31, 2018	*Variance*
Long-term debt, including current portion	$ 279,028	$ 260,306	*$ 18,722*	$ 279,028	$ 131,041	*$ 147,987*

[(1)]*Refer to* New Accounting Standards *under* Additional Information *for details regarding the impact of the adoption of IFRS 16 Leases*

The $3.0 million net increase in financial expenses for the nine-month period when compared to the same period last fiscal year mainly results from higher interest charges related to the financing of the four acquisitions completed since June 30, 2018 as well as the impact of the adoption of *IFRS 16 Leases* on April 1, 2019 ($0.9 million). Long-term debt stood at $279.0 million as at December 31, 2019 compared to $131.0 million as at March 31, 2018.

Income Tax Expense

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Income before income tax expense	$ 10,560	$ 9,140	$ 25,977	$ 16,641
Income tax expense	1,855	1,750	4,522	2,405
Effective tax rate	17.6%	19.1%	17.4%	14.5%
Canadian blended statutory income tax rate	26.5%	26.6%	26.5%	26.6%

For the quarter ended December 31, 2019, the Corporation's effective income tax rate mainly reflected the favourable impact of results in other tax jurisdictions of $1.0 million ($1.5 million in Fiscal 2019), partially offset by non-deductible expenses totaling $0.1 million ($0.7 million in Fiscal 2019).

For the nine-month period ended December 31, 2019, the Corporation's effective income tax rate mainly reflected the favourable impact of results in other tax jurisdictions of $3.0 million ($3.1 million in Fiscal 2019), partially offset by non-deductible expenses totaling $0.3 million ($1.1 million in Fiscal 2019).

Net Income

Net income increased from $7.4 million to $8.7 million during the quarter (or decreased from $9.4 million to $8.7 million, excluding non-recurring items net of taxes) and increased from $14.2 million to $21.5 million during the nine-month period (or increased from $17.6 million to $22.0 million, excluding non-recurring items net of taxes) compared to the same periods last fiscal year, mainly as a result of the factors described above.

NON-IFRS FINANCIAL MEASURES

This MD&A is based on earnings in accordance with IFRS and the following non-IFRS financial measures:

Adjusted operating income:	Operating income excluding non-recurring items.
EBITDA:	Earnings before financial expenses, income tax expense and amortization expense.
Adjusted EBITDA:	EBITDA as defined above excluding non-recurring items.
Adjusted net income:	Net income excluding non-recurring items net of taxes.
Adjusted earnings per share:	Diluted earnings per share calculated on the basis of adjusted net income.
Free cash flow:	Cash flows related to operating activities, less additions to property, plant and equipment and net increase or decrease in finite-life intangible assets.

These Non-IFRS financial measures do not have any standardized meaning prescribed by IFRS and may therefore not be comparable to similar measures presented by other issuers. Management considers these metrics to be information which may assist investors in evaluating the Corporation's profitability and enable better comparability of the results from one period to another and with peers who may employ similar measures.

These measures are not considered by management to be a substitute for IFRS measures, nor to be superior as they often do not fully reflect periodic costs, the long-term costs of investing or financing decisions or the impact of events which are not a result of operations.

The following are reconciliations of these items to their most comparable IFRS measures as well as additional information on what they represent, excluding free cash flow. For the reconciliation of free cash flow to cash flows related to operating activities, refer to *Liquidity and Capital Resources*.

The Corporation's adjusted operating income is calculated as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Operating income	$ 13,466	$ 11,904	$ 34,356	$ 22,050
Non-recurring items	—	2,069	615	3,305
Adjusted operating income	$ 13,466	$ 13,973	$ 34,971	$ 25,355

Management believes adjusted operating income provides investors with a figure that provides an alternative assessment of the Corporation's future profitability by excluding from operating income the impact of events which are not in the expected course of future operations, or which are not a result of operations.

The Corporation's EBITDA and adjusted EBITDA are calculated as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Net income	$ 8,705	$ 7,390	$ 21,455	$ 14,236
Income tax expense	1,855	1,750	4,522	2,405
Net financial expenses	2,906	2,764	8,379	5,409
Amortization expense	11,097	8,910	32,611	22,948
EBITDA	$ 24,563	$ 20,814	$ 66,967	$ 44,998
Non-recurring items	—	2,069	615	3,305
Adjusted EBITDA	$ 24,563	$ 22,883	$ 67,582	$ 48,303

Management believes EBITDA and adjusted EBITDA provide valuable insight into the Corporation's day-to-day operations as they exclude from earnings factors that are more reflective of long-term financing or investing decisions than of current performance.

