CAE

REMARKS FOR CAE'S THIRD-QUARTER FISCAL YEAR 2009

February 11, 2009

Time: 12:00 p.m.

Speakers:

Mr. Robert E. Brown, President and Chief Executive Officer

Mr. Marc Parent, Executive Vice-President, and Chief Operating Officer

Mr. Alain Raquepas, Vice-President, Finance, and Chief Financial Officer

Mr. Andrew Arnovitz, Vice-President, Investor Relations and Strategy

Andrew Arnovitz, Vice President, Investor Relations and Strategy

Good afternoon, everyone, and thank you for joining us today. Before we begin I need to read the following:

"Certain statements made during this conference, including, but not limited to, statements that are not historical facts, are forward-looking and are subject to important risks, uncertainties and assumptions. The results or events predicted in these forward-looking statements may differ materially from actual results or events. These statements do not reflect the potential impact of any non-recurring or other special items or events that are announced or completed after the date of this conference, including mergers, acquisitions, or other business combinations and divestitures.

You will find more information about the risks and uncertainties associated with our business in the MD&A section of our annual report and annual information form for the year ended March 31, 2008. These documents have been filed with the Canadian securities commissions and are available on our website (www.cae.com) and on SEDAR (www.sedar.com). They have also been filed with the U.S. Securities and Exchange Commission under Form 40-F and are available on EDGAR (www.sec.gov). Forward-looking statements in this conference represent our expectations as of February 11, 2009 and, accordingly, are subject to change after this date.

We do not update or revise forward-looking information even if new information becomes available unless legislation requires us to do so. You should not place undue reliance on forward-looking statements."

With me today are Robert E. Brown, CAE's President and Chief Executive Officer, Marc Parent, our Chief Operating Officer, and Alain Raquepas, our Chief Financial Officer.

After comments from Bob and Alain, we will take questions from financial analysts and institutional investors.

For your convenience, this conference call will be archived on CAE's Website: www.cae.com

Let me now turn the call over to Bob…

Robert E. Brown, President and Chief Executive Officer

Thank you, Andrew, and thank you everyone for joining us this afternoon.

I will begin with a discussion of our third-quarter performance and then conclude with some comments about the environment that we expect to face in the period ahead. Alain will take you through our results in more detail and then Marc, Alain and I will take your questions.

Our performance in the third quarter and year to date reflects the resilience of our diversified business model. Our combined military segments continued to deliver on expectations for increased growth and profitability, and our Civil Training and Services segment produced positive results notwithstanding the deterioration that has occurred in certain markets. In Simulation Products/Civil we continued to execute our backlog and concluded the quarter with good results in light of the unfavourable currency hedge position that we are still making our way through.

We have positioned CAE well over the past few years, which has enabled us to succeed in the face of a number of challenges like the once soaring Canadian dollar. It is no secret that the year ahead will present exceptional challenges for civil aviation—especially in the areas related to new aircraft deliveries, and to a lesser extent, areas that depend on the installed base. I will address this in my remarks at the end of the call.

Our success over the past few years has come largely from institutionalizing a culture of change. And we will need to take actions to confront the current economic environment, and to ensure that we are in a position to prosper when the civil aviation market eventually stabilizes.

Revenue in the third quarter grew 23% from last year to $424.6 million, and net earnings increased 35% to $53.3 million and our consolidated operating margin was 18.5%.

We took in $455 million in new orders and concluded the quarter with a $2.9 billion backlog.

In **Training & Services/Civil** we signed agreements with an expected value of $139 million and we had an average of 118 Revenue Simulator Equivalent Units in operation. We are feeling the effects of airline capacity reductions and decreased hours flown in business aviation. Training is integral to the operation of an aircraft and this segment of our business more rapidly feels the effects of changing market conditions that affect the installed base. Overall, our utilization rate was lower at 75% compared to 81% for the same period last year. I have cautioned in the past that this is not an overly consistent metric to follow, but it does reflect the lower demand that we are experiencing -- more acutely in the U.S., and to a lesser extent in other regions. We made good operational progress despite these headwinds. We continued to ramp-up the utilization of our recently installed training assets, which have helped to support our overall performance. Average annualized revenue per simulator increased to $4.1 million dollars from $3.4 million last year. The foreign exchange rates vis-à-vis the Canadian dollar are currently on our side and helping to offset a portion of the market softness.

In **Simulation Products/Civil**, we signed orders for 11 full-flight simulators during the quarter from customers including American Airlines, Continental Airlines, Air New Zealand, Saudi Arabian Airlines, Air China and the Hua Ou Training Centre in Beijing. Year to date, we have announced 31 sales and we continue to expect a total of 34 by March 31st.

In the **combined military segments**, we won new orders totalling $183.7 million. We signed a contract to supply the U.S. Navy with an MH-60S tactical operational flight trainer and we won upgrade work for the German Army on a Eurocopter EC135 simulator. As well, we received a contract option exercise related to the U.S. Army SE Core Program. In Training and Services, we signed contracts for C-130 simulator training and maintenance services for the U.S. Air Force; Danish Merlin pilot training at our training centre in the U.K; and simulator maintenance and support services for the German Army and Air Force.

