



CONSOLIDATED FINANCIAL STATEMENTS / MANAGEMENT'S DISCUSSION AND ANALYSIS

Third quarter ended December 31, 2022



INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Third quarter ended December 31, 2022

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DISCLOSURE OF NON-REVIEW OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE QUARTERS ENDED DECEMBER 31, 2022 AND 2021

Pursuant to National Instrument 51-102, Part 4, subsection 4.3(3)(a) issued by the Canadian Securities Administrators, if the external auditors have not performed a review of the financial statements, the financial statements must be accompanied by a notice indicating that they have not been reviewed by the external auditors.

The accompanying unaudited interim condensed consolidated financial statements of the Corporation for the quarters ended December 31, 2022 and 2021 have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting*, and are the responsibility of the Corporation's management.

The Corporation's external auditors, Ernst & Young LLP, have not performed a review of these interim condensed consolidated financial statements in accordance with the standards established by Chartered Professional Accountants Canada for a review of financial statements by the external auditors of an entity.

February 7, 2023

CONSOLIDATED BALANCE SHEETS

(In thousands of Canadian dollars) (Unaudited)

As at	Notes	December 31, 2022	March 31, 2022
ASSETS	10		
Current assets			
Cash		\$ 90,837	\$ 86,692
Accounts receivable		103,635	105,389
Income tax receivable		2,713	1,108
Inventories		247,001	200,342
Derivative financial instruments	9	310	5,500
Other current assets		18,095	16,419
		462,591	415,450
Property, plant and equipment, net		204,986	208,838
Finite-life intangible assets, net		49,756	47,320
Derivative financial instruments	9	501	14,329
Deferred income tax assets		10,948	6,557
Goodwill		110,466	108,200
Other long-term assets		12,402	12,664
Total assets		\$ 851,650	\$ 813,358
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		\$ 111,756	\$ 114,508
Provisions		17,102	21,925
Customer advances and progress billings		56,264	29,875
Income tax payable		462	826
Derivative financial instruments	9	7,068	1,852
Current portion of long-term debt	10	12,170	10,835
		204,822	179,821
Long-term debt	10	229,195	225,691
Provisions		15,486	14,828
Derivative financial instruments	9	5,732	830
Deferred income tax liabilities		9,923	8,567
Other liabilities		5,331	6,339
		470,489	436,076
Shareholders' equity			
Issued capital	11	82,854	82,189
Contributed surplus		6,410	5,767
Accumulated other comprehensive income	12	5,614	6,865
Retained earnings		286,283	282,461
		381,161	377,282
Total liabilities and shareholders' equity		\$ 851,650	\$ 813,358

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

CONSOLIDATED STATEMENTS OF INCOME

(In thousands of Canadian dollars, except per share data) (Unaudited)

	Notes	Three months ended December 31,		Nine months ended December 31,	
		2022	2021	2022	2021
Sales	3	\$ 140,875	\$ 131,147	\$ 387,644	\$ 388,628
Cost of sales	4, 5	120,959	109,800	336,850	323,424
Gross profit		19,916	21,347	50,794	65,204
Selling and administrative expenses	4, 5	14,805	10,802	35,694	31,909
Non-recurring items	6	—	—	(1,219)	—
Operating income		5,111	10,545	16,319	33,295
Net financial expenses	7	2,796	2,107	6,400	5,913
Income before income tax expense		2,315	8,438	9,919	27,382
Income tax expense		542	1,970	2,382	6,701
Net income		\$ 1,773	\$ 6,468	\$ 7,537	\$ 20,681
Attributable to:					
Equity holders of the parent		1,773	6,468	7,537	21,066
Non-controlling interest		—	—	—	(385)
		\$ 1,773	\$ 6,468	\$ 7,537	\$ 20,681
Earnings per share – basic and diluted	8	\$ 0.05	\$ 0.18	\$ 0.22	\$ 0.58

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands of Canadian dollars) (Unaudited)

		Three months ended December 31,		Nine months ended December 31,	
	Notes	2022	2021	2022	2021
	12				
Other comprehensive income (loss) :					
Items that may be reclassified to net income					
Gains (losses) arising from conversion of the financial statements of foreign operations		\$ 14,654	\$ (2,134)	\$ 14,659	\$ (1,398)
Cash flow hedges:					
Net gains (losses) on valuation of derivative financial instruments		7,551	1,670	(21,702)	(3,752)
Net losses (gains) on derivative financial instruments transferred to net income		3,888	(794)	5,354	(3,466)
Deferred income taxes		(3,020)	(231)	4,317	1,904
		8,419	645	(12,031)	(5,314)
Gains (losses) on hedges of net investments in foreign operations		766	2,232	(4,463)	1,926
Deferred income taxes		(105)	(293)	584	(257)
		661	1,939	(3,879)	1,669
Items that are never reclassified to net income					
Defined benefit pension plans:					
Gains (losses) from remeasurement		1,144	3	(109)	1,857
Deferred income taxes		(302)	(1)	28	(491)
		842	2	(81)	1,366
Other comprehensive income (loss)		\$ 24,576	\$ 452	\$ (1,332)	\$ (3,677)
Comprehensive income					
Net income		1,773	6,468	7,537	20,681
Other comprehensive income (loss)		24,576	452	(1,332)	(3,677)
Comprehensive income		\$ 26,349	\$ 6,920	\$ 6,205	\$ 17,004
Attributable to:					
Equity holders of the parent		26,349	6,920	6,205	17,389
Non-controlling interest		—	—	—	(385)
		\$ 26,349	\$ 6,920	\$ 6,205	\$ 17,004

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(In thousands of Canadian dollars) (Unaudited)

	Notes	Issued capital	Contributed surplus	Accumulated other comprehensive income (loss)	Retained earnings	Equity attributable to the equity holders of the parent	Non-Controlling interest	Shareholders' equity
Balance as at March 31, 2022		\$ 82,189	\$ 5,767	\$ 6,865	\$282,461	\$ 377,282	\$ —	\$ 377,282
Common shares issued under the stock option plan	11	1,437	(334)	—	—	1,103	—	1,103
Repurchase and cancellation of common shares	11	(772)	—	—	(3,634)	(4,406)	—	(4,406)
Stock-based compensation expense	11	—	977	—	—	977	—	977
Net income		—	—	—	7,537	7,537	—	7,537
Other comprehensive loss	12	—	—	(1,251)	(81)	(1,332)	—	(1,332)
Balance as at December 31, 2022		\$ 82,854	\$ 6,410	\$ 5,614	\$286,283	\$ 381,161	\$ —	\$ 381,161

