

MAGELLAN

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

FOR THE THREE AND SIX MONTH PERIODS ENDED JUNE 30, 2020



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

(unaudited) (expressed in thousands of Canadian dollars, except per share amounts)	Notes	Three month period ended June 30		Six month period ended June 30	
		2020	2019	2020	2019
Revenues	8	162,167	264,082	400,980	533,966
Cost of revenues		136,824	218,992	338,865	446,055
Gross profit		25,343	45,090	62,115	87,911
Administrative and general expenses		12,597	16,290	28,273	31,590
Restructuring		709	—	709	—
Other		944	(253)	(4,994)	305
Income before interest and income taxes		11,093	29,053	38,127	56,016
Interest expense		1,108	1,291	2,308	2,359
Income before income taxes		9,985	27,762	35,819	53,657
Income taxes					
Current	9	(1,152)	2,506	895	5,311
Deferred	9	5,034	3,540	8,747	6,221
		3,882	6,046	9,642	11,532
Net income		6,103	21,716	26,177	42,125
Other comprehensive income					
Other comprehensive (loss) income that may be reclassified to profit and loss in subsequent periods:					
Foreign currency translation		(24,947)	(16,334)	9,231	(23,044)
Items not to be reclassified to profit and loss in subsequent periods:					
Actuarial loss on defined benefit pension plans, net of taxes	5	(3,007)	(3,340)	(7,766)	(3,101)
Total comprehensive (loss) income, net of taxes		(21,851)	2,042	27,642	15,980
Net income per share					
Basic and diluted	6	0.10	0.37	0.45	0.72

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE CORPORATION
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION

(unaudited) (expressed in thousands of Canadian dollars)		Notes	June 30 2020	December 31 2019
Current assets				
Cash			61,730	69,637
Trade and other receivables			154,306	177,801
Contract assets			83,682	77,967
Inventories			228,009	196,823
Prepaid expenses and other			21,343	21,127
			549,070	543,355
Non-current assets				
Property, plant and equipment			430,848	439,102
Right-of-use assets			43,384	44,692
Investment properties			2,190	2,180
Intangible assets			66,209	65,373
Goodwill			34,328	34,137
Other assets			9,499	8,770
Deferred tax assets			427	3,556
			586,885	597,810
Total assets			1,135,955	1,141,165
Current liabilities				
Accounts payable and accrued liabilities and provisions	8		125,310	151,907
Debt due within one year			44,883	48,144
			170,193	200,051
Non-current liabilities				
Long-term debt			5,772	6,876
Lease liabilities			38,771	39,794
Borrowings subject to specific conditions			23,122	24,098
Other long-term liabilities and provisions	5		30,543	20,289
Deferred tax liabilities			36,744	34,181
			134,952	125,238
Equity				
Share capital	6		254,098	254,440
Contributed surplus			2,044	2,044
Other paid in capital			13,565	13,565
Retained earnings			522,956	516,911
Accumulated other comprehensive income			34,770	25,539
Equity attributable to equity holders of the Corporation			827,433	812,499
Non-controlling interest			3,377	3,377
Total equity			830,810	815,876
Total liabilities and equity			1,135,955	1,141,165

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE CORPORATION
CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

(unaudited) (expressed in thousands of Canadian dollars)	Attributable to equity holders of the Corporation					Total	Non- controlling interest	Total equity
	Share capital	Contributed surplus	Other paid in capital	Retained earnings	Foreign currency translation			
December 31, 2019	254,440	2,044	13,565	516,911	25,539	812,499	3,377	815,876
Net income for the period	—	—	—	26,177	—	26,177	—	26,177
Other comprehensive (loss) income for the period	—	—	—	(7,766)	9,231	1,465	—	1,465
Common share repurchase	(342)	—	—	(144)	—	(486)	—	(486)
Common share dividend	—	—	—	(12,222)	—	(12,222)	—	(12,222)
June 30, 2020	254,098	2,044	13,565	522,956	34,770	827,433	3,377	830,810
December 31, 2018	254,440	2,044	13,565	473,246	44,378	787,673	—	787,673
Business combination	—	—	—	—	—	—	2,344	2,344
Net income for the period	—	—	—	42,125	—	42,125	—	42,125
Other comprehensive loss for the period	—	—	—	(3,101)	(23,044)	(26,145)	—	(26,145)
Common share dividend	—	—	—	(11,642)	—	(11,642)	—	(11,642)
June 30, 2019	254,440	2,044	13,565	500,628	21,334	792,011	2,344	794,355

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE CORPORATION
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS

