

Management's Responsibility for Financial Statements

The Consolidated Financial Statements are the responsibility of the management of Hammond Power Solutions Inc. These statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), using management's best estimates and judgments where appropriate.

Management is responsible for the reliability and integrity of the Consolidated Financial Statements, the Notes to Consolidated Financial Statements and other financial information contained in the report. In the preparation of these statements, estimates were sometimes necessary because a precise determination of certain assets and liabilities is dependent on future events. Management believes such estimates have been based on careful judgment and have been properly reflected in the accompanying Consolidated Financial Statements. Management is responsible for the maintenance of a system of internal controls designed to provide reasonable assurances that the assets are safeguarded and that accounting systems provide timely, accurate and reliable financial information.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities through the Audit Committee of the Board, which is composed of all of the directors, of whom seven are non-management directors. The Audit Committee meets periodically with management and the auditors to satisfy itself that management's responsibilities are properly discharged, to review the Consolidated Financial Statements and to recommend approval of the Consolidated Financial Statements to the Board of Directors.

KPMG LLP, the independent auditors appointed by the shareholders, has audited the Company's Consolidated Financial Statements in accordance with Canadian generally accepted auditing standards, and their report follows. The independent auditors have full and unrestricted access to the Audit Committee to discuss their audit and related findings as to the integrity of the financial reporting process.



William G. Hammond
Chairman of the Board
& Chief Executive Officer



Christopher R. Huether
Corporate Secretary
& Chief Financial Officer

March 25, 2021

To the Shareholders of Hammond Power Solutions Inc.

Opinion

We have audited the consolidated financial statements of Hammond Power Solutions Inc. (the Entity), which comprise:

- the consolidated statements of financial position as at end of December 31, 2020 and end of December 31, 2019
- the consolidated statements of operations for the years then ended
- the consolidated statements of comprehensive income (loss) for the years then ended
- the consolidated statements of changes in equity for the years then ended
- the consolidated statements of cash flows for the years then ended
- and notes to the consolidated financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Entity as December 31, 2020 and December 31, 2019, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "**Auditors' Responsibilities for the Audit of the Financial Statements**" section of our auditors' report.

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements for the year ended December 31, 2020. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have determined the matters described below to be the key audit matters to be communicated in our auditors' report.

Evaluation of the carrying value of goodwill for the India cash generating unit**Description of the matter**

We draw attention to Notes 2(d)(ii), 3(g) and 12 of the financial statements. The goodwill balance is \$10,908 thousand, of which, \$8,728 thousand relates to the Hammond Power Solutions Private Limited ("India") cash generating unit ("CGU"). The Entity conducts its annual impairment assessment of goodwill on an annual basis or whenever events or changes in circumstances indicate that the carrying amount of a CGU may not be recoverable. Performing impairment testing requires management to determine the estimated recoverable amount of the relevant cash-generating units on the basis of projected future cash flows. The determination of the recoverable amount requires management to make significant estimates and assumptions which include projected revenue, projected gross margin rates, terminal growth rates, and the discount rate.

Why the matter is a key audit matter

We identified the evaluation of the goodwill impairment analysis for the India CGU as a key audit matter. The estimated recoverable amount of the India CGU approximated its carrying value. This indicated a significant risk of misstatement as changes to certain significant assumptions had a significant effect on the recoverable amount of the India CGU. As a result, significant auditor judgment was required in evaluating the results of the audit procedures.

How the matter was addressed in the audit

The following are the primary procedures we performed to address this key audit matter:

- We compared the Entity's historical projected revenue and projected gross margin rates to actual results to assess the Entity's ability to accurately project revenue and gross margin rates.
- We performed sensitivity analyses over the projected revenue and discount rate assumptions to assess their impact on the Entity's determination that the estimated recoverable amount of the CGU exceeded its carrying value.
- We evaluated the terminal growth rate by comparing to overall market and industry conditions and overall macro-economic conditions.
- We involved valuation professionals with specialized skills and knowledge, who assisted in evaluating the appropriateness of the discount rate assumption used in the estimated recoverable amount, by comparing it to a discount rate range that was independently developed using publicly available information and considering risks specific to the CGU.

Other Information

Management is responsible for the other information. Other information comprises:

- the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.
- the information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "Annual Report 2020".

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit and remain alert for indications that the other information appears to be materially misstated.

We obtained the information included in Management's Discussion and Analysis and the Annual Report 2020 filed with the relevant Canadian Securities Commissions as at the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report.

We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards (IFRS), and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group Entity to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.
- Determine, from the matters communicated with those charged with governance, those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our auditors' report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.



Chartered Professional Accountants,
Licensed Public Accountants
The engagement partner of the audit resulting in this auditors
report is R. Alexander Dilts

March 25, 2021
Waterloo, Canada

Consolidated Statements of Financial Position

(in thousands of dollars)

As at

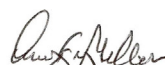
	December 31, 2020	December 31, 2019
Current assets		
Cash and cash equivalents	\$ 14,795	\$ 23,371
Accounts receivable (note 4)	53,078	64,004
Inventories (note 5)	49,206	50,926
Income taxes receivable	488	1,626
Prepaid expenses and other assets (note 6)	2,687	2,657
Total current assets	120,254	142,584
Non-current assets		
Long-term lease and note receivable (note 7)	3,201	3,180
Property, plant and equipment (note 8)	30,372	32,468
Investment in properties (note 9)	3,649	3,709
Investment in joint venture (note 10)	13,300	13,428
Deferred tax assets (note 16)	1,809	1,944
Intangible assets (note 11)	5,901	6,331
Goodwill (note 12)	10,908	11,309
Total non-current assets	69,140	72,369
Total assets	\$ 189,394	\$ 214,953
Liabilities		
Current liabilities		
Bank operating lines of credit (note 13)	\$ 16,073	\$ 32,697
Accounts payable and accrued liabilities (notes 17 and 29)	46,179	56,216
Income taxes payable	942	1,055
Provisions (note 20)	1,811	1,710
Current portion of lease liabilities (note 14)	2,144	2,237
Total current liabilities	\$ 67,149	\$ 93,915
Non-current liabilities		
Provisions (note 20)	317	285
Deferred tax liabilities (note 16)	836	1,819
Long-term portion of lease liabilities (note 14)	7,176	9,167
Total non-current liabilities	8,329	11,271
Total liabilities	\$ 75,478	\$ 105,186
Shareholders' Equity		
Share capital (note 17)	14,491	14,491
Contributed surplus	2,498	2,498
Accumulated other comprehensive income	1,519	7,439
Retained earnings	95,408	85,339
Total shareholder's equity	113,916	109,767
Commitments (note 15)		
Subsequent events (note 32)		
Total liabilities and shareholders' equity	\$ 189,394	\$ 214,953

See accompanying Notes to Consolidated Financial Statements.

On behalf of the Board:



William G. Hammond
Chairman of the Board & Chief Executive Officer



David J. FitzGibbon
Chairman Audit Committee

Consolidated Statements of Operations

Years ended December 31, 2020 and 2019 (in thousands of dollars except for per share)

	2020	2019
Sales (note 21)	\$ 322,097	\$ 358,782
Cost of sales (note 5 and note 22)	235,103	270,823
Gross margin	86,994	87,959
Selling and distribution (note 22)	40,217	41,476
General and administrative (note 22)	24,736	25,940
	\$ 64,953	\$ 67,416
Earnings from operations	22,041	20,543
Finance and other costs		
Interest expense	1,247	1,739
Foreign exchange gain	(123)	(234)
Share of income of investment in joint venture, net of tax (note 10)	(153)	(267)
Other	104	117
Net finance and other costs	1,075	1,355
Earnings before income taxes	20,966	19,188
Income tax expense (recovery) (note 16):		
Current	7,827	6,425
Deferred	(923)	(543)
	6,904	5,882
Net earnings from continuing operations	\$ 14,062	\$ 13,306
Loss from discontinued operations, net of tax (note 23)	–	(1,699)
Net earnings	14,062	11,607
Earnings per share (note 18)		
Basic earnings per share	\$ 1.20	\$ 0.99
Diluted earnings per share	\$ 1.20	\$ 0.99
Basic earnings per share from continuing operations	\$ 1.20	\$ 1.13
Diluted earnings per share from continuing operations	\$ 1.20	\$ 1.13

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income

Years ended December 31, 2020 and 2019 (in thousands of dollars)

	2020	2019
Net earnings	\$ 14,062	\$ 11,607
Other comprehensive loss		
Items that will be recognized within profit and loss:		
Foreign currency translation differences for foreign operations	(5,920)	(7,456)
Foreign currency translation differences for discontinued operations	–	2,155
Other comprehensive loss, net of income tax	(5,920)	(5,301)
Total comprehensive income	\$ 8,142	\$ 6,306

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Changes in Equity

Years ended December 31, 2020 and 2019 (in thousands of dollars)

	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2019	\$ 14,217	\$ 2,559	\$ 12,740	\$ 77,258	\$ 106,774
Total comprehensive income for the period					
Net income	–	–	–	11,607	11,607
Other comprehensive loss					
Foreign currency translation differences related to joint venture	–	–	(869)	–	(869)
Foreign currency translation differences	–	–	(4,432)	–	(4,432)
Total other comprehensive loss	–	–	(5,301)	–	(5,301)
Total comprehensive income for the period	–	–	(5,301)	11,607	6,306
Transactions with owners, recorded directly in equity					
Dividends to equity holders (note 17)	–	–	–	(3,287)	(3,287)
Stock options exercised (note 17)	339	(49)	–	–	290
Repurchase of shares (note 17)	(65)	(12)	–	(239)	(316)
Total transactions with owners	274	(61)	–	(3,526)	(3,313)
Balance at December 31, 2019	\$ 14,491	\$ 2,498	\$ 7,439	\$ 85,339	\$ 109,767
Balance at January 1, 2020	\$ 14,491	\$ 2,498	\$ 7,439	\$ 85,339	\$ 109,767
Total comprehensive income for the period					
Net income	–	–	–	14,062	14,062
Other comprehensive loss					
Foreign currency translation differences related to joint venture (note 10)	–	–	(281)	–	(281)
Foreign currency translation differences	–	–	(5,639)	–	(5,639)
Total other comprehensive loss	–	–	(5,920)	–	(5,920)
Total comprehensive income for the period	–	–	(5,920)	14,062	8,142
Transactions with owners, recorded directly in equity					
Dividends to equity holders (note 17)	–	–	–	(3,993)	(3,993)
Total transactions with owners	–	–	–	(3,993)	(3,993)
Balance at December 31, 2020	\$ 14,491	\$ 2,498	\$ 1,519	\$ 95,408	\$ 113,916

*AOCI – Accumulated other comprehensive income
See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

Years ended December 31, 2020 and 2019 (in thousands of dollars)

	2020	2019
Cash flows from operating activities		
Net earnings	\$ 14,062	\$ 11,607
Adjustments for:		
Share of income of investment in joint venture	(153)	(267)
Depreciation of property, plant and equipment and right-of-use assets	6,233	6,151
Amortization of intangible assets	1,036	1,097
Gain on disposal of right to use asset	(10)	–
Provisions	1,080	(132)
Interest expense	1,247	1,745
Loss on disposition (note 23)	–	687
Income tax expense	6,904	5,882
Unrealized loss on derivatives	560	2,997
Share-based compensation expense	518	364
	31,477	30,131
Change in non-cash working capital (note 27)	(4,992)	(6,374)
Cash generated from operating activities	26,485	23,757
Income tax paid	(6,802)	(5,947)
Net cash provided from operating activities	19,683	17,810
Cash flows from investing activities		
Investment in joint venture (note 10)	–	(728)
Proceeds on disposal of property, plant and equipment	–	1,583
Repayment of note and lease receivable	188	182
Acquisition of property, plant and equipment	(4,222)	(3,682)
Acquisition of intangible assets	(713)	(323)
Cash used in investing activities	(4,747)	(2,968)
Cash flows from financing activities		
Proceeds from issue of share capital	–	290
Cash dividends paid	(3,993)	(3,287)
Net (repayments) advances of bank operating lines of credit	(16,624)	96
Share repurchase (note 17)	–	(316)
Interest paid	(917)	(1,745)
Payment of lease liabilities (note 14)	(2,650)	(2,431)
Cash used in financing activities	(24,184)	(7,393)
Foreign exchange on cash and cash equivalents held in a foreign currency	672	377
(Decrease) increase in cash and cash equivalents	(8,576)	7,826
Cash and cash equivalents at beginning of period	23,371	15,545
Cash and cash equivalents at end of period	\$ 14,795	\$ 23,371

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

1. Reporting entity

Hammond Power Solutions Inc. ("HPS" or "the Company") is a corporation 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 consolidated financial statements of the Company comprise the Company and its subsidiaries (together referred to as the "Group" and individually as "Group entities"). The Group primarily is 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 Group has manufacturing plants in Canada, the United States ("U.S."), Mexico and India. The Company also holds a 55% economic interest in a joint venture located in Mexico called Corefficient de R.L. de C.V. ("Corefficient").