With that, I will now ask Alain to discuss our financial results.

Alain Raquepas, Chief Financial Officer

Thank you, Bob and good afternoon everyone.

In **Training and Services/Civil**, revenue was up 30% over last year to $121 million. We grew the average number of RSEUs in our network by 9 units and we incorporated the results from Sabena Flight Academy. Note that this acquisition is still being integrated and it caused some drag on the segment's operating margin in the quarter. Segment operating income was $21.6 million, which is 39% higher than last year and 13% higher than last quarter. The segment operating margin was 17.9% this quarter compared to 16.7% last year.

In **Simulation Products/Civil**, revenue was $119 million, up 15% from last year. Segment operating income decreased 10% from last year to $22.8 million because of a less favourable program mix and a less beneficial currency hedge position this year compared to last year. We are still working through orders that were hedged when the Canadian to U.S. dollar exchange rate was closer to par. These impacts were somewhat offset by our receipt from a customer of $1.7 million that had been deemed uncollectible and written-off several years ago. Assuming the Canadian dollar stays low, it will eventually help offset some of the weakness caused by softer demand.

In **Simulation Products/Military**, revenue was $126 million, 40% higher than last year. We had higher activity on a number of recently awarded programs and here again, we benefited from the lower Canadian dollar. Segment operating income was $25.7 million and the margin was 20.5% compared to 12.8% last year. The increase comes from a combination of higher volume, favourable FX, and higher utilization of funds from our Project Phoenix R&D cost sharing program.

In **Training and Services/Military**, revenue was equal to last year at $59 million. Segment operating income of $8.6 million was 9% lower than last year and the operating margin was 14.6% compared to 16.1% last year. In the third quarter last year we benefited from a revenue recovery related to our annual labour rate review with the Canadian government. This year we had a mix of revenue increases and decreases in training and maintenance services and we benefited from FX translation.

When evaluating trends in our combined military business, we encourage investors to consider periods of 12 months or longer, given the unevenness of performance from quarter to quarter. The combined operating margin for these two segments reached 18.6% this quarter. We expect the average margin will be around 15% for the foreseeable future.

Capital expenditures totalled $52 million this quarter, comprised of $38 million in growth capital expenditures in support of our prior investment commitments. We have continued to expand selectively our training network to address additional market share and to respond to training demands in new markets. The balance is attributed to maintenance capital expenditures that were $14 million.

Income taxes this quarter were $19.8 million, representing an effective tax rate of 27%, which is lower than usual because of a settlement of tax audits and changes in the mix of income from various tax jurisdictions. We still expect the effective income tax rate for the year to be about 30%.

Free cash flow was $71.7 million in the third quarter, up $21.9 million year over year. The increase was mainly due to a $52.7 million recovery in non-cash working capital, offset by a decrease of $20.1 million in cash provided by continuing operations, an increase in maintenance capital expenditures of $5.7 million and an increase in cash dividends of $4.9 million.

Finally, **net debt** increased $9.4 million from last quarter because of the lower Canadian dollar against our foreign denominated debt. This was partially offset by a net increase in cash.

Thank you for your attention. I will now turn the call back to Bob.

Robert E. Brown, President and Chief Executive Officer

Thanks, Alain.

Last quarter we commented on the high level of market uncertainty and how this makes forecasting in the civil aerospace market difficult. We also expressed our belief that things would likely get worse for civil aviation before things get better. Things have gotten worse, and the market in the period ahead will be very challenging.

IATA has predicted 3% lower commercial passenger traffic this year and several of the world's airlines have already taken steps, or have announced plans to reduce capacity – particularly in North America. These measures combined with the lower cost of fuel should eventually help bolster airline performance. As for new aircraft deliveries, so far Boeing and Airbus have maintained their record backlogs, which stand at seven years of deliveries at current production rates. They have managed to offset aircraft deferrals with demands for new aircraft. Orders for new aircraft were lower in 2008 but still exceeded deliveries by a good margin. Given the current climate, we expect aircraft orders to be substantially lower in 2009. What remains most unclear is the number of expected deliveries in the following few years, which may be impacted by deferrals and cancellations occurring this year. As well, it is unclear what the state of the aircraft financing market will be as we go through the period ahead. Export credit agencies in Europe have increased their commitment to help mitigate the apparent aircraft funding gap, and so have the OEMs. We expect this situation will become clearer in the coming months and this will be an important driver for orders in our Simulation Products / Civil segment. We have already assumed that aircraft deliveries will be lower this year than last and this will impact full-flight simulator orders.

During the last cycle downturn CAE was battling the impact of a Canadian dollar that increased from the mid-60 cent level to about 80 cents U.S. CAE's much higher cost base back then made it virtually impossible to make money with lower volumes and a strong dollar. This time we face the opposite situation with the dollar decreasing to around 80 cents from above par. Assuming the dollar remains around its current exchange level, this segment will be partially bolstered by the weaker dollar as our foreign currency hedges get closer to the prevailing exchange rates.

