

MAGELLAN

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2017



Magellan Aerospace Corporation – Management’s Discussion & Analysis

September 30, 2017

This Management’s Discussion and Analysis (“MD&A”) of the financial condition and results of operations of Magellan Aerospace Corporation (“Magellan” or the “Corporation”) should be read in conjunction with the unaudited condensed consolidated interim financial statements and the notes thereto for the three and nine month periods ended September 30, 2017, and the audited annual consolidated financial statements for the year ended December 31, 2016 (available on SEDAR at www.sedar.com). Unless otherwise noted, all financial information has been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”), specifically International Accounting Standard (“IAS”) 34, *Interim Financial Reporting* as issued by the International Accounting Standards Board (“IASB”), which is within the framework of International Financial Reporting Standards (“IFRS”). This MD&A provides a review of the significant developments that have impacted the Corporation’s performance during the three month period ended September 30, 2017 relative to the three month period ended September 30, 2016. The information contained in this report is as at November 3, 2017. All financial references are in Canadian dollars unless otherwise noted.

The MD&A contains forward-looking information that represents the Corporation’s internal projections, expectations, estimates or beliefs concerning, among other things, future operating results and various components thereof or the Corporation’s future economic performance. These statements relate to future events or future performance. All statements other than statements of historical facts may be forward-looking statements. In particular and without limitation there are forward looking statements under the heading “Overview”, “Results of Operations”, “Liquidity and Capital Resources”, “Future Changes in Accounting Policies” and “Outlook”. In some cases, forward-looking statements can be identified by terminology such as “may”, “will”, “should”, “expects”, “projects”, “plans”, “anticipates”, and similar expressions. The projections, estimates and beliefs contained in such forward-looking statements are based on management’s assumptions relating to the production performance of Magellan’s assets and competition throughout the aerospace industry and continuation of the current regulatory and tax regimes in the jurisdictions in which the Corporation operates, and necessarily involve known and unknown risks and uncertainties, including the business risks discussed in this MD&A, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. Accordingly, readers are cautioned that events or circumstances could cause results to differ materially from those predicted. Except as required by law, the Corporation does not undertake to update any forward-looking information in this document whether as to new information, future events or otherwise.

The MD&A presents certain non-IFRS financial measures to assist readers in understanding the Corporation’s performance. Non-IFRS financial measures are measures that either exclude or include amounts that are not excluded or included in the most directly comparable measures calculated and presented in accordance with GAAP. Throughout this discussion, reference is made to EBITDA (defined as net income before interest, income taxes, depreciation and amortization), which the Corporation considers to be an indicative measure of operating performance and a metric to evaluate profitability. EBITDA is not a generally accepted earnings measure and should not be considered as an alternative to net income (loss) or cash flows as determined in accordance with IFRS. As there is no standardized method of calculating this measure, the Corporation’s EBITDA may not be directly comparable with similarly titled measures used by other companies. Reconciliations of EBITDA to net income (loss) reported in accordance with IFRS are included in this MD&A.

1. Overview

A summary of Magellan’s business and significant updates

Magellan is a diversified supplier of components to the aerospace industry. Through its wholly owned subsidiaries, Magellan designs, engineers, and manufactures aeroengine and aerostructure components for aerospace markets, advanced products for defence and space markets, and complementary specialty products. The Corporation also supports the aftermarket through supply of spare parts as well as performing repair and overhaul services.

Magellan operates substantially all of its activities in one reportable segment, Aerospace, which is viewed as one segment by the chief operating decision-makers for the purpose of resource allocations, assessing performance and strategic planning. The Aerospace segment includes the design, development, manufacture, repair and overhaul, and sale of systems and components for defence and civil aviation.

Business Update

In September 2017 Magellan announced that the Corporation was selected by Airbus to design and build exhaust systems for the A320neo Pratt & Whitney 1100G-JM engines Nacelle. The first production units will enter service in 2022 with design activities commencing in the fourth quarter of 2017. It is expected that this program will generate in excess of CDN \$200 million in the first ten years of this “life of the program” contract. Magellan was successful in securing this contract based in large part on our technical expertise and our proven ability to manage the industrialization of complex assemblies.