2. Basis of preparation

(a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), and were approved by the Board of Directors on March 25, 2021.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for inventories carried at net realizable value, derivative financial instruments and share based payments which are measured at fair value, and the initial present value of finance leases receivable which are determined using cash flows implicit in the lease and a discount rate reflecting the interest rate implicit in the lease.

(c) Functional and presentation currency

The functional currency of the Group's entities is the currency of their primary economic environment.

In individual companies, transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction. Monetary assets and liabilities in foreign currencies at the reporting date are re-measured to the functional currency at the exchange rate at that date. Any resulting exchange differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

On consolidation, assets and liabilities of Group entities reported in their functional currencies are translated into the Canadian dollar, being the presentation currency, at the exchange rate on the reporting date. The income and expenses of foreign operations are translated to Canadian dollars using average exchange rates for the month during which the transactions occurred. Foreign currency differences are recognized in other comprehensive income in the cumulative translation account within accumulated other comprehensive income.

The functional currency of the Company's Canadian operations and its subsidiaries are as follows:

Canadian & Subsidiary Operations	Functional Currency	
Canada	Canadian dollar	(\$)
United States	U.S. dollar	(\$ USD)
Mexico	Mexican Peso	(Pesos)
Mexico – Corefficient	U.S. dollar	(\$ USD)
Italy	Euro	(EU €)
India	Rupee	(INR)

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

(d) Use of estimates and judgments

The preparation of the consolidated 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.

(i) Critical judgments in applying accounting policies

The following are the critical judgments, apart from those involving estimations, that Management has made in the process of applying the Group's accounting policies and that have the most significant effects on the amounts recognized in the consolidated financial statements.

Cash generating units

As indicated in note 3(g) and 3(k); the Group conducts its impairment tests at the individual asset level or, where the recoverable amount cannot be determined for an individual asset, or for goodwill, at the cash generating unit (CGU) level. The Group defines its CGUs based on the way it monitors and derives economic benefits from the acquired goodwill and intangibles. A cash-generating unit is the smallest group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The identification of a cash-generating unit involves judgment.

The Company has defined its cash generating units primarily as each manufacturing and contract manufacturing location, due to the fact that each location is managed separately and has its own dedicated human resources and property, plant and equipment. Each manufacturing facility produces products largely independent of the other facilities and is ultimately responsible for producing products that generate revenue.

The Company monitors the performance of each manufacturing unit through the use of profitability analysis, and also considers the profitability of each manufacturing unit relative to the Company's business plan.

Initial lease term

The Group leases certain manufacturing facilities, warehouse facilities, vehicles and other assets. In determining the value of a right-of-use asset and lease liability, IFRS 16 requires the Group to determine the lease payments to be made over the initial term of the lease, including renewal options which are reasonably certain to be exercised. Such payments are then discounted based on the interest rate implicit in the lease or the Group's incremental borrowing rate. In determining the initial lease term, Management makes an assessment of the renewal periods available to the Group within each lease and evaluates the likelihood and corresponding time horizon of available renewal options. Such assessments involve judgment and ultimately may differ from the terms of leases actually experienced.

Operating segments

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. The determination of operating segments involves judgment. Management has determined that the Group operates as a single operating segment, being the design, manufacture and sale of transformers.

(ii) Key sources of estimation uncertainty

The following are the key sources of estimation uncertainty at the end of the reporting period that have a significant risk of causing a material adjustment to the consolidated financial statements within the next twelve months.

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Recoverability of goodwill and intangible assets

The Group tests annually or more frequently if necessary, whether goodwill or other long-lived assets have suffered any impairment in accordance with the accounting policy provided in note 3(k). Performing impairment testing requires management to determine the estimated recoverable amount of the relevant cash-generating units on the basis of projected future cash flows using internal business plans or forecasts, and discounting these cash flows to appropriately reflect the time value of money.

The key assumptions made by management in deriving the recoverable amount are i) projected revenue, ii) projected gross margin rates, iii) terminal growth rates, and iv) the discount rate.

Impairment assessments inherently involve judgment as to assumptions about expected future cash flows and the impact of market conditions on those assumptions. Future events and changing market conditions may impact the Company's assumptions as to prices, costs or other factors that may result in changes in the Company's estimates of future cash flows. Failure to realize the assumed revenues at an appropriate gross margin or failure to improve the financial results of a CGU could result in impairment losses in the CGU in future periods.

For assumptions relating to impairment testing, refer to note 12.

Provisions for warranty claims

The Group records a provision for warranties based on historical warranty claim information and anticipated warranty claims, based on a weighted probability of possible outcomes.

The key assumptions made by management in recording the provision are i) warranty cost, ii) probability of claim, and iii) quantum of units which may be subject to any warranty claim.

Quantifying provisions inherently involves judgement, and future events and conditions may impact these assumptions. Differences in actual future experience from the assumptions utilized may result in a greater or lower warranty cost. For further information on the Group's provisions, refer to note 20.

3. Summary of significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and by all Group entities.

(a) Basis of consolidation

The consolidated financial statements include the accounts of Hammond Power Solutions Inc. and its wholly-owned subsidiaries, Hammond Power Solutions, Inc., Hammond Power Solutions, S.A. de C.V., Delta Transformers Inc., Hammond Power Solutions Private Limited., Continental Transformers s.r.l., and its wholly-owned subsidiary, Hammond Power Solutions S.p.A.

Joint operations arise from an arrangement in which the interested parties are bound by a contract which gives two or more parties joint control of the arrangement, and those parties have rights to the assets and obligations for the liabilities relating to the arrangement. The Company has a 50% interest in Glen Ewing Properties, an unincorporated co-tenancy. The consolidated financial statements include the Group's share of the entity's assets, liabilities, revenue and expenses with items of a similar nature on a line-by-line basis.

Joint ventures arise in which the interested parties are bound by a contract which gives two or more parties joint control of the arrangement, and those parties have rights to the net assets of the arrangement. The Company's interest in Corefficient is considered to represent a joint venture. Interests in joint ventures are initially recognized at cost. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and other comprehensive income.

All significant inter-company transactions and balances have been eliminated.

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

(b) Financial instruments

Financial assets and financial liabilities, including derivatives, are recognized on the consolidated statement of financial position when the Group becomes a party to the financial instrument or derivative contract.

The Group classifies its financial assets and financial liabilities in the following measurement categories i) those to be measured subsequently at fair value (either through other comprehensive income or through profit or loss) and ii) those to be measured at amortized cost. The classification of financial assets depends on the business model for managing the financial assets and the contractual terms of the cash flows. Financial liabilities are classified as those to be measured at amortized cost unless they are designated as those to be measured subsequently at fair value through profit or loss (irrevocable election at the time of recognition). For assets and liabilities measured at fair value, gains and losses are either recorded in profit or loss or other comprehensive income.

The Group reclassifies financial assets when and only when its business model for managing those assets changes. Financial liabilities are not reclassified.

The Group has applied the following classifications:

- Cash and cash equivalents, accounts receivable and long-term lease and note receivable are classified as assets at amortized cost and are measured using the effective interest rate method. Interest income is recorded in the consolidated statement of operations, as applicable.
- Accounts payable, accrued liabilities and bank operating lines of credit are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method. Interest expense is recorded in the consolidated statement of operations, as applicable.
- Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged and the type of hedge relationship designated. The Group has not historically designated such items as hedging instruments and accordingly changes in fair value are recorded through the statement of operations.

All financial instruments are required to be measured at fair value on initial recognition, plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss. Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Financial assets that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of the subsequent accounting periods.

The Group assesses all information available, including, on a forward-looking basis, the expected credit losses associated with its assets carried at amortized cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. To assess whether there is a significant increase in credit risk, the Group compares the risk of a default occurring on the asset as at the reporting date with the risk of default as at the date of initial recognition based on all information available, and reasonable and supportive forward-looking information. For trade receivables only, the Group applies the simplified approach as permitted by IFRS 9 which requires expected lifetime losses to be recognized from initial recognition of receivables.

(c) Cash and cash equivalents

Cash and cash equivalents include cash and short-term deposits with maturities of three months or less.

(d) Property, plant and equipment

Property, plant and equipment are shown in the statement of financial position at their historical cost. Cost includes

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expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and borrowing costs on qualifying assets. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Depreciation is provided on components that have homogenous useful lives by using the straight-line method so as to depreciate the initial cost down to the residual value over the estimated useful lives.

The estimated useful lives for the current and comparative periods are as follows:

- Buildings 14-30 years
- Leaseholds and improvements lesser of 5 years and lease term
- Machinery and equipment 4-10 years
- Office equipment 4-10 years
- Land is not depreciated

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

Assets included in construction-in-progress are not depreciated until the assets are available for use. Idle assets that are available for use are depreciated.

(e) Intangible assets other than goodwill

Intangible assets that are acquired either separately or in a business combination are recognized when they are identifiable and can be reliably measured. Intangible assets are considered to be identifiable if they arise from contractual or other rights, or if they are separable (i.e. they can be disposed of either individually or together with other assets). Intangible assets comprise finite life intangible assets.

Finite life intangible assets are those for which there is an expectation of obsolescence that limits their useful economic life or where the useful life is limited by contractual or other terms. They are amortized over the shorter of their contractual or useful economical lives.

The estimated useful lives for the current and comparative periods are as follows:

- Customer lists and relationships 15 years
- Technology 20 years
- Software and other 4 years
- Branding 5 years

Amortization methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

(f) Research and development expenses

Research expenses are recognized as expenses in the financial period incurred.

Development expenses are recognized as an intangible asset if the Group can demonstrate the technical feasibility of making the intangible asset ready for commissioning or sale; its intention to complete the intangible asset and use or sell it; its ability to use or sell the intangible asset; how the intangible asset will generate future economic benefits; the availability of the appropriate resources (technical, financial or other) to complete development and use or sell the intangible asset; and its ability to provide a reliable estimate of expenses attributable to the intangible asset during its development.

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(g) Goodwill

Acquisitions are accounted for using the acquisition method required by IFRS 3. Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amount allocated to the identifiable assets acquired, less liabilities assumed, based on their fair values. Goodwill is allocated as of the date of the business combination to the Company's cash generating units that are expected to benefit from the synergies of the business combination.

Goodwill is tested for impairment at least annually and upon the occurrence of an indication of impairment.