Adjusted EBITDA, in addition, provides an alternative assessment of future operating results as it excludes the impact of events which are not in the expected course of future operations, or which are not a result of operations. Adjusted EBITDA is also used by management to assess operational performance and is a component of certain performance-based employee remuneration.

The Corporation’s adjusted net income and adjusted earnings per share are calculated as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Net income	$ 8,705	$ 7,390	$ 21,455	$ 14,236
Non-recurring items, net of taxes	—	1,977	516	3,322
Adjusted net income	$ 8,705	$ 9,367	$ 21,971	$ 17,558
Non-controlling interests	(99)	—	(457)	—
Adjusted net income attributable to the equity holders of the parent	$ 8,804	$ 9,367	$ 22,428	$ 17,558
In dollars per share				
Earnings per share - basic and diluted	$ 0.24	$ 0.20	$ 0.60	$ 0.39
Non-recurring items, net of taxes	—	0.06	0.01	0.09
Adjusted earnings per share	$ 0.24	$ 0.26	$ 0.61	$ 0.48

Management believes adjusted net income and adjusted earnings per share provide investors with an alternative assessment of the Corporation’s current period results and future earnings prospects as they exclude from earnings the impact of events which are of a non-recurring nature or do not reflect current operations.

Free cash flow is explained and reconciled in *Liquidity and Capital Resources*.

BUSINESS ACQUISITIONS

Acquisition of Alta

On June 7, 2019, the Corporation completed the acquisition of all of the shares of Alta Précision Inc. (“Alta”), for $18.6 million, including a $0.5 million balance of sale and the assumption of Alta’s net outstanding debt amounting to $0.9 million. Located in Montreal, Canada, Alta is a manufacturer of high-precision landing gear components. This acquisition expands the Corporation's portfolio of commercial products by providing both access to new programs and additional content on existing platforms. The acquisition was financed with the Corporation’s available credit facilities and was treated as a business combination.

Alta was a minority shareholder of Tekalia. As a result of the acquisition, the Corporation increased its participation in Tekalia to 67% from 60% as at March 31, 2019.

Purchase Price

The preliminary purchase price allocation that reflect the fair value of the assets acquired and liabilities assumed during Fiscal 2020 with any excess allocated to goodwill was prepared using the acquisition method as follows:

Cash payment	$ 17,149
Long-term debt assumed [1]	903
Balance of purchase price payable	500
Total purchase price	$ 18,552

[1] Excludes lease liability related to IFRS 16

Purchase Price Allocation

	Purchase price allocation as originally reported	Adjustments and reclassifications	Adjusted purchase price allocation
Accounts receivable	$ 1,451	$ 4	$ 1,455
Inventories	11,374	193	11,567
Other current assets	439	(63)	376
	13,264	**134**	**13,398**
Property, plant and equipment, including right-of-use	18,040	1,506	19,546
Finite-life intangible assets	—	2,797	2,797
Deferred income tax assets	—	1,858	1,858
Other long-term assets	264	—	264
Investment in Tekalia	544	—	544
Total identifiable assets	**$ 32,112**	**$ 6,295**	**$ 38,407**
Accounts payable and accrued liabilities	6,866	(237)	6,629
Customer advances and progress billings	2,872	—	2,872
Provisions	906	6,012	6,918
Long-term debt [1]	6,844	—	6,844
Total identifiable liabilities	**$ 17,488**	**$ 5,775**	**$ 23,263**
Net identifiable assets and liabilities	**14,624**	**520**	**15,144**
Goodwill and other intangible assets	3,928	(3,928)	—
Goodwill	—	3,408	3,408
Total purchase price	**$ 18,552**	**$ —**	**$ 18,552**

[1] Corresponds to lease liabilities

During the previous quarter ended September 30, 2019, the Corporation amended its assessment of the fair value of certain customers' contracts, property, plant and equipment and finite-life intangible assets. The purchase price allocation remain preliminary for these items and their related tax impacts until management has gathered all the necessary information to complete the process. There were no changes to the purchase price allocation during the quarter ended December 31, 2019.

Acquisition of CESA

During the previous quarter ended September 30, 2019, the Corporation completed its final assessment of the fair value of assets acquired and liabilities assumed of Compañia Española de Sistemas Aeronauticos S.A. ("CESA"). Adjustments and reclassifications mainly relate to the final assessment of costs and liabilities associated to specific Aerospace programs. There were no changes to the purchase price allocation during the quarter ended December 31, 2019.