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Magellan has a long history working with Airbus supplying exhaust systems for both the A380 and A340 aircraft as well as a wide range of precision machined components and assemblies for the full range of Airbus aircraft including the A320, A330 and A350 families. This new project aligns with Magellan’s strategy to invest in advanced technologies and manufacturing processes to support our customers’ needs and requirements.

For additional information, please refer to the “Management’s Discussion and Analysis” section of the Corporation’s 2016 Annual Report available on www.sedar.com.

2. Results of Operations

A discussion of Magellan’s operating results for third quarter ended September 30, 2017

The Corporation reported revenue in the third quarter of 2017 of \$232.6 million as compared to \$238.0 million in the third quarter of 2016. Gross profit and net income for the third quarter of 2017 were \$41.7 million and \$19.3 million, respectively, increased from the gross profit of \$38.9 million and net income of \$18.8 million for the third quarter of 2016.

Consolidated Revenue

Expressed in thousands of dollars	Three month period ended September 30			Nine month period ended September 30		
	2017	2016	Change	2017	2016	Change
Canada	77,083	74,827	3.0%	234,359	248,684	(5.8%)
United States	73,981	84,590	(12.5%)	236,037	262,123	(10.0%)
Europe	81,585	78,625	3.8%	262,923	245,964	6.9%
Total revenues	232,649	238,042	(2.3%)	733,319	756,771	(3.1%)

Consolidated revenues for the three months ended September 30, 2017 were \$232.6 million, a \$5.4 million decrease from the \$238.0 million recorded for the same period in 2016. Revenues in Canada increased 3.0% in the third quarter of 2017 as compared to the third quarter of 2016, primarily driven by increases in repair and overhaul services and construction contract revenues, offset by unfavourable foreign exchange impact due to the weakening of the United States dollar relative to the Canadian dollar. On a currency neutral basis, Canadian revenues in the third quarter of 2017 increased by 5.3% over the same period of 2016.

Revenues in United States declined by 12.5% in the third quarter of 2017 compared to the third quarter of 2016 when measured in Canadian dollars mainly due to volume decreases in wide body aircraft and rotorcraft market, and unfavourable foreign exchange impact due to the weakening of the United States dollar against the Canadian dollar. On a currency neutral basis, revenues in the United States decreased 8.7% in the third quarter of 2017 over the same period in 2016.

European revenues increased 3.8% in the third quarter of 2017 compared to the same period in 2016 primarily driven by increased production rates for both single and wide body aircraft offset by an unfavourable foreign exchange impact as the British pound weakened relative to the Canadian dollar. On a constant currency basis, revenues in the third quarter of 2017 in Europe went up by 8.3% compared to the same period in 2016.

Gross Profit

Expressed in thousands of dollars	Three month period ended September 30			Nine month period ended September 30		
	2017	2016	Change	2017	2016	Change
Gross profit	41,338	38,863	6.4%	130,437	133,334	(2.2%)
Percentage of revenues	17.8%	16.3%		17.8%	17.6%	

Gross profit of \$41.3 million for the third quarter of 2017 was 6.4% higher than the \$38.9 million for the third quarter of 2016, and gross profit as a percentage of revenues was 17.8% for the third quarter of 2017, an increase from 16.3% for the same quarter in 2016. The gross profit in the current quarter was driven by higher repair and overhaul revenues and production volume increases offset by the unfavourable foreign exchange due to the weakening of the United States dollar and the British pound against the Canadian dollar year over year.

