Condensed Consolidated Statements of Financial Position

(unaudited) (tabular amounts in thousands of dollars)	As at March 31, 2018	December 31, 2017
Assets		
Current assets		
Cash	$ 10,830	$ 10,772
Accounts receivable	61,628	59,170
Inventories	40,911	38,340
Income taxes receivable	1,466	1,701
Prepaid expenses and other assets	3,187	3,419
Total current assets	118,022	113,402
Non-current assets		
Long-term lease and note receivable	4,772	4,605
Property, plant and equipment (note 4)	31,954	32,276
Investment in properties	1,044	1,044
Investment in joint venture (note 5)	12,215	12,158
Deferred tax assets	817	776
Goodwill	17,476	17,022
Intangible assets (note 6)	10,887	11,166
Total non-current assets	79,165	79,047
Total assets	$ 197,187	$ 192,449
Liabilities		
Current liabilities		
Bank operating lines of credit	$ 32,313	$ 27,755
Accounts payable and accrued liabilities	41,644	45,647
Income tax liabilities	43	137
Provisions	400	457
Total current liabilities	74,400	73,996
Non-current liabilities		
Provisions	100	100
Deferred tax liabilities	3,329	3,342
Total non-current liabilities	3,429	3,442
Total liabilities	$ 77,829	$ 77,438
Shareholders' Equity		
Share capital	14,070	13,986
Contributed surplus	2,586	2,600
Accumulated other comprehensive income (note 8)	7,522	1,916
Retained earnings	95,180	96,346
Total shareholders' equity attributable to equity holders of the Company	$ 119,358	$ 114,848
Non-controlling interests (note 9)	–	163
Total shareholder's equity	119,358	115,011
Total liabilities and shareholders' equity	$ 197,187	$ 192,449

See accompanying notes to condensed consolidated interim financial statements

Condensed Consolidated Statements of Earnings

(unaudited) (tabular amounts in thousands of dollars, except per share amounts)	Three Months Ending March 31, 2018	April 1, 2017
Sales (note 10)	$ 73,073	$ 72,362
Cost of sales	55,997	54,698
Gross margin	17,076	17,664
Selling and distribution	8,605	8,205
General and administrative	6,498	6,238
Restructuring charges (note 11)	–	816
Earnings from operations	1,973	2,405
Finance and other costs		
Interest expense	296	316
Foreign exchange (gain) loss	(162)	67
Share of loss of investment in joint venture (note 5)	279	257
Other	33	33
Net finance and other costs	446	673
Earnings before income taxes	1,527	1,732
Income tax expense	632	648
Net earnings	$ 895	$ 1,084
Net earnings attributable to non-controlling interests	–	18
Net earnings attributable to the equity holders of the Company	895	1,066
Net earnings	$ 895	$ 1,084
Earnings per share		
Basic earnings per share (dollars)	$ 0.08	$ 0.09
Diluted earnings per share (dollars)	$ 0.08	$ 0.09

See accompanying notes to condensed consolidated interim financial statements

Condensed Consolidated Statements of Comprehensive Income

(unaudited) (tabular amounts in thousands of dollars)	Three Months Ending March 31, 2018	Three Months Ending April 1, 2017
Net earnings	$ 895	$ 1,084
Other comprehensive income		
Foreign currency translation differences for foreign operations	5,597	1,683
Total comprehensive income for the period	$ 6,492	$ 2,767
Attributable to:		
Equity holders of the Company	$ 6,492	$ 2,574
Non-controlling interest	–	193
Total comprehensive income for the period	$ 6,492	$ 2,767

See accompanying notes to condensed consolidated interim financial statements

Condensed Consolidated Statements of Changes in Equity

(unaudited) For the three months ended March 31, 2018

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	NON-CONTROLLING INTEREST	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2018	$ 13,986	$ 2,600	$ 1,916	$ 96,346	$ 163	$ 115,011
Total comprehensive income for the year						
Net earnings	–	–	–	895	–	895
Other comprehensive income						
Foreign currency translation differences related to joint venture (note 5)	–	–	335	–	–	335
Foreign currency translation differences (note 8)	–	–	5,262	–	–	5,262
Total other comprehensive income	–	–	5,597	–	–	5,597
Total comprehensive income for the year	–	–	5,597	895	–	6,492
Transactions with owners, recorded directly in equity						
Stock options exercised (note 7)	84	(14)	–	–	–	70
Dividends to equity holders (note 7)	–	–	–	(704)	–	(704)
Non-controlling interest (note 9)	–	–	9	(1,357)	(163)	(1,511)
Total transactions with shareholders	84	(14)	9	(2,061)	(163)	(2,145)
Balance at March 31, 2018	$ 14,070	$ 2,586	$ 7,522	$ 95,180	$ –	$ 119,358

