



**CONSOLIDATED FINANCIAL
STATEMENTS / MANAGEMENT'S
DISCUSSION AND ANALYSIS**

Second quarter ended September 30, 2022



INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Second quarter ended September 30, 2022

TABLE OF CONTENTS

Interim condensed consolidated financial statements	5
Notes to the interim condensed consolidated financial statements	10
Note 1 Nature of activities and corporate information	10
Note 2 Basis of preparation	10
Note 3 Revenue from contracts with customers	10
Note 4 Government assistance	11
Note 5 Cost of sales, selling and administrative expenses	11
Note 6 Non-recurring items	11
Note 7 Net financial expenses	12
Note 8 Earnings per share	12
Note 9 Derivative financial instruments	12
Note 10 Long-term debt	13
Note 11 Issued capital	13
Note 12 Accumulated other comprehensive income	15
Note 13 Net change in non-cash items	16

DISCLOSURE OF NON-REVIEW OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE QUARTERS ENDED SEPTEMBER 30, 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 September 30, 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.

November 10, 2022

CONSOLIDATED BALANCE SHEETS

(In thousands of Canadian dollars) (Unaudited)

As at	Notes	September 30, 2022	March 31, 2022
ASSETS	10		
Current assets			
Cash		\$ 91,693	\$ 86,692
Accounts receivable		101,129	105,389
Income tax receivable		2,015	1,108
Inventories		230,684	200,342
Derivative financial instruments	9	—	5,500
Other current assets		20,032	16,419
		445,553	415,450
Property, plant and equipment, net	4	206,341	208,838
Finite-life intangible assets, net	4	48,008	47,320
Derivative financial instruments	9	35	14,329
Deferred income tax assets		8,329	6,557
Goodwill		104,217	108,200
Other long-term assets		11,293	12,664
Total assets		\$ 823,776	\$ 813,358
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		\$ 111,080	\$ 114,508
Provisions		18,983	21,925
Customer advances and progress billings		45,564	29,875
Income tax payable		1,532	826
Derivative financial instruments	9	13,132	1,852
Current portion of long-term debt	10	12,484	10,835
		202,775	179,821
Long-term debt	10	231,358	225,691
Provisions		15,013	14,828
Derivative financial instruments	9	10,482	830
Deferred income tax liabilities		3,297	8,567
Other liabilities		4,795	6,339
		467,720	436,076
Shareholders' equity			
Issued capital	11	83,146	82,189
Contributed surplus		6,086	5,767
Accumulated other comprehensive income (loss)	12	(18,120)	6,865
Retained earnings		284,944	282,461
		356,056	377,282
Total liabilities and shareholders' equity		\$ 823,776	\$ 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 September 30,		Six months ended September 30,	
		2022	2021	2022	2021
Sales	3	\$ 132,680	\$ 131,293	\$ 246,769	\$ 257,481
Cost of sales	4, 5	114,313	109,076	215,891	213,624
Gross profit		18,367	22,217	30,878	43,857
Selling and administrative expenses	4, 5	11,024	10,264	20,889	21,107
Non-recurring items	6	(1,219)	—	(1,219)	—
Operating income		8,562	11,953	11,208	22,750
Net financial expenses	7	2,228	1,913	3,604	3,806
Income before income tax expense		6,334	10,040	7,604	18,944
Income tax expense		1,535	2,530	1,840	4,731
Net income		\$ 4,799	\$ 7,510	\$ 5,764	\$ 14,213
Attributable to:					
Equity holders of the parent		4,799	7,756	5,764	14,598
Non-controlling interest		—	(246)	—	(385)
		\$ 4,799	\$ 7,510	\$ 5,764	\$ 14,213
Earnings per share – basic and diluted	8	\$ 0.14	\$ 0.21	\$ 0.17	\$ 0.40

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In thousands of Canadian dollars) (Unaudited)

		Three months ended September 30,		Six months ended September 30,	
	Notes	2022	2021	2022	2021
	12				
Other comprehensive loss :					
Items that may be reclassified to net income					
Gains arising from conversion of the financial statements of foreign operations		\$ 3,674	\$ 3,780	\$ 5	\$ 736
Cash flow hedges:					
Net losses on valuation of derivative financial instruments		(21,299)	(7,516)	(29,253)	(5,422)
Net losses (gains) on derivative financial instruments transferred to net income		1,019	(1,123)	1,466	(2,672)
Deferred income taxes		5,355	2,282	7,337	2,135
		(14,925)	(6,357)	(20,450)	(5,959)
Losses on hedges of net investments in foreign operations		(3,859)	(691)	(5,229)	(306)
Deferred income taxes		518	80	689	36
		(3,341)	(611)	(4,540)	(270)
Items that are never reclassified to net income					
Defined benefit pension plans:					
(Losses) gains from remeasurement		(1,180)	1,367	(1,253)	1,854
Deferred income taxes		311	(361)	330	(490)
		(869)	1,006	(923)	1,364
Other comprehensive loss		\$ (15,461)	\$ (2,182)	\$ (25,908)	\$ (4,129)
Comprehensive (loss) income					
Net income		4,799	7,510	5,764	14,213
Other comprehensive loss		(15,461)	(2,182)	(25,908)	(4,129)
Comprehensive (loss) income		\$ (10,662)	\$ 5,328	\$ (20,144)	\$ 10,084
Attributable to:					
Equity holders of the parent		(10,662)	5,574	(20,144)	10,469
Non-controlling interest		—	(246)	—	(385)
		\$ (10,662)	\$ 5,328	\$ (20,144)	\$ 10,084

