MAGELLAN
AEROSPACE

QUARTERLY REPORT

JUNE 30, 2019

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 six month periods ended June 30, 2019, and the audited annual consolidated financial statements for the year ended December 31, 2018 (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 June 30, 2019 relative to the three month period ended June 30, 2018. The information contained in this report is as at August 2, 2019. 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

On May 14, 2019, Magellan announced that it will continue producing F-35 Lightning II ("F-35") horizontal tail assemblies under an agreement with BAE Systems. The agreement is the continuation of contract awards previously granted to Magellan by BAE Systems and with the additional quantities awarded, Magellan will now on a go forward basis produce more than double the horizontal tails from what has so far been produced for the program. Annual deliveries will ramp up to 60 per year within the three year period. Magellan, through its operations in Winnipeg, Manitoba, and BAE Systems have been working together to produce horizontal tails for the global F-35 program for more than a decade, signing the original Letter of Intent for this agreement in 2006.

For additional information, please refer to the "Management's Discussion and Analysis" section of the Corporation's 2018 Annual Report available on www.sedar.com.

2. Results of Operations

A discussion of Magellan's operating results for second quarter ended June 30, 2019

The Corporation reported revenue in the second quarter of 2019 of $264.1 million, a $22.9 million improvement from the second quarter of 2018 of $241.2 million. Gross profit and net income for the second quarter of 2019 were $45.1 million and $21.7 million, respectively, in comparison to gross profit of $41.3 million and net income of $23.5 million for the second quarter of 2018.

Consolidated Revenue

	Three month period ended June 30			Six month period ended June 30		
Expressed in thousands of dollars	**2019**	2018	Change	**2019**	2018	Change
Canada	**96,185**	77,689	23.8%	**186,886**	156,345	19.5%
United States	**83,128**	83,509	(0.5%)	**167,947**	163,085	3.0%
Europe	**84,769**	80,023	5.9%	**179,133**	166,416	7.6%
Total revenues	**264,082**	241,221	9.5%	**533,966**	485,846	9.9%

Consolidated revenues for the three months ended June 30, 2019 were $264.1 million, an increase of $22.9 million from the $241.2 million recorded for the same period in 2018. Revenues in Canada increased 23.8% in the second quarter of 2019 in comparison to the same period in 2018, primarily due to higher volumes in repair and overhaul services and proprietary products, and the strengthening of the United States dollar relative to the Canadian dollar when compared to the prior period. On a currency neutral basis, Canadian revenues in the second quarter of 2019 increased by 21.6% over the same period of 2018.

Revenues in United States slightly decreased 0.5% in the second quarter of 2019 compared to the second quarter of 2018 when measured in Canadian dollars mainly due to single aisle aircraft volume decreases on the Boeing 737 Max, offset in part by favourable foreign exchange impact due to the strengthening of the United States dollar against the Canadian dollar. On a currency neutral basis, revenues in the United States decreased 3.8% in the second quarter of 2019 over the same period in 2018.

European revenues increased 5.9% in the second quarter of 2019 compared to the corresponding period in 2018 primarily driven by increased production rates for single aisle and wide body aircraft, and the strengthening of the United States dollar relative to the British pound, offset partially by the unfavourable foreign exchange impact due to the weakening of the British pound against the Canadian dollar. On a constant currency basis, revenues in the second quarter of 2019 in Europe increased 3.7% when compared to the same period in 2018.

Gross Profit

	Three month period ended June 30			Six month period ended June 30		
Expressed in thousands of dollars	**2019**	2018	Change	**2019**	2018	Change
Gross profit	**45,090**	41,273	9.2%	**87,911**	81,701	7.6%
Percentage of revenues	**17.1%**	17.1%		**16.5%**	16.8%	

Gross profit of $45.1 million for the second quarter of 2019 was $3.8 million higher than the second quarter of 2018 gross profit of $41.3 million, and gross profit as a percentage of revenues of 17.1% for the second quarter of 2019 was consistent with the same period in 2018. The gross profit in the current quarter was primarily driven by higher volumes in repair and overhaul services and proprietary products in Canada, and the favourable foreign exchange due to the strengthening year over year of the United States dollar against the Canadian dollar and the British pound, offset partially by lower production volumes in the United States.

Administrative and General Expenses

Expressed in thousands of dollars	Three month period ended June 30			Six month period ended June 30		
	2019	2018	Change	**2019**	2018	Change
Administrative and general expenses	**16,290**	14,184	14.8%	**31,590**	28,812	9.6%
Percentage of revenues	**6.2%**	5.9%		**5.9%**	5.9%	

Administrative and general expenses as a percentage of revenues of 6.2% for the second quarter of 2019 were 0.3% higher than the same period of 2018. Administrative and general expenses increased $2.1 million to $16.3 million in the second quarter of 2019 compared to $14.2 million in the second quarter of 2018 mainly due to costs incurred for the phased implementation of a new ERP program, and higher costs in relation to the Corporation’s India facilities. In the second quarter of 2018, a one-time gain of $0.5 million was recorded related to facility rental costs.

Other

Expressed in thousands of dollars	Three month period ended June 30		Six month period ended June 30	
	2019	2018	**2019**	2018
Foreign exchange gain	**(1,106)**	(3,774)	**(653)**	(1,604)
Loss (gain) on disposal of property, plant and equipment	**38**	24	**(47)**	112
Other	**815**	—	**1,005**	—
Total other	**(253)**	(3,750)	**305**	(1,492)

Other for the second quarter of 2019 included a $1.1 million compared to a $3.8 million foreign exchange gain in the same period of 2018, mainly driven by the movements in balances denominated in the foreign currencies and the fluctuations of the foreign exchange rates. In addition, $0.8 million of one-time relocation expenses were incurred for the Corporation’s Mississauga facility.

Interest Expense

Expressed in thousands of dollars	Three month period ended June 30		Six month period ended June 30	
	2019	2018	**2019**	2018
Interest on bank indebtedness and long-term debt	**166**	286	**126**	674
Accretion charge for borrowings, lease liabilities and long-term debt	**628**	248	**1,173**	510
Discount on sale of accounts receivable	**497**	536	**1,060**	964
Total interest expense	**1,291**	1,070	**2,359**	2,148

Total interest expense of $1.3 million in the second quarter of 2019 was $0.2 million higher than the second quarter of 2018 amount of $1.1 million mainly due to accretion charge for the lease liabilities as a result of adoption of the new lease accounting standard, partially offset by decreased interest on bank indebtedness and long-term debt as principal amounts were lower during the quarter.