	Notes	Issued capital	Contributed surplus	Accumulated other comprehensive income	Retained earnings	Equity attributable to the equity holders of the parent	Non-Controlling interest	Shareholders' equity
Balance as at March 31, 2021		\$ 86,222	\$ 5,126	\$ 16,279	\$282,831	\$ 390,458	\$1,274	\$ 391,732
Common shares issued under the stock option plan	11	1,961	(515)	—	—	1,446	—	1,446
Repurchase and cancellation of common shares	11	(5,452)	—	—	(33,169)	(38,621)	—	(38,621)
Stock-based compensation expense	11	—	878	—	—	878	—	878
Purchase of minority interests		—	—	—	(11)	(11)	(889)	(900)
Net income (loss)		—	—	—	21,066	21,066	(385)	20,681
Other comprehensive (loss) income	12	—	—	(5,043)	1,366	(3,677)	—	(3,677)
Balance as at December 31, 2021		\$ 82,731	\$ 5,489	\$ 11,236	\$272,083	\$ 371,539	\$ —	\$ 371,539

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands of Canadian dollars) (Unaudited)

		Three months ended December 31,		Nine months ended December 31,	
	Notes	2022	2021	2022	2021
Cash provided by (used for):					
Operating activities					
Net income		\$ 1,773	\$ 6,468	\$ 7,537	\$ 20,681
Items not requiring an outlay of cash:					
Amortization expense	5	9,018	9,149	26,671	27,605
Deferred income taxes		169	672	3,241	1,853
Gains on sale of property, plant and equipment		—	(910)	—	(910)
Net non-cash financial expenses	7	1,596	1,352	3,010	3,731
Stock-based compensation expense	11	324	289	977	878
Cash flows from operations		12,880	17,020	41,436	53,838
Net change in non-cash items	13	(7,643)	478	(15,894)	(688)
Cash flows related to operating activities		\$ 5,237	\$ 17,498	\$ 25,542	\$ 53,150
Investing activities					
Net additions to property, plant and equipment		(2,354)	(5,197)	(11,665)	(12,907)
Net change in finite-life intangible assets		(1,090)	836	(6,855)	(1,511)
Proceeds from a business divestiture	6	3,116	—	3,116	2,041
Purchase of minority interest		—	(900)	—	(900)
Proceeds of disposal of property, plant and equipment		—	319	—	319
Cash flows related to investing activities		\$ (328)	\$ (4,942)	\$ (15,404)	\$ (12,958)
Financing activities					
Proceeds from long-term debt		—	1,097	6,239	3,059
Repayment of long-term debt		(4,538)	(4,904)	(9,634)	(13,995)
Increase in deferred financing costs		—	—	(245)	(555)
Repurchase and cancellation of shares	11	(1,568)	(25,136)	(4,406)	(38,621)
Issuance of common shares under the stock option plan		—	397	1,103	1,446
Cash flows related to financing activities		\$ (6,106)	\$ (28,546)	\$ (6,943)	\$ (48,666)
Effect of changes in exchange rates on cash		341	(391)	950	(160)
Change in cash during the periods		(856)	(16,381)	4,145	(8,634)
Cash at beginning of periods		91,693	103,217	86,692	95,470
Cash at end of periods		\$ 90,837	\$ 86,836	\$ 90,837	\$ 86,836
Interest and income taxes reflected in operating activities:					
Interest paid		\$ 1,964	\$ 1,860	\$ 4,835	\$ 5,526
Interest received		\$ 764	\$ 129	\$ 1,445	\$ 423
Income taxes paid		\$ 1,624	\$ 3,816	\$ 2,889	\$ 6,213

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the quarters and nine-month periods ended December 31, 2022 and 2021
(In thousands of Canadian dollars, except per share data) (Unaudited)

NOTE 1. NATURE OF ACTIVITIES AND CORPORATE INFORMATION

Héroux-Devtek Inc. is incorporated under the laws of Québec. Its head office is domiciled at Complexe St-Charles, 1111 St-Charles Street West, suite 600, West Tower, Longueuil (Québec), Canada. Héroux-Devtek Inc. and its subsidiaries ("Héroux-Devtek" or the "Corporation") specialize in the design, development, manufacture, repair and overhaul of aircraft landing gear, hydraulic and electromechanical flight control actuators, custom ball screws and fracture-critical components.

The Corporation only operates in one reporting segment, which is the Aerospace segment.

The Corporation's common shares are traded on the Toronto Stock Exchange under the symbol "HRX".

NOTE 2. BASIS OF PREPARATION

The interim condensed consolidated financial statements for the quarter ended December 31, 2022, were prepared in accordance with IAS 34, *Interim Financial Reporting*, therefore certain information and disclosures have been omitted or condensed. The same accounting policies and methods of computation were followed in the preparation of these interim condensed consolidated financial statements as were followed in the preparation of the most recent annual audited consolidated financial statements. Accordingly, these interim condensed consolidated financial statements should be read together with the annual audited consolidated financial statements and notes thereto included in the Corporation's Annual Report for the fiscal year ended March 31, 2022.

These interim condensed consolidated financial statements were approved for issue by the Board of Directors of the Corporation on February 7, 2023.

NOTE 3. REVENUE FROM CONTRACTS WITH CUSTOMERS

The disaggregation of the Corporation's revenue from contracts with customers was as follows :

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Geographic markets				
Canada	\$ 8,817	\$ 8,148	\$ 23,560	\$ 25,413
United States of America	84,189	73,258	241,118	224,981
United Kingdom	9,370	7,769	26,014	29,737
Spain	7,867	8,621	20,444	27,932
Rest of Europe	19,328	21,781	47,486	50,253
Other countries	11,304	11,570	29,022	30,312
	\$ 140,875	\$ 131,147	\$ 387,644	\$ 388,628
Sectors				
Civil	\$ 45,108	\$ 36,501	\$ 121,780	\$ 111,427
Defence	95,767	94,646	265,864	277,201
	\$ 140,875	\$ 131,147	\$ 387,644	\$ 388,628

Geographic market is based on the customer's location.

NOTE 4. GOVERNMENT ASSISTANCE

Government assistance was deducted from the cost of related assets or recognized as a reduction of expenses as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Finite-life intangible assets	\$ 267	\$ —	\$ 670	\$ 566
Property, plant and equipment	\$ 43	\$ —	\$ 57	\$ —
Cost of sales and selling and administrative expenses	\$ 1,798	\$ 2,625	\$ 4,375	\$ 10,944

Government assistance includes mainly research and development tax credits, other credits and grants, including the Canadian Emergency Wage Subsidy for the three and nine-month periods ended December 31, 2021.