(unaudited) (expressed in thousands of Canadian dollars)	Notes	Three month period ended June 30		Six month period ended June 30	
		2020	2019	2020	2019
Cash flow from operating activities					
Net income		6,103	21,716	26,177	42,125
Amortization/depreciation of intangible assets, right-of-use assets and property, plant and equipment		13,723	13,622	28,232	27,152
(Gain) loss on disposal of property, plant and equipment		(62)	38	(43)	(47)
Gain on disposal of joint venture investment		—	—	—	(881)
Increase in defined benefit plans		232	287	348	133
Accretion		795	628	1,609	1,173
Deferred taxes		4,365	1,555	7,427	3,373
Loss (income) on investments in joint ventures		30	(111)	(106)	(281)
Changes to non-cash working capital		21,553	(12,150)	(35,897)	(39,106)
Net cash provided by operating activities		46,739	25,585	27,747	33,641
Cash flow from investing activities					
Business combination, net of cash acquired		—	—	—	(2,661)
Purchase of property, plant and equipment		(2,475)	(8,839)	(6,685)	(18,346)
Proceeds from disposal of property, plant and equipment		107	124	107	359
Increase in intangible and other assets		(4,216)	(3,163)	(7,207)	(9,229)
Net cash used in investing activities		(6,584)	(11,878)	(13,785)	(29,877)
Cash flow from financing activities					
Decrease in debt due within one year		(951)	(1,600)	(3,948)	(8,484)
Decrease in long-term debt		(646)	(802)	(1,238)	(1,449)
Lease liability payments		(1,709)	(783)	(3,467)	(1,684)
Decrease in long-term liabilities and provisions		(547)	(144)	(802)	(179)
Increase (decrease) in borrowings subject to specific conditions, net		10	(822)	39	(822)
Common share repurchases	6	(486)	—	(486)	—
Common share dividend	6	(6,110)	(5,821)	(12,222)	(11,642)
Net cash used in financing activities		(10,439)	(9,972)	(22,124)	(24,260)
Increase (decrease) in cash during the period					
		29,716	3,735	(8,162)	(20,496)
Cash at beginning of the period		32,430	38,463	69,637	63,316
Effect of exchange rate differences		(416)	(825)	255	(1,447)
Cash at end of the period		61,730	41,373	61,730	41,373

See accompanying notes to condensed consolidated interim financial statements

MAGELLAN AEROSPACE CORPORATION

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(Unaudited, expressed in thousands of dollars except share and per share data)

NOTE 1. DESCRIPTION OF BUSINESS AND NATURE OF OPERATIONS

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

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

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") and using the same accounting policies and methods as were used for the Corporation's consolidated financial statements and the notes thereto for the year ended December 31, 2019, except for the new accounting pronouncements which have been adopted as disclosed in note 3.

These unaudited condensed consolidated interim financial statements do not include all the information required for full annual financial statements and should be read in conjunction with the Corporation's annual financial statements for the year ended December 31, 2019, which are available at www.sedar.com and on the Corporation's website at www.magellan.aero.

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

These condensed consolidated interim financial statements were authorized for issuance by the Board of Directors of the Corporation on August 7, 2020.

NOTE 3. ADOPTION OF NEW STANDARDS, INTERPRETATIONS AND AMENDMENTS

The Corporation has adopted the new and amended pronouncements issued by International Financial Reporting Standards ("IFRS") and the International Financial Reporting Interpretations Committees ("IFRIC") as listed below as at January 1, 2020, in accordance with the transitional provisions outlined in the respective standards.

- Amendments to IAS 1, *Presentation of Financial Statements* and IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*, clarifying the definition of "material".
- Amendments to IFRS 3, *Business Combination*, to help entities determine whether an acquired set of activities and assets is a business or not.
- On May 28, 2020, the IASB published 'Covid-19-Related Rent Concessions (Amendment to IFRS 16, *Leases*)' amending the standard to provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification. The amendment is effective for annual reporting periods beginning on or after June 1, 2020.

The IASB has issued new standards and amendments to existing standards. These changes are not yet adopted by the Corporation and could have an impact on future periods.

- On January 23, 2020, the IASB issued amendments to IAS 1 *Presentation of Financial Statements* (the "amendments") to clarify the requirements for classifying liabilities as current or non-current. More specifically, the amendments specify that the conditions which exist at the end of the reporting period are those which will be used to determine if a right to defer settlement of a liability exists; management expectations about events after the balance sheet date, for example on whether a covenant will be breached, or whether early settlement will take place, are not relevant; and the amendments clarify the situations that are considered settlement of a liability. The new guidance will be effective for annual periods starting on or after January 1, 2022.
- On May 14, 2020, the IASB issued amendments to IAS 16, *Property, Plant and Equipment – Proceeds before Intended Use*, regarding proceeds from selling items produced while bringing an asset into the location and condition necessary for it to be capable of operating in the manner intended by management. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