Provision for Income Taxes

Expressed in thousands of dollars	Three month period ended June 30		Six month period ended June 30	
	2019	2018	**2019**	2018
Current income tax expense	**2,506**	3,812	**5,311**	7,690
Deferred income tax expense	**3,540**	2,493	**6,221**	3,615
Income tax expense	**6,046**	6,305	**11,532**	11,305
Effective tax rate	**21.8%**	21.2%	**21.5%**	21.6%

Income tax expense for the three months ended June 30, 2019 was $6.0 million, representing an effective income tax rate of 21.8% compared to 21.2% for the same period of 2018. The change in effective tax rate and current and deferred income tax expenses year over year was primarily due to change in mix of income across the different jurisdictions in which the Corporation operates.

3. Selected Quarterly Financial Information

A summary view of Magellan's quarterly financial performance

	2019					2018		2017
Expressed in millions of dollars, except per share amounts	**Jun 30**	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31[2]	Sep 30[2]
Revenues	**264.1**	269.9	254.4	226.5	241.2	244.6	232.7	222.6
Income before taxes	**29.1**	25.9	38.5	23.4	29.8	22.5	28.4	23.6
Net Income	**21.7**	20.4	29.5	18.6	23.5	17.5	31.9	18.1
Net Income per share								
Basic and diluted	**0.37**	0.35	0.51	0.32	0.40	0.30	0.55	0.31
EBITDA[1]	**42.7**	40.5	50.7	35.5	41.8	34.1	40.1	35.8

[1] EBITDA is not an IFRS financial measure. Please see the "Reconciliation of Net Income to EBITDA" section for more information.
[2] Restated using revenue recognition policies in accordance with IFRS 15, *Revenue from Contracts with Customers.*

Revenues and net income reported in the quarterly financial information 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 the British pound impact the Corporation's United States dollar exposures in its European operations. During the periods reported, the average exchange rate of the United States dollar relative to the Canadian dollar fluctuated between a high of 1.3292 in the first quarter of 2019 and a low of 1.2526 in the third quarter of 2017. The average exchange rate of the British pound relative to the Canadian dollar moved from a high of 1.7607 in the first quarter of 2018 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 1.3920 in the first quarter of 2018 and hit a low of 1.2703 in the second quarter of 2019.

Revenue for the second quarter of 2019 of $264.1 million was higher than that in the second quarter of 2018. The average exchange rate of the United States dollar relative to the Canadian dollar in the second quarter of 2019 was 1.3375 versus 1.2912 in the same period of 2018. The average exchange rate of British pound relative to the Canadian dollar decreased from 1.7567 in the second quarter of 2018 to 1.7190 during the current quarter. The average exchange rate of the British pound relative to the United States dollar decreased from 1.3605 in the second quarter of 2018 to 1.2852 in the current quarter. Had the foreign exchange rates remained at levels experienced in the second quarter of 2018, reported revenues in the second quarter of 2019 would have been lower by $6.2 million.

As discussed above, net income reported in the quarterly information was also impacted by the foreign exchange movements. In the third quarter of 2017, the Corporation recorded a gain of $2.2 million on the disposition of an investment property. In the fourth quarter of 2017, the Corporation recognized the future tax benefit attributable to a reduction in the United States federal corporate income tax as a result of new legislation. In the fourth quarter of 2018, the Corporation recorded a net gain of $9.7 million related to prior acquisitions.

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.

	Three month period ended June 30		Six month period ended June 30	
Expressed in thousands of dollars	**2019**	2018	**2019**	2018
Net income	**21,716**	23,464	**42,125**	40,928
Interest	**1,291**	1,070	**2,359**	2,148
Taxes	**6,046**	6,305	**11,532**	11,305
Depreciation and amortization	**13,622**	10,947	**27,152**	21,543
EBITDA	**42,675**	41,786	**83,168**	75,924

EBITDA increased $0.9 million or 2.2% to $42.7 million for the second quarter of 2019, compared to $41.8 million in the second quarter of 2018 mainly as a result of higher interest, and depreciation and amortization expenses mainly driven by the implementation of new accounting standard, offset by lower net income and taxes.

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 June 30		Six month period ended June 30	
Expressed in thousands of dollars	**2019**	2018	**2019**	2018
Decrease (increase) in accounts receivable	**9,020**	1,904	**(13,686)**	(14,299)
Increase in contract assets	**(6,588)**	(17,113)	**(18,324)**	(23,912)
(Increase) decrease in inventories	**(5,962)**	(2,366)	**(8,024)**	1,498
Increase in prepaid expenses and other	**(590)**	(2,358)	**(3,416)**	(5,420)
(Decrease) increase in accounts payable, accrued liabilities and provisions	**(7,941)**	862	**4,475**	(13,465)
Changes in non-cash working capital balances	**(12,061)**	(19,071)	**(38,975)**	(55,598)
Cash provided by operating activities	**25,674**	17,174	**33,772**	8,579

For the three months ended June 30, 2019 the Corporation generated $25.7 million from operating activities, compared to $17.2 million in the second quarter of 2018. The quarter over quarter increase in cash flow from operations was as a result of the favourable movement of non-cash working capital balances, largely due to changes in accounts receivable and contract assets from the timing of production and billing related to products transferred over time, respectively. This was offset in part by the decrease in accounts payable, accrued liabilities and provisions due to the nature of purchases and timing of payments.

Investing Activities

	Three month period ended June 30		Six month period ended June 30	
Expressed in thousands of dollars	**2019**	2018	**2019**	2018
Business combination, net of cash acquired	—	—	**(2,661)**	—
Purchase of property, plant and equipment	**(8,839)**	(5,497)	**(18,346)**	(13,063)
Proceeds of disposals of property, plant and equipment	**124**	178	**359**	199
(Increase) decrease in intangible and other assets	**(3,163)**	2,831	**(9,229)**	2,077
Change in restricted cash	—	2,714	—	—
Cash (used in) provided by investing activities	**(11,878)**	226	**(29,877)**	(10,787)

Investing activities used $11.9 million in cash for the second quarter of 2019 compared to providing $0.2 million in the same quarter of the prior year, a significant change from the prior year primarily due to higher level of investment in property, plant and equipment, and higher deposits recorded in the other assets during the quarter. The Corporation continues to invest in capital expenditures to enhance its manufacturing capabilities in various geographies and to support new customer programs.