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	(480)	—	—	(2,358)	(2,838)	—	(2,838)
Stock-based compensation expense	11	—	653	—	—	653	—	653
Net income		—	—	—	5,764	5,764	—	5,764
Other comprehensive loss	12	—	—	(24,985)	(923)	(25,908)	—	(25,908)
Balance as at September 30, 2022		\$ 83,146	\$ 6,086	\$ (18,120)	\$ 284,944	\$ 356,056	\$ —	\$ 356,056

	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	1,419	(370)	—	—	1,049	—	1,049
Repurchase and cancellation of common shares	11	(1,834)	—	—	(11,651)	(13,485)	—	(13,485)
Stock-based compensation expense	11	—	589	—	—	589	—	589
Net income (loss)		—	—	—	14,598	14,598	(385)	14,213
Other comprehensive (loss) income	12	—	—	(5,493)	1,364	(4,129)	—	(4,129)
Balance as at September 30, 2021		\$ 85,807	\$ 5,345	\$ 10,786	\$ 287,142	\$ 389,080	\$ 889	\$ 389,969

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 September 30,		Six months ended September 30,	
	Notes	2022	2021	2022	2021
Cash provided by (used for):					
Operating activities					
Net income		\$ 4,799	\$ 7,510	\$ 5,764	\$ 14,213
Items not requiring an outlay of cash:					
Amortization expense	5	8,873	9,204	17,653	18,456
Deferred income taxes		2,345	(88)	3,072	1,181
Net non-cash financial expenses	7	1,072	1,315	1,414	2,379
Stock-based compensation expense	11	340	371	653	589
Cash flows from operations		17,429	18,312	28,556	36,818
Net change in non-cash items	13	(9,165)	(845)	(8,251)	(1,166)
Cash flows related to operating activities		\$ 8,264	\$ 17,467	\$ 20,305	\$ 35,652
Investing activities					
Net additions to property, plant and equipment		(3,557)	(4,438)	(9,311)	(7,710)
Net change in finite-life intangible assets		(4,008)	(1,817)	(5,765)	(2,347)
Proceeds from a business divestiture		—	—	—	2,041
Cash flows related to investing activities		\$ (7,565)	\$ (6,255)	\$ (15,076)	\$ (8,016)
Financing activities					
Proceeds from long-term debt		5,549	1,962	6,239	1,962
Repayment of long-term debt		(2,194)	(2,591)	(5,096)	(9,091)
Increase in deferred financing costs		—	—	(245)	(555)
Repurchase and cancellation of shares	11	(1,177)	(6,831)	(2,838)	(13,485)
Issuance of common shares under the stock option plan		—	544	1,103	1,049
Cash flows related to financing activities		\$ 2,178	\$ (6,916)	\$ (837)	\$ (20,120)
Effect of changes in exchange rates on cash		509	327	609	231
Change in cash during the periods		3,386	4,623	5,001	7,747
Cash at beginning of periods		88,307	98,594	86,692	95,470
Cash at end of periods		\$ 91,693	\$ 103,217	\$ 91,693	\$ 103,217
Interest and income taxes reflected in operating activities:					
Interest paid		\$ 1,622	\$ 1,726	\$ 2,871	\$ 3,666
Interest received		\$ 466	\$ 152	\$ 681	\$ 294
Income taxes paid		\$ 228	\$ (254)	\$ 1,265	\$ 2,397

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 six-month periods ended September 30, 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 September 30, 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 November 10, 2022.

NOTE 3. REVENUE FROM CONTRACTS WITH CUSTOMERS

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

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Geographic markets				
Canada	\$ 7,225	\$ 5,865	\$ 14,743	\$ 17,265
United States of America	85,250	81,882	156,929	151,723
United Kingdom	9,692	9,875	16,644	21,968
Spain	5,615	9,337	12,577	19,311
Rest of Europe	15,376	15,060	28,158	28,472
Other countries	9,522	9,274	17,718	18,742
	\$ 132,680	\$ 131,293	\$ 246,769	\$ 257,481
Sectors				
Civil	\$ 41,274	\$ 37,287	\$ 76,672	\$ 74,926
Defence	91,406	94,006	170,097	182,555
	\$ 132,680	\$ 131,293	\$ 246,769	\$ 257,481

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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Finite-life intangible assets	\$ 123	\$ 566	\$ 403	\$ 566
Property, plant and equipment	\$ —	\$ —	\$ 14	\$ —
Cost of sales and selling and administrative expenses	\$ 949	\$ 3,676	\$ 2,577	\$ 7,152

Government assistance includes mainly research and development tax credits, other credits and grants, including the Canadian Emergency Wage Subsidy for the three and six-month periods ended September 30, 2021.