The impairment tests are performed at the cash generating unit ("CGU") level. The Group defines its CGUs based on the way it monitors and derives economic benefits from the acquired goodwill and intangibles. The impairment tests are performed by comparing the carrying value of the assets of these CGUs with the greater of its value in use and its fair value, less costs to sell. The value in use is based on their future projected cash flows discounted to the present value at an appropriate pre-tax discount rate. The cash flows correspond to estimates made by Group management in financial and strategic business plans covering a period of five years. They are then projected beyond five years using a steady or declining terminal growth rate given that the Group businesses are of a long-term nature. The Group assesses the uncertainty of these estimates by conducting sensitivity analyses. The discount rate used approximates the CGUs weighted average cost of capital, with business risk incorporated into the development of the cash flow projections.

An impairment loss in respect of goodwill is never subsequently reversed. The Group completed its annual goodwill impairment tests at December 31, 2020.

(h) Investment property

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business use in the production or supply of goods or services or for administrative purposes. The Group measures its investment properties, being the property held by Glen Ewing Properties, at historical cost.

In a period in which a change of use of a property occurs such that it becomes an investment property, depreciation ceases and its then carrying value becomes its cost.

(i) Joint Venture

The Company applies the equity method of accounting for its investment in the joint venture. Under the equity method of accounting, interests in joint ventures are initially recognized in the Consolidated Statements of Financial Position at initial cost and adjusted thereafter to recognize the Group's share of profits or losses and movements in other comprehensive income in the income statement and in other comprehensive income respectively. When the Group's share of losses in a joint venture equals or exceeds its interest in the joint venture, the Group does not recognize further losses unless it has incurred obligations or made payments on behalf of the joint venture.

Unrealized gains or transactions between the Group and its joint venture are eliminated to the extent of the Group's interest in the joint venture. Unrealized losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred.

(j) Inventories

Inventories are valued at the lower of cost and net realizable value.

The cost of inventories is based on the first-in first-out principle and includes expenditures incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

When circumstances which previously caused inventories to be written down to their net realizable value no longer exist, the previous impairment is reversed.

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(k) Impairment of property, plant and equipment and finite life intangible assets

The Group periodically reviews the useful lives and the carrying values of its long-lived assets for continued appropriateness. Consideration is given at each reporting date to determine whether there is any indication of impairment of the carrying amounts of the Group's property, plant and equipment and finite life intangible assets. The Group reviews for impairment of long-lived assets, or asset groups, held and used whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable.

The recoverable amount is the greater of the fair value less cost of disposal and value in use. If the recoverable amount cannot be determined for one individual asset, the Group conducts its impairment test at the CGU level. In assessing value in use, the estimated future cash flows are discounted to their present value, based on the time value of money and the risks specific to the country where the assets are located. Assets that suffer impairment are assessed for possible reversal of the impairment at each reporting date.

(l) Share-based payment transactions

Stock Option Plan

The Group has a stock-based compensation plan, which is described in note 17. The Group accounts for all stock-based payments using the fair value based method.

Under the fair value based method, compensation cost for stock options and direct awards of stock is measured at fair value at the grant date. Compensation cost is recognized in earnings on a straight-line basis over the relevant vesting period, with a corresponding amount recorded in contributed surplus. The amount recognized as an expense, is adjusted to reflect the number of awards for which the related services are expected to be met. Upon exercise of a stock option, share capital is recorded at the sum of the proceeds received and the related amount of contributed surplus.

Deferred Share Unit Plan

The Company implemented a deferred share unit plan ("DSU Plan") for its senior-executive management and Directors. Under the DSU Plan, participants may elect to defer compensation and receive DSUs equal to the value of the deferred compensation. DSUs are increased by the dividend rate on a quarterly basis.

Under IFRS, DSUs are classified as cash-settled share-based payment transactions as the participants shall receive cash following a Redemption Event, as defined in the DSU Plan. DSUs do not contain any vesting conditions or forfeiture provisions, as they are issued in exchange for deferred compensation. As such, the Company recognizes the expense and the liability to pay for eventual redemption when DSUs are issued. Thereafter, the Company re-measures the fair-value of the liability at the end of each reporting date and the date of settlement, with the difference recognized in income or expense for the period. The fair value of DSUs is determined in accordance with the DSU Plan, which uses the average closing price for HPS shares for the five trading days immediately preceding the relevant date. DSU liability is included in accrued liabilities.

(m) Provisions

Provisions comprise liabilities of uncertain timing or amounts that arise from restructuring plans, environmental, litigation, commercial or other risks. Provisions are recognized when there exists a legal or constructive obligation stemming from a past event and when the future cash outflows can be reliably estimated. A provision for warranties is recognized when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities. A restructuring provision relating to a sale or termination of a line of business, the closure of business locations in a country or region, changes in management structure or fundamental reorganizations that have a material effect of the nature or focus of the Group's operations are recognized when the Group has a detailed, formal plan for the restructuring that identifies:

- the business or part of a business concerned;

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- the principal locations affected;
- the location, function and approximate number of employees affected;
- the expenditures that will be undertaken; and
- when the plan will be implanted.

Notwithstanding the above, no provision is recorded until such time a valid expectation by those affected by the plan has been raised.

(n) Revenue

The Group recognizes revenue using a 5-step approach:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the Group satisfies a performance obligation.

The Group considers a performance obligation satisfied when “control” of the goods or services underlying the particular performance obligation is transferred to the customer. A performance obligation represents a good and service (or a bundle of goods or services) that is distinct or a series of distinct goods or services that are substantially the same. The Group typically satisfies its performance obligation upon shipment of its transformers. Any required testing or compliance requirements will have been satisfied prior to shipment of the transformer. Payment is typically due within 30 days of shipment, with limited customers being granted extended terms of up to 60 days – consideration is generally fixed and does not contain any significant financing components. The Group has a return policy for credit on standard stocked items and no custom build product can be returned. Historically, returns have been minimal and are expected to continue to remain low. The Group’s product is purchased with a standard warranty and there is no option to purchase any additional warranty coverage.

A contract asset represents the Group’s right to consideration in exchange for goods or services that the Group has transferred to a customer that is not yet unconditional. In contrast, a receivable represents the Group’s unconditional right to consideration in that only the passage of time is required before payment of that consideration is due.

A contract liability represents the Group’s obligation to transfer goods or services to a customer for which the Group has received consideration (or an amount of consideration is due) from the customer.

Incremental costs to obtain a contract are typically short-term in nature and the Group applies the practical expedient permitted under IFRS 15 to recognize such costs as an expense when incurred if the amortization of the asset that the Group would have otherwise recognized is less than one year.

(o) Income taxes

Income tax expense comprises current and deferred tax. Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years. Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

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(p) Employee benefits

The Group maintains a defined contribution plan, which is described in note 19, and have short-term employee benefits.

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, are recognized as an employee benefit expense in profit or loss in the periods in which services are rendered by employees.

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(q) Finance income and finance costs

Finance income and finance costs comprise interest income, interest expense on borrowings, foreign currency losses (including changes in fair value of derivative foreign currency financial instruments measured at fair value through profit and loss), the Group's share of income or losses arising from its investment in joint ventures and other finance costs.

Foreign currency gains and losses are reported on a net basis.

(r) Earnings per share

The Group presents basic and diluted earnings per share ("EPS") data for its common shares. Basic EPS is calculated by dividing net earnings of the Group by the weighted average number of common shares outstanding during the reporting period. Diluted EPS are computed similar to basic EPS except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of stock options, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options were exercised and that proceeds from such exercises along with any unamortized stock-based compensation were used to acquire common shares at the average market price during the year.

(s) Leases

The Group recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, and subsequently at cost less any accumulated depreciation and impairment losses, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate. The group applies a single discount rate to the portfolio of leases with reasonably similar characteristics.

The lease liability is subsequently increased by the interest cost on the lease liability and decreased by lease payments made. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in the estimate or the amount expected to be payable under a residual value guarantee, or as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

The Group does not recognize right-of-use assets and lease liabilities for contracts that have a lease term of 12 months or less or are low-value assets (under \$5,000).

(t) Government assistance

The Group recognizes government assistance in the statement of operations on a systematic basis over the periods in which the entity recognises expenses for the related costs for which the assistance is intended to compensate.

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(u) New accounting pronouncements adopted during the period

Definition of a Business (Amendments to IFRS 3)

On October 22, 2018, the IASB issued amendments to IFRS 3 Business Combinations, that seeks to clarify whether a transaction results in an asset or a business acquisition. The amendments apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020.

The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or as a group of similar identifiable assets. If the preparer chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process.

The Company adopted the amendments in its financial statements for the annual period beginning on January 1, 2020. The adoption of the amendments did not have a material impact on the consolidated financial statements.

(v) New accounting pronouncements

The International Accounting Standards Board has issued the following Standards, Interpretations and Amendments to Standards that are not yet effective, have not yet been adopted by the Group and are not expected to have a material impact on the consolidated financial statements.

The Group intends to adopt the following amendments in its financial statements for the annual period beginning on January 1, 2022:

- Property, Plant and Equipment – Proceeds before Intended Use (Amendments to IAS 16)
- Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)
- Reference to the Conceptual Framework (Amendments to IFRS 3)
- Annual Improvements to IFRS Standard 2018-2020

The Group intends to adopt the following amendment in its financial statements for the annual period beginning on January 1, 2023:

- Classification of Liabilities as Current or Non-Current (Amendments to IAS 1)

The Group intends to adopt the following amendment once an effective date has been announced:

- Sale or Contribution of Assets Between an Investor and its Associate or Joint Venture

4. Accounts receivable

	December 31, 2020	December 31, 2019
Trade accounts receivable	\$ 49,129	\$ 60,589
Other receivables	3,949	3,415
	\$ 53,078	\$ 64,004

Trade accounts receivable is presented net of expected credit losses of \$2,577,000 (December 31, 2019 – \$2,997,000).

A continuity of the Group's allowance for doubtful accounts is as follows:

	December 31, 2020	December 31, 2019
Opening balance	\$ 2,997	\$ 2,481
Additional allowances	494	379
Writeoffs	(25)	(116)
Adjustments	(889)	253
	\$ 2,577	\$ 2,997

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5. Inventories

	December 31, 2020	December 31, 2019
Raw materials	\$ 19,002	\$ 20,974
Work in progress	1,867	2,276
Finished goods	28,337	27,676
	\$ 49,206	\$ 50,926

Raw materials and changes in finished goods, and work in progress recognized as cost of sales during the year amounted to \$234,395,000 (2019 – \$271,475,000), of which \$nil (2019 – \$1,461,000) is included in discontinued operations. In addition, during the year, reversal of write-downs in the amount of \$4,000 were recognized (2019 – \$24,000). Inventories carried at net realisable value as at December 31, 2020 were \$821,000 (December 31, 2019 – \$1,190,000).

6. Prepaid and other assets

	December 31, 2020	December 31, 2019
Prepaid expenses	\$ 2,455	\$ 2,440
Current portion of long-term lease and note receivable (note 7)	232	217
	\$ 2,687	\$ 2,657

7. Long-term lease and note receivable

On October 31, 2017, the Group sold the assets and disposed of certain liabilities of its Vacuum Pressure Impregnated (VPI) transformers product line located in Italy. Consideration due to the Group in connection with the transaction included a note receivable in the amount of 1,158,000 Euros (approximately \$1,687,000).

Concurrent with the disposal of the VPI product line, the Group entered into a lease agreement (“agreement”) for one of its manufacturing facilities in Italy, under which the purchaser will have the use of the plant, which includes both the land and the building, to 2023. Consideration was in the form of a lease receivable, which the Company has determined meets the definition of a finance lease.

The lease receivable is calculated based on the present value of the future principal and interest cash flows, discounted at the market rate of interest at the lease inception date, determined to be 1.15%. Unless one of the Parties sends to the other a twelve month prior written notice of termination, at the end of each six year term, the agreement will be automatically renewed by an equal period.

In fiscal 2018, the Group recorded a provision for amounts outstanding in respect of the note receivable, as the purchaser had ceased making payments and was disputing the value of certain of the acquired assets, amongst other matters.