Financing Activities

	Three month period ended June 30		Six month period ended June 30	
Expressed in thousands of dollars	**2019**	2018	**2019**	2018
(Decrease) increase in bank indebtedness	**(89)**	(8,495)	**(131)**	6,951
(Decrease) increase in debt due within one year	**(1,600)**	1,211	**(8,484)**	(5,822)
Decrease in long-term debt	**(802)**	(608)	**(1,449)**	(13,874)
Lease liability payments	**(783)**	—	**(1,684)**	—
Decrease in long-term liabilities and provisions	**(144)**	(57)	**(179)**	(131)
(Decrease) increase in borrowings subject to specific conditions, net	**(822)**	1,285	**(822)**	1,310
Common share dividend	**(5,821)**	(4,948)	**(11,642)**	(9,896)
Cash used in financing activities	**(10,061)**	(11,612)	**(24,391)**	(21,462)

On September 13, 2018, the Corporation amended its credit agreement with its existing lenders. The Corporation has a multi-currency operating credit facility with a syndicate of banks, with a Canadian dollar limit of $75 million. Under the terms of the amended credit agreement, the operating credit facility expires on September 13, 2020. Extensions of the facility are subject to mutual consent of the syndicate of lenders and the Corporation. The credit agreement also includes a $75 million uncommitted accordion provision which will provide the Corporation with the option to increase the size of the operating credit facility.

The Corporation used $10.1 million in financing activities in the second quarter of 2019 mainly to repay debt due within one year, long-term debt, lease liabilities, borrowings subject to specific conditions, and the payment of dividends.

As at June 30, 2019 the Corporation had made contractual commitments to purchase $13.1 million of capital assets.

Dividends

During the first and second quarter of 2019, the Corporation declared and paid quarterly cash dividends of $0.10 per common shares representing an aggregating dividend payment of $11.6 million.

Subsequent to June 30, 2019, the Corporation announced that its Board of Directors had declared a quarterly cash dividend on its common shares of $0.10 per common share. The dividend will be payable on September 30, 2019 to shareholders of record at the close of business on September 16, 2019.

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 August 2, 2019, 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. As at June 30, 2019, the Corporation had $19.0 million USD/CAD foreign exchange contracts outstanding with an immaterial fair value, expiring monthly until December 2019.

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 six month periods ended June 30, 2019, 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, 2018 and to the information under "Risks Inherent in Magellan's Business" in the Corporation's Annual Information Form for the year ended December 31, 2018, 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, 2019 and have been applied in preparing the consolidated interim financial statements.

Leases
Effective January 1, 2019, the Corporation adopted IFRS 16, *Leases* ("IFRS 16"), replacing IAS 17, *Leases* ("IAS 17"), IFRIC 4, *Determining whether an Arrangement contains a Lease* ("IFRIC 4"), SIC-15, *Operating Leases-Incentives* and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

IFRS 16 introduced a single on-balance sheet model for lessees unless the underlying asset is of low value and the short-term lease recognition exemption is being applied. A lessee is required to recognize, on its statement of financial position, a right-of-use asset, representing its right to use the underlying leased asset, and a lease liability, representing its obligation to make lease payments. As a result of adopting IFRS 16, the Corporation recognized a $24.2 million increase to assets and liabilities, respectively, on the unaudited condensed consolidated interim statement of financial position. Subsequent to the adoption, operating costs decrease due to the removal of rent expense for leases, depreciation and amortization expense increases due to depreciation of right-of-use assets, and finance costs increase due to accretion of the lease liability. The accounting treatment for lessors remains largely the same as under IAS 17.

The Corporation adopted IFRS 16 under the modified retrospective approach and did not restate the comparatives for 2018. At transition, the Corporation applied the practical expedient available to the Corporation that allows the continuation of the lease assessments under IAS 17 and IFRIC 4 for existing contracts. Therefore, the definition of a lease under IFRS 16 was applied only to contracts entered into or changed after January 1, 2019.

For leases that were classified as operating leases under IAS 17, lease liabilities at transition have been measured at the present value of remaining lease payments, discounted at the incremental borrowing rate as at January 1, 2019. Right-of-use assets at transition have been measured at an amount equal to the corresponding lease liabilities, adjusted for any prepaid or accrued rent relating to that lease.

When applying IFRS 16 to leases previously classified as operating leases, the following practical expedients were applied:

- a single discount rate to a portfolio of leases with similar characteristics;
- used hindsight in determining the lease term where the contract contains purchase, extension, or termination options;
- relied upon our assessment of whether leases are onerous under the requirements of IAS 37, *Provisions, contingent liabilities and contingent assets* as at December 31, 2018 as an alternative to reviewing our right-of-use assets for impairment; and
- excluded short-term leases or low-value leases.

There was no significant impact for contracts in which the Corporation is the lessor.

Prior to adopting IFRS 16, the total minimum operating lease commitments as at December 31, 2018 were $37.9 million. The weighted average discount rate applied to the total lease liabilities recognized on transition was 3.82%. The difference between the total of the minimum lease payments set out in Note 21 to the 2018 annual consolidated financial statements and the total lease liabilities recognized on transition was a result of:

- the effect of discounting on the minimum lease payments;
- the exclusion of lease payments related to reasonably certain termination options that had not been exercised as at December 31, 2018; and
- the exclusion of short-term leases.

Accounting pronouncements adopted

The following pronouncements were adopted by the Corporation as of January 1, 2019 and do not have an impact on the Corporation's unaudited condensed consolidated interim financial statements. These changes are described in detail in the Corporation's 2018 consolidated financial statements.

- IFRIC Interpretation 23, *Uncertainty over Income Tax Treatments*
- Amendments to IAS 19, *Plan Amendment, Curtailment or Settlement*
- Annual Improvements to IFRS Standards 2015 – 2017: IFRS 3, *Business Combination*
- Annual Improvements to IFRS Standards 2015 – 2017: IAS 12, *Income Taxes*

10. Critical Accounting Estimates

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

In the 2018 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, 2018 for a discussion regarding the critical accounting estimates.

11. 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 June 30, 2019 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.

12. Outlook

The outlook for Magellan's business in 2019

Magellan Aerospace participated in the 53rd Paris International Air Show ("PIAS") held between June 17th and June 23rd 2019. PIAS officials recorded a total of 2,453 exhibitors representing 48 countries. There were 866 commercial aircraft order commitments plus options announced worth $140 billion. Orders statistics were down from the 2018 Farnborough Air Show and the 2017 PIAS which recorded 1,464 and 1,226 orders respectively.