The Simulation Products/Civil segment of our business is tied to aircraft deliveries and it is important to note that we have been deliberately diversifying CAE to become less dependent on the delivery cycle and to become more dependent on the already-installed base of aircraft. Year-to-date, Simulation Products/Civil accounted for 30% of CAE's revenue, which is substantially lower than in past market cycles. Our strategy has been to grow the other parts of our business at a faster pace.

In business aviation, the number of hours flown were down 19% in December and 12% for the year overall. “For sale” or used aircraft represented 17% of the installed base at year-end and will for some time compete with new aircraft orders. The impact of the downturn on training demand is most acute on the small- and medium-sized jets and especially on the older models. Recent announcements from the business jet manufacturers have confirmed large numbers of order deferrals and cancellations. The OEMs have taken action to drop production capacity on a range of platforms. The larger business aircraft tend to be more resilient in economic downturns and so far production on the high-end models appears to be stable.

Our Training and Services/Civil segment tends to be more related to the already-installed base of aircraft, which means that it is inherently more stable than a business that relies exclusively on new aircraft deliveries. The number of hours flown globally has dropped significantly – less so internationally and more so in North America. As we said earlier on the call, we are already experiencing the impacts of lower demand – especially for training on the older and smaller aircraft.

We have been getting some relief from FX as the dollar has fallen from last year’s highs. As well, we have been advancing CAE’s position in adjacent service areas, which helps to bolster our revenue per simulator. On balance, we expect the period ahead to be more challenging and we are already taking steps to lower our costs and scale our training operations around the world. The training network is well diversified and while we expect continued drag from the current conditions, we think we can demonstrate relative resilience with this segment’s performance.

Now, turning to the **Military** half of our business, we expect to continue to produce strong results in the period ahead, which should help to offset the impact of the civil aerospace downturn. We believe that we can sustain an average annual revenue growth rate of 10% and an EBIT margin of about 15% for the foreseeable future.

CAE plays an important role internationally, serving the simulation-based training needs of more than 30 national defence forces. We are in a strong position on a number of aircraft platforms like the NH90 helicopter and C130-J transport aircraft that have extensive global reach and a high degree of relevance in today’s defence environment. Here in Canada we are hopeful of concluding soon a substantial agreement to provide an equipment and multi-year training services solution to the Canadian Forces in support of its new airlift capability.

The U.S. defence market is the largest by far and defence spending is expected to remain stable at least through the 2010 budget year. The new administration has made it clear that defence and security will remain a top priority, as well as the preservation of jobs in the defence industry. The U.S. Secretary for Defense has reiterated their focus on operational readiness and we believe that simulation-based training is integral to that view.

Our best intelligence and forecasting, however, indicates that there are several trends and factors lending support to our optimism in our military business. First, aircraft platforms such as helicopters and transports are the workhorses for militaries worldwide, and these platforms are where CAE has experience and capability. Second, training and readiness remains a top priority, and there is a continued growth in the use of simulation for more and more training requirements. Third, militaries globally outsource training support services to industry so that active-duty personnel can focus on operational requirements, and we see a number of opportunities over the next several years in this area. Finally, there is growing acceptance in the use of simulation beyond training, for analysis and operations, so we see growth prospects for our professional services business.

The Global War on Terror is front and center for all governments and their security needs. With this reality, defence forces and other public security agencies must prepare and train for known and unknown threats. CAE's simulation-based solutions are central to achieving a higher level of readiness.

In conclusion, we are operating in a very challenging civil aerospace environment but we designed CAE's strategy for this eventuality, and our balanced portfolio is proving its strength. We will adapt as required to scale and position our business appropriately. In recent years we have shown our ability to adapt to highly volatile markets. We will continue to take a sober approach and we are already taking steps to help ensure that we can make the most of the current conditions:

- first, we are assessing our operations globally to reduce costs and right-size capacity;
- second, we are identifying ways to create more variability in our overall cost structure;
- third, our COO, Marc Parent, is working to drive new synergies between our four business segments;

- fourth, we are evaluating our R&D programs to ensure that we are running at a suitable pace. Our strategic priority is to maintain our technological leadership and this needs to be balanced with constraints suggested by the current environment; and finally,
- and finally, we are working with financial entities to help our customers gain access to financing in this highly irregular credit market.

We believe we have a realistic view of the highly volatile situation we face and we will respond in a way that takes all aspects of our business into consideration, including the positive prospects for our defence business; our new growth initiatives; and the relative durability of our service business.

Thank you for your attention. We are now ready to take your questions.

Andrew?

Andrew Arnovitz, Vice President, Investor Relations and Strategy

Operator, we would now be pleased to take questions from analysts and institutional investors.

Before we open the lines, let me first ask in the interest of fairness that you limit yourself to a single, one-part question. If you have additional questions and time permits, please feel free to re-enter the queue.