*AOCI – Accumulated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Condensed Consolidated Statements of Changes in Equity

(unaudited) For the three months ended April 1, 2017

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	NON-CONTROLLING INTEREST	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2017	$ 13,843	$ 2,605	$ 10,992	$ 93,001	$ 212	$ 120,653
Total comprehensive income for the year						
Net earnings	–	–	–	1,066	18	1,084
Other comprehensive income						
Foreign currency translation differences related to joint venture (note 5)	–	–	782	–	–	782
Foreign currency translation differences (note 8)	–	–	726	–	175	901
Total other comprehensive income	–	–	1,508	–	175	1,683
Total comprehensive income for the year	–	–	1,508	1,066	193	2,767
Transactions with owners, recorded directly in equity						
Share-based payment transactions	–	14	–	–	–	14
Dividends to equity holders (note 7)	–	–	–	(702)	–	(702)
Total transactions with shareholders	–	14	–	(702)	–	(688)
Balance at April 1, 2017	$ 13,843	$ 2,619	$ 12,500	$ 93,365	$ 405	$ 122,732

*AOCI – Accumulated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Condensed Consolidated Statements of Cash Flows

(unaudited) tabular amounts in thousands of dollars)	Three Months Ending March 31, 2018	Three Months Ending April 1, 2017
Cash flows from operating activities		
Net earnings	$ 895	$ 1,084
Adjustments for:		
Share of loss of investment in joint venture	279	257
Amortization of property, plant and equipment	1,157	1,353
Amortization of intangible assets	651	501
Provisions	(57)	30
Interest expense	296	316
Income tax expense	632	648
Change in unrealized (loss) gain on derivatives	(317)	83
Stock-based compensation expense	–	17
	3,536	4,289
Change in non-cash working capital (note 13)	(4,952)	(11,455)
Cash (used in) generated by operating activities	(1,416)	(7,166)
Income tax paid	(491)	(456)
Net cash used in operating activities	(1,907)	(7,622)
Cash flows from investing activities		
Purchase of non-controlling interest (note 9)	(1,511)	–
Investment in joint venture	–	(626)
Acquisition of property, plant and equipment	(345)	(520)
Acquisition of intangible assets	(168)	(143)
Cash used in investing activities	(2,024)	(1,289)
Cash flows from financing activities		
Advances (repayments) of borrowings	4,558	(3,275)
Receipt of lease receivable payment	70	–
Issue of common shares	70	–
Cash dividends paid (note 7)	(704)	(702)
Interest paid	(296)	(316)
Cash generated (used) in financing activities	3,698	(4,293)
Foreign exchange on cash held in a foreign currency	291	(228)
Increase (decrease) in cash	58	(13,432)
Cash and cash equivalents at beginning of period	10,772	25,189
Cash and cash equivalents at end of period	$ 10,830	$ 11,757

See accompanying notes to condensed consolidated interim financial statements

Notes to the Condensed Consolidated Financial Statements

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

The accompanying unaudited interim financial statements of Hammond Power Solutions Inc., ("HPS" or the "Company") have been prepared by and are the responsibility of the Company's Management. The Company's independent auditor has not performed a review of these financial statements in accordance with standards adopted by the Canadian Institute of Charted Accountants ("CICA") for a review of interim financial statements by an entity's auditor.

1. Reporting entity

Hammond Power Solutions Inc. is a company domiciled in Canada. The address of the Company's registered office is 595 Southgate Drive Guelph, Ontario. The Company's Class A subordinate voting shares are listed on the Toronto Stock Exchange and trade under the symbol HPS.A.

The Condensed Consolidated Interim Financial Statements of the Company as at and for the first quarter ended March 31, 2018 comprise the Company and its subsidiaries (together referred to as the "Group" and individually as "Group entities"). The Group is primarily involved in the design and manufacture of custom electrical magnetics, cast resin, custom liquid filled distribution and power transformers and standard electrical transformers, serving the electrical and electronic industries. The Company has manufacturing plants in Canada, the United States ("U.S."), Mexico, Italy, and India, the latter being Hammond Power Solutions Private Limited, a subsidiary in which the Company now holds an 100% equity ownership. The Company also holds a 55% economic interest in a joint venture located in Mexico called Correfficient de R.L. de C.V. ("Corefficient").