Boeing presented its updated commercial market outlook in Paris. Boeing estimates the world fleet will grow from 25,830 aircraft to 50,660 aircraft by 2038, comprising of 19,210 replacements, 24,830 market growth aircraft and 6,620 retained aircraft. A majority (39%) of the 44,040 replacement and growth aircraft are expected to come from the Asia-Pacific region with North America and Europe representing 21% and 20% respectively. Although commercial aircraft order backlogs for Airbus and Boeing are down slightly from the records set by the end of 2018, backlogs still remain strong. As of June 30, 2019, Airbus' backlog was at 7,276 jets on order and Boeing's backlog was at 5,733.

In the single aisle market, Boeing continues to build 737's at a temporarily reduced production rate of 42 aircraft per month. It was announced in June that an additional fix was required on the grounded 737 MAX aircraft, making October the earliest possible return to service date. This is significantly later than most airlines had expected. The impact of the lower production rate is continually being assessed by Magellan as additional information is obtained. The build rate was originally planned to grow from 52 to 57.7 aircraft per month by the third quarter of this year. Despite program delays however, Boeing secured a deal with International Airlines Group in Paris for 200 of the 737 MAX aircraft.

Airbus is currently producing the A320 at a rate of 58 aircraft per month, with plans to reach 63 aircraft per month later in 2019. During PIAS 2019, Airbus launched a new longer-range model of their A321 aimed at the mid-market category where Boeing was to launch its New Midsize Airplane. The new A321XLR program secured orders and commitments, including conversions for 249 aircraft at the show. In addition, Airbus was successful in securing commitments for 85 A220 aircraft, the first new business recorded for the program since 2018.

In the large commercial aircraft market, Boeing's 787 program is now running at 14 aircraft per month, up from a rate of 12 aircraft per month in the first quarter of 2019. The 777 program rate remains steady at 5 aircraft per month as 777X production ramps up and other 777 models ramp down. Boeing is expected to deliver three 777X aircraft in 2019. Airbus' A330 build rate is now at 3.5 aircraft per month, down from 4.5 aircraft per month. The A350XWB rate is at 9.8 aircraft per month. Finally Airbus plans to end A380 production in July 2020.

The regional turboprop segment was successful at PIAS 2019 with orders and options placed for 153 aircraft. ATR claimed orders for 78 ATR-42 and 67 ATR-72 aircraft. The new ATR 42-600S short take-off and landing variant was officially launched in Paris, and received orders from three customers. In June 2019, Longview Aviation Capital completed its acquisition of the Dash 8 from Bombardier and placed the programme into a newly formed holding company called De Havilland Aircraft of Canada Limited. De Havilland Aircraft inherited a backlog of 51 Q400's and announced orders for 6 Q400's in Paris.

In the U.S. defence market, the Defense Department's 2020 budget proposal focuses on "stabilizing or reducing" current production aircraft "while ramping up spending on the next generation of military technology", according to Aviation Week. Although some analysts consider the US$750 billion budget proposal to be a ceiling, the U.S. Defense Department's spending plan calls for annual increases through fiscal 2024. A percentage of the budget will go towards Future Vertical Lift programs.

In the fighter segment, France, Germany and Spain launched a sixth-generation Future Combat Air System programme during PIAS 2019. France's Dassault will serve as the prime contractor, with Airbus leading the development of accompanying carrier vehicles and systems, and Safran and MTU collaborating on engines. The first flight is expected in 2026.

Lockheed Martin's F-35 program achieved several significant milestones during the second quarter of 2019. The first was that 200,000 flight hours were achieved across all global operations. The second was that 400 F-35's had been delivered, comprising of 283 F-35A's, 87 F-35B's and 30 F-35C's. The most important milestone was that the F-35 Joint Program Office and Lockheed Martin had reached an agreement to deliver an F-35A unit cost below $80 million in Lot 13 in 2019, one

year earlier than committed. The record agreement covers more than 470 total F-35s worth US$34 billion over three separate contracts, known as Lots 12 to 14.
In Canada, the Future Fighter Replacement Program is progressing with four of the original five aircraft continuing in the competition, Lockheed Martin's F-35, Boeing's Super Hornet, the Eurofighter Typhoon, and Saab's Gripen. The final request for proposal ("RFP") was issued to the bidders in July 2019. A considerable level of effort was directed at various elements of the RFP documentation based on feedback received from the prospective bidders. Two bid responses have been requested by the Government. The first response is scheduled for fall of 2019 and the final proposal is due in the spring 2020. A down selection is expected in 2020 or 2021 followed by the identification of the selected bidder which is expected in early 2022. The first aircraft delivery is planned to be in 2025.

As a final note, further industry consolidation is set to take place in early 2020 with the merger of United Technologies Corporation and Raytheon Company. It was announced in June 2019 that they had entered into an agreement to combine in an all-stock "merger of equals", creating a combined company named Raytheon Technologies Corporation.

MAGELLAN AEROSPACE CORPORATION
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(unaudited) (expressed in thousands of Canadian dollars, except per share amounts)	Notes	Three month period ended June 30 2019	 2018	Six month period ended June 30 2019	 2018
Revenues	10	**264,082**	241,221	**533,966**	485,846
Cost of revenues		**218,992**	199,948	**446,055**	404,145
Gross profit		**45,090**	41,273	**87,911**	81,701
Administrative and general expenses		**16,290**	14,184	**31,590**	28,812
Other	4	**(253)**	(3,750)	**305**	(1,492)
Income before interest and income taxes		**29,053**	30,839	**56,016**	54,381
Interest expense		**1,291**	1,070	**2,359**	2,148
Income before income taxes		**27,762**	29,769	**53,657**	52,233
Income taxes					
Current	11	**2,506**	3,812	**5,311**	7,690
Deferred	11	**3,540**	2,493	**6,221**	3,615
		6,046	6,305	**11,532**	11,305
Net income		**21,716**	23,464	**42,125**	40,928
Other comprehensive income					
Other comprehensive (loss) income that may be reclassified to profit and loss in subsequent periods:					
Foreign currency translation		**(16,334)**	(5,949)	**(23,044)**	15,033
Items not to be reclassified to profit and loss in subsequent periods:					
Actuarial (loss) gain on defined benefit pension plans, net of taxes	7	**(3,340)**	2,559	**(3,101)**	1,914
Total comprehensive income, net of taxes		**2,042**	20,074	**15,980**	57,875
Net income per share					
Basic and diluted	8	**0.37**	0.40	**0.72**	0.70

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE

MAGELLAN AEROSPACE CORPORATION
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION