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Administrative and General Expenses

Expressed in thousands of dollars	Three month period ended September 30			Nine month period ended September 30		
	2017	2016	Change	2017	2016	Change
Administrative and general expenses	13,990	13,997	–	44,523	42,779	5.6%
Percentage of revenues	6.0%	5.9%		6.1%	5.7%	

Administrative and general expenses as a percentage of revenues were 6.0% for the third quarter of 2017, slightly higher than 5.9% in the corresponding period of 2016. Administrative and general expenses of \$14.0 million in the third quarter of 2017 were consistent with the third quarter of 2016.

Other

Expressed in thousands of dollars	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Foreign exchange loss (gain)	2,790	(1,888)	5,882	(2,737)
Business closure costs	–	–	–	2,208
Loss (gain) on disposal of property, plant and equipment	12	56	(26,576)	241
Gain on disposition of investment property	(2,183)	–	(2,183)	–
Other	–	–	4,010	–
Total other	619	(1,832)	(18,867)	(288)

Other expense of \$0.6 million for the third quarter of 2017 consisted of \$2.8 million foreign exchange losses compared to a \$1.9 million foreign exchange gains recorded in the corresponding period of 2016. The movements in balances denominated in foreign currencies and the fluctuations of the foreign exchange rates impact the net foreign exchange loss or gain recorded in a quarter. During the third quarter of 2017, the Corporation sold one of its investment properties for \$3.9 million and recorded a \$2.2 million gain.

Interest Expense

Expressed in thousands of dollars	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Interest on bank indebtedness and long-term debt	691	974	2,083	3,144
Accretion charge on borrowings and long-term debt	210	210	696	678
Discount on sale of accounts receivable	448	308	1,212	955
Total interest expense	1,349	1,492	3,991	4,777

Total interest expense of \$1.3 million in the third quarter of 2017 was slightly lower than the \$1.5 million in the third quarter of 2016, mainly due to lower interest on bank indebtedness and long-term debt driven by lower principal amounts outstanding during the third quarter of 2017 than the same period in 2016, offset by a higher discount on sale of accounts receivables due to a larger volume of receivables sold under factoring programs for the third quarter of 2017 as compared to the same period in the prior year.

Provision for Income Taxes

Expressed in thousands of dollars	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Current income tax expense	3,407	4,716	12,039	12,463
Deferred income tax expense	2,629	1,659	9,623	9,023
Income tax expense	6,036	6,375	21,662	21,486
Effective tax rate	23.8%	25.3%	21.5%	25.0%

Income tax expense for the three months ended September 30, 2017 was \$6.0 million, representing an effective income tax rate of 23.8% compared to 25.3% for the same period of 2016. The effective tax rate and the changes to current and deferred income tax expenses year over year were primarily due to change in mix of income across the different jurisdictions in which the Corporation operates. In addition, the lower tax rate applicable to the capital gain on the sale of the investment property during the current quarter further decreased the effective tax rate.

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3. Selected Quarterly Financial Information

A summary view of Magellan’s quarterly financial performance

Expressed in millions of dollars, except per share amounts	2017				2016				2015			
	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31
Revenues	232.6	253.5	247.2	247.1	238.0	252.7	266.1	252.6	238.0	252.7	266.1	252.6
Income before taxes	25.4	26.9	48.5	31.3	25.2	29.6	31.3	27.1	25.2	29.6	31.3	27.1
Net Income	19.3	20.4	39.4	24.0	18.8	22.3	23.4	25.5	18.8	22.3	23.4	25.5
Net Income per share												
Basic and diluted	0.33	0.35	0.68	0.41	0.32	0.38	0.40	0.44	0.32	0.38	0.40	0.44
EBITDA ¹	37.6	40.4	62.3	45.3	38.4	44.7	45.8	43.1	38.4	44.7	45.8	43.1

¹ EBITDA is not an IFRS financial measure. Please see the “Reconciliation of Net Income to EBITDA” section for more information.