In October 2020, the dispute with the purchase was resolved and the note receivable was settled in the amount of 614,000 Euros (approximately \$956,000). As a result, 614,000 Euros of the allowance for doubtful accounts was reversed and recorded as a recovery in the statement of earnings in general and administrative expenses.

Put and call option

The lease agreement includes a put and call option related to the leased premises, exercisable within 60 days after September 30, 2023. The call option grants the purchaser an option to purchase the premises for consideration equal to 2,225,000 Euros (approximately \$3,400,000). The put option grants HPS an option to sell the plant to the purchaser for consideration equal to the initial plant purchase price of 2,225,000 Euros. Under both the call and put option the plant purchase price will be reduced by 50% of the monthly rent installments received, to a maximum of 375,000

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Euros (approximately \$573,000). If the purchaser fails to execute the put option, the purchaser will pay 500,000 Euros (approximately \$764,000) in damages. The put and call options expire November 23, 2023.

As at December 31, 2019 consideration receivable consists of:

	December 31, 2020	December 31, 2019
Lease receivable of 2,208 EUR (2019 – 2,332 EUR), with monthly lease payments of 13 EUR, bearing interest of 1.15% per annum.	\$ 3,538	\$ 3,538
Gross cash entitlement:		
Less: unearned finance income	(105)	(141)
Net lease receivable	3,433	3,397
(2019 - Note receivable of 1,158 EUR, repayment schedule of 1,158 due immediately non-interest bearing, secured by the property, plant and equipment of the VPI business)	–	1,687
Less: allowance for doubtful accounts	–	(1,687)
	\$ 3,433	\$ 3,397
Less: current portion included within prepaid and other assets	232	217
	\$ 3,201	\$ 3,180

The aggregate amount of principal payments to be received in each of the next four years is as follows:

2021	232
2022	232
2023	2,969
	\$ 3,433

8. Property, plant and equipment

Property, plant and equipment comprise owned and leased assets that do not meet the definition of investment property. Carrying amounts of owned and right-of-use assets are as follows:

	December 31, 2020	December 31, 2019
Property, plant and equipment owned	\$ 23,648	\$ 23,415
Right-of-use assets (note 14)	6,724	9,053
	\$ 30,372	\$ 32,468

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	Land	Building	Leaseholds & Improvements	Machinery & Equipment	Office Equipment	Construction In Progress & Deposits	Total
Cost							
Balance at January 1, 2019	\$ 4,892	\$ 21,207	\$ 1,520	\$ 58,958	\$ 10,972	\$ 276	\$ 97,825
Additions	–	140	95	2,089	511	847	3,682
Disposals	–	–	–	(7,513)	(19)	–	(7,532)
Transfer to investment property (note 9)	(583)	(3,179)	–	–	–	–	(3,762)
Effect of movements in exchange rates	(77)	(444)	(33)	(506)	(389)	–	(1,449)
Balance at December 31, 2019	\$ 4,232	\$ 17,724	\$ 1,582	\$ 53,028	\$ 11,075	\$ 1,123	\$ 88,764
Balance at January 1, 2020	\$ 4,232	\$ 17,724	\$ 1,582	\$ 53,028	\$ 11,075	\$ 1,123	\$ 88,764
Additions	–	301	325	1,612	489	1,495	4,222
Effect of movements in exchange rates	(22)	(46)	(107)	(574)	(106)	–	(855)
Balance at December 31, 2020	\$ 4,210	\$ 17,979	\$ 1,800	\$ 54,066	\$ 11,458	\$ 2,618	\$ 92,131

Accumulated Depreciation

Balance at January 1, 2019	\$ –	\$ 11,569	\$ 1,317	\$ 46,095	\$ 9,806	\$ –	\$ 68,787
Depreciation for the year	–	969	103	2,777	435	–	4,284
Disposals	–	–	(257)	(5,974)	(45)	–	(6,276)
Transfer to investment property (note 9)	–	(1,097)	–	–	–	–	(1,097)
Effect of movements in exchange rates	–	(91)	(30)	(62)	(166)	–	(349)
Balance at December 31, 2019	\$ –	\$ 11,350	\$ 1,133	\$ 42,836	\$ 10,030	\$ –	\$ 65,349
Balance at January 1, 2020	\$ –	\$ 11,350	\$ 1,133	\$ 42,836	\$ 10,030	\$ –	\$ 65,349
Depreciation for the year	–	779	106	2,456	416	–	3,757
Effect of movements in exchange rates	–	(19)	(80)	(444)	(80)	–	(623)
Balance at December 31, 2020	\$ –	\$ 12,110	\$ 1,159	\$ 44,848	\$ 10,366	\$ –	\$ 68,483

Carrying amounts

At December 31, 2019	\$ 4,232	\$ 6,374	\$ 449	\$ 10,192	\$ 1,045	\$ 1,123	\$ 23,415
At December 31, 2020	\$ 4,210	\$ 5,869	\$ 641	\$ 9,218	\$ 1,092	\$ 2,618	\$ 23,648

Depreciation is recorded in the statement of earnings as follows: cost of sales \$3,430,000 (2019 – \$3,357,000), selling and distribution \$5,000 (2019 – \$5,000), general and administrative \$322,000 (2019 – \$319,000) and discontinued operations \$Nil (2019 – \$603,000).

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9. Investment in properties

	December 31, 2020	December 31, 2019
Glen Ewing Property	\$ 1,044	\$ 1,044
Marnate Property (net of accumulated depreciation of \$942 (2019 - \$706))	2,605	2,665
	\$ 3,649	\$ 3,709

Glen Ewing Property

The Group has a 50% ownership interest in a property in Georgetown, Ontario, (referred to as the Glen Ewing Property). It is a vacant plot of land currently under environmental remediation, and no revenue was derived from it in 2020 or 2019. The property is carried at cost. The estimated fair value of the property as at December 31, 2020 is \$1,150,000 (2019 – \$1,150,000). The fair value was determined based on independent available market evidence, with reference to comparable market transactions. The Group's share of ongoing legal, consulting and remediation costs during the year was \$121,000 (2019 – \$109,000).

Marnate Property

The Group owns a property in Marnate, Italy, (referred to as the Marnate Property). As part of the sale transaction of certain of the assets and liabilities of the Italian company, as outlined in note 23, the purchaser has leased the Marnate Property for a period of six years at an annual rental amount of 90,000 EUR (approximately \$137,000). The operating expenses for this property were 202,000 EUR (approximately \$307,000) in 2020. In 2019, concurrent with the change in use of the property, the Company reclassified it from an item of property, plant and equipment to an investment property. Depreciation on the facility was recorded in the statement of earnings as general and administrative expenses in the amount of \$236,000. The estimated fair value of the property as at December 31, 2020 is 2,280,000 Euros (approximately \$3,544,000). The fair value was determined based on independent available market evidence, based on comparable property sales, by an independent valuator.

10. Investment in 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 distributions of dividends and returns of capital from Corefficient are subject to unanimous Corefficient shareholder approval. Accordingly, the Company jointly controls Corefficient and has treated its investment 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:

	December 31, 2020	December 31, 2019
Cost of investment in joint venture	\$ 20,023	\$ 20,023
Cumulative share of loss in investment in joint venture, net of tax	(3,233)	(3,386)
Foreign currency translation differences related to the joint venture	(3,490)	(3,209)
	\$ 13,300	\$ 13,428

During the year the Company made an additional contribution of \$nil (2019 – \$728,000) and recognized its share of the income of \$153,000 (2019 – \$267,000).

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Selected financial information relating to Corefficient is as follows:

	December 31, 2020	December 31, 2019
Cash	\$ 3,553	\$ 4,341
Trade and other receivables	8,155	11,286
Inventories	2,932	3,047
Other current assets	89	118
Total current assets	\$ 14,729	\$ 18,792
Non-current assets	16,425	19,697
Total assets	\$ 31,154	\$ 38,489
Current liabilities	\$ 6,508	\$ 12,744
Non-current liabilities	746	1,603
Total liabilities	\$ 7,254	\$ 14,347

	2020	2019
Revenue	\$ 56,605	\$ 58,423
Income for the year	278	485

Net income for the year ended December 31, 2020 includes depreciation and amortization expense of \$3,118,000 (2019 – \$2,149,000), net interest expense of \$62,000 (2019 – \$66,000) and an income tax expense of \$nil (2019 – \$3,000) related to Corefficient.

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11. Intangible assets and goodwill

Intangible assets	Technology	Customer lists relationships and branding	Externally acquired software	Total
Cost				
Balance at January 1, 2019	\$ 6,600	\$ 8,957	\$ 6,416	\$ 21,973
Additions	–	–	323	323
Effect of movements in exchange rates	(359)	(211)	(49)	(619)
Balance at December 31, 2019	\$ 6,241	\$ 8,746	\$ 6,690	\$ 21,677
Balance at January 1, 2020	\$ 6,241	\$ 8,746	\$ 6,690	\$ 21,677
Additions	–	–	713	713
Effect of movements in exchange rates	(122)	(87)	35	(174)
Balance at December 31, 2020	\$ 6,119	\$ 8,659	\$ 7,438	\$ 22,216
Accumulated Amortization				
Balance at January 1, 2019	\$ 4,631	\$ 6,404	\$ 3,628	\$ 14,663
Amortization for the year	145	487	465	1,097
Effect of movements in exchange rates	(231)	(141)	(42)	(414)
Balance at December 31, 2019	\$ 4,545	\$ 6,750	\$ 4,051	\$ 15,346
Balance at January 1, 2020	\$ 4,545	\$ 6,750	\$ 4,051	\$ 15,346
Amortization for the year	138	481	417	1,036
Effect of movements in exchange rates	(53)	(50)	36	(67)
Balance at December 31, 2020	\$ 4,630	\$ 7,181	\$ 4,504	\$ 16,315
Balance at				
At December 31, 2019	\$ 1,696	\$ 1,996	\$ 2,639	\$ 6,331
At December 31, 2020	\$ 1,489	\$ 1,478	\$ 2,934	\$ 5,901

Amortization of \$342,000 (2019 – \$347,000) has been recognized in cost of sales, \$131,000 (2019 – \$137,000) has been recognized in selling and distribution, \$563,000 (2019 – \$549,000) has been recognized in general and administrative and \$nil (2019 – \$64,000) has been recorded within discontinued operations.

None of the intangible assets has been internally developed.

Research and development expenses of \$704,000 (2019 – \$785,000) have been recognized in cost of sales in the consolidated statements of earnings. No research and development costs have been capitalized (2019 – \$nil).

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

12. Goodwill and impairment testing for cash-generating units

Goodwill	December 31, 2020	December 31, 2019
Opening balance	\$ 11,309	\$ 11,961
Effect of movements of exchange rates	(401)	(652)
Ending balance	\$ 10,908	\$ 11,309

The Company conducts its annual impairment assessment of goodwill, intangible assets and property, plant and equipment in the fourth quarter of each year, which corresponds with its annual planning cycle, and whenever events or changes in circumstances indicate that the carrying amount of an asset or CGU may not be recoverable. The Company did not identify any triggering events during the course of 2020 indicating that the carrying amount of its assets and CGUs may not be recoverable, which would require the performance of an impairment test for those CGUs which did not contain goodwill.

Impairment testing for cash-generating units containing goodwill

The Company has two subsidiaries identified as CGUs that contain goodwill. The CGUs and their respective goodwill balances are as follows: Delta Transformers Inc. ("Delta") \$2,180,000 (2019 – \$2,180,000) and Hammond Power Solutions Private Limited ("India") \$8,728,000 (2019 – \$9,129,000).

For its 2020 annual impairment assessment of CGUs containing goodwill, the Company used cash flow projections based primarily on its business plan for the following year, and projections for the ensuing four year period. The Company's business plan is primarily based on financial projections submitted by its subsidiaries in the fourth quarter of each year, together with inputs from customer teams. This plan is subjected to reviews by various levels of management as part of its annual planning cycle, and is approved by the Board of Directors. The values used in the cash flow projections are based on historical sales, internal growth rate assumptions, and available market data.