- On May 14, 2020, the IASB issued amendments to IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, clarifying the standard regarding costs a company should include as the cost of fulfilling a contract when assessing whether a contract is onerous. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

NOTE 4. BANK INDEBTEDNESS

The Corporation has a multi-currency operating credit facility with a syndicate of banks, with a Canadian dollar limit of \$75,000. Extensions of the facility are subject to mutual consent of the syndicate of lenders and the Corporation. The credit agreement also includes a \$75,000 uncommitted accordion provision which will provide the Corporation with the option to increase the size of the operating credit facility. On October 28, 2019 the Corporation extended the credit agreement to September 13, 2021. As at June 30, 2020, the Corporation was debt-free under its credit facility. Bank indebtedness bears interest at the bankers' acceptance or LIBOR rates plus 1.00%. At June 30, 2020, the Corporation had letters of credit outstanding totalling \$4,648 such that \$70,352 was unused and available. A fixed and floating charge debenture on accounts receivable, inventories and property, plant and equipment is pledged as collateral for the operating credit facility.

NOTE 5. EMPLOYEE FUTURE BENEFITS

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

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

	June 30 2020	December 31 2019
Pension Benefit Plans	22,785	12,000
Other Benefit Plan	1,000	1,009
	23,785	13,009

As at June 30, 2020, the Corporation changed the assumed discount rate for the Canadian pension plans to 2.7% from the 3.7% and 3.1% rates used in calculating the pension obligation as at March 31, 2020 and December 31, 2019, respectively, as the market interest rates of high-quality, fixed rate debt securities decreased at the end of the period. The assumed discount rate for the U.S. pension plan decreased to 2.5% as at June 30, 2020 from 3.1% rates determined at both March 31, 2020 and December 31, 2019. In addition, the return on plan assets exceeded the expected return during the three month period ended June 30, 2020 although underperformed against the expected return during the six month period ended June 30, 2020. The change in the discount rate assumptions and the difference between the actual and expected rate of return on the plan assets resulted in an actuarial loss of \$3,007 and \$7,766, net of taxes of \$1,042 and \$2,692, respectively, recorded in other comprehensive income in the three and six month periods ended June 30, 2020.

NOTE 6. SHARE CAPITAL

Net income per share

	Three month period ended June 30		Six month period ended June 30	
	2020	2019	2020	2019
Net income	6,103	21,716	26,177	42,125
Weighted average number of shares	58,180	58,209	58,192	58,209
Basic and diluted net income per share	0.10	0.37	0.45	0.72

Dividends

On March 31, 2020 and June 30, 2020, the Corporation paid quarterly dividends on 58,209,001 and 58,194,891 common shares respectively, of \$0.105 per common share, amounting to \$12,222 in the aggregate.

Subsequent to June 30, 2020, the Corporation declared dividends to holders of common shares in the amount of \$0.105 per common share payable on September 30, 2020, for shareholders of record at the close of business on September 16, 2020.

Normal Course Issuer Bid

On May 25, 2020, the Toronto Stock Exchange ("TSX") accepted the Corporation's intention to commence a normal course issuer bid ("NCIB") which allows the Corporation to repurchase up to 2,910,450 of the Corporation's issued and outstanding common shares (the "Shares") in the open market or otherwise permitted by the TSX. Common shares purchased by the Corporation are cancelled. The program commenced on May 27, 2020 and will terminate on May 26, 2021, or on such earlier date as the Corporation completes its purchase pursuant to the NCIB. During the three month period ended June 30, 2020, 78,160 Shares were purchased for cancellation for \$486 at a volume weighted average price paid of \$6.21 per Share.

NOTE 7. FINANCIAL INSTRUMENTS

Fair value hierarchy

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

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

Fair values

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

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

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

Foreign exchange contracts

The Corporation enters into foreign forward exchange contracts to mitigate future cash flow exposures in United States dollars. Under these contracts the Corporation is obliged to purchase specific amounts at predetermined dates and exchange rates. These contracts are matched with anticipated operational cash flows in United States dollars. There were no outstanding forward foreign exchange contracts as at June 30, 2020.

Long-term debt

The carrying amount of the Corporation's long-term debt of \$8,215 would approximate its fair value as at June 30, 2020.

Borrowings subject to specific conditions

As at June 30, 2020, the Corporation has recognized \$25,686 as the amount repayable to Canadian government agencies. The contributions are repayable as future royalty payments; a liability is recorded for the amounts received that will be repaid based on future estimated sales.

Collateral

As at June 30, 2020, the carrying amount of the financial assets that the Corporation has pledged as collateral for its long-term debt facilities was \$44,358.