NOTE 5. COST OF SALES, SELLING AND ADMINISTRATIVE EXPENSES

The main components of these expenses were as follows:

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Raw materials and purchased parts	\$ 52,470	\$ 50,540	\$ 91,835	\$ 95,872
Employee costs	45,006	44,074	89,916	89,351
Amortization of property, plant and equipment and finite-life intangible assets	8,873	9,204	17,653	18,456
Others	18,988	15,522	37,376	31,052
	\$ 125,337	\$ 119,340	\$ 236,780	\$ 234,731
Including:				
Foreign exchange gains upon conversion of net monetary items	\$ (71)	\$ (926)	\$ (810)	\$ (1,013)
Amortization of customer relationships	\$ 909	\$ 1,142	\$ 1,839	\$ 2,129

NOTE 6. NON-RECURRING ITEMS

The commercial objectives included in the agreement for the sale of Bolton to Ontic Engineering & Manufacturing UK Limited that occurred on May 4, 2021 were achieved during the quarter ended September 30, 2022 and a net non-recurring gain of \$1,219 was recognized.

NOTE 7. NET FINANCIAL EXPENSES

Net financial expenses comprise the following:

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Interest accretion on governmental authorities loans	\$ 710	\$ 796	\$ 1,459	\$ 1,598
Interest on defined benefit obligations	20	24	39	48
Interest on leases	197	304	410	521
Amortization of deferred financing costs	117	123	240	306
Other accretion and adjustments	28	68	(734)	(94)
Net non-cash financial expenses	\$ 1,072	\$ 1,315	\$ 1,414	\$ 2,379
Interest on long-term debt	\$ 1,622	\$ 750	\$ 2,871	\$ 1,721
Interest income on cash	(466)	(152)	(681)	(294)
	\$ 2,228	\$ 1,913	\$ 3,604	\$ 3,806

NOTE 8. EARNINGS PER SHARE

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

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Weighted-average number of common shares outstanding	34,460,861	36,242,291	34,479,456	36,468,106
Dilutive effect of stock options	93,501	333,804	110,784	286,987
Weighted-average number of common diluted shares outstanding	34,554,362	36,576,095	34,590,240	36,755,093
Options excluded from diluted earnings per share calculation	1,298,000	—	1,298,000	197,000

NOTE 9. DERIVATIVE FINANCIAL INSTRUMENTS

Forward foreign exchange contracts

As at September 30, 2022, the Corporation had forward foreign exchange contracts outstanding for a notional amount of \$359,187 (\$341,604 at March 31, 2022) denominated in USD, EUR and GBP. This amount includes contracts with nominal value of US\$215,430 (US\$219,500 at March 31, 2022) convertible into Canadian dollars at an average rate of 1.2947 (1.2888 at March 31, 2022). These contracts mature at various dates between October 2022 and June 2027, 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 September 30, 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	September 30, 2022	March 31, 2022
Senior Secured Syndicated Revolving Credit Facility ("Revolving Facility")	\$ 64,507	\$ 58,821
Governmental authorities loans	89,443	84,508
Unsecured Subordinated Term Loan Facility ("Term Loan")	75,000	75,000
Lease liabilities	17,197	20,497
Deferred financing costs, net	(2,305)	(2,300)
	\$ 243,842	\$ 236,526
Less: current portion	12,484	10,835
Long-term debt	\$ 231,358	\$ 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 + 1.0% representing an effective rate of 4.1% (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 September 30, 2022		Six months ended September 30, 2022	
	Number	Issued capital	Number	Issued capital
Opening balance	34,481,941	\$ 83,365	34,486,776	\$ 82,189
Issued for cash on exercise of stock options	—	—	103,000	1,437
Repurchase and cancellation	(90,825)	(219)	(198,660)	(480)
Closing balance	34,391,116	\$ 83,146	34,391,116	\$ 83,146

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 September 30, 2022, the Company has purchased and cancelled 198,660 common shares for a cash consideration of \$2,838, representing a weighted average price of \$14.29 per share. The \$2,358 excess of purchase price over the carrying value was charged to retained earnings.

B. Stock option plan

For the quarters ended September 30, 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	1,600,301	\$14.04
Exercised	—	—	(48,551)	11.20
Closing balance	1,645,500	\$14.60	1,551,750	\$14.13
Stock-based compensation expense		\$ 340		\$ 371

⁽¹⁾ Weighted average exercise price

For the six months ended September 30, 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	(94,345)	11.12
Expired	(2,250)	10.71	—	—
Closing balance	1,645,500	\$14.60	1,551,750	\$14.13
Stock-based compensation expense		\$ 653		\$ 589

⁽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 September 30, 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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
DSUs				
<i>In number of DSUs</i>				
Opening balance	199,471	193,526	199,471	192,108
Issued	55,359	30,258	55,359	31,676
Settled	—	(24,313)	—	(24,313)
Closing balance of DSUs outstanding	254,830	199,471	254,830	199,471
DSU expense (income) for the periods	\$ 92	\$ 349	\$ (483)	\$ 538
Fair value of vested outstanding DSUs, end of periods	\$ 2,860	\$ 3,330	\$ 2,860	\$ 3,330

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
PSUs				
<i>In number of PSUs</i>				
Opening balance	404,550	383,600	285,350	300,150
Issued	5,850	—	125,550	86,150
Cancelled/Forfeited	(6,350)	(3,000)	(6,850)	(5,700)
Closing balance of PSUs outstanding	404,050	380,600	404,050	380,600
PSU expense (income) for the periods	\$ (108)	\$ 365	\$ (551)	\$ 783
Fair value of vested outstanding PSUs, end of periods	\$ 3,448	\$ 4,872	\$ 3,448	\$ 4,872