Purchase Price Allocation

	Purchase price allocation as originally reported	Adjustments and reclassifications	Final purchase price allocation
Accounts receivable	$ 28,293	$ —	$ 28,293
Inventories	36,692	—	36,692
Income tax receivable	505	—	505
Other current assets	596	—	596
	66,086	**—**	**66,086**
Property, plant and equipment	44,923	—	44,923
Finite-life intangible assets	40,407	—	40,407
Other long-term assets - Tax credits receivable	7,843	—	7,843
Total identifiable assets	**$ 159,259**	**$ —**	**$ 159,259**
Accounts payable and accrued liabilities	16,773	—	16,773
Provisions	11,897	4,506	16,403
Customer advances and progress billings	4,188	—	4,188
	32,858	**4,506**	**37,364**
Provisions	4,308	—	4,308
Deferred income tax liabilities	3,465	(1,126)	2,339
Other liabilities - long-term accounts payable	4,365	—	4,365
Total identifiable liabilities	**$ 44,996**	**$ 3,380**	**$ 48,376**
Net identifiable assets and liabilities	**114,263**	**(3,380)**	**110,883**
Goodwill	81,553	3,380	84,933
Total purchase price	**$ 195,816**	**$ —**	**$ 195,816**

LIQUIDITY AND CAPITAL RESOURCES

CREDIT FACILITIES AND NET DEBT POSITION

Senior Secured Syndicated Revolving Credit Facility ("Revolving Facility")

The Corporation has a Revolving Facility with a syndicate of five Canadian banks and their U.S. affiliates or branches and a Canadian branch of a U.S. bank. This facility allows the Corporation and its subsidiaries to borrow up to $250.0 million, either in Canadian dollars, US dollars, British Pounds, Euro or equivalent currencies. It also includes an accordion feature to increase available credit by an additional $100.0 million during the term of this agreement, subject to the approval of the lenders.

During the quarter, the Corporation reached an agreement with its syndicate of banks to extend the term of its Revolving Facility from May 2022 to December 2024.

As at December 31, 2019, the Corporation had $88.3 million drawn against the Revolving Facility, compared to $94.9 million as at March 31, 2019. This decrease is mainly related to a repayment of US$12.0 million ($15.9 million) net of a drawing of US$9.0 million ($12.1 million) made in order to finance the Alta acquisition.

Unsecured Subordinated Term Loan Facility ("Term Loan Facility")

The Corporation has a Term Loan Facility with *Fonds de Solidarité FTQ* for an amount of up to $75.0 million. A first tranche of $50.0 million was drawn to finance the acquisition of CESA in October 2018 and a second of $10 million was drawn in June 2019 for the acquisition of Alta. Additional financing of $15 million is available under this facility until September 30, 2020, subject to certain conditions.

The initial $50.0 million loan, drawn on September 25, 2018, bears interest at 5.70% and is repayable at maturity on September 30, 2025. The second tranche of $10.0 million drawn on June 11, 2019, bears interest at 4.73% and is also repayable at maturity on September 30, 2025. Starting on September 30, 2021, the Corporation will have the option to make early repayments subject to certain fees.

Net Debt Position

	December 31, 2019	April 1, 2019 [2]	March 31, 2019
Long-term debt, including current portion[1]	$ 282,171	$ 278,150	$ 263,258
Less: Cash and cash equivalents	25,346	35,128	35,128
Net debt position	$ 256,825	$ 243,022	$ 228,130

[1] *Excluding net deferred financing costs of $3.1 million and $3.0 million as at December 31, 2019 and March 31, 2019, respectively.*

[2] *Pro-forma including the effect of the adoption of IFRS 16,* Leases.

On April 1, 2019, the Corporation adopted the new IFRS 16, *Leases* accounting standard (Refer to the *New Accounting Standards* under *Additional Information* for further details). The new standard requires all leases to be recognized as debt on the Corporation's balance sheet. As a result, long-term debt included $14.9 million and $26.4 million of leases as at April 1, 2019 and December 31, 2019, respectively, which would have been accounted for as operating leases under the previous standard.

Considering the Corporation's cash and cash equivalents position, its available credit facilities and level of expected capital investments and results, the Corporation's management does not expect any significant liquidity risk in the foreseeable future.