NOTE 5. COST OF SALES, SELLING AND ADMINISTRATIVE EXPENSES

The main components of these expenses were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Raw materials and purchased parts	\$ 53,220	\$ 45,776	\$ 145,055	\$ 141,648
Employee costs	49,575	44,798	139,491	134,149
Amortization of property, plant and equipment and finite-life intangible assets	9,018	9,149	26,671	27,605
Others	23,951	20,879	61,327	51,931
	\$ 135,764	\$ 120,602	\$ 372,544	\$ 355,333
Including:				
Foreign exchange losses (gains) upon conversion of net monetary items	\$ 1,595	\$ (64)	\$ 785	\$ (1,077)
Amortization of customer relationships	\$ 954	\$ 1,187	\$ 2,793	\$ 3,316

NOTE 6. NON-RECURRING ITEMS

The commercial objectives included in the agreement for the sale of Bolton operations to Ontic Engineering & Manufacturing UK Limited that occurred on May 4, 2021, were achieved in September 2022, resulting in a net non-recurring gain of \$1,219 in the second quarter and nine-month period, of which \$718 has been collected to date.

The \$3,116 proceeds of divestiture included in the consolidated statement of cash flows also include the collection of the \$2,398 balance of sale during the nine-month period.

NOTE 7. NET FINANCIAL EXPENSES

Net financial expenses comprise the following:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Interest accretion on governmental authorities loans	\$ 859	\$ 679	\$ 2,318	\$ 2,277
Interest on defined benefit obligations	17	24	56	72
Interest on leases	199	252	609	773
Amortization of deferred financing costs	118	124	358	430
Other accretion and adjustments	403	273	(331)	179
Net non-cash financial expenses	\$ 1,596	\$ 1,352	\$ 3,010	\$ 3,731
Interest on long-term debt	\$ 1,964	\$ 884	\$ 4,835	\$ 2,605
Interest income on cash	(764)	(129)	(1,445)	(423)
	\$ 2,796	\$ 2,107	\$ 6,400	\$ 5,913

NOTE 8. EARNINGS PER SHARE

The following table sets forth the elements used to compute basic and diluted earnings per share:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Weighted-average number of common shares outstanding	34,373,578	35,440,464	34,444,035	36,124,313
Dilutive effect of stock options	76,855	300,489	101,628	280,245
Weighted-average number of common diluted shares outstanding	34,450,433	35,740,953	34,545,663	36,404,558
Options excluded from diluted earnings per share calculation	1,288,000	—	1,288,000	189,000

NOTE 9. DERIVATIVE FINANCIAL INSTRUMENTS

Forward foreign exchange contracts

As at December 31, 2022, the Corporation had sale forward foreign exchange contracts outstanding for a notional amount of \$425,328 (\$341,604 at March 31, 2022) denominated in USD, EUR and GBP. This amount includes contracts with nominal value of US\$264,550 (US\$219,500 at March 31, 2022) convertible into Canadian dollars at an average rate of 1.3110 (1.2888 at March 31, 2022). These contracts mature at various dates between January 2023 and June 2028, with the majority maturing this fiscal year and the next.

Cross-currency interest rate swaps

As at March 31, 2022, the Corporation had three cross-currency interest rate swap agreements exchanging CAD and USD-denominated debt to EUR for a total notional amount of €90,468 in order to mitigate foreign exchange and interest rate risks. These agreements matured between May 2022 and September 2028, and mainly bore interest at a weighted average fixed rate of 2.4%.

During the quarter ended June 30, 2022, one of these swaps expired and the other two were unwound for cash proceeds totaling \$11,260.

Equity swap agreement

As at December 31, 2022, the Corporation had entered into an equity swap agreement fixing 400,000 common shares of the Corporation at a price of \$13.39 (300,000 common shares at a price of \$13.52 as at March 31, 2022). This agreement manages the Corporation's exposure to fluctuations of its share price and resulting effect on the value of outstanding Performance Share Units and Deferred Share Units and expires in June 2023 (June 2023 as at March 31, 2022).

NOTE 10. LONG-TERM DEBT

As at	December 31, 2022	March 31, 2022
Senior Secured Syndicated Revolving Credit Facility ("Revolving Facility")	\$ 63,733	\$ 58,821
Governmental authorities loans	88,626	84,508
Unsecured Subordinated Term Loan Facility ("Term Loan")	75,000	75,000
Lease liabilities	16,193	20,497
Deferred financing costs, net	(2,187)	(2,300)
	\$ 241,365	\$ 236,526
Less: current portion	12,170	10,835
Long-term debt	\$ 229,195	\$ 225,691

Revolving Facility

In May 2022, the Corporation reached an agreement to extend its \$250-million Revolving Facility to a new maturity of June 2027 (as at March 31, 2022 - June 2026). The other terms and conditions remain relatively unchanged.

The Revolving Facility bears interest at SOFR + 1.1% representing an effective rate of 5.2% (Libor + 1.0% representing 1.3% as at March 31, 2022) and is secured by essentially all assets of the Corporation and its subsidiaries.

Term Loan

The Term Loan Facility is fully drawn, bears interest at 5.0%, (5.0% as at March 31, 2022) and matures in September 2028.

NOTE 11. ISSUED CAPITAL

A. Share capital

Capital stock varied as follows:

	Three months ended December 31, 2022		Nine months ended December 31, 2022	
	Number	Issued capital	Number	Issued capital
Opening balance	34,391,116	\$ 83,146	34,486,776	\$ 82,189
Issued for cash on exercise of stock options	—	—	103,000	1,437
Repurchase and cancellation	(120,800)	(292)	(319,460)	(772)
Closing balance	34,270,316	\$ 82,854	34,270,316	\$ 82,854

On May 19, 2022, the Corporation announced a Normal Course Issuer Bid ("NCIB") for the purchase for cancellation of up to 1,896,079 common shares on the open market through the TSX or alternative trading facilities. The NCIB began on May 25, 2022, and will end on May 24, 2023, or on such earlier date when the Company has either acquired the maximum number of common shares allowable under the NCIB or decided not to make any further purchases under it.

As at December 31, 2022, the Company has purchased and cancelled 319,460 common shares for a cash consideration of \$4,406, representing a weighted average price of \$13.79 per share. The \$3,634 excess of purchase price over the carrying value was charged to retained earnings.