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 June 30, 2022	\$ (664)	\$ (888)	\$ (1,976)	\$ (3,528)
Other comprehensive income (loss)	3,674	(14,925)	(3,341)	(14,592)
Balance as at September 30, 2022	\$ 3,010	\$ (15,813)	\$ (5,317)	\$ (18,120)
Balance as at March 31, 2022	\$ 3,005	\$ 4,637	\$ (777)	\$ 6,865
Other comprehensive income (loss)	5	(20,450)	(4,540)	(24,985)
Balance as at September 30, 2022	\$ 3,010	\$ (15,813)	\$ (5,317)	\$ (18,120)
	Exchange differences on conversion of foreign operations	Cash flow hedges	Hedge of net investments in foreign operations	Total
Balance as at June 30, 2021	\$ 11,020	\$ 8,929	\$ (5,975)	\$ 13,974
Other comprehensive income (loss)	3,780	(6,357)	(611)	(3,188)
Balance as at September 30, 2021	\$ 14,800	\$ 2,572	\$ (6,586)	\$ 10,786
Balance as at March 31, 2021	\$ 14,064	\$ 8,531	\$ (6,316)	\$ 16,279
Other comprehensive income (loss)	736	(5,959)	(270)	(5,493)
Balance as at September 30, 2021	\$ 14,800	\$ 2,572	\$ (6,586)	\$ 10,786

NOTE 13. NET CHANGE IN NON-CASH ITEMS

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

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Accounts receivable	\$ (9,459)	\$ (8,486)	\$ 4,195	\$ 14,056
Inventories	(11,420)	6,671	(29,402)	475
Other assets and derivatives (note 9)	(1,758)	2,051	9,156	(3,002)
Accounts payable and accrued liabilities	8,174	(3,211)	(529)	(7,722)
Provisions	(1,627)	(1,034)	(2,065)	(2,947)
Customer advances and progress billings	9,299	1,757	15,145	(2,110)
Other Liabilities	(2,374)	1,407	(4,751)	84
	\$ (9,165)	\$ (845)	\$ (8,251)	\$ (1,166)



MANAGEMENT'S DISCUSSION AND ANALYSIS

Second quarter ended September 30, 2022

TABLE OF CONTENTS

OVERVIEW	19
<i>Forward-looking Statements</i>	19
<i>Highlights</i>	20
OPERATING RESULTS	21
<i>Non-IFRS Financial Measures</i>	24
LIQUIDITY AND CAPITAL RESOURCES	26
<i>Credit Facilities and Net Debt Position</i>	26
<i>Variations in Cash</i>	26
<i>Normal Course Issuer Bid</i>	29
<i>Free Cash flow</i>	29
FINANCIAL POSITION	30
<i>Consolidated Balance Sheets</i>	30
ADDITIONAL INFORMATION	31
<i>Foreign Exchange</i>	31
<i>Derivatives</i>	31
<i>Internal Controls and Procedures</i>	32
<i>Selected Quarterly Financial Information</i>	32
<i>Risks and Uncertainties</i>	32
<i>Shareholder Information</i>	33

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 September 30, 2022. It also compares the operating results and cash flows for the quarter and six-month period ended September 30, 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 September 30, 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 November 10, 2022.

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 ongoing 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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Sales	\$ 132,680	\$ 131,293	\$ 246,769	\$ 257,481
Operating income	8,562	11,953	11,208	22,750
Adjusted operating income ⁽¹⁾	7,343	11,953	9,989	22,750
Adjusted EBITDA ⁽¹⁾	16,216	21,157	27,642	41,206
Net income	4,799	7,510	5,764	14,213
Adjusted net income ⁽¹⁾	3,580	7,510	4,545	14,213
Cash flows related to operating activities	8,264	17,467	20,305	35,652
Free cash flow ⁽¹⁾	699	11,212	5,229	25,595
<i>In dollars per share</i>				
Earnings per share - basic and diluted	\$ 0.14	\$ 0.21	\$ 0.17	\$ 0.40
Adjusted EPS ⁽¹⁾	0.10	0.21	0.13	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.

Operating Environment

Héroux-Devtek's throughput in the second quarter improved significantly compared to the first, with sales reaching \$132.7 million compared to \$114.1 million in the first quarter despite planned shutdowns and summer vacation. As a result, operating income and Adjusted EBITDA respectively improved to \$8.6 million and \$16.2 million from \$2.6 million and \$11.4 million. In order to stabilize the Corporation's production system and prepare for the second half of the fiscal year, inventory was increased by a further \$13.3 million since June 30, 2022 (\$30.3 million since March 31, 2022), driving a reduction in cash flows related to operating activities and free cash flow when compared to last year.

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

- COVID-19 continues to cause higher absenteeism compared to last year;
- The Corporation's supply chain is also impacted by the COVID-related absenteeism and the labour shortages observed in the Aerospace industry;
- Lead times for the procurement of raw material continue to increase and Russia's invasion of Ukraine limits the supply of certain material; and,
- Inflation continues to be high and central banks are still responding by raising base interest rates, therefore increasing financing costs and putting pressure on financially fragile companies.

The Corporation's order book remains strong, and has in fact recently been bolstered by aftermarket and business jet orders. Héroux-Devtek's teams are committed to coping with the challenges in order to increase throughput and satisfy customer demand.