VARIATIONS IN CASH AND CASH EQUIVALENTS

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Cash and cash equivalents at beginning of periods	$ 19,630	$ 196,717	$ 35,128	$ 93,209
Cash flows related to operating activities	9,664	12,651	25,863	32,788
Cash flows related to investing activities	(1,230)	(170,648)	(24,893)	(200,693)
Cash flows related to financing activities	(2,405)	(10,821)	(10,064)	102,416
Effect of changes in exchange rates on cash and cash equivalents	(313)	740	(688)	919
Cash and cash equivalents at end of periods	$ 25,346	$ 28,639	$ 25,346	$ 28,639

Operating Activities

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

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Cash flows from operations	$ 20,817	$ 17,398	$ 56,604	$ 38,645
Net change in non-cash items	(11,153)	(4,747)	(30,741)	(5,857)
Cash flows related to operating activities	$ 9,664	$ 12,651	$ 25,863	$ 32,788

For the quarter ended December 31, 2019, the increase of $3.4 million in cash flows from operations compared to the same periods last year mainly relate to the higher adjusted EBITDA.

For the nine-month period ended December 31, 2019, the increase of $18.0 million in cash flows from operations compared to the same period last year mainly relate to the contribution of CESA as well as increased volume in the legacy businesses.

The net change in non-cash items can be summarized as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Accounts receivable	$ (1,011)	$ (24,741)	$ 13,944	$ (78)
Inventories	(12,034)	2,417	(35,364)	(1,820)
Other current assets	1,461	156	341	818
Accounts payable and accrued liabilities	(3,329)	11,194	(6,372)	1,415
Income taxes payable and receivable	(1,261)	(289)	(1,540)	(1,955)
Customer advances and progress billings	3,983	2,004	4,138	(2,609)
Provisions	167	(60)	(2,178)	(4,173)
Effect of changes in exchange rates	871	4,572	(3,710)	2,545
	$ (11,153)	$ (4,747)	$ (30,741)	$ (5,857)

For the quarter ended December 31, 2019, the negative net change in non-cash items mainly reflects an increase in inventory due to upcoming organic growth from various programs, including the Boeing F-18 and MQ-25.

For the nine-month period ended December 31, 2019, the negative net change in non-cash items mainly reflects:

- An increase in inventory due to the above-mentioned upcoming organic growth;
- A lower number of days payables outstanding at the end of December when compared to March 31, 2019; and
- The negative effect of changes in exchange rates.

These factors were partially offset by the decrease in accounts receivable resulting from an improvement in days receivable at December 31, 2019.

For the quarter ended December 31, 2018, the negative net change in non-cash items mainly reflected:

- An increase in accounts receivable following the higher level of activity during the quarter.

This negative factor was partly offset by increases in accounts payable and accrued liabilities and customer advances and progress billings as well as a positive effect of changes in exchange rates.

For the nine-month period ended December 31, 2018, the negative net change in non-cash items mainly reflected:

- A decrease in provisions mainly due to utilization of the restructuring provision;
- A decrease in customer advances following revenue recognition; and,
- An increase in inventories mainly related to the ramp-up of the Boeing 777 and 777X contract.

These negative factors were partly offset by the positive effect of changes in exchange rates.

Investing Activities

The Corporation's investing activities were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Cash payments for business acquisitions	$ —	$ (170,930)	$ (17,149)	$ (194,601)
Net additions to property, plant and equipment	(5,152)	(2,991)	(13,307)	(8,345)
Capital contribution from a non-controlling interest in a subsidiary	495	—	495	—
Net decrease in finite-life intangible assets	3,427	3,250	1,043	2,223
Proceeds on disposal of property, plant and equipment	—	23	4,025	30
Cash flows related to investing activities	$ (1,230)	$ (170,648)	$ (24,893)	$ (200,693)

The decrease in cash used related to investing activities during the quarter and nine-month period ended December 31, 2019 compared to the same period last fiscal year mainly relates to the $170.9 million payment made for the acquisition of CESA in Fiscal 2019.

This table reconciles the additions to property, plant and equipment for the quarters and the nine-month periods ended December 31:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Additions to property, plant and equipment	$ 2,950	$ 4,000	$ 17,405	$ 8,590
Variation in unpaid additions included in Accounts payable - other and other liabilities	2,215	(1,009)	2,524	(245)
Non-cash additions made through leasing agreements	(13)	—	(6,622)	—
Additions, as per statements of cash flows	$ 5,152	$ 2,991	$ 13,307	$ 8,345

Financing Activities

The Corporation's financing activities were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Increase in long-term debt	$ 2,906	$ —	$ 25,950	$ 116,605
Repayment of long-term debt	(4,842)	(9,728)	(35,197)	(12,546)
Issuance of common shares	—	133	—	924
Increase in deferred financing costs	(469)	(1,226)	(817)	(2,567)
Cash flows related to financing activities	$ (2,405)	$ (10,821)	$ (10,064)	$ 102,416

The $4.9 million decrease in long-term debt repayments during the quarter compared to the same period last fiscal year mainly relate to a US5.0 million ($6.6 million) repayment made last fiscal year, partially offset by the impact of payments made per under debt and lease agreements that would have been accounted for as operating leases prior to the adoption of IFRS 16 (See *New Accounting Standards* under *Additional Information* for further details).