Revenues and net income reported in the table above were impacted by the movements in the Canadian dollar relative to the United States dollar and British pound when the Corporation translates its foreign operations to Canadian dollars. Further, the movements in the United States dollar relative to British pound impact the Corporation’s United States dollar exposures in its European operations. During the periods reported, the average exchange rate of United States dollar relative to the Canadian dollar fluctuated between a high of 1.3748 in the first quarter of 2016 and a low of 1.2526 in the third quarter of 2017. The average exchange rate of British pound relative to the Canadian dollar moved from a high of 2.0253 in the fourth quarter of 2015 to a low of 1.6398 in the third quarter of 2017. The average exchange rate of the British pound relative to the United States dollar reached its high of 1.5168 in the fourth quarter of 2015 and hit a low of 1.2395 in the first quarter of 2017.

Revenue for the third quarter of 2017 of \$232.6 million was \$5.4 million lower than that in the third quarter of 2016. The average exchange rate of the United States dollar relative to the Canadian dollar in the third quarter of 2017 was 1.2501 versus 1.3053 in the same period of 2016. The average exchange rate of British pound relative to the Canadian dollar moved from 1.7135 in the third quarter of 2016 to 1.6397 during the current quarter. The average exchange rate of the British pound relative to the United States dollar was consistent in the third quarter of both years. Had the foreign exchange rates remained at levels experienced in the third quarter of 2016, reported revenues in the third quarter of 2017 would have been higher by \$8.6 million.

As discussed above, net income reported in the quarterly information was also impacted by the foreign exchange movements. The Corporation reported its highest net income in the first quarter of 2017 mainly driven by the recording of the gain on the sale of the land and building of its Mississauga facility. In the third quarter of 2017, the Corporation recorded a gain of \$2.2 million on the disposition of an investment property. The Corporation recorded business closure costs related to the closure of a small operating facility in the United States in the second quarter of 2016, and a margin adjustment related to one of its construction contracts in the third quarter of 2016. In the fourth quarter of 2015, the Corporation recognized an adjustment in corporation taxation rates in the income tax jurisdictions in which the Corporation operates.

4. Reconciliation of Net Income to EBITDA

A description and reconciliation of certain non-IFRS measures used by management

In addition to the primary measures of earnings and earnings per share (basic and diluted) in accordance with IFRS, the Corporation includes EBITDA (earnings before interest expense, income taxes and depreciation and amortization) in this quarterly statement. The Corporation has provided this measure because it believes this information is used by certain investors to assess financial performance and that EBITDA is a useful supplemental measure as it provides an indication of the results generated by the Corporation’s principal business activities prior to consideration of how these activities are financed and how the results are taxed in the various jurisdictions. Each of the components of this measure are calculated in accordance with IFRS, but EBITDA is not a recognized measure under IFRS, and the Corporation’s method of calculation may not be comparable with that of other companies. Accordingly, EBITDA should not be used as an alternative to net income as determined in accordance with IFRS or as an alternative to cash provided by or used in operations.

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	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Expressed in thousands of dollars				
Net income	19,344	18,831	79,128	64,580
Interest	1,349	1,492	3,991	4,777
Taxes	6,036	6,375	21,662	21,486
Depreciation and amortization	10,862	11,695	35,554	38,118
EBITDA	37,591	38,393	140,335	128,961

EBITDA decreased slightly by 2.1% to \$37.6 million for the third quarter of 2017 from the \$38.4 million in the third quarter of 2016 as a result of lower interest, taxes and depreciation and amortization expenses, offset by higher net income.

5. Liquidity and Capital Resources

A discussion of Magellan’s cash flow, liquidity, credit facilities and other disclosures

The Corporation’s liquidity needs can be met through a variety of sources including cash on hand, cash provided by operations, short-term borrowings from its credit facility and accounts receivable securitization program, and long-term debt and equity capacity. Principal uses of cash are for operational requirements, capital expenditures and dividend payments. Based on current funds available and expected cash flow from operating activities, management believes that the Corporation has sufficient funds available to meet its liquidity requirements at any point in time. However, if cash from operating activities is lower than expected or capital projects exceed current estimates, or if the Corporation incurs major unanticipated expenses, it may be required to seek additional capital in the form of debt or equity or a combination of both.