Events of the Quarter

- The Corporation generated consolidated sales of \$132.7 million, on par with \$131.3 million a year earlier, in spite of a more complex operating environment than last year.
- Operating income decreased to \$8.6 million from \$12.0 million last fiscal year, and Adjusted EBITDA decreased to \$16.2 million, or 12.2% of sales compared to \$21.2 million or 16.1% last year. The decrease in profitability is mainly the result of production system inefficiencies driven by the challenging environment described above and a less favourable product mix, while last year's COVID-19 disruptions were compensated for by the Canadian Emergency Wage Subsidy (none this year, representing an impact of 1.7% of sales).
- Subsequent to the end of the quarter, 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 E195 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 September 30,			Six months ended September 30,		
	2022	2021	Variance	2022	2021	Variance
Sales	\$ 132,680	\$ 131,293	\$ 1,387	\$ 246,769	\$ 257,481	\$ (10,712)
Gross profit	18,367	22,217	(3,850)	30,878	43,857	(12,979)
Selling and administrative expenses	11,024	10,264	760	20,889	21,107	(218)
Adjusted operating income ⁽¹⁾	7,343	11,953	(4,610)	9,989	22,750	(12,761)
Non-recurring items	(1,219)	—	(1,219)	(1,219)	—	(1,219)
Operating income	8,562	11,953	(3,391)	11,208	22,750	(11,542)
Net financial expenses	2,228	1,913	315	3,604	3,806	(202)
Income tax expense	1,535	2,530	(995)	1,840	4,731	(2,891)
Net income	\$ 4,799	\$ 7,510	\$ (2,711)	\$ 5,764	\$ 14,213	\$ (8,449)
Adjusted net income ⁽¹⁾	\$ 3,580	\$ 7,510	\$ (3,930)	\$ 4,545	\$ 14,213	\$ (9,668)
<i>As a percentage of sales</i>						
Gross profit	13.8%	16.9%	-310 bps	12.5%	17.0%	-450 bps
Selling and administrative expenses	8.3%	7.8%	50 bps	8.5%	8.2%	30 bps
Operating income	6.5%	9.1%	-260 bps	4.5%	8.8%	-430 bps
Adjusted operating income ⁽¹⁾	5.5%	9.1%	-360 bps	4.0%	8.8%	-480 bps
<i>In dollars per share</i>						
Earnings per share - basic and diluted	\$ 0.14	\$ 0.21	\$ (0.07)	\$ 0.17	\$ 0.40	\$ (0.23)
Adjusted EPS ⁽¹⁾	\$ 0.10	\$ 0.21	\$ (0.11)	\$ 0.13	\$ 0.40	\$ (0.27)

⁽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 September 30,				
	2022	2021	FX impact	Net variance	
Defence ⁽¹⁾	\$ 91,406	\$ 94,006	\$ (349)	\$ (2,251)	(2.4)%
Civil	41,274	37,287	(162)	4,149	11.1 %
Total	\$ 132,680	\$ 131,293	\$ (511)	\$ 1,898	1.4 %

	Six months ended September 30,				
	2022	2021	FX impact	Net variance	
Defence ⁽¹⁾	\$ 170,097	\$ 182,555	\$ (347)	\$ (12,111)	(6.6)%
Civil	76,672	74,926	(157)	1,903	2.5 %
Total	\$ 246,769	\$ 257,481	\$ (504)	\$ (10,208)	(4.0)%

⁽¹⁾ Includes defence sales to civil customers and governments

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

Defence

The respective 2.4% and 6.6% decreases in defence sales for the quarter and six month period were mainly related to the challenges of the current operating environment as described in the *Highlights* section under *Overview*. These elements were partly offset by the ramp-up of deliveries for the Boeing F-18 program.

Civil

The \$4.1 million and \$1.9 million respective increases in civil sales for the quarter and six-month period compared to last year were mainly driven by an increase in deliveries for the Embraer Praetor and Boeing 777 programs.

Gross Profit

Gross profit for the quarter and the six-month period decreased to 13.8% and 12.5% of sales, from 16.9% and 17.0% of sales respectively last year, mainly due to:

- Inefficiencies resulting from the production system disruptions mentioned above;
- A less favourable product mix; and,
- Lower throughput in the first quarter of the fiscal year.

Last year's Covid-related disruptions were compensated for by the Canadian Emergency Wage Subsidy, representing a 1.8% impact on gross profit for the quarter and six-month periods (none this year).

Selling and Administrative Expenses

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Selling and Administrative Expenses	\$ 11,024	\$ 10,264	\$ 20,889	\$ 21,107
Less: Net gains on conversion of net monetary items	(71)	(926)	(810)	(1,013)
Selling and Administrative expenses excluding conversion of monetary items	\$ 11,095	\$ 11,190	\$ 21,699	\$ 22,120
<i>As a percentage of sales</i>	8.4%	8.5%	8.8%	8.6%

When excluding the effect of the conversion of net monetary items, selling and administrative expenses for the six-month period ended September 30, 2022 increased to 8.8% of sales compared to 8.6% for the previous year due to lower sales, while remaining stable for the quarter.

Non-recurring items

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Achievement of commercial objective - sale of Bolton	\$ (1,219)	\$ —	\$ (1,219)	\$ —
Non-recurring items in operating income	\$ (1,219)	\$ —	\$ (1,219)	\$ —

The commercial objectives included in the agreement for the sale of Bolton to Ontic Engineering & Manufacturing UK Limited that occurred on May 4, 2021 were achieved during the quarter ended September 30, 2022 resulting in a gain of \$1.2 million.