B. Stock option plan

For the quarters ended December 31, variances in stock options outstanding and related compensation expense were as follows:

	2022		2021	
	Number of stock options	Exercise price ⁽¹⁾	Number of stock options	Exercise price ⁽¹⁾
Opening balance	1,645,500	\$14.60	1,551,750	\$14.13
Exercised	—	—	(35,000)	11.34
Cancelled / forfeited	(10,000)	15.42	(8,000)	17.45
Closing balance	1,635,500	\$14.59	1,508,750	\$14.18
Stock-based compensation expense		\$ 324		\$ 289

⁽¹⁾ Weighted average exercise price

For the nine months ended December 31, variances in stock options outstanding and related compensation expense were as follows:

	2022		2021	
	Number of stock options	Exercise price ⁽¹⁾	Number of stock options	Exercise price ⁽¹⁾
Opening balance	1,503,750	\$14.19	1,449,095	\$13.48
Granted	247,000	15.42	197,000	17.45
Exercised	(103,000)	10.71	(129,345)	11.18
Expired	(2,250)	10.71	—	—
Cancelled / forfeited	(10,000)	15.42	(8,000)	17.45
Closing balance	1,635,500	\$14.59	1,508,750	\$14.18
Stock-based compensation expense		\$ 977		\$ 878

⁽¹⁾ Weighted average exercise price

2,808,257 common share are reserved for issuance under the plan, of which 2,122,662 had not been issued yet as at December 31, 2022 (2,225,662 at March 31, 2022).

C. Deferred Share Unit ("DSU") and Performance Share Unit ("PSU") plans

Movements in outstanding DSUs and PSUs and related expenses were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
DSUs				
<i>In number of DSUs</i>				
Opening balance	254,830	199,471	199,471	192,108
Issued	—	—	55,359	31,676
Settled	—	—	—	(24,313)
Closing balance of DSUs outstanding	254,830	199,471	254,830	199,471
DSU expense (income) for the periods	\$ 298	\$ 120	\$ (185)	\$ 658
Fair value of vested outstanding DSUs, end of periods	\$ 3,148	\$ 3,229	\$ 3,148	\$ 3,229

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
PSUs				
<i>In number of PSUs</i>				
Opening balance	404,050	380,600	285,350	300,150
Issued	3,750	2,000	129,300	88,150
Settled	(98,200)	(72,050)	(98,200)	(72,050)
Cancelled/Forfeited	(4,750)	(10,450)	(11,600)	(16,150)
Closing balance of PSUs outstanding	304,850	300,100	304,850	300,100
PSU expense (income) for the periods	\$ 553	\$ 381	\$ 2	\$ 1,164
Fair value of vested outstanding PSUs, end of periods	\$ 2,798	\$ 4,004	\$ 2,798	\$ 4,004

NOTE 12. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Changes in accumulated other comprehensive income (loss) were as follows:

	Exchange differences on conversion of foreign operations	Cash flow hedges	Hedge of net investments in foreign operations	Total
Balance as at September 30, 2022	\$ 3,010	\$ (15,813)	\$ (5,317)	\$ (18,120)
Other comprehensive income	14,654	8,419	661	23,734
Balance as at December 31, 2022	\$ 17,664	\$ (7,394)	\$ (4,656)	\$ 5,614
Balance as at March 31, 2022	\$ 3,005	\$ 4,637	\$ (777)	\$ 6,865
Other comprehensive income (loss)	14,659	(12,031)	(3,879)	(1,251)
Balance as at December 31, 2022	\$ 17,664	\$ (7,394)	\$ (4,656)	\$ 5,614

	Exchange differences on conversion of foreign operations	Cash flow hedges	Hedge of net investments in foreign operations	Total
Balance as at September 30, 2021	\$ 14,800	\$ 2,572	\$ (6,586)	\$ 10,786
Other comprehensive income (loss)	(2,134)	645	1,939	450
Balance as at December 31, 2021	\$ 12,666	\$ 3,217	\$ (4,647)	\$ 11,236
Balance as at March 31, 2021	\$ 14,064	\$ 8,531	\$ (6,316)	\$ 16,279
Other comprehensive income (loss)	(1,398)	(5,314)	1,669	(5,043)
Balance as at December 31, 2021	\$ 12,666	\$ 3,217	\$ (4,647)	\$ 11,236

NOTE 13. NET CHANGE IN NON-CASH ITEMS

The net change in non-cash items were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Accounts receivable	\$ (18)	\$ (1,871)	\$ 4,177	\$ 12,185
Inventories	(11,513)	1,585	(40,915)	2,060
Other assets and derivatives (note 9)	(2,149)	3,414	7,007	412
Accounts payable and accrued liabilities	(598)	4,530	(1,127)	(3,192)
Provisions	(2,559)	(3,947)	(4,624)	(6,894)
Customer advances and progress billings	10,003	(731)	25,148	(2,841)
Other Liabilities	(809)	(2,502)	(5,560)	(2,418)
	\$ (7,643)	\$ 478	\$ (15,894)	\$ (688)



MANAGEMENT'S DISCUSSION AND ANALYSIS

Third quarter ended December 31, 2022

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OVERVIEW

The purpose of this management discussion and analysis (“MD&A”) is to provide the reader with an overview of how the financial position of Héroux-Devtek Inc. and its subsidiaries (“Héroux-Devtek”, the “Corporation” or “Management”) evolved between March 31, 2022, and December 31, 2022. It also compares the operating results and cash flows for the quarter and nine-month periods ended December 31, 2022, to those of the same periods of the prior fiscal year.

This MD&A is based on the unaudited interim condensed consolidated financial statements for the quarter ended December 31, 2022, and should be read in conjunction with them as well as with the audited consolidated financial statements and MD&A for the fiscal year ended March 31, 2022, all of which are available on the Corporation’s website at www.herouxdevtek.com and on SEDAR at www.sedar.com. All amounts in this MD&A are in thousands of Canadian dollars unless otherwise indicated. This MD&A was approved by the Audit Committee and Board of Directors of the Corporation on February 7, 2023.

IFRS and non-IFRS financial measures

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

Materiality for disclosures

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

FORWARD-LOOKING STATEMENTS

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

They may be impacted by factors including, but not limited to: the effect of the COVID-19 pandemic on Héroux-Devtek’s operations, customers, supply chain, the aerospace industry and the economy in general; the impact of other worldwide geopolitical and general economic conditions; the war in Ukraine; industry conditions including changes in laws and regulations; increased competition; the lack of availability of qualified personnel or management; availability of commodities and fluctuations in commodity prices; financial and operational performance of suppliers and customers; foreign exchange or interest rate fluctuations; and the impact of accounting policies issued by international standard setters. For further details, please see the Risk Management section of the Corporation’s MD&A for the fiscal year ended March 31, 2022. Readers are cautioned that the foregoing list of factors that may affect future growth, results and performance is not exhaustive, and undue reliance should not be placed on forward-looking statements.