(unaudited) **(expressed in thousands of Canadian dollars)**	Notes	**June 30 2019**	December 31 2018
Current assets			
Cash		**41,373**	63,316
Trade and other receivables		**200,499**	187,897
Contract assets		**83,560**	66,436
Inventories		**179,455**	175,082
Prepaid expenses and other		**22,904**	20,058
		527,791	512,789
Non-current assets			
Property, plant and equipment		**420,893**	428,878
Right-of-use assets	3, 6	**22,292**	—
Investment properties		**2,187**	2,305
Intangible assets		**61,369**	62,745
Goodwill		**33,543**	35,104
Other assets		**16,841**	19,666
Deferred tax assets		**8,844**	11,393
		565,969	560,091
Total assets		**1,093,760**	1,072,880
Current liabilities			
Accounts payable and accrued liabilities and provisions	10	**155,075**	154,407
Debt due within one year	3, 6	**38,894**	44,393
		193,969	198,800
Non-current liabilities			
Long-term debt		**7,940**	9,064
Lease liabilities	3, 6	**18,802**	—
Borrowings subject to specific conditions		**23,648**	24,510
Other long-term liabilities and provisions	7	**23,645**	19,668
Deferred tax liabilities		**31,401**	33,165
		105,436	86,407
Equity			
Share capital		**254,440**	254,440
Contributed surplus		**2,044**	2,044
Other paid in capital		**13,565**	13,565
Retained earnings		**500,628**	473,246
Accumulated other comprehensive income		**21,334**	44,378
Equity attributable to equity holder of the Corporation		**792,011**	787,673
Non-controlling interest	4	**2,344**	—
Total equity		**794,355**	787,673
Total liabilities and equity		**1,093,760**	1,072,880

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE CORPORATION
CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

	Attributable to equity holder of the Corporation							
(unaudited) **(expressed in thousands of Canadian dollars)**	Share capital	Contributed surplus	Other paid in capital	Retained earnings	Foreign currency translation	Total	Non-controlling interest	Total equity
December 31, 2018	254,440	2,044	13,565	473,246	44,378	787,673	—	787,673
Business combination	—	—	—	—	—	—	2,344	2,344
Net income for the period	—	—	—	42,125	—	42,125	—	42,125
Other comprehensive loss for the period	—	—	—	(3,101)	(23,044)	(26,145)	—	(26,145)
Common share dividend	—	—	—	(11,642)	—	(11,642)	—	(11,642)
June 30, 2019	254,440	2,044	13,565	500,628	21,334	792,011	2,344	794,355
December 31, 2017	254,440	2,044	13,565	410,992	18,207	699,248	—	699,248
IFRS 9 adjustment, net of tax	—	—	—	(999)	—	(999)	—	(999)
January 1, 2018 Adjusted	254,440	2,044	13,565	409,993	18,207	698,249	—	698,249
Net income for the period	—	—	—	40,928	—	40,928	—	40,928
Other comprehensive income for the period	—	—	—	1,914	15,033	16,947	—	16,947
Common share dividend	—	—	—	(9,896)	—	(9,896)	—	(9,896)
June 30, 2018	254,440	2,044	13,565	442,939	33,240	746,228	—	746,228

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE

MAGELLAN AEROSPACE CORPORATION
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS

(unaudited) (expressed in thousands of Canadian dollars)	Notes	Three month period ended June 30 2019	 2018	Six month period ended June 30 2019	 2018
Cash flow from operating activities					
Net income		**21,716**	23,464	**42,125**	40,928
Amortization/depreciation of intangible assets, right-of-use assets and property, plant and equipment		**13,622**	10,947	**27,152**	21,543
Loss (gain) on disposal of property, plant and equipment		**38**	24	**(47)**	112
Gain on disposal of joint venture investment	4	**—**	—	**(881)**	—
Increase (decrease) in defined benefit plans		**287**	136	**133**	(393)
Accretion		**628**	248	**1,173**	510
Deferred taxes		**1,555**	1,548	**3,373**	1,715
Income on investments in joint ventures		**(111)**	(122)	**(281)**	(238)
Changes to non-cash working capital		**(12,061)**	(19,071)	**(38,975)**	(55,598)
Net cash provided by operating activities		**25,674**	17,174	**33,772**	8,579
Cash flow from investing activities					
Business combination, net of cash acquired	4	**—**	—	**(2,661)**	—
Purchase of property, plant and equipment		**(8,839)**	(5,497)	**(18,346)**	(13,063)
Proceeds from disposal of property, plant and equipment		**124**	178	**359**	199
(Increase) decrease in intangible and other assets		**(3,163)**	2,831	**(9,229)**	2,077
Change in restricted cash		**—**	2,714	**—**	—
Net cash (used in) provided by investing activities		**(11,878)**	226	**(29,877)**	(10,787)
Cash flow from financing activities					
(Decrease) increase in bank indebtedness	5	**(89)**	(8,495)	**(131)**	6,951
(Decrease) increase in debt due within one year		**(1,600)**	1,211	**(8,484)**	(5,822)
Decrease in long-term debt		**(802)**	(608)	**(1,449)**	(13,874)
Lease liability payments		**(783)**	—	**(1,684)**	—
Decrease in long-term liabilities and provisions		**(144)**	(57)	**(179)**	(131)
(Decrease) increase in borrowings subject to specific conditions, net		**(822)**	1,285	**(822)**	1,310
Common share dividend	8	**(5,821)**	(4,948)	**(11,642)**	(9,896)
Net cash used in financing activities		**(10,061)**	(11,612)	**(24,391)**	(21,462)
Increase (decrease) in cash during the period		**3,735**	5,788	**(20,496)**	(23,670)
Cash at beginning of the period		**38,463**	12,080	**63,316**	40,394
Effect of exchange rate differences		**(825)**	(406)	**(1,447)**	738
Cash at end of the period		**41,373**	17,462	**41,373**	17,462

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE

MAGELLAN AEROSPACE CORPORATION
NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
(Unaudited, expressed in thousands of dollars except share and per share data)

NOTE 1. DESCRIPTION OF BUSINESS AND NATURE OF OPERATIONS

Magellan Aerospace Corporation (the "Corporation" or "Magellan") is a publicly listed company incorporated in Ontario, Canada under the Ontario Business Corporations Act and its shares are listed on the Toronto Stock Exchange. The registered and head office of the Corporation is located at 3160 Derry Road East, Mississauga, Ontario, Canada, L4T 1A9.

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

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") and using the same accounting policies and methods as were used for the Corporation's consolidated financial statements and the notes thereto for the year ended December 31, 2018, except for the new accounting pronouncements which have been adopted as disclosed in note 3.