Operating Income

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Operating income	\$ 8,562	\$ 11,953	\$ 11,208	\$ 22,750
Non-recurring items	(1,219)	—	(1,219)	—
Adjusted operating income	\$ 7,343	\$ 11,953	\$ 9,989	\$ 22,750
<i>As a percentage of sales</i>				
Operating income	6.5%	9.1%	4.5%	8.8%
Adjusted operating income	5.5%	9.1%	4.0%	8.8%

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

Net Financial Expenses

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Interest accretion on governmental authorities loans	\$ 710	\$ 796	\$ 1,459	\$ 1,598
Interest on defined benefit obligations	20	24	39	48
Interest on leases	197	304	410	521
Amortization of deferred financing costs	117	123	240	306
Other accretion and adjustments	28	68	(734)	(94)
Net non-cash financial expenses	\$ 1,072	\$ 1,315	\$ 1,414	\$ 2,379
Interest on long-term debt	\$ 1,622	\$ 750	\$ 2,871	\$ 1,721
Interest income on cash	(466)	(152)	(681)	(294)
	\$ 2,228	\$ 1,913	\$ 3,604	\$ 3,806

The increase in net financial expenses for the quarter mainly relate to higher interest on long-term debt as a result of the increase of the effective interest rate at period end from 1.1% to 4.1% on the Revolving Facility and the effect of unwinding the Corporation's cross-currency interest rate swaps, partly offset by positive impact of higher interest income on cash.

The decrease in net financial expense for the six-month period mainly relate to the positive impact of discount rate variation and the increase on interest income on cash, partly offset by the increase of the effective interest rate at period end from 1.1% to 4.1% on the Revolving Facility and the effect of unwinding the Corporation's cross-currency interest rate swaps.

Income Tax Expense

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Income before income tax expense	\$ 6,334	\$ 10,040	\$ 7,604	\$ 18,944
Income tax expense	1,535	2,530	1,840	4,731
Effective tax rate	24.2%	25.2%	24.2%	25.0%
Canadian blended statutory income tax rate	26.5%	26.4%	26.5%	26.4%

For the quarter ended September 30, 2022, the Corporation's effective income tax rate mainly reflected the favorable impact of the non-recurring gain following the achievement of the commercial objectives of the sale of its Bolton operations for \$0.3 million, partially offset by non-deductible expenses totaling \$0.1 million (\$0.3 million in Fiscal 2022). The results from other tax jurisdictions had no impact this quarter (favourable impact of \$0.5 million in Fiscal 2022).

For the six-month period ended September 30, 2022, the Corporation's effective income tax rate mainly reflected the favorable impact of results in other tax jurisdictions of \$0.3 million (\$0.8 million in Fiscal 2022), partially offset by non-deductible expenses totaling \$0.4 million (\$0.5 million in Fiscal 2022). The effective income tax rate for the six-month period ended September 30, 2022 also reflected favorable adjustments related the non-recurring gain following the achievement of the commercial objectives of the sale of its Bolton operations for \$0.3 million.

Net Income

Net income decreased from \$7.5 million to \$4.8 million during the quarter (or decreased from \$7.5 million to \$3.6 million excluding non-recurring items net of taxes) and from \$14.2 million to \$5.8 million (or decrease from \$14.2 million to \$4.5 million excluding non-recurring items net of taxes) during six-month period, compared to the same periods last fiscal year, mainly as a result of lower sales and the factors described above.

Earnings per Share

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Net income attributable to equity holders of the Corporation	\$ 4,799	\$ 7,756	\$ 5,764	\$ 14,598
Weighted-average number of common diluted shares outstanding, in thousands	34,554	36,576	34,590	36,755
Diluted earnings per share	\$ 0.14	\$ 0.21	\$ 0.17	\$ 0.40
Non-recurring items net of taxes	(0.04)	\$ —	(0.04)	\$ —
Adjusted earnings per share	\$ 0.10	\$ 0.21	\$ 0.13	\$ 0.40

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.

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.

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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Operating income	8,562	11,953	11,208	22,750
Non-recurring items	(1,219)	—	(1,219)	—
Adjusted operating income	\$ 7,343	\$ 11,953	\$ 9,989	\$ 22,750

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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Operating income	8,562	11,953	11,208	22,750
Amortization expense	8,873	9,204	17,653	18,456
Non-recurring items	(1,219)	—	(1,219)	—
Adjusted EBITDA	\$ 16,216	\$ 21,157	\$ 27,642	\$ 41,206

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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Net income	\$ 4,799	\$ 7,510	\$ 5,764	\$ 14,213
Non-recurring items, net of taxes	(1,219)	—	(1,219)	—
Adjusted net income	\$ 3,580	\$ 7,510	\$ 4,545	\$ 14,213
Non-controlling interests ⁽¹⁾	—	(246)	—	(385)
Adjusted net income attributable to the equity holders of the parent	\$ 3,580	\$ 7,756	\$ 4,545	\$ 14,598
<i>In dollars per share</i>				
Earnings per share - basic and diluted	\$ 0.14	\$ 0.21	\$ 0.17	\$ 0.40
Non-recurring items, net of taxes	(0.04)	—	(0.04)	—
Adjusted earnings per share	\$ 0.10	\$ 0.21	\$ 0.13	\$ 0.40

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

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 September 30, 2022 and March 31, 2022, the Corporation had US\$47.0 million drawn against the facility, worth \$64.5 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% (March 31, 2022 - 5.0%). The Corporation has the option to make early repayments as of September 2024, subject to certain fees.