Based on these projections, a five year cash flow forecast was completed and discounted to present-value using discount rates specific to each CGU ranging from 12.3% – 21.9% (2019 – 12.5% - 20.8%) depending on the location of the CGU. Through the five year cash flow projections, the Company's model also incorporated year 1 sales growth rates in the range of 4.7% – 80.3%, which reflects returning to normal production levels post COVID-19 pandemic as well as manufacturing of a new product line in India. The annual sales growth rates for year 2 to year 5 are in the range of 2.4% – 39.2% (2019 – year 1 to year 5 – 1.4% – 52.6%) depending on location, the CGUs operating history and strategic sales growth initiatives. Cash flows beyond the five year period have been extrapolated using terminal growth rates ranging from 2% – 8% (2019 – 2% – 8%), depending on the geography of the manufacturing unit. This was then compared to the carrying value of the CGU to determine if there was impairment.

Management's approach to determining projected revenue includes consideration of current bookings, committed product line expansions (for which no additional capital expenditure is required), consultation with its salesforce and historical results. The Company's process for determining projected gross margin rates includes consideration of current pricing information from suppliers and historical gross margin rates realized by the Company. The Company determines the terminal growth rate with reference to published economic data pertaining to the applicable industry and country in which the cash generating unit operates. The discount rate is determined with reference to the cash generating unit's weighted average cost of capital.

While management believes that estimates of future cash flows and discount rates are reasonable, different assumptions regarding future cash flows or discount rates could materially affect the outcome of the impairment

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

test. Management believes that certain reasonable possible changes in the key assumptions on which the recoverable amounts are based could cause the carrying amount to exceed the recoverable amount in the India CGU. As of December 31, 2020, a discount rate increase of 2.1% or a 3.5% lower terminal growth rate than the assumptions utilized would cause the estimated recoverable amount to be equal to the carrying amount for this CGU.

For the Delta Transformers Inc. CGU, management believes that any reasonable possible change in the key assumptions on which the recoverable amounts are based would not cause the carrying amount to exceed the recoverable amount.

Upon completion of the 2020 annual impairment assessment of goodwill it was determined that the recoverable amount of the CGUs exceeded their respective carrying values and no impairment existed at December 31, 2020.

13. Bank operating lines of credit

The Group's North American current banking agreement, which expires in June 2021, consists of a \$40,000,000 U.S. revolving credit facility and a \$10,000,000 U.S. delayed draw credit facility. The revolving credit facility can be drawn in of U.S. Prime borrowings, Canadian Prime borrowings, Canadian Dollar Offered Rate ("CDOR") borrowings or London Inter-Bank Offered rate ("LIBOR") borrowings. The delayed draw facility does not charge any fees on the unutilized balance. The use of the delayed draw facility needs to be approved by the bank. The draw is available in a minimum of two tranches of \$5,000,000 U.S. each. The facilities are unsecured.

The delayed draw credit facility was unutilized at December 31, 2020 and December 31, 2019. Under the terms of the facility, the Group pays a commitment fee at rates ranging from 0.30% to 0.40% payable quarterly in arrears, on the daily amount of the unused portion of the revolving North American commitment.

Interest on the revolving credit lines is dependent on certain financial ratios and ranges from Canadian bank prime rate minus 0.50% to Canadian bank prime rate for the Canadian dollar denominated revolving credit lines or, if designated, the bank's CDOR rate plus 1.25% to 1.75% and from U.S. base rate minus 1.50% to U.S. base rate minus 1.00% for the U.S. dollar denominated revolving credit lines or, if designated, the bank's LIBOR rate plus 1.25% to 1.75%.

The Group also has a 4,070,000 unsecured Euro facility that matures May 2021 and may be renewed in writing each year to extend the maturity date for the facility for a further 365 days, subject to approval from the lender. The facility is comprised of a 3,750,000 Euro revolver and 250,000 Euro overdraft facility, as well as a 70,000 Euro letter of credit line. The revolver facility bears interest at Euro Interbank Offered Rate ("Euribor") plus margin of 2.25% (2019 – plus margin of 1.75%, Euribor on December 31, 2020 – 0.499%, Euribor on December 31, 2019 – 0.249%).

Hammond Power Solutions Private Limited maintains an additional demand credit facility for an unsecured working capital loan up to 375,000,000 INR (2019 – 375,000,000 INR) consisting of the sub-facilities of a 131,000,000 INR (2019 – 131,000,000 INR) short-term working capital demand loan, a 244,000,000 INR (2019 – 244,000,000 INR) facility for bank guarantees. The demand loan bears interest at a MCLR + 2.5% and the bank guarantees are at a rate of 1.0%. As at December 31, 2020, there was \$nil Canadian dollar equivalent of Rupees drawn against the working capital demand loan (2019 – \$nil). At December 31, 2020 there was nil INR (2019 – nil INR) drawings against the bank guarantees.

Based on exchange rates in effect at December 31, 2020, the combined Canadian dollar equivalent available across all facilities, prior to any utilization of the facilities was \$76,477,000 (2019 – \$77,737,000).

As at December 31, 2020, the Canadian dollar equivalent outstanding under the U.S. dollar revolving credit line was \$11,215,000, consisting of \$7,577,000 Canadian dollars drawn and \$3,638,000 U.S. dollars drawn (2019 – \$28,145,000 – consisting of \$17,546,000 Canadian dollars drawn and \$10,599,000 U.S. dollars drawn). As well, \$4,858,000 (2019 – \$4,552,000) Canadian dollar equivalent of Euros was outstanding under the Euro facility, and \$nil (2019 – \$nil) Canadian dollar equivalent of Indian rupees under the Rupee facility. Amounts drawn on the facility have been recognized as current liabilities based on the Company's anticipated repayment plans.

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

14. Lease assets and liabilities

Lease assets

The Group leases many assets including buildings, vehicles and office equipment. Information about leases for which the Group is a lessee is presented below.

		Buildings	Vehicles	Office Equipment	Total
Balance at January 1, 2019	\$	8,539	\$ 470	\$ 49	\$ 9,058
Additions		1,471	366	–	1,837
Depreciation		(1,529)	(315)	(23)	(1,867)
Effect of movement in exchange rates		22	2	1	25
Balance at December 31, 2019	\$	8,503	\$ 523	\$ 27	\$ 9,053
Balance at January 1, 2020	\$	8,503	\$ 523	\$ 27	\$ 9,053
Additions		–	343	–	343
Disposals		–	(15)	–	(15)
Depreciation		(1,909)	(313)	(18)	(2,240)
Effect of movement in exchange rates		(407)	(9)	(1)	(417)
Balance at December 31, 2020	\$	6,187	\$ 529	\$ 8	\$ 6,724

Certain building leases maintained by the Group contain renewal options. Where practicable, the Group seeks to include extension options in new leases to provide operational flexibility. The majority of the Group's lease payments related to its production facilities located in Mexico. The first renewal option commenced in May 2020, with annual lease payments of \$621,000, and is for a five-year term. The Group retains rights to renew this lease for 3 successive 5-year periods. The Group's lease on its second Mexican production facility expires in March 2023 and carries annual lease payments of \$581,000. The Group holds a right to renew this lease for one four-year period following the expiry of the current lease term. The extension options held are exercisable only by the Group and not by the lessors. The Group assesses at lease commencement whether it is reasonably certain to exercise the options.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Lease liabilities

Maturity analysis – contractual undiscounted cash flows

	December 31, 2020	December 31, 2019
Less than one year	\$ 2,719	\$ 2,602
One to five years	7,017	9,318
More than five years	705	696
Total undiscounted lease liabilities	\$ 10,441	\$ 12,616
Less: effect of discounting	\$ (1,121)	\$ (1,121)
Lease liabilities included in the statement of financial position	\$ 9,320	\$ 11,404
Current	\$ 2,144	\$ 2,237
Non-current	\$ 7,176	\$ 9,167

Amounts recognized in statement of operations

	Year Ended December 31, 2020	Year Ended December 31, 2019
Interest on lease liabilities	\$ 330	\$ 325

Amounts recognized in statement of cash flows

	Year Ended December 31, 2019	Year Ended December 31, 2019
Payment of lease liabilities	\$ 2,650	\$ 2,431

15. Commitments

	December 31, 2020	December 31, 2019
Capital expenditure commitments	\$ 1,029	\$ 80

16. Income taxes

Income tax expense	2020	2019
Current tax expense		
Current period	\$ 7,827	\$ 6,425
Deferred tax expense (recovery)		
Origination and reversal of temporary differences	(924)	(579)
Decrease in tax rate	1	36
	(923)	(543)
Total income tax expense	\$ 6,904	\$ 5,882

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For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Reconciliation of effective tax rate

	2020	2020	2019	2019
Net earnings		\$ 14,062		\$ 11,607
Income tax expense		6,904		5,882
Earnings before income taxes		\$ 20,966		\$ 17,489
Income tax (recovery) using the Company's domestic tax rate	39.50%	8,282	39.50%	6,908
Effect of tax rates in foreign jurisdictions	(12.03%)	(2,522)	(10.36%)	(1,811)
Decrease in tax rate	0.00%	–	0.20%	36
Non-deductible expenses/non-taxable income	0.43%	90	2.23%	390
Reduced rate for active business and manufacturing and processing	(2.69%)	(564)	(4.25%)	(744)
Losses for which no deferred tax asset was recognized	(1.40%)	(294)	3.56%	623
Dividend withholding tax	6.11%	1,281	3.72%	650
Other	3.01%	631	(0.97%)	(170)
	32.93%	\$ 6,904	33.63%	\$ 5,882

Unrecognized temporary differences

At December 31, 2020, pre-tax temporary differences of \$80,250,000 (2019 – \$96,643,000) related to investments in subsidiaries were not recognized because the Company controls whether the liability will be incurred and it is satisfied that it will not be incurred in the foreseeable future. The tax liability in the event the Company were to sell these investments would be \$10,031,000 (2019– \$12,080,000) based on current tax rates.

Deferred tax assets have not been recognized in respect of the following items:

	2020	2019
Tax losses	\$ 13,777	\$ 12,458
Basis difference in subsidiary	31,361	37,356
Financial interests deductible in a future period	3,381	2,875
Expected credit losses	–	900
Inventory provisions	332	361
	\$ 48,851	\$ 53,950

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The tax losses, financial interests deductible, expected credit losses and inventory provisions carry forward indefinitely and relate to HPS S.p.A and Continental Transformers s.r.l. The basis difference in subsidiary, when realized, will provide the Company a capital loss that carries forward indefinitely. The benefit of these items has not been reflected in the consolidated financial statements as it is uncertain as to whether the Company will be able to utilize the deductions.