Cash Flow from Operations

	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Expressed in thousands of dollars				
Decrease (increase) in accounts receivable	10,822	(3,856)	(9,537)	(21,999)
(Increase) decrease in inventories	(1,268)	959	(4,380)	(9,158)
Decrease (increase) in prepaid expenses and other	969	(1,974)	1,202	(1,468)
Increase (decrease) in accounts payable, accrued liabilities and provisions	1,409	1	(18,993)	(490)
Changes to non-cash working capital	11,932	(4,870)	(31,708)	(33,115)
Cash provided by operating activities	41,460	25,530	62,049	73,291

The Corporation generated \$41.5 million during the third quarter of 2017 from operating activities, compared to \$25.5 million in the third quarter of 2016. The increase in cash flow from operations was primarily impacted by the favourable movement in non-cash working capital balances resulting from the sale of receivables under a new program during the third quarter of 2017.

Investing Activities

	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Expressed in thousands of dollars				
Purchase of property, plant and equipment	(11,330)	(8,986)	(37,472)	(20,576)
Proceeds of disposals of property, plant and equipment	43	60	32,721	223
Proceeds on disposition of investment property	3,900	–	3,900	–
Increase in intangible and other assets	(660)	(1,970)	(6,553)	(9,025)
Change in restricted cash	(3,900)	198	(235)	5,423
Cash used in investing activities	(11,947)	(10,698)	(7,639)	(23,955)

Cash used in investing activities for the third quarter of 2017 was \$11.9 million compared to \$10.7 million in the same quarter of 2016, an increase of \$1.2 million primarily attributed to higher investment in property, plant and equipment. The Corporation continues to invest in capital expenditures to enhance its manufacturing capabilities in various geographies and to support new customer programs. During the quarter, the Corporation sold one of its investment properties for proceeds of \$3.9 million, which was placed in an escrow account as at September 30, 2016 and subsequently released from escrow in early October 2017. This was reflected as a change in restricted cash during the quarter.

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Financing Activities

Expressed in thousands of dollars	Three month period ended September 30		Nine month period ended September 30	
	2017	2016	2017	2016
Decrease in bank indebtedness	(5,357)	(11,578)	(24,522)	(40,791)
(Decrease) increase in debt due within one year	(8,802)	(2,354)	(3,995)	352
Decrease in long-term debt	(10,580)	(1,156)	(12,909)	(3,407)
Increase (decrease) in long-term liabilities and provisions	101	(177)	1,241	31
Increase in borrowings subject to specific conditions	411	1,988	2,962	2,795
Common share dividend	(3,784)	(3,347)	(11,351)	(10,041)
Cash used in financing activities	(28,011)	(16,624)	(48,574)	(51,061)

The Corporation has an operating credit facility, with a syndicate of banks, with a Canadian dollar limit of \$95.0 million, a US dollar limit of US\$35.0 million and a British pound limit of £11.0 million. Under the terms of the amended credit agreement, the operating credit facility expires on September 30, 2018. Extensions of the facility are subject to mutual consent of the syndicate of lenders and the Corporation. The credit agreement also includes a Canadian \$50.0 million uncommitted accordion provision which provides the Corporation with the option to increase the size of the operating credit facility.

The Corporation used \$28.0 million in the third quarter of 2017 mainly to repay bank indebtedness, debt due within one year, and long-term debt, and to pay dividends.

As at September 30, 2017 the Corporation has made contractual commitments to purchase \$25.2 million of capital assets.

Dividends

During the third quarter of 2017, the Corporation declared and paid quarterly cash dividends of \$0.065 per common shares representing an aggregating dividend payment of \$3.8 million.

Subsequent to September 30, 2017, the Corporation announced that its Board of Directors had declared a quarterly cash dividend on its common shares of \$0.085 per common share. The dividend will be payable on December 29, 2017 to shareholders of record at the close of business on December 15, 2017.