Net Debt Position

As at	September 30, 2022	March 31, 2022
Long-term debt ⁽¹⁾	\$ 246,147	\$ 238,826
Less: Cash	91,693	86,692
Net debt position	\$ 154,454	\$ 152,134
Adjusted EBITDA ⁽²⁾ - trailing 12 months	69,485	83,049
Net debt to adjusted EBITDA ratio	2.2:1	1.8:1

⁽¹⁾ Excluding net deferred financing costs of \$2.3 million and \$2.3 million as at September 30, 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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Cash at beginning of periods	\$ 88,307	\$ 98,594	\$ 86,692	\$ 95,470
Cash flows related to operating activities	8,264	17,467	20,305	35,652
Cash flows related to investing activities	(7,565)	(6,255)	(15,076)	(8,016)
Cash flows related to financing activities	2,178	(6,916)	(837)	(20,120)
Effect of changes in exchange rates on cash	509	327	609	231
Cash at end of periods	\$ 91,693	\$ 103,217	\$ 91,693	\$ 103,217

Operating Activities

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

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Cash flows from operations	\$ 17,429	\$ 18,312	\$ 28,556	\$ 36,818
Net change in non-cash items	(9,165)	(845)	(8,251)	(1,166)
Cash flows related to operating activities	\$ 8,264	\$ 17,467	\$ 20,305	\$ 35,652

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 current income tax expense.

For the six month period, the decrease in cash flows from operations was mainly driven by lower throughput as 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 September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Accounts receivable	\$ (9,459)	\$ (8,486)	\$ 4,195	\$ 14,056
Inventories	(11,420)	6,671	(29,402)	475
Other assets and derivatives	(1,758)	2,051	9,156	(3,002)
Accounts payable and accrued liabilities	8,174	(3,211)	(529)	(7,722)
Provisions	(1,627)	(1,034)	(2,065)	(2,947)
Customer advances and progress billings	9,299	1,757	15,145	(2,110)
Other Liabilities	(2,374)	1,407	(4,751)	84
	\$ (9,165)	\$ (845)	\$ (8,251)	\$ (1,166)

For the quarter ended September 30, 2022, the negative net change in non-cash items mainly reflects:

- An increase in inventory levels to stabilize the production system and prepare for the sales ramp-up of the second half of the fiscal year, and,
- An increase in accounts receivable following the higher level of activity during the current quarter compared to the previous quarter.

These negative elements were partly offset by:

- An increase in accounts payable as a result of a higher overall level of activity compared to the prior quarter, and;
- An increase in customer advances and progress billings.

For the quarter ended September 30, 2021, the negative net change in non-cash items mainly reflected an increase in accounts receivable due to timing of sales, partly offset by a decrease in civil inventory.

For the six-month period ended September 30, 2022, the negative net change in non-cash items mainly reflects an increase in inventory levels to stabilize the production system and prepare for the sales ramp-up of the second half of the fiscal year, partly offset by:

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

For the six-month period ended September 30, 2021, the negative net change in non-cash items mainly reflected a seasonal decrease in accounts receivable and payable related to a lower level of activity than during the fourth quarter of fiscal 2021, as well as the utilization of restructuring provisions.

Investing Activities

The Corporation's investing activities were as follows:

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Net additions to property, plant and equipment	\$ (3,557)	\$ (4,438)	\$ (9,311)	\$ (7,710)
Net change in finite-life intangible assets	(4,008)	(1,817)	(5,765)	(2,347)
Proceeds from a business divestiture	—	—	—	2,041
Cash flows related to investing activities	\$ (7,565)	\$ (6,255)	\$ (15,076)	\$ (8,016)

The increase in investment in finite-life intangible assets mainly relates to the ongoing development of the Falcon 10X program.

The proceeds of a business divestiture last year related to the sale of the Corporation's Bolton, UK activities.

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

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Additions to property, plant and equipment	\$ 3,749	\$ 3,468	\$ 7,816	\$ 5,723
Government assistance	—	—	(14)	—
Variation in unpaid additions included in Accounts payable and accrued liabilities	(192)	1,100	1,545	2,287
Non-cash additions made through leasing agreements	—	(130)	(36)	(300)
Additions, as per statements of cash flows	\$ 3,557	\$ 4,438	\$ 9,311	\$ 7,710

Financing Activities

The Corporation's financing activities were as follows:

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Increase in long-term debt	\$ 5,549	\$ 1,962	\$ 6,239	\$ 1,962
Repayment of long-term debt	(2,194)	(2,591)	(5,096)	(9,091)
Increase in deferred financing costs	—	—	(245)	(555)
Repurchase and cancellation of shares	(1,177)	(6,831)	(2,838)	(13,485)
Issuance of common shares	—	544	1,103	1,049
Cash flows related to financing activities	\$ 2,178	\$ (6,916)	\$ (837)	\$ (20,120)

The increase in long-term debt during the quarter and six-month period relates to governmental loans.