Recognized deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities	
	2020	2019	2020	2019
Property, plant and equipment	\$ 849	\$ 766	\$ (4,075)	\$ (4,763)
Intangible assets	4	–	(641)	(767)
Scientific research and experimental development	44	9	(32)	(46)
Inventories	291	228	–	–
Long-term lease and note receivable	–	–	(3,636)	(2,974)
Loans and borrowings	2,414	3,123	–	–
Employee benefits	340	233	(160)	(153)
Unrealized losses (gains) on forward contracts and foreign-currency denominated loans payable/receivable	201	728	(71)	–
Provisions and tax reserves	1,964	1,465	(2)	(2)
Tax loss carry-forwards	2,035	1,151	–	–
Charitable donation carry-forwards	–	–	–	–
Basis difference in subsidiary	1,448	1,127	–	–
Tax assets (liabilities)	9,590	8,830	(8,617)	(8,705)
Set off of tax	(7,781)	(6,886)	7,781	6,886
Net tax assets (liabilities)	\$ 1,809	\$ 1,944	\$ (836)	\$ (1,819)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Movement in temporary differences during the year ended December 31, 2020

	Balance December 31, 2019	Recognized in retained earnings	Recognized in profit or loss	Recognized in other comprehensive income	Balance December 31, 2020
Property, plant and equipment	\$ 3,997	\$ –	\$ (771)	\$ –	\$ 3,226
Intangible assets	767	–	(130)	–	637
Scientific research and experimental development	37	–	(49)	–	(12)
Inventories	(228)	–	(63)	–	(291)
Long-term lease and note receivable	2,974	–	662	–	3,636
Loans and borrowings	(3,123)	–	709	–	(2,414)
Employee benefits	(80)	–	(100)	–	(180)
Unrealized gains on forward contracts and foreign-denominated loans payable/receivable	(728)	–	598	–	(130)
Provisions and tax reserves	(1,463)	–	(499)	–	(1,962)
Tax loss carry-forwards	(1,151)	–	(884)	–	(2,035)
Basis difference in subsidiary	(1,127)	–	(321)	–	(1,448)
	\$ (125)	\$ –	\$ (848)	\$ –	\$ (973)
Foreign exchange			\$ (75)		
Income tax expense			\$ (923)		

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For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Movement in temporary differences during the year ended December 31, 2019:

	Balance December 31, 2018	Recognized in retained earnings	Recognized in profit or loss	Recognized in other comprehensive income	Balance December 31, 2019
Property, plant and equipment	\$ 2,011	\$ 1,686	\$ 300	\$ –	\$ 3,997
Intangible assets	882	–	(115)	–	767
Scientific research and experimental development	59	–	(22)	–	37
Inventories	(234)	–	6	–	(228)
Long-term lease and note receivable	3,245	–	(271)	–	2,974
Loans and borrowing	–	(2,325)	(798)	–	(3,123)
Employee benefits	(14)	–	(66)	–	(80)
Unrealized gains on forward contracts and foreign-denominated loans payable/receivable	(752)	–	24	–	(728)
Provisions and tax reserves	(1,779)	–	316	–	(1,463)
Tax loss carry-forwards	(858)	–	(293)	–	(1,151)
Basis difference in subsidiary	(1,467)	–	340	–	(1,127)
Charitable donation carry-forwards	(3)	–	3	–	–
	\$ 1,090	\$ (639)	\$ (576)	\$ –	\$ (125)
Foreign exchange			\$ 33		
Income tax expense			\$ (543)		

17. Share capital

(a) Authorized:

Unlimited number of special shares, discretionary dividends, non-voting, redeemable and retractable.

Unlimited number of Class A subordinate voting shares, no par value.

Unlimited number of Class B common shares with four votes per share, convertible into Class A subordinate voting shares on a one-for-one basis. Annual dividends on the Class B common shares may not exceed the annual dividends on the Class A subordinate voting shares, no par value.

(b) Issued:

	December 31, 2020	December 31, 2019
8,966,624 Class A subordinate voting shares (2019 – 8,966,624)	\$ 14,484	\$ 14,484
2,778,300 Class B common shares (2019 – 2,778,300)	7	7
11,744,924 Total A and B shares (2019 – 11,744,924)	\$ 14,491	\$ 14,491

During the year ended December 31, 2020 there were no stock options exercised. During the year ended December 31, 2019, 45,000 Class A shares were issued upon exercise of stock options, resulting in cash proceeds of \$290,000 and a transfer of \$49,000 from contributed surplus.

During 2019, the company purchased and cancelled 40,800 Class A shares under a normal course issuer bid at a cost of

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For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

\$316,000 of which \$65,000, \$12,000, \$239,000 was applied against share capital, contributed surplus and retained earnings respectively. The normal course issuer bid was completed in Quarter 3, 2019. There was no share repurchase transactions during 2020.

The following dividends were declared and paid by the Company:

	December 31, 2020	December 31, 2019
34 cents per Class A subordinate voting shares (2019 – 28 cents)	\$ 3,048	\$ 2,509
34 cents per Class B common shares (2019 – 28 cents)	945	778
	\$ 3,993	\$ 3,287

(c) Stock option plan

The Company uses a stock option plan to attract and retain key employees, officers and directors. Shareholders have approved a maximum of 1,200,000 Class A shares for issuance under the Stock Option Plan, with the maximum reserved for issuance to any one person at 5% of the Class A shares outstanding calculated immediately prior to the time of the grant. As per the Stock Option Plan, the Board of Directors may, at its sole discretion, determine the time during which the options shall vest and the method of vesting, or that no vesting restriction shall exist. The stock option exercise price is the price of the Company's common shares on the Toronto Stock Exchange at closing for the day prior to the grant date on which the Class A shares traded. The period during which an option will be outstanding shall be 7 years, or such other time fixed by the Board of Directors, subject to earlier termination upon the option holder ceasing to be a director, officer or employee of the Company. Options issued under the plan are non-transferable unless specifically provided in the Stock Option Plan. Any option granted, which is cancelled or terminated for any reason prior to exercise, shall become available for future stock option grants. All options are to be settled by physical delivery of shares.

There were no options granted for the year ended December 31, 2020, or the year ended December 31, 2019.

Options outstanding and exercisable as at December 31, 2020:

	December 31, 2020		December 31, 2019	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding, beginning of year	330,000	\$ 7.99	509,000	\$ 8.32
Exercised	0	–	(45,000)	6.43
Cancelled	(10,000)	6.20	(15,000)	9.17
Expired	(130,000)	10.00	(119,000)	9.74
Outstanding, end of year	190,000	\$ 6.77	330,000	\$ 7.99

Options outstanding				Options exercisable	
Exercise price	Number of options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
\$ 7.50	65,000	0.2	7.50	65,000	7.50
6.62	55,000	1.2	6.62	55,000	6.62
6.20	70,000	2.2	6.20	70,000	6.20
	190,000	1.2	\$ 6.77	190,000	\$ 7.99

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Terms and conditions of the stock option plan

Options grants detailed below vest as follows:

- Options granted to directors vest immediately.
- Options granted to officers and senior management vest evenly over two or three years from the grant date, with one-half of the grant vesting immediately for grants with a two-year vesting period, and one-third of the grant vesting immediately for grants with a three-year vesting period.

The contractual life of the options granted below is seven years from the grant date.

Option Grant Date	Number of Options	Recipients
March 13, 2014	65,000	Board of Directors, Officers and Senior Management
March 12, 2015	55,000	Board of Directors and Officers
March 10, 2016	70,000	Board of Directors and Officers
Total stock options outstanding	190,000	

(d) Deferred Share Units

Under the Company's 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 ("FMV") of DSUs, defined in 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 FMV 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 deferred compensation, nor are they performance based. Under the DSU Plan, outstanding DSUs as at the record date are increased by the dividend rate whenever dividends are paid to shareholders.

The movement in DSUs for the years ended December 31, 2019 and 2020 is as follows:

	Number of DSUs	Closing Share Price
Balance at January 1, 2019	69,151	\$ 5.70
DSUs Issued	61,447	–
DSUs redeemed	(9,027)	7.65
Balance at December 31, 2019	121,571	\$ 7.68

	Number of DSUs	Closing Share Price
Balance at January 1, 2020	121,571	\$ 7.68
DSUs Issued	65,905	6.99
DSUs redeemed	(14,788)	6.24
DSUs forfeited	(12,154)	7.17
Balance at December 31, 2020	160,534	\$ 8.47

An expense of \$518,000 (2019 – \$367,000) was recorded in general and administrative expenses. The liability of \$1,360,000 (2019 – \$934,000) related to these DSUs is included in accounts payable and accrued liabilities.

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

18. Earnings per share

The computations for basic and diluted earnings per share from continuing operations are as follows:
(earnings in thousands of dollars)

	2020	2019
Basic earnings per share from continuing operations	\$ 1.20	\$ 1.13
Calculated as:		
Net Earnings attributable to the equity holders of the Company from continuing operations	\$ 14,062	\$ 13,306
Weighted average number of shares outstanding	11,744,924	11,735,495
Fully diluted earnings per share from continuing operations	\$ 1.20	\$ 1.13
Calculated as:		
Net Earnings attributable to the equity holders of the Company from continuing operations	\$ 14,062	\$ 13,306
Weighted average number of shares outstanding including effects of dilutive potential ordinary shares	11,748,360	11,755,662
Reconciliation of weighted average number of shares outstanding:		
Weighted average number of shares outstanding used to calculate basic earnings per share	11,744,924	11,735,495
Adjustment for dilutive effect of stock option plan	3,436	20,167
Weighted average number of shares outstanding used to calculate diluted earnings per share	11,748,360	11,755,662

As at December 31, 2020, 120,000 options (2019 – 195,000) are excluded from the diluted average number of shares calculation as their effect would have been anti-dilutive.

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The computations for basic and diluted loss per share from discontinued operations are as follows:

	2020	2019
Basic loss per share from discontinued operations	\$ –	\$ (0.14)
Calculated as:		
Net loss attributable to the equity holders of the Company from discontinued operations	\$ –	\$ (1,699)
Weighted average number of shares outstanding	11,744,924	11,735,495
Fully diluted loss per share from discontinued operations	\$ –	\$ (0.14)
Calculated as:		
Net loss attributable to the equity holders of the Company from discontinued operations	\$ –	\$ (1,699)
Weighted average number of shares outstanding including effects of dilutive potential ordinary shares	11,744,924	11,735,495
Reconciliation of weighted average number of shares outstanding:		
Weighted average number of shares outstanding used to calculate basic earnings per share	11,744,924	11,735,495
Adjustment for dilutive effect of stock option plan	–	–
Weighted average number of shares outstanding used to calculate diluted earnings per share	11,744,924	11,735,495

	2020	2019
Basic earnings per share	\$ 1.20	\$ 0.99
Calculated as:		
Net Earnings attributable to the equity holders of the Company	\$ 14,062	\$ 11,607
Weighted average number of shares outstanding	11,744,924	11,735,495
Fully diluted earnings per share	\$ 1.20	\$ 0.99
Calculated as:		
Net Earnings attributable to the equity holders of the Company	\$ 14,062	\$ 11,607
Weighted average number of shares outstanding including effects of dilutive potential ordinary shares	11,748,360	11,755,662
Reconciliation of weighted average number of shares outstanding:		
Weighted average number of shares outstanding used to calculate basic earnings per share	11,744,924	11,735,495
Adjustment for dilutive effect of stock option plan	3,436	20,167
Weighted average number of shares outstanding used to calculate diluted earnings per share	11,748,360	11,755,662

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

19. Pension plans

Defined contribution plan:

The Group has defined contribution pension plans that are available to virtually all of its Canadian employees with eligible employee contributions based on 2.00% – 6.75% of annual earnings. The Group's contributions of \$1,655,000 (2019 – \$1,586,000) matches the employee contributions. The Group's contributions related to its defined contribution pension plans are recorded as follows: \$1,240,000 (2019 – \$1,190,000) in cost of sales, \$205,000 (2019 – \$197,000) in selling and distribution, and \$210,000 (2019 – \$199,000) in general and administrative.

20. Provisions

	Warranties	Site restoration	Benefits	Restructuring	Total
Balance at January 1, 2019	\$ 581	\$ 178	\$ 296	\$ 6,232	\$ 7,287
Provisions made during the period	807	130	19	947	1,903
Provisions used during the period	(768)	(109)	(86)	(4,197)	(5,160)
Recovery of provisions (note 24)	–	–	–	(2,035)	(2,035)
Balance at December 31, 2019	\$ 620	\$ 199	\$ 229	\$ 947	\$ 1,995
Balance at January 1, 2020	\$ 620	\$ 199	\$ 229	\$ 947	\$ 1,995
Provisions made during the period	1,439	257	61	–	1,757
Provisions used during the period (note 24)	(392)	(225)	(60)	(855)	(1,532)
Recovery of provisions (note 24)	–	–	–	(92)	(92)
Balance at December 31, 2020	\$ 1,667	\$ 231	\$ 230	\$ –	\$ 2,128
Current portion	\$ 1,667	\$ 86	\$ 58	\$ –	\$ 1,811
Non-current portion	\$ –	\$ 145	\$ 172	\$ –	\$ 317

Warranties

The provision for warranties relates mainly to transformers sold during the years ended December 31, 2020 and December 31, 2019. The provision is based on estimates made from historical warranty data associated with similar products and claims experience. The Group expects to incur most of the liability over the next year.