2. Basis of preparation

(a) Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with requirements of IAS 34, Interim Financial Reporting and do not include all of the information required for full annual financial statements.

These condensed consolidated interim financial statements were approved by the Board of Directors on May 3, 2018.

(b) Use of estimates and judgments

The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In preparing these condensed consolidated interim financial statements, the significant judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended December 31, 2017.

3. Summary of significant accounting policies:

These condensed consolidated interim financial statements should be read in conjunction with the Group's 2017 annual audited financial statements, which are available on the System for Electronic Document Analysis and Retrieval ("SEDAR"). The significant accounting policies applied by the Company in these condensed consolidated interim financial statements are the same as those applied by the Company in its Consolidated Financial Statements as at and for the year ended December 31, 2017, with the exception of items noted below:

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

Changes to accounting policies

Classification and Measurement of Share-Based Payment Transactions

On June 20, 2016 the IASB issued amendments to IFRS 2 Share-Based Payments clarifying how to account for certain types of share-based payment transactions. The amendments apply for annual periods beginning on or after January 1, 2017. As a practical simplification, the amendments can be applied prospectively. Retrospective, or early, application is permitted if information is available without the use of hindsight.

The amendments provide requirements on the accounting for:

- The effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments;
- Share-based payment transactions with a net settlement feature for withholding tax obligations; and
- A modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity settled.

The Group intends to adopt the amendments to IFRS 2 in its consolidated financial statements for the annual period ending December 31, 2018. The adoption of the amendment did not have a material impact on the consolidated financial statements.

Revenue from contracts with customers

On May 28, 2014 the IASB issued IFRS 15, Revenue from Contracts with Customers. This new standard is effective for annual and interim periods beginning on or after January 1, 2018. IFRS 15 will replace IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programs, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfer of Assets from Customers and SIC 31 Revenue – Barter Transactions Involving Advertising Services. On April 12, 2016, the IASB issued Clarification to IFRS 15, Revenue from Contracts with Customers, which is effective at the same time as IFRS 15.

The standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue – at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized.

Transition considerations

IFRS 15 can be applied using one of the following two methods: retrospectively to each prior reporting period presented in accordance with IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, or retrospectively with the cumulative effect of initially applying IFRS 15 recognized in opening retained earnings at the date of initial application (the "modified retrospective method"). The Group decided to adopt IFRS 15 using the modified retrospective method, without restatement of comparative figures.

IFRS 15 provides for certain optional practical expedients, including upon the initial adoption of the standard. The Group applied the following practical expedients upon adoption of IFRS 15 on January 1, 2018:

- Completed contract – the Group applied IFRS 15 retrospectively only to contracts that were not completed contracts as at January 1, 2018. There were no uncompleted contracts at January 1, 2018.
- Contract modifications – the Group did not apply IFRS 15 retrospectively to contract modifications that occurred before January 1, 2018.

The adoption of IFRS 15 did not have a material impact on the consolidated financial statements.

Financial instruments

On July 24, 2014 the IASB issued the complete IFRS 9 Financial Instruments (IFRS 9 (2014)). The mandatory effective date of IFRS 9 is for annual and interim periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions. The restatement of prior periods is not required and is only permitted if information is available without the use of hindsight. IFRS 9 (2014) introduces new requirements for the classification and measurement of financial assets. Under IFRS 9 (2014), financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. The standard introduces additional changes relating to financial liabilities. It also amends the impairment model by introducing a new 'expected credit loss' model for calculating impairment.

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

IFRS 9 (2014) also includes a new general hedge accounting standard which aligns hedge accounting more closely with risk management. This new standard does not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness, however it will provide more hedging strategies that are used for risk management to qualify for hedge accounting and introduce more judgment to assess the effectiveness of a hedging relationship. Special transitional requirements have been set for the application of the new general hedging model. The Group has adopted IFRS 9 (2014) in its consolidated financial statements for the annual and interim periods beginning on January 1, 2018.

The adoption of IFRS 9 did not have a material impact on the consolidated financial statements.