Outstanding Share Information

The authorized capital of the Corporation consists of an unlimited number of Preference Shares, issuable in series, and an unlimited number of common shares. As at November 3, 2017, 58,209,001 common shares were outstanding and no preference shares were outstanding.

6. Financial Instruments

A summary of Magellan’s financial instruments

Derivative Contracts

The Corporation operates internationally, which gives rise to a risk that its income, cash flows and shareholders’ equity may be adversely impacted by fluctuations in foreign exchange rates. Currency risk arises because the amount of the local currency receivable or payable for transactions denominated in foreign currencies may vary due to changes in exchange rates and because the non-Canadian dollar denominated financial statements of the Corporation’s subsidiaries may vary on consolidation into the reporting currency of Canadian dollars. The Corporation from time to time may use derivative financial instruments to help manage foreign exchange risk with the objective of reducing transaction exposures and the resulting volatility of the Corporation’s earnings. The Corporation does not trade in derivatives for speculative purposes. Under these contracts the Corporation is obligated to purchase specified amounts at predetermined dates and exchange rates. These contracts are matched with anticipated cash flows in United States dollars. The counterparties to the foreign currency contracts are all major financial institutions with high credit ratings. The Corporation had no foreign exchange contracts outstanding as at September 30, 2017.

Off Balance Sheet Arrangements

The Corporation does not have any off-balance sheet arrangements that have or reasonably are likely to have a material effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources. As a result, the Corporation is not exposed materially to any financing, liquidity, market or credit risk that could arise if it had engaged in these arrangements.

7. Related Party Transactions

A summary of Magellan’s transactions with related parties

For the three and nine month periods ended September 30, 2017, the Corporation had no material transactions with related parties as defined in IAS 24 - *Related Party Disclosures*.

8. Risk Factors

A summary of risks and uncertainties facing Magellan

The Corporation manages a number of risks in each of its businesses in order to achieve an acceptable level of risk without hindering the ability to maximize returns. Management has procedures to help identify and manage significant operational and financial risks.

For more information in relation to the risks inherent in Magellan’s business, reference is made to the information under “Risk Factors” in the Corporation’s Management’s Discussion and Analysis for the year ended December 31, 2016 and to the information under “Risks Inherent in Magellan’s Business” in the Corporation’s Annual Information Form for the year ended December 31, 2016, which have been filed with SEDAR at www.sedar.com.

9. Changes in Accounting Policies

A description of accounting standards adopted in the current year

The following new standards, and amendments to standards and interpretations, are effective for the first time for interim periods beginning on or after January 1, 2017 and have been applied in preparing the consolidated interim financial statements.

Disclosure Initiative

In 2016, the IASB issued amendments to IAS 7, Statement of Cash Flows (“IAS 7”). The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). They are effective for annual periods beginning on or after January 1, 2017, with earlier adoption permitted. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. The Corporation is not required to provide additional disclosures in its condensed interim consolidated financial statements, but will disclose additional information in its annual consolidated financial statements for the year ended December 31, 2017.

10. Future Changes in Accounting Policies

A description of new accounting standards and interpretations not yet adopted

A number of new standards, and amendments to standards and interpretations, are not yet effective for the interim period ended September 30, 2017, and have not been applied in preparing these condensed consolidated interim financial statements. These changes are not yet adopted by the Corporation and could have an impact on future periods. These changes are described in detail in the Corporation’s 2016 audited annual consolidated financial statements.

- IFRS 15, *Revenue from Contracts with Customers* (“IFRS 15”)
- IFRS 9, *Financial Instruments*
- IFRS 16, *Leases*
- Amendments to IFRS 2, *Classification and Measurement of Share-based Payment Transactions*
- IFRIC Interpretation 22, *Foreign Currency Transactions and Advance Consideration*
- IFRIC Interpretation 23, *Uncertainty over Income Tax Treatments* (“IFRIC 23”)

In June 2017, IASB issued IFRIC 23 which clarifies application of recognition and measurement requirements in IAS 12, Income Taxes when there is uncertainty over income tax treatments. IFRIC 23 is effective for annual reporting periods beginning on or after 1 January 2019. Earlier application is permitted.