Repayment of long-term debt during the three-month and the six-month periods ended September 30, 2022 and 2021, is comprised of lease payments and scheduled reimbursements of governmental loans.

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
Total	198,660	\$ 14.29	\$ 2,838

FREE CASH FLOW⁽¹⁾

	Three months ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
Cash flows related to operating activities	\$ 8,264	\$ 17,467	\$ 20,305	\$ 35,652
Net additions to property, plant and equipment	(3,557)	(4,438)	(9,311)	(7,710)
Net change in finite-life intangible assets	(4,008)	(1,817)	(5,765)	(2,347)
Free cash flow	\$ 699	\$ 11,212	\$ 5,229	\$ 25,595

⁽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 six-month periods compared to last year were mainly driven by the strategic increase in inventory described previously.

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	September 30, 2022	March 31, 2022	Variance	
Current assets	\$ 445,553	\$ 415,450	\$ 30,103	7.2 %
Current liabilities	202,775	179,821	22,954	12.8 %
Working capital	\$ 242,778	\$ 235,629	\$ 7,149	3.0 %
Working capital ratio	2.20	2.31		

The increase in current assets is mainly explained by a \$30.3 million increase in inventory as described under *Liquidity and Capital Resources*.

The increase in current liabilities is mainly explained by a \$15.7 million increase in customer advances and progress billings and a \$11.3 million increase in derivatives financial instruments, partly offset by a \$3.4 million reduction in accounts payable and accrued liabilities.

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

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

	September 30, 2022	March 31, 2022	Variance	
Long-term assets	\$ 378,223	\$ 397,908	\$ (19,685)	(4.9)%
Long-term liabilities	264,945	256,255	\$ 8,690	3.4 %
Shareholders' equity	\$ 356,056	\$ 377,282	\$ (21,226)	(5.6)%
Net debt-to-equity ratio ⁽¹⁾	0.43:1	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 \$19.7 million decrease in long-term assets is mainly explained by a \$14.3 million decrease in derivative financial instruments mainly due to the unwinding of cross-currency interest rate swaps.

The \$8.7 million increase in long-term liabilities is mainly explained by a \$9.7 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.

The \$21.2 million reduction in Shareholder's Equity is essentially driven by the \$20.5 million negative impact of foreign exchange variations on the valuation of the Corporation's derivative financial instruments.

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:

	September 30, 2022	March 31, 2022
USD (Canadian equivalent of US\$1.0)	1.3707	1.2496
GBP (Canadian equivalent of £1.0)	1.5098	1.6417
EUR (Canadian equivalent of €1.0)	1.3383	1.3853

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

	Quarters ended September 30,		Six months ended September 30,	
	2022	2021	2022	2021
USD (Canadian equivalent of US\$1.0)	1.3061	1.2601	1.2913	1.2441
GBP (Canadian equivalent of £1.0)	1.5350	1.7363	1.5691	1.7267
EUR (Canadian equivalent of €1.0)	1.3140	1.4851	1.3365	1.4827

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 September 30, 2022, the Corporation had forward foreign exchange contracts outstanding for a notional amount of \$359.2 million (\$341.6 million at March 31, 2022) denominated in USD, EUR and GBP. This amount includes contracts with nominal value of US\$215.4 million (US\$219.5 million at March 31, 2022) convertible into Canadian dollars at an average rate of 1.2947 (1.2888 at March 31, 2022). These contracts mature at various dates between October 2022 and June 2027, 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 September 30, 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 September 30, 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	
	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth quarter	Third Quarter
Sales	\$ 132,680	\$ 114,089	\$ 147,459	\$ 131,147	\$ 131,293	\$ 126,188	\$ 154,989	\$ 150,298
Operating income	8,562	2,646	11,463	10,545	11,953	10,797	12,229	13,362
Adjusted EBITDA ⁽¹⁾	16,216	11,426	22,149	19,694	21,157	20,049	24,975	23,731
Net income	4,799	965	11,459	6,468	7,510	6,703	8,802	8,486
Adjusted Net Income ⁽¹⁾	3,580	965	13,158	6,468	7,510	6,703	10,169	9,365
<i>In dollars per share</i>								
Earnings per share - Diluted	\$ 0.17	\$ 0.03	\$ 0.33	\$ 0.18	\$ 0.21	\$ 0.19	\$ 0.24	\$ 0.24
Adjusted earnings per share ⁽¹⁾	0.10	0.03	0.38	0.18	0.21	0.19	0.28	0.26
<i>In thousands of shares</i>								
Weighted-average number of common diluted shares outstanding	34,554	34,633	34,868	35,741	36,576	36,981	36,523	36,510

⁽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	November 10, 2022
Common shares issued and outstanding	34,391,116
Stock options issued and outstanding	1,645,500

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	
Third quarter	February 8, 2023
Fourth quarter	May 18, 2023
Fiscal 2024	
First quarter	August 8, 2023
Second quarter	November 10, 2023

Contact information

Héroux-Devtek Inc.
1111 St-Charles Street West,
Suite 600, West Tower,
Longueuil, Québec, Canada, J4K 5G4
450-679-3330
IR@HerouxDevtek.com

November 10, 2022



HEROUXDEVTEK.COM

CONTACT INFORMATION

1111 Saint-Charles street West, suite 600
West Tower, Saint-Charles Complex
Longueuil (Québec) Canada J4K 5G4
450 679-3330