These unaudited condensed consolidated interim financial statements do not include all the information required for full annual financial statements and should be read in conjunction with the Corporation's annual consolidated financial statements for the year ended December 31, 2018, which are available at www.sedar.com and on the Corporation's website at www.magellan.aero.

The timely preparation of the unaudited condensed consolidated interim financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies, if any, as at the date of the financial statements and the reported amounts of revenue and expenses during the period. By their nature, estimates are subject to measurement uncertainty and changes in such estimates in future years could require a material change in the unaudited condensed consolidated interim financial statements.

These unaudited condensed consolidated interim financial statements were authorized for issuance by the Board of Directors of the Corporation on August 2, 2019.

NOTE 3. ADOPTION OF NEW STANDARDS, INTERPRETATIONS AND AMENDMENTS

The Corporation has adopted the new and amended pronouncements issued by International Financial Reporting Standards ("IFRS") and the International Financial Reporting Interpretations Committees ("IFRIC") as listed below as at January 1, 2019, in accordance with the transitional provisions outlined in the respective standards.

Leases

Effective January 1, 2019, the Corporation adopted IFRS 16, *Leases* ("IFRS 16"), replacing IAS 17, *Leases* ("IAS 17"), IFRIC 4, *Determining whether an Arrangement contains a Lease* ("IFRIC 4"), SIC-15, *Operating Leases-Incentives* and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

IFRS 16 introduced a single on-balance sheet model for lessees unless the underlying asset is of low value and the short-term lease recognition exemption is being applied. A lessee is required to recognize, on its statement of financial position, a right-of-use asset, representing its right to use the underlying leased asset, and a lease liability, representing its obligation to make lease payments. As a result of adopting IFRS 16, the Corporation recognized a $24.2 million increase to assets and liabilities, respectively, on the unaudited condensed consolidated interim statement of financial position. Subsequent to the adoption, operating costs decrease due to the removal of rent expense for leases, depreciation and amortization expense increases due to depreciation of right-of-use assets, and finance costs increase due to accretion of the lease liability. The accounting treatment for lessors remains largely the same as under IAS 17.

The Corporation adopted IFRS 16 under the modified retrospective approach and did not restate the comparatives for 2018. At transition, the Corporation applied the practical expedient available to the Corporation that allows the continuation of the lease assessments under IAS 17 and IFRIC 4 for existing contracts. Therefore, the definition of a lease under IFRS 16 was applied only to contracts entered into or changed after January 1, 2019.

For leases that were classified as operating leases under IAS 17, lease liabilities at transition have been measured at the present value of remaining lease payments, discounted at the incremental borrowing rate as at January 1, 2019. Right-of-use assets at transition have been measured at an amount equal to the corresponding lease liabilities, adjusted for any prepaid or accrued rent relating to that lease.

When applying IFRS 16 to leases previously classified as operating leases, the following practical expedients were applied:

- a single discount rate to a portfolio of leases with similar characteristics;
- used hindsight in determining the lease term where the contract contains purchase, extension, or termination options;
- relied upon our assessment of whether leases are onerous under the requirements of IAS 37, *Provisions, contingent liabilities and contingent assets* as at December 31, 2018 as an alternative to reviewing our right-of-use assets for impairment; and
- excluded short-term leases or low-value leases.

There was no significant impact for contracts in which the Corporation is the lessor.

Prior to adopting IFRS 16, the total minimum operating lease commitments as at December 31, 2018 were $37.9 million. The weighted average discount rate applied to the total lease liabilities recognized on transition was 3.82%. The difference between the total of the minimum lease payments set out in Note 21 to the 2018 annual consolidated financial statements and the total lease liabilities recognized on transition was a result of:

- the effect of discounting on the minimum lease payments;
- the exclusion of lease payments related to reasonably certain termination options that had not been exercised as at December 31, 2018; and
- the exclusion of short-term leases.

Accounting pronouncements adopted

The following pronouncements were adopted by the Corporation as of January 1, 2019 and do not have an impact on the Corporation's unaudited condensed consolidated interim financial statements. These changes are described in detail in the Corporation's 2018 consolidated financial statements.

- IFRIC Interpretation 23, *Uncertainty over Income Tax Treatments*
- Amendments to IAS 19, *Plan Amendment, Curtailment or Settlement*
- Annual Improvements to IFRS Standards 2015 – 2017: IFRS 3, *Business Combination*
- Annual Improvements to IFRS Standards 2015 – 2017: IAS 12, *Income Taxes*

NOTE 4. BUSINESS COMBINATION

In line with the Corporation's low cost sourcing strategy, an additional 26% of the issued and outstanding shares of the capital stock of Triveni Aeronautics Private Limited ("Triveni") was acquired in the first quarter of 2019 for $3,780 to obtain a 75% controlling interest.

Prior to the effective date February 28, 2019, the Corporation accounted for its previously held 49% interest in Triveni as a joint venture using the equity method with a carrying value of $5,498. As at February 28, 2019, the Corporation remeasured its previously held equity interest at fair value and recognized the resulting gain of $881 in Other in the unaudited condensed consolidated interim statement of income.

At February 28, 2019, the Corporation recognized $4,765 current assets, $5,208 non-current assets, $3,126 intangible assets and goodwill, $596 current liabilities and $2,344 non-controlling interest based on the provisional fair value of the identifiable assets and liabilities. The Corporation is in the process of obtaining information to assist in determining the fair value of the net assets acquired at the acquisition date and expects to finalize the purchase price allocation for the step acquisition during the measurement period. The net income recorded in the three and six month periods ended June 30, 2019 includes an immaterial amount attributable to the non-controlling interest.

NOTE 5. BANK INDEBTEDNESS

On September 13, 2018, the Corporation amended its credit agreement with its existing lenders. The Corporation has a multi-currency operating credit facility with a syndicate of banks, with a Canadian dollar limit of $75,000. Under the terms of the amended credit agreement, the operating credit facility expires on September 13, 2020. Extensions of the facility are subject to mutual consent of the syndicate of lenders and the Corporation. The credit agreement also includes a $75,000 uncommitted accordion provision which will provide the Corporation with the option to increase the size of the operating credit facility. As at June 30, 2019, the Corporation was debt-free under its credit facility. Bank indebtedness bears interest at the bankers' acceptance or LIBOR rates plus 1.20%. At June 30, 2019, the Corporation had letters of credit outstanding totalling $5,716 such that $69,284 was unused and available. A fixed and floating charge debenture on accounts receivable, inventories and property, plant and equipment is pledged as collateral for the operating credit facility.