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

HIGHLIGHTS

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Sales	\$ 140,875	\$ 131,147	\$ 387,644	\$ 388,628
Operating income	5,111	10,545	16,319	33,295
Adjusted operating income ⁽¹⁾	5,111	10,545	15,100	33,295
Adjusted EBITDA ⁽¹⁾	14,129	19,694	41,771	60,900
Net income	1,773	6,468	7,537	20,681
Adjusted net income ⁽¹⁾	1,773	6,468	6,318	20,681
Cash flows related to operating activities	5,237	17,498	25,542	53,150
Free cash flow ⁽¹⁾	1,793	13,456	7,022	39,051
<i>In dollars per share</i>				
Earnings per share - basic and diluted	\$ 0.05	\$ 0.18	\$ 0.22	\$ 0.58
Adjusted EPS ⁽¹⁾	0.05	0.18	0.18	0.58

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

Operating Environment

Héroux-Devtek's throughput continued to improve compared to the second and first quarter, with sales reaching \$140.9 million compared to \$132.7 million and \$114.1 million respectively. However, the positive impact of this improvement on profitability was more than offset by the continued effect of supply chain disruptions and inflation on production costs. These factors, combined with the negative impact of foreign exchange, resulted in a decrease in operating income compared to the previous quarter and last fiscal year.

The operating environment remains volatile and several factors are still rendering the consistent generation of throughput challenging:

- Lead times for the procurement of raw material continue to increase and Russia's invasion of Ukraine limits the supply of certain material;
- Inflation continues to be high and central banks are responding by raising base interest rates, therefore increasing financing costs and putting pressure on financially fragile companies; and,
- Workforce availability remains a challenge as the tight labour market and COVID-19-related absenteeism continue to impact both Héroux-Devtek and its supply chain.

The Corporation's order book has further increased, reaching \$870 million, bolstered by both civil and defence orders. Héroux-Devtek's teams are dedicated to stabilizing the production system in order to increase throughput, profitability and to deliver on that backlog.

Events of the Quarter

- The Corporation generated consolidated sales of \$140.9 million, compared to \$131.1 million a year earlier, due mainly to higher deliveries for large commercial and business jet programs.
- Operating income decreased to \$5.1 million from \$10.5 million last fiscal year, and Adjusted EBITDA decreased to \$14.1 million, or 10.0% of sales compared to \$19.7 million or 15.0% last year. The decrease in profitability is mainly the result of inflation and production system inefficiencies driven by the challenging environment described above and a less favourable product mix, while last year's COVID-19 disruptions were partly compensated for by government relief measures bearing a positive impact of 1.4% of sales (none this year).
- In November 2022, the Corporation announced a contract with Embraer to design, develop and manufacture the main deck cargo door actuation system for the E190F and E195F Freighter conversion program. The agreement will be fulfilled by Héroux-Devtek's team in Spain and includes the delivery of spare parts and aftermarket services for the life of the program.

OPERATING RESULTS

	Three months ended December 31,			Nine months ended December 31,		
	2022	2021	Variance	2022	2021	Variance
Sales	\$ 140,875	\$ 131,147	\$ 9,728	\$ 387,644	\$ 388,628	\$ (984)
Gross profit	19,916	21,347	(1,431)	50,794	65,204	(14,410)
Selling and administrative expenses	14,805	10,802	4,003	35,694	31,909	3,785
Adjusted operating income ⁽¹⁾	5,111	10,545	(5,434)	15,100	33,295	(18,195)
Non-recurring items	—	—	—	(1,219)	—	(1,219)
Operating income	5,111	10,545	(5,434)	16,319	33,295	(16,976)
Net financial expenses	2,796	2,107	689	6,400	5,913	487
Income tax expense	542	1,970	(1,428)	2,382	6,701	(4,319)
Net income	\$ 1,773	\$ 6,468	\$ (4,695)	\$ 7,537	\$ 20,681	\$ (13,144)
Adjusted net income ⁽¹⁾	\$ 1,773	\$ 6,468	\$ (4,695)	\$ 6,318	\$ 20,681	\$ (14,363)
<i>As a percentage of sales</i>						
Gross profit	14.1%	16.3%	-220 bps	13.1%	16.8%	-370 bps
Selling and administrative expenses	10.5%	8.2%	230 bps	9.2%	8.2%	100 bps
Operating income	3.6%	8.0%	-440 bps	4.2%	8.6%	-440 bps
Adjusted operating income ⁽¹⁾	3.6%	8.0%	-440 bps	3.9%	8.6%	-470 bps
<i>In dollars per share</i>						
Earnings per share - basic and diluted	\$ 0.05	\$ 0.18	\$ (0.13)	\$ 0.22	\$ 0.58	\$ (0.36)
Adjusted EPS ⁽¹⁾	\$ 0.05	\$ 0.18	\$ (0.13)	\$ 0.18	\$ 0.58	\$ (0.40)

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

Sales

Sales by sector were as follows:

	Three months ended December 31,				
	2022	2021	FX impact	Net variance	
Defence ⁽¹⁾	\$ 95,767	\$ 94,646	\$ 2,522	\$ (1,401)	(1.5)%
Civil	45,108	36,501	1,152	7,455	20.4 %
Total	\$ 140,875	\$ 131,147	\$ 3,674	\$ 6,054	4.6 %

	Nine months ended December 31,				
	2022	2021	FX impact	Net variance	
Defence ⁽¹⁾	\$ 265,864	\$ 277,201	\$ 2,174	\$ (13,511)	(4.9)%
Civil	121,780	111,427	996	9,357	8.4 %
Total	\$ 387,644	\$ 388,628	\$ 3,170	\$ (4,154)	(1.1)%

⁽¹⁾ Includes defence sales to civil customers and governments

The following analysis excludes the impact of foreign exchange described above:

Defence

While defence sales were relatively stable over the three-month period when compared to last fiscal year, the challenges of the current operating environment drove a 4.9% decrease over the nine-month period that was partly offset by the ramp-up of deliveries for the Boeing F-18 program.

Civil

The \$7.5 million and \$9.4 million respective increases in civil sales for the quarter and nine-month periods compared to last year were mainly driven by an increase in deliveries for the Boeing 777, Embraer Praetor and Falcon 6X programs.

Gross Profit

Gross profit for the quarter and the nine-month period decreased to 14.1% and 13.1% of sales, from 16.3% and 16.8% of sales respectively last year, mainly due to:

- Inefficiencies resulting from the production system disruptions mentioned above;
- The effect of inflation, more specifically on workshop supplies and utilities; and,
- A less favourable product mix.

During the quarter and nine-month period ended December 31, 2021, Covid-related disruptions were partly compensated for by government relief measures bearing respective 1.4% and 1.7% favorable impacts on gross profit (none this year).

Selling and Administrative Expenses

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Selling and Administrative Expenses	\$ 14,805	\$ 10,802	\$ 35,694	\$ 31,909
Less: Net losses (gains) on conversion of net monetary items	1,595	(64)	785	(1,077)
Selling and Administrative expenses excluding conversion of monetary items	\$ 13,210	\$ 10,866	\$ 34,909	\$ 32,986
<i>As a percentage of sales</i>	9.4%	8.3%	9.0%	8.5%

When excluding the effect of the conversion of net monetary items, selling and administrative expenses for the quarter and nine-month period ended December 31, 2022, increased to 9.4% and 9.0% of sales compared to 8.3% and 8.5% in the previous fiscal year due to higher employee-related costs and the effect of share price fluctuations on stock-based compensation expenses during the quarter.