The increased repayments of long-term debt during the nine-month period compared to the same period last fiscal year mainly relate to a $15.9 million repayment (US$12.0 million) on the Revolving facility and the impact of payments made per agreements that would have been accounted for as operating leases prior to the adoption of IFRS 16 .

The increase in long-term debt during the nine-month period is mainly related to a US$9.0 million ($12.1 million) drawing on the Revolving Facility and a $10.0 million drawing on the Term Loan Facility, both used to finance the acquisition of Alta.

As at December 31, 2019, the Corporation was in compliance with all of its restrictive debt covenants and expects to continue to comply with these restrictive financial covenants through the current fiscal year.

FREE CASH FLOW[1]

	Three months ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
Cash flows related to operating activities	$ 9,664	$ 12,651	$ 25,863	$ 32,788
Net additions to property, plant and equipment	(5,152)	(4,000)	(13,307)	(8,590)
Net decrease in finite-life intangible assets	3,427	3,250	1,043	2,223
Free cash flow	$ 7,939	$ 11,901	$ 13,599	$ 26,421

[1] *Non-IFRS financial measure. Refer to the* Non-IFRS financial measures *section under* Operating Results *for the definition of this metric.*

Management considers free cash flow to be a good indicator of financial strength and profitability because it shows how much cash generated by operations is available for distribution, to repay debt or fund other investments.

FINANCIAL POSITION

ISSUED CAPITAL

Capital stock varied as follows:

	Quarter ended December 31, 2019		Nine months ended December 31, 2019	
	Number	**Issued capital**	Number	Issued capital
Opening balance	36,362,210	$ 79,676	36,362,210	$79,676
Closing balance	36,362,210	$ 79,676	36,362,210	$79,676

No shares have been issued since the beginning of the fiscal year and as at February 5, 2020, the number of common shares outstanding stood at 36,362,210.

Stock options varied as follows:

	Quarter ended December 31, 2019		Nine months ended December 31, 2019	
	Number of stock options	Weighted-average exercise price	Number of stock options	Weighted-average exercise price
Opening balance	1,508,595	$ 13.87	1,167,095	$ 13.23
Granted	—	—	341,500	16.03
Closing balance	1,508,595	$ 13.87	1,508,595	$ 13.87

The Corporation grants stock options at a subscription price representing the average closing price of the Corporation's common shares on the Toronto Stock Exchange for the five trading days preceding the grant date. 2,808,257 common shares are reserved for issuance by the Corporation of which 2,762,507 had not been issued yet at December 31, 2019 (2,762,507 as at March 31, 2019).

As at February 5, 2020, the number of stock options outstanding stood at 1,508,595.

CONSOLIDATED BALANCE SHEETS

The acquisition of Alta contributed assets and liabilities to the Corporation's balance sheet as at December 31, 2019, as detailed in the *Business Acquisitions* section under *Operating Results*.

Working capital

As at	December 31, 2019	April 1, 2019	March 31, 2019	*Variance*	
Current assets	$ 389,297	$ 364,467	$ 364,467	*$ 24,830*	*6.8%*
Current liabilities	197,157	193,860	191,340	*3,297*	*1.7%*
Working capital	$ 192,140	$ 170,607	$ 173,127	*$ 21,533*	*12.6%*
Working capital ratio	1.97	1.88	1.90		

(1) Pro-forma including the effect of the adoption of IFRS 16 Leases.

The $24.8 million increase in current assets is mainly due to an increase in inventory of $35.4 million, partially offset by a $9.8 million decrease in cash and cash equivalents.

Long-term assets, Long-term liabilities and Shareholders' Equity

The Corporation's long-term assets and liabilities were as follows, as at:

	December 31, 2019	April 1, 2019 (2)	March 31, 2019	*Variance*	
Long-term assets	$ 533,608	$ 527,791	$ 513,648	*$ 5,817*	*1.1%*
Long-term liabilities	$ 302,196	$ 295,049	$ 282,677	*$ 7,147*	*2.4%*
Shareholders' equity	$ 423,552	$ 404,098	$ 404,098	*$ 19,454*	*4.8%*
Net debt-to-equity ratio(1)	0.61:1	0.60:1	0.56:1		

(1) Defined as total long-term debt, including the current portion but excluding deferred financing costs, less cash and cash equivalents over shareholders' equity.

(2) Pro-forma including the effect of the adoption of IFRS 16 Leases.