NOTE 6. LEASES

Accounting policy

At inception of a contract, the Corporation assesses whether the contract is, or contains, a lease. A contract is a lease if the contract conveys the right to control the use of an identified asset. The Corporation assesses whether:

- the contract involves the use of an identified asset;
- it has the right to obtain substantially all of the economic benefits from use of the identified asset throughout the period of use; and
- it has the right to direct the use of the asset.

Lease accounting

The Corporation records a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at costs, consisting of:

- the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date; plus
- any initial direct costs incurred; and
- an estimate of costs to dismantle and remove the underlying asset or restore the site on which it is located, less
- any lease incentives received.

The right-of-use asset is typically depreciated on a straight-line basis over the lease term, unless the Corporation expects to obtain ownership of the leased asset at the end of the lease. The lease term consists of:

- the non-cancellable period of the lease;
- periods covered by options to extend the lease, where it is reasonably certain to exercise the option; and
- periods covered by options to terminate the lease, where it is reasonably certain not to exercise the option.

If the Corporation expects to obtain ownership of the leased asset at the end of the lease, the right-of-use asset will be depreciated over the underlying asset's estimated useful life. In addition, the right-of-use asset carrying amount is assessed for impairment when indicators of impairment exist, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Corporation's incremental borrowing rate. The lease liability is subsequently measured at amortized cost using the effective interest rate method.

Lease payments included in the measurement of the lease liability include:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or rate;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that is reasonably certain to be exercised, lease payments in an optional renewal period if they are reasonably certain to be exercised as an extension option, and contractual penalties for early termination of a lease unless it is reasonably certain that the lease will not be terminated early.

The lease liability is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the amount expected to be payable under a residual value guarantee, or if there is a change in the assessment of whether or not the purchase, extension or termination option will be exercised. When the lease liability is remeasured, a corresponding adjustment is made to the carrying amount of the right-of-use asset.

The lease liability is also remeasured when the underlying lease contract is amended. When there is a decrease in contract scope, the lease liability and right-of-use asset will decrease relative to this change with the difference recorded in net income prior to the remeasurement of the lease liability.

Variable lease payments

Certain leases contain provisions that result in differing lease payments over the term as a result of market rate reviews or changes in the Consumer Price Index or other similar indices. The Corporation reassesses the lease liabilities related to these leases when the index or other data is available to calculate the change in lease payments.

Certain leases require the Corporation to make payments that relate to property taxes, insurance, and other non-rental costs. These non-rental costs are typically variable and not dependent on index and rate and are not included in the calculation of the right-of-use asset or lease liability.

Lessor accounting

When the Corporation acts as a lessor, it determines at lease inception whether each lease is a finance lease or an operating lease.

In order to classify each lease as either finance or operating, the Corporation makes an overall assessment of whether the lease transfers to the leasee substantially all of the risks and rewards incidental to ownership of the underlying asset. If it does, the lease is a finance lease, if not, it is an operating lease.

Significant estimates and judgements

The Corporation determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend or terminate the lease. The lease term is estimated by considering the facts and circumstances that can create an economic incentive to exercise an extension option, or not exercise the termination option. Both qualitative and quantitative assumptions are considered when deriving the value of the economic incentive.

The Corporation makes judgments in determining whether a contract contains an identified asset. The identified asset should be physically distinct or represent substantially all of the capacity of the asset, and should provide the Corporation with the right to substantially all of the economic benefits from the use of the asset.

Judgments are made by the Corporation in determining the incremental borrowing rate used to measure the lease liability for each lease contract, including an estimate of the asset-specific security impact. The incremental borrowing rate should reflect the interest rate that the Corporation would have to pay to borrow at a similar term and with a similar security.

Certain of the Corporation's leases contain extension or renewal options. At lease commencement, the Corporation assesses whether it will be reasonably certain to exercise any of the extension options based on its expected economic return from the lease. The Corporation periodically reassesses whether it will be reasonably certain to exercise the options and accounts for any changes at the date of the reassessment.

The majority of the Corporation's leases relate to the rental of land and buildings. Below is a summary of the activity related to the Corporation's lease liabilities for the six month period ended June 30, 2019.

	Lease liabilities
At January 1, 2019	24,338
Additions	358
Interest on lease liabilities	422
Payments	(1,684)
Foreign exchange and other	(990)
At June 30, 2019	22,444
Less current portion	(3,642)
	18,802

NOTE 7. EMPLOYEE FUTURE BENEFITS

The Corporation has a number of defined benefit and defined contribution plans providing pension, other retirement and post-employment benefits to substantially all of its employees.

The employee benefit obligation reflected in the unaudited condensed consolidated interim statement of financial position is as follows:

	June 30 2019	December 31 2018
Pension Benefit Plans	16,194	11,850
Other Benefit Plan	941	976
	17,135	12,826

The discount rate assumption used in determining the obligation for pension and other benefit plans is selected based on a review of current market interest rates of high-quality, fixed rate debt securities adjusted to reflect the duration of the expected future cash outflows for pension benefit payments. As at June 30, 2019, the Corporation changed the assumed discount rate for the Canadian pension plans to 2.9% from the 3.3% and 3.8% rates used in calculating the pension obligation as at March 31, 2019 and December 31, 2018, respectively, as the market interest rates of high-quality, fixed rate debt securities decreased at the end of the period. The assumed discount rate for the U.S. pension plan decreased to 3.3% as at June 30, 2019 from 3.6% and 4.1% rates determined as at March 31, 2019 and December 31, 2018, respectively. In addition, the return on plan assets exceeded the expected return during the three and six month periods ended June 30, 2019. The change in the discount rate assumptions and the difference between the actual and expected rate of return on the plan assets resulted in an actuarial loss of $3,340 and $3,101, net of taxes of $1,156 and $1,094, respectively, recorded in other comprehensive income in the three and six month periods ended June 30, 2019.

NOTE 8. SHARE CAPITAL

Net income per share

	Three month period ended June 30		Six month period ended June 30	
	2019	2018	2019	2018
Net income	21,716	23,464	42,125	40,928
Weighted average number of shares	58,209	58,209	58,209	58,209
Basic and diluted net income per share	0.37	0.40	0.72	0.70

Dividends

On March 29, 2019 and June 28, 2019, the Corporation paid quarterly dividends on 58,209,001 common shares of $0.10 per common share, amounting to $11,642 in the aggregate.

Subsequent to June 30, 2019, the Corporation declared dividends to holders of common shares in the amount of $0.10 per common share payable on September 30, 2019, for shareholders of record at the close of business on September 16, 2019.