Non-recurring items

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Achievement of commercial objective - sale of Bolton operations	\$ —	\$ —	\$ (1,219)	\$ —
Non-recurring items in operating income	\$ —	\$ —	\$ (1,219)	\$ —

The commercial objectives included in the agreement for the sale of Bolton operations to Ontic Engineering & Manufacturing UK Limited that occurred on May 4, 2021, were achieved in September 2022. This resulted in a net non-recurring gain of \$1.2 million in the second quarter and nine-month period.

Operating Income

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Operating income	\$ 5,111	\$ 10,545	\$ 16,319	\$ 33,295
Non-recurring items	—	—	(1,219)	—
Adjusted operating income	\$ 5,111	\$ 10,545	\$ 15,100	\$ 33,295
<i>As a percentage of sales</i>				
Operating income	3.6%	8.0%	4.2%	8.6%
Adjusted operating income	3.6%	8.0%	3.9%	8.6%

As a percentage of sales, when compared to the same periods last fiscal year, operating income decreased this quarter and nine-month period as a result of the factors described above.

Year-over-year, foreign exchange had a negative impact of 0.6% on operating income for the quarter, while its effect was negligible on the nine-month period.

Net Financial Expenses

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Interest accretion on governmental authorities loans	\$ 859	\$ 679	\$ 2,318	\$ 2,277
Interest on defined benefit obligations	17	24	56	72
Interest on leases	199	252	609	773
Amortization of deferred financing costs	118	124	358	430
Other accretion and adjustments	403	273	(331)	179
Net non-cash financial expenses	\$ 1,596	\$ 1,352	\$ 3,010	\$ 3,731
Interest on long-term debt	\$ 1,964	\$ 884	\$ 4,835	\$ 2,605
Interest income on cash	(764)	(129)	(1,445)	(423)
	\$ 2,796	\$ 2,107	\$ 6,400	\$ 5,913

The increase in prevailing interest rates had the effects of increasing the effective interest rate payable on the Corporation's Revolving Facility from 1.1% at March 31, 2022 to 5.2% at period end while increasing the interest rate received on average cash balances outstanding from 0.8% to 4.8%. These factors largely offset each other during the quarter and nine-month period.

Interest on long-term debt otherwise increased during the quarter and nine-month period due to unwinding of the Corporation's cross-currency interest rate swaps (\$0.4 million per quarter).

Other accretion and adjustments were positively impacted during the nine-month period by a reversal of accretion following an increase in discount rates on provisions.

Income Tax Expense

	Three months ended December 31,				Nine months ended December 31,			
	2022		2021		2022		2021	
Income before income tax expense	\$ 2,315		\$ 8,438		\$ 9,919		\$ 27,382	
Income tax expense at Canadian blended statutory tax	613	26.5%	2,228	26.4%	2,629	26.5%	7,229	26.4%
Results coming from foreign jurisdictions	186		(676)		25		(1,504)	
Non-deductible expenses	109		338		145		565	
Prior year adjustments	(365)		(205)		(417)		(167)	
Net non-recognition of tax benefits	—		285		—		593	
Income tax expense	\$ 543	23.5%	\$ 1,970	23.3%	\$ 2,382	24.0%	\$ 6,716	24.5%

The statutory and effective tax rates remained relatively stable over the quarter and the nine-month period.

Net Income

Net income decreased from \$6.5 million to \$1.8 million during the quarter and from \$20.7 million to \$7.5 million during the nine-month period, compared to the same periods last fiscal year, mainly as a result of the factors described above.

NON-IFRS FINANCIAL MEASURES

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

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

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

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

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

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

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Operating income	5,111	10,545	16,319	33,295
Non-recurring items	—	—	(1,219)	—
Adjusted operating income	\$ 5,111	\$ 10,545	\$ 15,100	\$ 33,295

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

The Corporation's adjusted EBITDA is calculated as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Operating income	5,111	10,545	16,319	33,295
Amortization expense	9,018	9,149	26,671	27,605
Non-recurring items	—	—	(1,219)	—
Adjusted EBITDA	\$ 14,129	\$ 19,694	\$ 41,771	\$ 60,900

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

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

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

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Net income	\$ 1,773	\$ 6,468	\$ 7,537	\$ 20,681
Non-recurring items, net of taxes	—	—	(1,219)	—
Adjusted net income	\$ 1,773	\$ 6,468	\$ 6,318	\$ 20,681
Non-controlling interests ⁽¹⁾	—	—	—	(385)
Adjusted net income attributable to the equity holders of the parent	\$ 1,773	\$ 6,468	\$ 6,318	\$ 21,066
<i>In dollars per share</i>				
Earnings per share - basic and diluted	\$ 0.05	\$ 0.18	\$ 0.22	\$ 0.58
Non-recurring items, net of taxes	—	—	(0.04)	—
Adjusted earnings per share	\$ 0.05	\$ 0.18	\$ 0.18	\$ 0.58

⁽¹⁾ Following the acquisition of the minority interest in Tekalia during the third quarter of fiscal 2022, there is no further non-controlling interest.

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

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

LIQUIDITY AND CAPITAL RESOURCES

CREDIT FACILITIES AND NET DEBT POSITION

Senior Secured Syndicated Revolving Credit Facility (“Revolving Facility”)

The Corporation has a Revolving Facility with a syndicate of six banks that allows the Corporation to borrow up to \$250 million. In May 2022, Héroux-Devtek reached an agreement to extend the Revolving Facility to a new maturity of June 2027 (as at March 31, 2022, June 2026), the other terms and conditions remain relatively unchanged. The Revolving facility also includes an accordion feature, which allow Héroux-Devtek to draw an additional \$200 million subject to lenders' consent.

As at December 31, 2022, and March 31, 2022, the Corporation had US\$47.0 million drawn against the facility at a interest rate of 5.2% (March 31, 2022, 1.3%), worth \$63.7 million and \$58.8 million, respectively, reflecting USD/CAD exchange rate fluctuations.

Unsecured Subordinated Term Loan Facility (“Term Loan Facility”)

The Corporation has a Term Loan Facility with *Fonds de Solidarité FTQ* for an amount of \$75.0 million that matures in September 2028. This facility is fully drawn and bears interest at a rate of 5.0% (5.0% as at March 31, 2022). The Corporation has the option to make early repayments as of September 2024, subject to certain fees.