4. Property, plant and equipment

The Group had acquisitions of fixed assets for the three months ended March 31, 2018 in the amount of $345,000 of machinery and equipment (2017 – $520,000).

5. Joint venture

The Company has a 55% economic and voting interest in Corefficient. By virtue of the contractual arrangement with National Material L.P., the other shareholder in Corefficient, decisions about significant, relevant, operating and strategic activities require the unanimous consent of both parties, and therefore the Company jointly controls Corefficient. Distributions of dividends and returns of capital from Corefficient are subject to unanimous Corefficient shareholder approval. Accordingly, the Company has treated its investment in Corefficient as a joint arrangement. Corefficient's principal place of business is in Monterrey, Mexico. The carrying value of the Company's interest in Corefficient is as follows:

	March 31, 2018	December 31, 2017
Cost of investment in joint venture	$ 19,304	$ 19,304
Cumulative share of loss in investment in joint venture	(4,056)	(3,778)
Foreign currency translation differences related to the joint venture	(3,033)	(3,368)
	$ 12,215	$ 12,158

Selected financial information relating to Corefficient is as follows:

	March 31, 2018	December 31, 2017
Cash	$ **2,121**	$ 2,261
Trade and other receivables	**5,247**	5,546
Inventories	**879**	1,050
Other current assets	**174**	162
Total current assets	$ **8,421**	$ 9,019
Non-current assets	**16,606**	16,487
Total assets	$ **25,027**	$ 25,506
Current liabilities	$ **3,128**	$ 3,671
Non-current liabilities	**–**	–
Total liabilities	$ **3,218**	$ 3,671

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

	Three Months Ending			
		March 31, 2018		April 1, 2017
Revenue	$	**5,910**	$	3,897
Loss for the period		**507**		625

The loss for the three months ended March 31, 2018 includes depreciation and amortization expense of $520,000 (Quarter 1, 2017 – $498,000), interest income of $73,000 (Quarter 1, 2017 – $17,000) and an income tax expense of $7,000 (Quarter 1, 2017 – recovery of $268,000) related to Corefficient.

6. Intangible assets

The Group had acquisitions of intangible assets for the three months ended March 31, 2018 in the amount of $168,000 (Quarter 1, 2017 – $143,000), for the addition of software. None of the intangible assets have been developed internally.

7. Share capital

(a) Dividends:

The following dividends were declared and paid by the Company:

	Three Months Ending			
		March 31, 2018		April 1, 2017
6 cents per Class A common share (2017: 6 cents)	$	537	$	535
6 cents per Class B common share (2017: 6 cents)		167		167
	$	704	$	702

(b) Stock option plan:

There were no stock options issued during the three months ended March 31, 2018 or April 1, 2017. Stock-based compensation recognized the amount credited to contributed surplus during the period is nil (Quarter 1, 2017 – $14,000) and relates to options granted in prior years that vested during the period.

During the three months ended March 31, 2018 there were 10,000 options exercised, 5,000 at an exercise price of $6.62 and 5,000 at an exercise price of $7.50.

(c) Deferred Stock Units:

During 2017, the Company enacted a deferred share unit plan (the “DSU Plan”) in order to issue deferred share units (“DSUs”) to non-employee directors and senior-executives (collectively “participants”) of HPS. The DSU Plan was adopted to allow participants the opportunity to defer compensation and encourage a sense of ownership in HPS. Under the DSU Plan, participants may elect to defer compensation and receive DSUs equal to the value of the deferred compensation. The first DSUs were issued in March 2017. The number of DSUs was determined by dividing the amount of deferred compensation by the Fair Market Value of DSUs, defined under the DSU Plan as the weighted average closing price of HPS shares for the five business days immediately preceding the relevant date. Upon the occurrence of the Redemption Event, which could include ceasing to hold any position in the Company and/or any Subsidiary or upon death of the participant, the affected participant will be entitled to receive a lump sum cash payment, net of applicable withholding taxes, equal to the product of number of DSUs held by that participant and the Fair Market Value on the date of the Redemption Event. The DSUs do not contain any vesting conditions or forfeiture provisions, as they are issued in exchange for past service. Under the DSU Plan, outstanding DSUs as at the record date, are increased by the dividend rate whenever dividends are paid to shareholders.

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

The DSUs issued are not performance based.