Site restoration

The Group has committed to undertaking a joint remediation plan for the Glen Ewing property with the owner of an adjoining industrial property and the co-owner of the property. The Group has recorded a liability for its estimated portion of the joint remediation.

Benefits

The benefit provision relates to statutory pension and leave benefits related to the India facility. Substantially all of this benefit is long-term.

Restructuring charges

The restructuring charges relate to estimated severance, termination benefits and closure costs in respect of the closure of the Italian operations. Such costs are anticipated to be settled within the following year. See note 24 for details.

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

21. Sales

	2020	2019
Canada	\$ 109,080	\$ 116,996
United States and Mexico	198,324	225,709
India	14,693	16,077
	322,097	358,782
Italy – discontinued operations	–	281
	\$ 322,097	\$ 359,063

As at December 31, 2020 the Company had contract liabilities of \$204,000 (2019 – \$268,000) included in accounts payable and accrued liabilities.

22. Government assistance

The Government of Canada implemented the Canada Emergency Wage Subsidy program (“CEWS”) that provides a subsidy of up to 75% of eligible remuneration paid by an eligible entity that experienced significant revenue declines due to the COVID-19 global pandemic. In 2020, the Company has qualified for subsidy payments. The subsidy amounts relating to the year have been recorded as a reduction in expenses as follows: cost of sales \$5,557,000, selling and distribution \$776,000 and general and administrative \$1,950,000 for a total of \$8,283,000.

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23. Discontinued operations

In December 2018, the Company closed the Italian operations due to low sales volume and a weak economy. Prior to this, the Italian operation was not previously classified as a discontinued operation. The 2019 consolidated statements of operations have been presented for the years ended to show the discontinued operation separately from continuing operations.

The 2020 Italy operations consist of an investment property which continues to be presented within continuing operations.

	2019
Revenue	\$ 281
Cost of sales	1,461
Gross loss	(1,180)
Selling and distribution	225
General and administrative	335
Impairment of goodwill, intangibles and plant and equipment	–
Restructuring charges (recovery)	(728)
Loss from operations	(1,012)
Interest income	–
Loss on disposition of assets	(687)
Loss from discontinued operations before tax	(1,699)
Income tax	–
Loss from discontinued operations, net of tax	\$ (1,669)

In November 2019, the Group entered into an agreement to sell the inventory and certain equipment of the Italian operation, and for the purchaser to assume certain of the employee obligations and lease the manufacturing facility from the Group. Cash consideration paid to the Group in connection with the transaction was 1,086,000 EUR (approximately \$1,583,000 Canadian dollars). The transaction resulted in a loss on disposition in the amount of \$687,000, calculated as follows:

	Canadian dollar values
Total consideration	\$ 1,583
Property, plant and equipment	\$ 1,539
Inventory	885
Employee liabilities	(154)
Carrying value of net assets sold	\$ 2,270
Loss on disposition	\$ 687

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Cash flows from discontinued operations

Cash flows from discontinued operations, are included within the following components of the Statements of Cash Flows:

		2019
Net cash used in operating activities	\$	(643)
Net cash generated by investing activities		1,460
Net cash used in financing activities		–

24. Restructuring charges

2019 activity

During 2019 additional information regarding restructuring costs was identified related to the closure of the Italian operations, as outlined below. The following table highlights the amounts charged to expense for the twelve month period ending December 31, 2019:

		Restructuring Charges
Cancellation and closure costs	\$	947
Expected credit loss – VAT Receivable		360
	\$	1,307

The amount of the cancellation and closure costs have been included in provisions in the amount of \$947,000.

2020 activity

During 2020 the cancellation and closure costs of \$855,000 were paid and \$92,000 of the provision was reversed into income to bring the provision balance to nil. The expected credit loss related to the VAT receivable continues to be provided for and is included in the net accounts receivable value in the amount of \$339,000.

25. Related party transactions

Related parties

Arathorn Investments Inc. beneficially owns 2,778,300 (2019 – 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 1,065,191 (2019 – 1,063,152) Class A subordinate voting shares of the Company, representing approximately 11.9% (2019 – 11.9%) of the issued and outstanding Class A subordinate voting shares of the Company and as a result controls the Company. All of the issued and outstanding shares of Arathorn Investments Inc. are owned by William G. Hammond, Chief Executive Officer and Chairman of the Company. Total dividends paid during the year, directly and indirectly to William G. Hammond were \$1,306,000 (2019 – \$1,075,000).

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

Key management personnel compensation

Key management personnel include the Company's directors and members of the executive management team. Compensation awarded to key management is as follows:

	2020		2019	
Salaries and benefits	\$	2,809	\$	2,308
Share-based awards		518		367
	\$	3,327	\$	2,675

26. Personnel expenses

	2020		2019	
Wages and salaries	\$	57,246	\$	58,972
Group portion of government pension and employment pension and employment benefits		16,636		16,314
Contributions to defined contribution plans		1,655		1,586
	\$	75,537	\$	76,872

27. Change in operating working capital

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

	2020		2019	
Accounts receivable	\$	10,926	\$	5,006
Inventories		1,720		(2,290)
Prepaid expenses and other assets		(15)		(384)
Accounts payable and accrued liabilities		(11,115)		119
Provisions		(947)		(5,160)
Foreign exchange		(5,561)		(3,665)
	\$	(4,992)	\$	(6,374)

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

28. Segment disclosures

The Company operates in a single operating segment, being a manufacturer of transformers. The Company and its subsidiaries operate in Canada, the United States, Mexico, Italy and India. Inter-segment sales are made at fair market value.

Geographic Segments	2020		2019	
Sales				
Canada	\$	109,080	\$	116,996
United States and Mexico		198,324		225,709
India		14,693		16,077
		322,097		358,782
Italy – discontinued operations		–		281
	\$	322,097	\$	359,063
Property, plant and equipment and right-of-use assets – net				
Canada	\$	15,981	\$	17,667
United States		7,767		6,769
Mexico		3,929		5,183
Italy		75		95
India		2,620		2,754
	\$	30,372	\$	32,468
Investment in properties				
Canada	\$	1,044	\$	1,044
Italy		2,605		2,665
	\$	3,649	\$	3,709
Investment in joint venture				
Mexico	\$	13,300	\$	13,428
Intangibles, net				
Canada	\$	3,593	\$	3,641
Italy		8		17
India		2,300		2,673
	\$	5,901	\$	6,331
Goodwill				
Canada	\$	2,180	\$	2,180
India		8,728		9,129
	\$	10,908	\$	11,309

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29. Financial instruments

Fair value

The fair value of the Group's financial instruments measured at fair value has been segregated into three levels. 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. Fair value of assets and liabilities included in Level 2 include valuations using inputs other than quoted prices for which all significant inputs are observable, either directly or indirectly. Fair value of assets and liabilities included in Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement.

The Group's financial instruments measured at fair value consist of foreign exchange forward contracts with a fair value of a net liability of \$1,952,000 (2019 – net liability of \$1,392,000) and are included in Level 2 in the fair value hierarchy. To determine the fair value of the contracts, Management used a valuation technique in which all significant inputs were based on observable market data. There have been no transfers between levels in 2020 or 2019. The gains and losses from these contracts are grouped with foreign exchange gain on the statement of operations.

The carrying values of cash and cash equivalents, accounts receivable, bank operating lines of credit, and accounts payable and accrued liabilities and other liabilities approximate their fair value due to the relatively short period to maturity of the instruments. The Group's note receivable is valued at the present value of the future receipts and has a fair value of \$nil due to collection concerns. The lease receivable is valued at the present value of the future receipts which approximates the fair value

Derivative instruments

The Group has entered into forward foreign exchange contracts in order to reduce the Company's exposure to changes in the exchange rate of the U.S. dollar, Euro, Mexican Peso and Indian Rupee as compared to the Canadian dollar. At December 31, 2020, the Company had outstanding forward foreign exchange contracts to buy and sell the following contracts, all with maturity dates in January 2021.

Buy/Sell	Buy Currency	Selling Currency	Amount of Buy Currency	Traded Rate
BUY	EUR	CAD	11,800	1.5540
BUY	EUR	USD	5,700	1.2210
BUY	USD	CAD	83,500	1.2704 - 1.3099
BUY	USD	INR	8,949	73.0300 - 74.4800
BUY	USD	MXN	12,657	19.892
Buy/Sell	Sell Currency	Buying Currency	Amount of Sell Currency	Traded Rate
SELL	USD	MXN	25,000	19.9260 – 20.1420
SELL	EUR	CAD	23,600	1.5541-1.5550
SELL	EUR	USD	11,400	1.1846 – 1.2221
SELL	USD	CAD	46,500	1.2702
SELL	USD	INR	4,529	72.8500

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At December 31, 2019, the Company has outstanding forward foreign exchange contracts to buy and sell the following contracts, all with maturity dates in January 2020.

Buy/Sell	Buy Currency	Selling Currency	Amount of Buy Currency	Traded Rate
BUY	EUR	CAD	9,200	1.4562
BUY	EUR	USD	8,000	1.1212
BUY	USD	CAD	104,000	1.2990 - 1.3306
BUY	USD	INR	9,198	71.4200 - 72.0900
BUY	USD	MXN	12,357	18.9440
Buy/Sell	Buy Currency	Selling Currency	Amount of Buy Currency	Traded Rate
SELL	USD	MXN	24,000	18.9898 - 19.5083
SELL	EUR	CAD	18,400	1.4574 - 1.4682
SELL	EUR	USD	16,000	1.1041 - 1.1222
SELL	USD	CAD	52,000	1.2985
SELL	USD	INR	4,634	71.2000

As at December 31, 2020 the Group has recognized a net unrealized loss of \$1,952,000 representing the fair value of these forward foreign exchange contracts, comprised of an obligation recognized within accounts payable and accrued liabilities. As at December 31, 2019 the Group recognized a net unrealized loss of \$1,392,000, comprised of obligation recognized within accounts payable and accrued liabilities.

Financial risk management

The Group is exposed to a variety of financial risks by virtue of its activities: market risk (including currency risk, interest rate risk and commodity price risk) credit risk and liquidity risk. The overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on financial performance. There were no changes to types of risk arising from the Group's financial instruments from the previous period.

Risk management is carried out by the finance department under the guidance of the Board of Directors. This department identifies and evaluates financial risks in close cooperation with management. The finance department is charged with the responsibility of establishing controls and procedures to ensure that financial risks are mitigated.

Currency risk

The Group operates internationally and is exposed to foreign exchange risk from various currencies, primarily U.S. dollars, Mexican Pesos, the Euro and the Indian Rupee. Foreign exchange risk arises mainly from U.S. dollar denominated purchases in Canada and Canadian sales to the U.S. as well as recognized financial assets and liabilities denominated in foreign currencies. The Company manages its foreign exchange risk by having geographically diverse manufacturing facilities and purchasing U.S. dollar raw materials in Canada. The Company also monitors forecasted cash flows in foreign currencies and attempts to mitigate the risk by entering into forward foreign exchange contracts. Forward foreign exchange contracts are only entered into for the purposes of managing foreign exchange risk and not for speculative purposes.