The Corporation is in the process of evaluating the impact of adopting these standards on the Corporation’s consolidated financial statements. Specifically, IFRS 15 is effective for annual periods beginning on or after January 1, 2018. The Corporation is required to retrospectively apply IFRS 15 to all contracts that are not complete on the date of initial

application. The Corporation intends to make a policy choice to restate each prior period presented and recognize the cumulative effect of initially applying IFRS 15 as an adjustment to the opening balance of equity at the beginning of the earliest period presented, subject to certain practical expedients the Corporation anticipates adopting.

The Corporation has undertaken a project to assess the impact of IFRS 15 and ensure the Corporation’s compliance with IFRS 15. The Corporation has collected an inventory of significant contracts with customers in scope for IFRS 15 assessment and identified preliminary accounting topics that may impact the Corporation’s reported results based on the review of a sample of contracts from each revenue stream. The Corporation is in the process of reviewing contracts with customers to ensure revenue recognition practices are in accordance with IFRS 15 and evaluating potential changes to revenue processes and systems. The Corporation has identified contracts in which performance obligations are satisfied over time as control transfers during production. For these contracts, the revenue recognition pattern will change with revenue being recognized earlier in the year of adoption as compared to under the legacy accounting policy. Contracts that do not meet the criteria for over time recognition will continue to be recognized at a point in time. The Corporation continues to assess the impact of this standard on the consolidated financial statements and it is not yet in a position to make a reliable estimate of its impact. The Corporation plans to disclose the estimated financial effects of the adoption of IFRS 15 in its 2017 annual consolidated financial statements.

11. Critical Accounting Estimates

A description of accounting estimates that are critical to determining Magellan’s financial results

In the 2016 audited annual consolidated financial statements and management’s discussion and analysis, the Corporation identified the accounting policies and estimates that are critical to the understanding of the business and results of operations. Please refer to note 1 to the audited consolidated financial statements for the year ended December 31, 2016 for a discussion regarding the critical accounting estimates.

12. Controls and Procedures

A description of Magellan’s disclosure controls and internal controls over financial reporting

Based on the current Canadian Securities Administrators (the “CSA”) rules under National Instrument 52-109 Certification of Disclosure in Issuers’ Annual and Interim Filings, the Chief Executive Officer and Chief Financial Officer (or individuals performing similar functions as a chief executive officer or chief financial officer) are required to certify as at September 30, 2017 that they are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting.

Management does not expect disclosure controls and procedures and internal control over financial reporting to prevent all errors, misstatements or fraud. In addition, internal control over financial reporting that management has designed and established may be circumvented and rendered ineffective as a result of unauthorized acts of individuals through collusion or management override. A system of control, no matter how well conceived and operated, can provide only reasonable, but not absolute, assurance that control objectives are met. Due to the inherent limitations in a system of control, there is no absolute assurance that all controls issues, which may result in errors, misstatements, or fraud, can be prevented or detected. The inherent limitations include, amongst other things: (i) management’s assumptions and judgements could ultimately prove to be incorrect under varying conditions and circumstances; (ii) the impact of isolated errors; (iii) assumptions about the likelihood of future events.

No changes were made in the Corporation’s internal control over financial reporting during the Corporation’s most recent interim period, that have materially affected, or are reasonably likely to materially affect, the Corporation’s internal control over financial reporting.