The increase in long-term assets is mainly due to $28.2 million of assets acquired with Alta, partially offset by the unfavourable effect of exchange rate fluctuations on the conversion of the Corporation's foreign operations.

The increase in long-term liabilities is mainly due to the acquisition of Alta.

ADDITIONAL INFORMATION

FOREIGN EXCHANGE ("FX")

The Corporation is subject to foreign currency fluctuations from the translation of revenues (sales), expenses, assets and liabilities of its foreign operations and from transactions denominated mainly in US dollars, in British pounds ("GBP") and in Euros ("EUR"). Transactions denominated in foreign currencies are initially recorded at the functional currency rate of exchange at the date of the transactions, excluding the impact of forward foreign exchange contracts ("FFEC"), while the statement of income of foreign operations is translated at the average exchange rate for the period.

The foreign exchange rates used to translate assets and liabilities into Canadian dollars were as follows, as at:

	December 31, 2019	March 31, 2019
USD (Canadian equivalent of US$1.0)	1.2988	1.3363
GBP (Canadian equivalent of £1.0)	1.7174	1.7418
EUR (Canadian equivalent of €1.0)	1.4583	1.5002

The foreign exchange rates used to translate revenues and expenses into Canadian dollars were as follows:

	Quarters ended December 31,		Nine months ended December 31,	
	2019	2018	2019	2018
USD (Canadian equivalent of US$1.0)	1.3200	1.3214	1.3260	1.3065
GBP (Canadian equivalent of £1.0)	1.7004	1.6992	1.6824	1.7199
EUR (Canadian equivalent of €1.0)	1.4617	1.5080	1.4775	1.5225

The Corporation manages its exposure to fluctuations in FX rates using FFEC. Therefore, the variances in the rates presented above may not be representative of the actual impact of FX on financial results.

DERIVATIVES

Forward foreign exchange contracts

As at December 31, 2019, the Corporation had forward foreign exchange contracts outstanding for a notional amount of $280.9 million ($228.4 million at March 31, 2019) denominated in USD, EUR and and GBP. This amount includes contracts with nominal value of US$189.4 million (US$146.9 million at March 31, 2019) convertible into Canadian dollars at an average rate of 1.3159 (1.3060 at March 31, 2019). These contracts mature at various dates between January 2020 and March 2023, with the majority maturing this fiscal year and the next.

Cross-currency interest rate swaps

As at December 31, 2019, the Corporation had entered into the following cross-currency interest rate swap agreements in order to mitigate foreign exchange and interest rate risks:

	Notional	EURO equivalent	Interest rate	Inception	Maturity
US$	29,370	€ 25,000	1.86 %	October 2017	May 2022
C$	50,000	€ 34,110	3.40 %	October 2017	September 2025
US$	17,523	€ 15,000	Euribor 1 month + 1.74%	September 2018	May 2022
US$	17,100	€ 15,000	Euribor 1 month + 1.76%	November 2018	March 2020
C$	10,000	€ 6,658	2.68 %	June 2019	September 2025

Equity swap agreement

As at December 31, 2019, the Corporation had entered into an equity swap agreement fixing 300,000 common shares of the Corporation (245,000 at March 31, 2019) at a price of $13.52 ($12.68 at March 31, 2019). This agreement manages the Corporation's exposure to fluctuations of its share price driven by outstanding Performance Share Units and Deferred Share Units. It is a derivative that is not part of a designated hedging relationship and matures in June 2020.

NEW ACCOUNTING STANDARDS

The Company adopted the following new accounting standard effective April 1, 2019.

IFRS 16, Leases

IFRS 16, which replaces IAS 17, represents a major revision of the way in which companies account for leases. It sets out the principles that both parties to a contract, i.e. the customer ("lessee") and the supplier ("lessor"), apply to provide relevant information about leases in a manner that faithfully represents those transactions. To meet this objective, a lessee is required to recognize assets and liabilities arising from a lease following a single model where previously leases were classified as either finance leases or operating leases. Most leases are recognized on the Corporation's consolidated balance sheet. Certain exemptions apply for short-term leases and leases of low-value assets.

The adoption of IFRS 16 had an impact on the consolidated balance sheet and statement of income as operating leases have been capitalized, corresponding lease liabilities have been recognized, rent expense has been replaced by the amortization expense of the right to use the related assets and the interest accretion expense from the liability recorded.

In addition, the principal repayments of lease liabilities are now presented as financing activities in the consolidated statements of cash flows, whereas under the previous standard these payments were presented as operating activities prior to April 1, 2019.