Net Debt Position

As at	December 31, 2022	March 31, 2022
Long-term debt ⁽¹⁾	\$ 243,552	\$ 238,826
Less: Cash	90,837	86,692
Net debt position	\$ 152,715	\$ 152,134
Adjusted EBITDA ⁽²⁾ - trailing 12 months	63,920	83,049
Net debt to adjusted EBITDA ratio	2.4:1	1.8:1

⁽¹⁾ Excluding net deferred financing costs of \$2.2 million and \$2.3 million as at December 31, 2022 and March 31, 2022, respectively.

⁽²⁾ Non-IFRS financial measure. Refer to the Non-IFRS financial measures section for definitions and reconciliations to the most comparable IFRS measures and to the Selected Quarterly Financial Information.

VARIATIONS IN CASH

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Cash at beginning of periods	\$ 91,693	\$ 103,217	\$ 86,692	\$ 95,470
Cash flows related to operating activities	5,237	17,498	25,542	53,150
Cash flows related to investing activities	(328)	(4,942)	(15,404)	(12,958)
Cash flows related to financing activities	(6,106)	(28,546)	(6,943)	(48,666)
Effect of changes in exchange rates on cash	341	(391)	950	(160)
Cash at end of periods	\$ 90,837	\$ 86,836	\$ 90,837	\$ 86,836

Operating Activities

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

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Cash flows from operations	\$ 12,880	\$ 17,020	\$ 41,436	\$ 53,838
Net change in non-cash items	(7,643)	478	(15,894)	(688)
Cash flows related to operating activities	\$ 5,237	\$ 17,498	\$ 25,542	\$ 53,150

The decrease in cash flows from operations during the quarter is mainly the result of lower margins described under *Operating Results*, partly offset by lower cash tax expense.

For the nine-month period, the decrease in cash flows from operations was mainly driven by lower throughput in the first quarter of the fiscal year and the lower margin described under *Operating Results*, partly offset by lower current income tax expenses.

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

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Accounts receivable	\$ (18)	\$ (1,871)	\$ 4,177	\$ 12,185
Inventories	(11,513)	1,585	(40,915)	2,060
Other assets and derivatives	(2,149)	3,414	7,007	412
Accounts payable and accrued liabilities	(598)	4,530	(1,127)	(3,192)
Provisions	(2,559)	(3,947)	(4,624)	(6,894)
Customer advances and progress billings	10,003	(731)	25,148	(2,841)
Other Liabilities	(809)	(2,502)	(5,560)	(2,418)
	\$ (7,643)	\$ 478	\$ (15,894)	\$ (688)

For the quarter ended December 31, 2022, the negative net change in non-cash items mainly reflects an increase in inventory levels to stabilize the production system and mitigate the effect of supply chain delays, partly offset by an increase in customer advances.

For the quarter ended December 31, 2021, the positive net change in non-cash items mainly reflected an increase in accounts payable due to the timing of purchase, partly offset by the utilization of restructuring provisions.

For the nine-month period ended December 31, 2022, the negative net change in non-cash items mainly reflects an increase in inventory levels to stabilize the production system and mitigate the effect of supply chain delays, partly offset by:

- An increase in customer advances and progress billings; and,
- A decrease in other assets mainly resulting from the unwinding of the Corporation's cross-currency interest rate swaps for proceeds totaling \$11.3 million.

For the nine-month period ended December 31, 2021, the negative net change in non-cash items mainly reflected the utilization of restructuring provisions and seasonal decreases in account payable and accounts receivable related to a lower level of activity than during the fourth quarter of fiscal 2021.

Investing Activities

The Corporation's investing activities were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Net additions to property, plant and equipment	\$ (2,354)	\$ (5,197)	\$ (11,665)	\$ (12,907)
Net change in finite-life intangible assets	(1,090)	836	(6,855)	(1,511)
Proceeds from a business divestiture	3,116	—	3,116	2,041
Proceeds on disposal of property, plant and equipment	—	319	—	319
Purchase of minority interest	—	(900)	—	(900)
Cash flows related to investing activities	\$ (328)	\$ (4,942)	\$ (15,404)	\$ (12,958)

The increase in investment in finite-life intangible assets mainly relates to the ongoing development of civil aircraft development programs.

The \$3.1 million proceeds from a business divestiture relate to the sale of Bolton operations to Ontic Engineering & Manufacturing UK Limited. The balance of \$0.7 million (£0.5 million) will be collected in the next 6 months.

The following table reconciles additions to property, plant and equipment to the additions as per the statements of cash flows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Additions to property, plant and equipment	\$ 2,713	\$ 5,802	\$ 10,529	\$ 11,525
Government assistance	(43)	—	(57)	—
Variation in unpaid additions included in Accounts payable and accrued liabilities	(127)	(200)	1,418	2,087
Non-cash additions made through leasing agreements	(189)	(405)	(225)	(705)
Additions, as per statements of cash flows	\$ 2,354	\$ 5,197	\$ 11,665	\$ 12,907

Financing Activities

The Corporation's financing activities were as follows:

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Increase in long-term debt	\$ —	\$ 1,097	\$ 6,239	\$ 3,059
Repayment of long-term debt	(4,538)	(4,904)	(9,634)	(13,995)
Increase in deferred financing costs	—	—	(245)	(555)
Repurchase and cancellation of shares	(1,568)	(25,136)	(4,406)	(38,621)
Issuance of common shares	—	397	1,103	1,446
Cash flows related to financing activities	\$ (6,106)	\$ (28,546)	\$ (6,943)	\$ (48,666)

The increases in long-term debt relate to governmental loans in support of development programs.

Repayment of long-term debt during the three and nine-month periods is comprised of lease payments and scheduled reimbursements of governmental loans.

Refer to the *Normal Course Issuer Bid* section below for details regarding the repurchase and cancellation of shares.

NORMAL COURSE ISSUER BID

On May 19, 2022, the Corporation announced a Normal Course Issuer Bid ("NCIB") for the purchase for cancellation of up to 1,896,079 common shares on the open market through the TSX or alternative trading facilities. The NCIB began on May 25, 2022, and will end on May 24, 2023, or on such earlier date when the Company has either acquired the maximum number of common shares allowable under the NCIB or decided not to make any further purchases under it.

	During the period		
	Number of shares	Average cost per share	Total cost
Quarter ended June 30, 2022	107,835	\$ 15.40	\$ 1,661
Quarter ended September 30, 2022	90,825	12.96	1,177
Quarter ended December 31, 2022	120,800	12.98	1,568
Through February 7, 2023	10,300	13.40	138
Total	329,760	\$ 13.78	\$ 4,544

FREE CASH FLOW⁽¹⁾

	Three months ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
Cash flows related to operating activities	\$ 5,237	\$ 17,498	\$ 25,542	\$ 53,150
Net additions to property, plant and equipment	(2,354)	(5,197)	(11,665)	(12,907)
Net change in finite-life intangible assets	(1,090)	836	(6,855)	(1,511)
Proceeds of disposal of property, plant and equipment	—	319	—	319
Free cash flow	\$ 1,793	\$ 13,456	\$ 7,022	\$ 39,051

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

The decreases in free cash flow for the quarter and nine-month period compared to last year were mainly driven by the strategic increase in inventory described previously and lower profitability.