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The following table represents the Group's balance sheet exposure to currency risk as at December 31, 2020:

	U.S. Dollars		Mexican Pesos		Euros		Indian Rupees	
	2020	2019	2020	2019	2020	2019	2020	2019
Cash	\$ 5,928	\$ 10,639	852	3,680	€ 1,526	€ 1,717	187,323	71,670
Accounts receivable	20,526	28,575	24,377	26,387	831	1,238	227,817	289,551
Long-term lease receivable	–	–	–	–	2,208	2,332	–	–
Bank operating lines of credit	(4,622)	(8,160)	–	–	(3,074)	(3,144)	–	–
Accounts payable	(13,373)	(19,507)	(9,612)	(10,376)	(88)	(359)	(111,871)	(93,427)
Lease obligation	(6,836)	(8,170)	–	–	–	–	(6,317)	(9,295)
Net exposure	\$ 1,623	\$ 3,377	15,617	19,691	€ 1,403	€ 1,784	296,952	258,499

A one cent (\$0.01) decline in the Canadian dollar against the U.S. dollar as at December 31, 2020 would have decreased net earnings by \$119,000 and increased equity by \$22,000. This analysis assumes that all other variables, in particular interest rates, remained constant. Inversely, a one cent (\$0.01) increase in the Canadian dollar against the U.S. dollar as at December 31, 2020 would have had an equal but opposite effect.

A one cent (\$0.01) decline in the Canadian dollar against the Euro as at December 31, 2020 would have decreased net earnings by \$47,000 and increased equity by \$21,000. Inversely, a one cent (\$0.01) increase in the Canadian dollar against the Euro as at December 31, 2020 would have had an equal but opposite effect.

A one cent (\$0.01) decline in the Canadian dollar against the Indian Rupee as at December 31, 2020 would have increased net earnings and equity by \$54,000. Inversely, a one cent (\$0.01) increase in the Canadian dollar against the Indian Rupee as at December 31, 2020 would have had an equal but opposite effect.

A one cent (\$0.01) decline in the Canadian dollar against the Peso as at December 31, 2020 would have decreased net earnings by \$2,000 and increased equity by \$10,000. Inversely, a one cent (\$0.01) increase in the Canadian dollar against the Peso as at December 31, 2020 would have had an equal but opposite effect.

Credit risk

Credit risk arises from the possibility that the Group's customers and counter parties may experience difficulty and be unable to fulfill their contractual obligations. The Group manages this risk by applying credit procedures whereby analyses are performed to control the granting of credit to its customer and counter parties based on their credit rating. As at December 31, 2020, the Group's accounts receivable are not subject to significant concentrations of credit risk. The long-term lease receivable is subject to credit risk, which is mitigated by the security of the related plant. The Company's maximum exposure to credit risk associated with the Group's financial instruments is limited to their carrying amount.

The Group's exposure to customer credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the factors that may influence the credit risk of its customer base, including the default risk associated with the industry and country in which customers operate.

Management has a credit policy under which each new customer is analysed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered. The Group's review includes external ratings, if they are available, financial statements, credit agency information, industry information and in some cases bank references. Sale limits are established for each customer and reviewed quarterly. Any sales exceeding those limits require approval from Executive management.

The Group limits its exposure to credit risk from trade receivables by establishing a reasonable payment period. Many of the Group's customers have been transacting with the Group for a number of years, and none of these customers'

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balances have been written off or are credit-impaired at the reporting date.

In monitoring customer credit risk, customers are grouped according to their credit characteristics, including their geographic location, industry, trading history with the Group and existence of previous financial difficulties.

An allowance account for accounts receivable is used to record impairment losses unless the Group is satisfied that no recovery of the amount owing is possible; at which point the amounts are considered to be uncollectible and are written off against the specific accounts receivable amount attributable to a customer. The number of days outstanding of an individual receivable balance is the key indicator for determining whether an account is at risk of being impaired.

Expected credit losses are required to be measured through a loss allowance at an amount equal to the 12-month expected credit losses or full lifetime expected credit losses. The Group has used past due information to determine that there have been no significant increases in credit risk since initial recognition. There are balances in excess of 30 days past due but the Group does not presume that credit risk has increased given the characteristics of the Group's customers, the industries in which they operate, the customer payment track records and the nature of the products the Group sells.

During the year, the expected credit losses for trade accounts receivables decreased \$420,000 (2019 – increased \$516,000), for which a recovery (2019 – expense) was recognized in general and administrative expenses. The aging of accounts receivable and the related allowance is as follows:

	December 31, 2020		December 31, 2019	
	Gross	Allowance	Gross	Allowance
Not past due	\$ 35,192	\$ –	\$ 43,287	\$ –
Past due 0-30 days	10,461	–	11,251	–
Past due 31-120 days	6,405	–	6,991	–
Past due more than 120 days	3,597	2,577	5,472	2,997
	\$ 55,655	\$ 2,577	\$ 67,001	\$ 2,997

Credit risk

The carrying amount of financial assets representing the maximum exposure to credit risk at the reporting date was:

	December 31, 2020		December 31, 2019	
	Carrying Amount			
Cash and cash equivalents	\$	14,795	\$	23,371
Accounts receivable		53,078		64,004
Lease receivable		3,433		3,397
	\$	71,306	\$	90,772

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The maximum exposure to credit risk for accounts receivable at the reporting date by geographic region was:

	Carrying Amount	
	December 31, 2020	December 31, 2019
Canada	\$ 19,711	\$ 17,435
United States	26,297	36,987
Mexico	1,561	1,818
Italy	268	827
India	5,241	6,937
	\$ 53,078	\$ 64,004

Interest rate risk

Interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Financial assets and financial liabilities with variable interest rates expose the Group to cash flow interest rate risk. Changes in market interest rates also directly affect cash flows associated with the Group's bank operating lines of credit that bear interest at floating interest rates.

The Group manages its interest rate risk by minimizing the bank operating lines of credit balances by applying excess funds while maintaining the liquidity necessary to conduct operations on a day-to-day basis as well as actively monitoring interest rates. A 1% increase or decrease in interest rates as at December 31, 2020 would increase or decrease net earnings by approximately \$161,000 (2019 – \$327,000) respectively.

Commodity price risk

A large component of the Group's cost of sales is comprised of copper and steel, the costs of which can vary significantly with movements in demand for these resources and other macroeconomic factors. To manage its exposure to changes in commodity prices, the Group will enter into supply contracts with certain suppliers, and from time to time will enter into forward commodity purchase contracts. As at December 31, 2020, no forward commodity purchase contracts were outstanding (2019 – none).

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its obligations as they become due.

The Group manages its liquidity risk by forecasting cash flows from operations and anticipated investing and financing activities. Senior Management is also actively involved in the review and approval of planned expenditures.

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The following are the carrying amounts and related contractual maturities of the Group's financial liabilities:

December 31, 2020	Carrying amount	1 year or less	1-2 years	2-5 years
Bank operating lines of credit	\$ 16,073	\$ 16,073	\$ –	–
Accounts payable and accrued liabilities	44,227	44,227	–	–
Derivative liabilities	1,952	1,952	–	–
	\$ 62,252	\$ 62,252	\$ –	\$ –
December 31, 2019	Carrying amount	1 year or less	1-2 years	2-5 years
Bank operating lines of credit	\$ 32,697	\$ –	\$ 32,697	–
Accounts payable and accrued liabilities	54,824	54,824	–	–
Derivative liabilities	1,392	1,392	–	–
	\$ 88,913	\$ 56,216	\$ 32,697	\$ –

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Reconciliation of movements of liabilities to cash flows arising from financing activities.

The following is a reconciliation between the opening and closing balances for liabilities arising from financing activities:

	Liabilities		Equity		
	Bank Operating Lines of Credit	Lease Liabilities	Share Capital	Retained Earnings	Total
Balance January 1, 2020	\$ 32,697	\$ 11,404	\$ 14,491	\$ 85,339	\$ 143,931
Advances of bank operating lines of credit	(16,624)	–	–	–	(16,624)
Interest payments	(917)	–	–	–	(917)
Cash dividends paid	–	–	–	(3,993)	(3,993)
Repayment of lease liability	–	(2,650)	–	–	(2,650)
Total changes from financing	\$ (17,541)	\$ (2,650)	\$ –	\$ (3,993)	\$ (24,184)
Other changes					
Liability-related					
Interest expense	917	330	–	–	1,247
Foreign exchange	–	(107)	–	–	(107)
Non-cash additions to lease liabilities	–	343	–	–	343
Total liability-related other changes	\$ 917	\$ 566	\$ –	\$ –	\$ 1,483
Equity-related					
Net income	–	–	–	14,062	14,062
Total equity-related other changes	\$ –	–	\$ –	\$ 14,062	\$ 14,062
Balance December 31, 2020	\$ 16,073	\$ 9,320	\$ 14,491	\$ 95,408	\$ 135,292

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	Liabilities		Equity		
	Bank Operating Lines of Credit	Lease Liabilities	Share Capital	Retained Earnings	Total
Balance January 1, 2019	\$ 32,601	\$ 11,657	\$ 14,217	\$ 79,218	\$ 137,693
Implementation of accounting standard	–	–	–	(1,960)	(1,960)
Adjusted balance January 1, 2019	\$ 32,601	\$ 11,657	\$ 14,217	\$ 77,258	\$ 135,733
Advances of bank operating lines of credit	96	–	–	–	96
Interest payments	(1,420)	(325)	–	–	(1,745)
Proceeds from issue of share capital	–	–	290	–	290
Share repurchase	–	–	(77)	(239)	(316)
Cash dividends paid	–	–	–	(3,287)	(3,287)
Repayment of lease liability	–	(2,431)	–	–	(2,431)
Total changes from financing	\$ (1,324)	\$ (2,756)	\$ 213	\$ (3,526)	\$ (7,393)
Other changes					
Liability-related					
Interest expense	1,420	–	–	–	1,420
Non-cash additions to lease liabilities	–	1,853	–	–	1,853
Total liability-related other changes	\$ 1,420	\$ 1,853	\$ –	\$ –	\$ 3,273
Equity-related					
Share repurchase	–	–	12	–	12
Exercise of stock options	–	–	49	–	49
Net income	–	–	–	11,607	11,607
Total equity-related other changes	\$ –	–	\$ 61	\$ 11,607	\$ 11,668
Balance December 31, 2019	\$ 32,697	\$ 10,754	\$ 14,491	\$ 85,339	\$ 143,281

For the years ended December 31, 2020 and 2019 (tabular amounts in thousands of dollars, except share and per share amounts)

30. Capital risk management

The Group's objective is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future business development. The Group includes cash, bank operating lines, long-term debt and equity, comprising of share capital, contributed surplus and retained earnings in the definition of capital. The Group is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital risk management strategy during the year ended December 31, 2020.

The following table sets out the Group's capital quantitatively at the following reporting dates:

	December 31, 2020	December 31, 2019
Cash and cash equivalents	\$ 14,795	\$ 23,371
Bank operating lines of credit	(16,073)	(32,697)
Lease liabilities	(9,320)	(11,404)
Share capital	14,491	14,491
Contributed surplus	2,498	2,498
Retained earnings	95,408	85,339
	\$ 101,799	\$ 81,598

31. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the Notes specific to that asset or liability.

(a) Derivatives

The fair value of forward exchange contracts is based on valuations obtained from third parties, based on observable market inputs.

Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Group entity and counterparty when appropriate.

(b) Non-derivative financial assets

The fair value of the lease receivable is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

(c) Share-based payment transactions

The fair value of DSUs is determined in accordance with the DSU Plan, which uses the average closing price for HPS shares for the five trading days immediately preceding the relevant date.

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(d) Investment property

The fair values of the investment properties are based on available market evidence as determined by third party valuers using comparable property sale transactions and is considered to be valued at Level 3 of the fair value hierarchy.

32. Subsequent events

Dividends

On March 5, 2021, the Company declared a dividend of eight and a half cents (\$0.085) per Class A subordinate voting shares of HPS and a quarterly cash dividend of eight and a half cents (\$0.085) per Class B common shares of HPS payable on March 25, 2021 to shareholders of record at the close of business on March 18, 2021. The ex-dividend date is March 17, 2021.