NOTE 8. SEGMENTED INFORMATION

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

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

	Three month period ended June 30		Six month period ended June 30	
	2020	2019	2020	2019
Sale of goods	129,014	229,803	330,232	459,074
Services	33,153	34,279	70,748	74,892
	162,167	264,082	400,980	533,966

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

	Three month period ended June 30		Six month period ended June 30	
	2020	2019	2020	2019
At a point of time	102,168	154,583	255,110	327,642
Over time	59,999	109,499	145,870	206,324
	162,167	264,082	400,980	533,966

Advance payments received for contracts in progress in excess of revenue recognized were recorded as contract liabilities and included in accounts payable, accrued liabilities and provisions on the condensed consolidated interim statement of financial position. As at June 30, 2020 contract liabilities were \$16,626 [December 31, 2019 - \$10,605].

Revenues from the Corporation's three and two largest customers accounted for 38.6% and 32.0% respectively of total sales for the three and six month periods ended June 30, 2020 [June 30, 2019 – two largest customers accounted for 38.4% and 40.2% respectively of total sales for the three and six month periods ended].

Geographic segments:

	2020				Three month period ended June 30 2019			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Revenue	83,595	45,288	33,284	162,167	96,185	83,128	84,769	264,082
Export revenue ¹	59,379	6,681	3,372	69,432	61,183	18,903	27,638	107,724

	2020				Six month period ended June 30 2019			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Revenue	177,838	110,006	113,136	400,980	186,886	167,947	179,133	533,966
Export revenue ¹	124,620	19,683	28,942	173,245	123,838	36,115	59,033	218,986

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

	June 30, 2020				December 31, 2019			
	Canada	United States	Europe	Total	Canada	United States	Europe	Total
Property, plant and equipment, right-of-use assets, intangible assets and goodwill	193,367	197,173	184,229	574,769	200,484	191,411	191,409	583,304

NOTE 9. TAXATION

The Corporation's tax expense is calculated by using the rates applicable in each of the tax jurisdictions that the Corporation operates in, adjusted for the main permanent differences identified. The effective tax rate for the three and six month periods ended June 30, 2020 was 38.9% and 26.9% respectively [21.8% and 21.5% respectively for the three and six month periods ended June 30, 2019]. The difference between the effective tax rate and the standard tax rate is primarily attributable to the change in mix of income and loss across the different jurisdictions in which the Corporation operates.

NOTE 10. MANAGEMENT OF CAPITAL

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

Total managed capital as at June 30, 2020 of \$871,791 is comprised of shareholders' equity attributable to equity holders of the Corporation of \$827,433 and interest-bearing debt of \$44,358.

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

NOTE 11. CONTINGENT LIABILITIES AND COMMITMENTS

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

At June 30, 2020 capital commitments in respect of purchase of property, plant and equipment totalled \$14,081, all of which had been ordered. There were no other material capital commitments at the end of the period.

NOTE 12. COVID-19

In March 2020 the World Health Organization declared coronavirus COVID-19 a global pandemic. This contagious disease outbreak, which has continued to spread, has resulted in governments worldwide enacting emergency measures to combat the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods and social distancing, have caused a material disruption to businesses globally resulting in an economic slowdown and decreased demand in the aerospace industry.

As an emerging risk, the duration and full financial effect of the COVID-19 pandemic is unknown at this time, as is the efficacy of the government and central bank interventions, the Corporation's business continuity plan and other mitigating measures. Any estimate of the length and severity of these developments is therefore subject to significant uncertainty, and accordingly estimates of the extent to which the COVID-19 pandemic may materially and adversely affect the Corporation's operations, financial results and condition in future periods are also subject to significant uncertainty. Therefore, uncertainty about judgments, estimates and assumptions made by management during the preparation of the Corporation's consolidated financial statements related to potential impacts of the COVID-19 outbreak on revenue, expenses, assets, liabilities, and note disclosures could result in a material adjustment to the carrying value of the asset or liability affected.

The Corporation will continue to closely monitor the COVID-19 situation and should the duration, spread or intensity of the pandemic further develop in 2020, the supply chain and customer demand will likely be further affected. These factors may further impact the Corporation's operating plan, its liquidity and cash flows.

In response to COVID-19, the Government of Canada announced the Canada Emergency Wage Subsidy ("CEWS") program in March 2020. CEWS provides a wage subsidy on eligible remuneration, subject to a maximum per employee, to eligible employers based on meeting certain eligibility criteria. The Company has determined that it has qualified for this subsidy. Included in personnel and compensation expenses in the second quarter of 2020 is \$8,612 relating to the CEWS program in order to reduce the expense that the grant is intended to offset.