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

FINANCIAL POSITION

CONSOLIDATED BALANCE SHEETS

Working capital

As at	December 31, 2022	March 31, 2022	Variance	
Current assets	\$ 462,591	\$ 415,450	\$ 47,141	11.3 %
Current liabilities	204,822	179,821	25,001	13.9 %
Working capital	\$ 257,769	\$ 235,629	\$ 22,140	9.4 %
Working capital ratio	2.26	2.31		

The increase in current assets is mainly explained by a \$46.7 million increase in inventory as described under *Liquidity and Capital Resources*.

The increase in current liabilities is mainly explained by a \$26.4 million increase in customer advances and progress billings.

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

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

	December 31, 2022	March 31, 2022	Variance	
Long-term assets	\$ 389,059	\$ 397,908	\$ (8,849)	(2.2) %
Long-term liabilities	265,667	256,255	\$ 9,412	3.7 %
Shareholders' equity	\$ 381,161	\$ 377,282	\$ 3,879	1.0 %
Net debt-to-equity ratio ⁽¹⁾	0.40:1	0.40:1		

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

The \$8.8 million decrease in long-term assets is mainly explained by a \$13.8 million decrease in derivative financial instruments mainly due to the unwinding of cross-currency interest rate swaps.

The \$9.4 million increase in long-term liabilities is mainly explained by a \$4.9 million increase in derivative financial instruments due to the effect of foreign exchange rates on the fair value of the Corporation's forward foreign exchange contracts and \$3.5 million increase in long-term debt mainly due to foreign exchange variations.

The \$3.9 million increase in Shareholder's Equity is essentially driven by the \$7.5 million net income for the nine-months period, partly offset by the allocation of \$4.4 million to the NCIB.

ADDITIONAL INFORMATION

FOREIGN EXCHANGE (“FX”)

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

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

	December 31, 2022	March 31, 2022
USD (Canadian equivalent of US\$1.0)	1.3544	1.2496
GBP (Canadian equivalent of £1.0)	1.6322	1.6417
EUR (Canadian equivalent of €1.0)	1.4458	1.3853

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

	Quarters ended December 31,		Nine months ended December 31,	
	2022	2021	2022	2021
USD (Canadian equivalent of US\$1.0)	1.3580	1.2600	1.3135	1.2494
GBP (Canadian equivalent of £1.0)	1.5953	1.6991	1.5778	1.7175
EUR (Canadian equivalent of €1.0)	1.3864	1.4409	1.3531	1.4688

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

DERIVATIVES

Forward foreign exchange contracts

As at December 31, 2022, the Corporation had sale forward foreign exchange contracts outstanding for a notional amount of \$425.3 million (\$341.6 million at March 31, 2022) denominated in USD, EUR and and GBP. This amount includes contracts with nominal value of US\$264.6 million (US\$219.5 million at March 31, 2022) convertible into Canadian dollars at an average rate of 1.3110 (1.2888 at March 31, 2022). These contracts mature at various dates between January 2023 and June 2028, with the majority maturing this fiscal year and the next.

Cross-currency interest rate swaps

As at March 31, 2022, the Corporation had three cross-currency interest rate swap agreements exchanging CAD and USD-denominated debt to EUR for a total notional amount of € 90.5 million in order to mitigate foreign exchange and interest rate risks. These agreements matured between May 2022 and September 2028, and mainly bore interest at a weighted average fixed rate of 2.4%.

During the quarter ended June 30, 2022, one of these swaps expired, and the other two were unwound for cash proceeds of \$11.3 million.

Equity swap agreement

As at December 31, 2022, the Corporation had entered into an equity swap agreement fixing 400,000 common shares of the Corporation at a price of \$13.39 (300,000 common shares at a price of \$13.52 as at March 31, 2022). This agreement manages the Corporation’s exposure to fluctuations of its share price and resulting effect on the value of outstanding Performance Share Units and Deferred Share Units, and expires in June 2023.

INTERNAL CONTROLS AND PROCEDURES

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

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

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

No changes were made to the Corporation's internal controls over financial reporting during the quarter ended December 31, 2022, that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

SELECTED QUARTERLY FINANCIAL INFORMATION

Fiscal year	2023			2022				2021
	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth quarter
Sales	\$ 140,875	\$ 132,680	\$ 114,089	\$ 147,459	\$ 131,147	\$ 131,293	\$ 126,188	\$ 154,989
Operating income	5,111	8,562	2,646	11,463	10,545	11,953	10,797	12,229
Adjusted EBITDA ⁽¹⁾	14,129	16,216	11,426	22,149	19,694	21,157	20,049	24,975
Net income	1,773	4,799	965	11,459	6,468	7,510	6,703	8,802
Adjusted Net Income ⁽¹⁾	1,773	3,580	965	13,158	6,468	7,510	6,703	10,169
<i>In dollars per share</i>								
Earnings per share - Diluted	\$ 0.05	\$ 0.14	\$ 0.03	\$ 0.33	\$ 0.18	\$ 0.21	\$ 0.19	\$ 0.24
Adjusted earnings per share ⁽¹⁾	0.05	0.10	0.03	0.38	0.18	0.21	0.19	0.28
<i>In thousands of shares</i>								
Weighted-average number of common diluted shares outstanding	34,450	34,554	34,633	34,868	35,741	36,576	36,981	36,523

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

Seasonal trends

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

RISKS AND UNCERTAINTIES

Héroux-Devtek operates in industry sectors that have a variety of risk factors and uncertainties. Risk and uncertainties that could materially affect the Corporation's business, financial condition and results of operations in an adverse manner are described in the Corporation's MD&A for the fiscal year ended March 31, 2022. Additional risks and uncertainties not presently known to the Corporation or that the Corporation currently believes to be immaterial may also adversely affect its business.

SHAREHOLDER INFORMATION

ISSUED CAPITAL		February 7, 2023
Common shares issued and outstanding		34,260,016
Stock options issued and outstanding		1,635,500

Héroux-Devtek's shares are traded on the Toronto Stock Exchange under the ticker "HRX" and Computershare Trust acts as registrar and transfer agent.

EXPECTED ISSUANCE OF FINANCIAL RESULTS	
Fiscal 2023	
Fourth quarter	May 18, 2023
Fiscal 2024	
First quarter	August 8, 2023
Second quarter	November 10, 2023
Third quarter	February 7, 2024

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February 7, 2023



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