The movement in DSUs for the three months ended:

	March 31, 2018			March 31, 2017		
	Number of DSUs	Weighted Average Share Price	Carrying Amount	Number of DSUs	Weighted Average Share Price	Carrying Amount
Opening Balance	32,578	$ 9.16	$ 285	–	$ –	$ –
DSUs Issued	9,418	$ 9.44	105	7,481	$ 6.30	47
Balance at March 31, 2018	41,996	$ 9.30	$ 391	7,481	$ 6.30	$ 47

Given the DSUs are cash settled instruments, they have been included within accounts payable and accrued liabilities in the condensed consolidated statement of financial position.

8. Accumulated Other Comprehensive Income

Changes to the accumulated other comprehensive income ("AOCI") balance include foreign currency translation differences relating to the net assets of foreign operations. Total other comprehensive income for the three months ended March 31, 2018 was $5,597,000 (Quarter 1, 2017 – $1,508,000), resulting in an ending balance as at March 31, 2018 of accumulated other comprehensive income of $7,522,000 (April 1, 2017 – $12,500,000).

9. Non-controlling interest

On January 10, 2018, the terms and conditions under an agreement to acquire the remaining 15% economic interest of Hammond Power Solutions Private Limited from a minority shareholder, which included the mutually agreed upon resignation from the Board of the minority shareholder, at a discounted amount of 76,933,000 INR (approximately $1,511,000 Canadian dollars) were fulfilled, resulting in the Company's equity ownership in Hammond Power Solutions Private Limited becoming 100%. As a result, the Company recorded an elimination of non-controlling interests on the condensed consolidated statement of financial position in the amount of $163,000, a reduction in retained earnings of $1,357,000, and an increase in accumulated other comprehensive income in the amount of $9,000.

10. Sales

	Three Months Ending	
	March 31, 2018	April 1, 2017
Canada	$ 20,720	$ 16,939
United States and Mexico	44,712	42,671
Italy	2,676	4,784
India	4.965	7,968
	$ 73,073	$ 72,362

As at March 31, 2018 the Company has deferred revenue of $1 (2016 - $55).

Three months ended March 31, 2018 and April 1, 2017 (amounts in thousands of dollars except share and per share amounts)

11. Restructuring charges

During 2017, the Company incurred restructuring charges. These charges were comprised of severance and benefit costs relating to workforce reductions. The restructuring activities were undertaken to adjust the Company's cost structure, to streamline various support activities in consideration of the current and expected industry market conditions. These charges are reported in the restructuring charge line within the consolidated statement of earnings.

The following table highlights the activity and balance of the restructuring charges for the three month period ending March 31, 2018:

	Employee Termination Benefits	
Opening balance January 1, 2018	$	329
Cash payments		(188)
Accrued balance at March 31, 2018	$	141

12. Related party transactions

Related parties

Arathorn Investments Inc. beneficially owns 2,778,300 (2017 – 2,778,300) Class B common shares of the Company, representing 100% of the issued and outstanding Class B common shares of the Company and 1,057,918 (2017 – 1,055,287) Class A subordinate voting shares of the Company, representing approximately 11.8% (2017 – 11.8%) of the issued and outstanding Class A subordinate voting shares of the Company and as a result controls the Company. William G. Hammond, Chief Executive Officer and Chairman of the Company, owns all of the issued and outstanding shares of Arathorn Investments Inc. Total dividends paid during the quarter, directly and indirectly to William G. Hammond were $230,000 (Quarter 1 2017– $230,000).

Transactions with key management personnel

During the three months ended March 31, 2018, the Company purchased $69,000 (2017 – $55,000) of inventory from ILSCO of Canada Limited ("ILSCO"), a company in which HPS director David J. FitzGibbon serves as a Vice Chairman. The Company purchases a component part from ILSCO, which is utilized in the manufacture of transformers. The purchases were measured at the exchange amount. Accounts payable and accrued liabilities include $30,000 (2017 – $29,000), which is owed to this company.

13. Change in non-cash operating working capital

The table below depicts the receipt of (use of) cash for working capital purposes by the Company:

	Three Months Ending			
		March 31, 2018		April 1, 2017
Accounts receivable	$	(2,458)	$	(10,308)
Inventories		(2,571)		(1,476)
Prepaid expenses		345		160
Accounts payable and accrued liabilities		(3,736)		(282)
Foreign exchange		3,468		451
	$	(4,952)	$	(11,455)