Right-of-Use Assets

Right-of-use assets are measured at cost. The cost is based on the initial amount of the lease liability plus initial direct costs incurred and estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located adjusted for any lease payments made at or before the commencement date, less any lease incentives received, if any.

The cost of right-of-use assets are periodically reduced by depreciation expenses and impairment losses, if any, and adjusted for certain remeasurement of the lease liability. Right-of-use assets are amortized to the lesser of the useful life or the lease term using the straight-line method as this reflects the expected pattern of consumption of the future economic benefits. The lease term includes the renewal option only if it is reasonably certain to exercise that option. Lease terms range from 1 to 20 years for buildings and 1 to 6 years for machinery, equipment and tooling.

Lease Liabilities

At the commencement date of the lease, the Corporation recognizes lease liabilities measured at the present value of lease payments to be made over the lease term. Lease payments mainly include fixed payments less any lease incentives receivable and the exercise price of a purchase option reasonably certain to be exercised. Variable lease payments that do not depend on an index or a rate are recognized as an expense in the period during which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Corporation uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect accretion of interest and reduced for lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment of whether the underlying asset will be purchased.

Significant judgment in determining the lease term of contracts with renewal options

The Corporation determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised. After the commencement date, the Corporation reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not to exercise) the option to renew (e.g., a change in business strategy).

The Corporation has applied this standard using the modified retrospective approach (without restating comparative figures) for the fiscal year beginning April 1, 2019. Certain leases were not brought on the Corporation's consolidated balance sheet as they are covered by practical expedients. The Corporation has elected to apply the following practical expedients:

- Account for leases for which the remaining lease term ends within 12 months of the effective date as short-term leases; and
- Recognize short-term leases and low value leases on a straight-line basis as part of operating expenses in the consolidated statements of income.

The adoption of IFRS 16 had the following impacts on the consolidated statement of income:

Increase (decrease)	Quarter ended December 31, 2019	Nine months ended December 31, 2019
Cost of sales, Selling and administrative expenses		
Depreciation and amortization	$ 764	$ 2,220
Other (rent expense)	(933)	(2,595)
Operating income	169	375
Financial expenses	345	919
Deferred income tax expense	(44)	(136)
Net income and comprehensive income	$ (132)	$ (408)

Increase (decrease)	As of April 1, 2019
Property, plant and equipment, net	$ 14,892
Long-term debt [(1)]	14,892

[(1)] The current portion of long-term debt impact corresponds to $2,520 as at April 1, 2019

The following table presents the reconciliation between the operating leases commitments as of March 31, 2019 and the additional lease liabilities as of April 1, 2019:

Operating lease commitments as at March 31, 2019	$	16,823
Discounting operating leases as at April 1, 2019 [1]		(1,068)
Commitments relating to the change in the lease term assumptions and inclusion of non-lease components		1,002
Leases committed but not yet commenced as at April 1, 2019		(1,865)
Additional lease liabilities as at April 1, 2019	$	14,892
Pre-existing capital leases as at April 1, 2019		20,411
Total lease liabilities as at April 1, 2019	$	35,303

[1] At the date of adoption of IFRS 16, the weighted average incremental borrowing rate was 4.2%

The following tables reconciles the right-of-use assets for the Company as at December 31, 2019:

	Building and leasehold improvements	Machinery, equipment and tooling [1]	Other	Total
Cost:				
At April 1, 2019	$ 12,969	$ 41,368	$ 1,271	$ 55,608
Additions	6,498	—	124	6,622
Business acquisition	6,844	—	—	6,844
Effect of changes in exchange rates	(257)	(4)	(28)	(289)
As at December 31, 2019	$ 26,054	41,364	$ 1,367	$ 68,785
Accumulated amortization:				
At April 1, 2019	$ —	$ (10,006)	$ —	$ (10,006)
Amortization expense	(1,593)	(4,255)	(388)	(6,236)
Effect of changes in exchange rates	22	2	10	34
As at December 31, 2019	$ (1,571)	$ (14,259)	$ (378)	$ (16,208)
Net book value as at December 31, 2019	$ 24,483	$ 27,105	$ 989	$ 52,577

[1] Includes the pre-existing assets under capital leases (net book value of $30,710 as at April 1, 2019)

The following table presents the lease liabilities for the Company as at December 31, 2019:

	Lease liabilities
Balance at April 1, 2019	$ 35,303
Additions	6,622
Business acquisition	6,844
Lease payments	(6,546)
Interest expense on lease liabilities	1,341
Effect of changes in exchange rates	(1,012)
Balance as at December 31, 2019	$ 42,552

INTERNAL CONTROLS AND PROCEDURES

In compliance with the Canadian Securities Administrators' Regulation 52-109, the Corporation has filed certifications signed by the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") that, among other things, report on disclosure controls and procedures and the design of internal controls over financial reporting.