NOTE 9. FINANCIAL INSTRUMENTS

Fair value hierarchy

The Corporation's financial assets and liabilities recorded at fair value on the unaudited condensed consolidated interim statement of financial position have been categorized into three categories based on a fair value hierarchy. Fair value of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than the quoted prices for which all significant inputs are based on observable market data, either directly or indirectly. Level 3 valuations are based on inputs that are not based on observable market data.

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

Fair values

The Corporation has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies; however, considerable judgement is required to develop these estimates. Accordingly, these estimated fair values are not necessarily indicative of the amounts the Corporation could realize in a current market exchange. The estimated fair value amounts can be materially affected by the use of different assumptions or methodologies. The methods and assumptions used to estimate the fair value of financial instruments are described as follows:

Cash, trade and other receivables, bank indebtedness and accounts payable and accrued liabilities

Due to the short period to maturity of these instruments, the carrying values as presented in the unaudited condensed consolidated interim statement of financial positions approximate their fair values.

Foreign exchange contracts

The Corporation enters into foreign forward exchange contracts to mitigate future cash flow exposures in United States dollars and Euros. Under these contracts the Corporation is obliged to purchase specific amounts at predetermined dates and exchange rates. These contracts are matched with anticipated operational cash flows in United States dollars and Euros.

The Company had forward foreign exchange contracts outstanding as at June 30, 2019 as follows:

	Amount	Floor	Ceiling
Maturity – less than 1 year – US dollar	19,000	1.2850	1.3263

As at June 30, 2019, the fair value of the outstanding foreign exchange contracts financial liabilities was immaterial, which was categorized within Level 2 of the fair value hierarchy.

Long-term debt

The carrying amount of the Corporation's long-term debt of $10,401 would approximate its fair value as at June 30, 2019.

Borrowings subject to specific conditions

As at June 30, 2019, the Corporation has recognized $23,648 as the amount repayable to Canadian government agencies. The contributions are repayable as future royalty payments; a liability is recorded for the amounts received that will be repaid based on future estimated sales.

Collateral
As at June 30, 2019, the carrying amount of the financial assets that the Corporation has pledged as collateral for its long-term debt facilities was $43,192.

NOTE 10. SEGMENTED INFORMATION

Operating segments are defined as components of the Corporation for which separate financial information is available that is evaluated
regularly by the chief operating decision maker in allocating resources and assessing performance. The chief operating decision maker of the Corporation is the President and Chief Executive Officer. The Corporation operates substantially all of its activities in one reportable segment, Aerospace, which includes the design, development, manufacture, repair and overhaul and sale of systems and components for defence and civil aviation.

The Corporation's primary sources of revenue are as follows:

	Three month period ended June 30		Six month period ended June 30	
	2019	2018	2019	2018
Sale of goods	229,803	204,840	459,074	414,478
Services	34,279	36,381	74,892	71,368
	264,082	241,221	533,966	485,846

Timing of revenue recognition based on transfer of control is as follows:

	Three month period ended June 30		Six month period ended June 30	
	2019	2018	2019	2018
At a point of time	154,583	151,717	327,642	303,433
Over time	109,499	89,504	206,324	182,413
	264,082	241,221	533,966	485,846

Advance payments received for contracts in progress in excess of revenue recognized were recorded as contract liabilities and included in accounts payable, accrued liabilities and provisions on the unaudited condensed consolidated interim statement of financial position. As at June 30, 2019 contract liabilities were $10,529 [December 31, 2018 - $9,029].

Revenues from the Corporation's two largest customers accounted for 38.4% and 40.2% respectively of total sales for the three and six month periods ended June 30, 2019 [June 30, 2018 – two largest customers accounted for 40.4% and 41.0% respectively of total sales in the three and six month periods ended].

Geographic segments:

	Three month period ended June 30							
	2019				2018			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Revenue	96,185	83,128	84,769	264,082	77,689	83,509	80,023	241,221
Export revenue[1]	61,183	18,903	27,638	107,724	56,675	17,009	26,722	100,406

	Six month period ended June 30							
	2019				2018			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Revenue	186,886	167,947	179,133	533,966	156,345	163,085	166,416	485,846
Export revenue[1]	123,838	36,115	59,033	218,986	114,127	33,281	55,794	203,202

[1]Export revenue is attributed to countries based on the location of the customers

	June 30, 2019				December 31, 2018			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Property, plant and equipment, right-of-use assets, intangible assets and goodwill	174,731	191,586	171,780	538,097	189,294	185,032	152,401	526,727

NOTE 11. TAXATION

The Corporation's tax expense is calculated by using the rates applicable in each of the tax jurisdictions that the Corporation operates in, adjusted for the main permanent differences identified. The effective tax rate for the three and six month periods ended June 30, 2019 was 21.8% and 21.5% respectively [21.2% and 21.6% respectively for the three and six month periods ended June 30, 2018]. The difference between the effective tax rate and the standard tax rate is primarily attributable to the change in mix of income across the different jurisdictions in which the Corporation operates.

NOTE 12. MANAGEMENT OF CAPITAL

The Corporation's objective is to maintain a capital base sufficient to maintain investor, creditor and market confidence and to sustain future development of the business. Management defines capital as the Corporation's shareholders' equity and interest bearing debt, including the debt and equity components of the convertible debentures.

Total managed capital as at June 30, 2019 of $835,203 is comprised of shareholders' equity attributable to equity holders of the Corporation of $792,011 and interest-bearing debt of $43,192.

The Corporation manages its capital structure and makes adjustments to it in light of economic conditions, the risk characteristics of the underlying assets and the Corporation's working capital requirements. In order to maintain or adjust its capital structure, the Corporation, upon approval from its Board of Directors, may issue or repay long-term debt, issue shares, repurchase shares through the normal course issuer bid, pay dividends or undertake other activities as deemed appropriate under the specific circumstances. The Board of Directors reviews and approves any material transactions out of the ordinary course of business, including proposals on acquisitions or other major investments or divestitures, as well as capital and operating budgets. There were no changes in the Corporation's approach to capital management during the period.

NOTE 13. CONTINGENT LIABILITES AND COMMITMENTS

In the ordinary course of business activities, the Corporation may be contingently liable for litigation and claims with, among others, customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required. Although, it is not possible to accurately estimate the extent of the potential costs and losses, if any, management believes, but can provide no assurance, that the ultimate resolution of such contingencies would not have a material adverse effect on the financial position of the Corporation.

At June 30, 2019 capital commitments in respect of the purchase of property, plant and equipment totalled $13,085, all of which had been ordered. There were no other material capital commitments at the end of the period.