13. Outlook

The outlook for Magellan’s business in 2017

The commercial aircraft industry is maintaining its upward trend with more than 12,000 jetliners on order at Airbus and Boeing. It is expected that this prolonged growth will continue through to the end of the decade when forecasters predict demands will reach a peak. However, it has become evident that there is a shift taking place in the industry where Original Equipment Manufacturers (“OEMs”) are attempting to increase their margins through increasing vertical integration, the repatriation of work packages in-house, including higher margin maintenance, repair and overhaul work, and by continuing to pressure suppliers to reduce prices. Tier I suppliers are reacting with similar or counter strategies to preserve their margins as in the recent announcement by UTC to acquire Rockwell Collins. Such reorganizations will challenge lower tier II and III suppliers to realign their strategies to fit into this new model. The recent award of the A320 NEO (PW1100) Exhaust system by Airbus to Magellan is a successful example of Magellan realigning its strategy with that of the OEMs.

Commercial aircraft build rates remain largely unchanged from the second quarter of 2017. Boeing’s 737 build rate is currently at 47 aircraft (“A/C”) per month, with 52 A/C per month planned for 2018 and 58 A/C per month in 2019. Although production mix changes between Airbus’ A320ceo and A320neo were required in 2017, the overall program build rate remains at 55 A/C per month with expectations that this production rate will peak at 60 A/C per month in 2019. There remains some supply chain challenges that both Boeing and Airbus are managing as they continue to ramp up production rates.

In the wide body market, Boeing’s 777 build rate has reduced to 5 A/C per month from 7 A/C per month. The 787 build rate is holding at 12 A/C per month and the 747-8 freighter is at 0.5 A/C per month. Boeing’s 767 build rate has stepped up to 2.5 A/C per month from 2 A/C per month in support of the KC-46 tanker program. Airbus announced the A380 build rate will drop in the fourth quarter of 2017 from 1.06 A/C per month to 0.71 A/C per month, which is slightly lower than previously forecasted. A330 rates are holding at 7 A/C per month as the A350XWB continues its production ramp-up to 13 A/C per month by 2020.

There have been no significant changes in the regional turboprop market and the current view is that the market is not large enough for three manufacturers to maintain volume production. Additional market dilution is a possibility with the new entrants from Russia and China. ATR and Bombardier currently dominate this comparatively small market.

The business jet market is forecasting to remain flat until 2019 as a generous supply of used aircraft continues to limit demand for new aircraft. The market has not appreciably recovered since the 2008 recession. Traditional market trend indicators such as increased corporate profits, no longer seem to have the same influence as they did prior to the recession. Magellan supports the turboprop and business jet market predominately through its castings and aerostructure commodity groups.

There are indications that the global rotorcraft market is starting to recover partially fueled by the development of new commercial products as OEM’s attempt to stimulate the market. A number of new helicopters such as the Airbus’ H160, Bell’s 525 Relentless, 505 Jet Ranger X, and Leonardo’s AW189 and AW609 are a few of the new products. There are also new market entrants such as Turkey’s TAI T625 and the Marengo Swisshelicopter SH09. Additionally the market is seeing strong indications that major defence procurement initiatives are now anticipated in the defence sector which will have a positive effect on existing legacy programs and new program variants which are planned for the mid 2020’s.

In the defense market, of specific interest to Magellan, over 240 Lockheed Martin F-35 Lightning II aircraft have been delivered since the start of the program, with 150 aircraft currently in the production flow. Lockheed is expecting to exceed 60 aircraft delivered in 2017 as rates continue to increase year over year. Integral to the program’s affordability agenda, the next procurement tranche is being planned around anticipated cost efficiencies associated with combining a three year buy of approximately 440 aircraft. The U.S. Government budgeting process has progressed beyond the Armed Services Committees with both the Senate and House committees adding more aircraft to the Bill. Increased levels of potential program sales have also been anticipated from countries where fighter replacement programs have been announced or are imminent.

In summary, except for the continued strength of the commercial aircraft market, other aerospace markets remain stable but relatively flat. Defence markets anticipate future opportunities from a number of current platform replacement programs that are on the horizon. In today’s market, one of the key growth strategies for Magellan is to insure that we stay in constant alignment with our customer’s procurement strategies.