The CEO and the CFO have designed disclosure controls and procedures, or have caused them to be designed under their supervision, to provide reasonable assurance that material information relating to the Corporation has been made known to them and has been properly disclosed in the interim and annual filings.

The CEO and CFO have also designed internal controls over financial reporting, or have caused them to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

No changes were made to the Corporation's internal controls over financial reporting during the three-month ended December 31, 2019 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

SELECTED QUARTERLY FINANCIAL INFORMATION

Fiscal year	2020			2019				2018
	Third Quarter	Second Quarter	First Quarter	Fourth quarter	Third Quarter	Second Quarter	First Quarter	Fourth quarter
Sales	$ 157,253	$ 145,516	$ 143,427	$ 157,914	$ 144,528	$ 95,665	$ 85,770	$ 113,024
Operating income	13,466	10,519	10,371	15,190	11,904	5,289	4,857	6,697
Adjusted operating income (1)	13,466	10,519	10,986	16,208	13,973	6,165	5,217	12,089
Adjusted EBITDA (1)	24,563	21,510	21,509	25,910	22,883	13,176	12,244	19,369
Net Income	8,705	6,307	6,443	11,958	7,390	3,294	3,552	5,858
Adjusted Net Income (1)	8,705	6,307	6,959	12,794	9,367	4,405	3,786	10,439
In dollars per share								
Earnings per share - Basic & Diluted	$ 0.24	$ 0.18	$ 0.18	$ 0.34	$ 0.20	$ 0.09	$ 0.10	$ 0.16
Adjusted earnings per share (1)	0.24	0.18	0.19	0.36	0.26	0.12	0.10	0.29
In millions of shares								
Weighted-average number of common diluted shares outstanding	36.7	36.7	36.6	36.5	36.4	36.5	36.4	36.4
Backlog (in million)	$ 839	$ 769	$ 747	$ 624	$ 629	$ 479	$ 454	$ 466

(1) *Non-IFRS financial measure. Refer to the* Non-IFRS financial measures *section under* Operating Results *for definitions and reconciliations to the most comparable IFRS measures.*

Seasonal trends

Héroux-Devtek's first semester is usually slower than the last one due to seasonality such as plant shutdowns and summer vacations.

RISKS AND UNCERTAINTIES

Héroux-Devtek operates in industry sectors that have a variety of risk factors and uncertainties. Risk and uncertainties that could materially affect the Corporation's business, financial condition and results of operations in an adverse manner are described in the Corporation's MD&A for the fiscal year ended March 31, 2019. Additional risks and uncertainties not presently known to the Corporation or that the Corporation currently believes to be immaterial may also adversely affect its business.

GUIDANCE[1]

Metric	Initial fiscal 2020 guidance	Updated Fiscal 2020 guidance
Fiscal 2020 sales	Sales of $560 to $580 million	Sales of $600 to $610 million
Long-term sales growth	Fiscal 2022 sales of $620 to $650 million	Fiscal 2022 sales of $650 to $680 million

[1] *Refer to* Forward-Looking Statements *in* Overview *for further information regarding forward-looking statements and related risks.*

In February 2020, Management increased its fiscal 2020 sales guidance in order to reflect stronger than expected growth. The long-term sales growth guidance that was updated in August 2019 to reflect the expected contributions of Alta Précision to Héroux-Devtek's performance and remains the same.

Management has prepared the foregoing guidance using the best information available upon preparing this MD&A, and based it on assumptions and sources of information including, but not limited to:

- Héroux-Devtek's backlog, long-term sales contracts and estimated future order intake, including those of Alta Précision but no other material acquisition;
- Existing OEM backlogs, production rates and disclosed production and delivery expectations;
- Stability of government defence budgets, spending climates, trends and expectations;
- Stability of overall economic conditions;
- Stability of foreign exchange rates;
- The Corporation's ability to deliver on key contract initiatives; and,
- The successful deployment of integration and cross-selling initiatives.

Refer to the *Risk Management* section of the Corporation's MD&A for the fiscal year ended March 31, 2019 for discussion of certain other factors which may cause future results to differ from this guidance.

SHAREHOLDER INFORMATION

Expected issuance date of financial results	
Fiscal 2020	
Fourth quarter	May 21, 2020
Fiscal 2021	
First quarter	August 7, 2020
Second quarter	November 13, 2020
Third quarter	February 5, 2021

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