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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 40-F

(Check One)

o Registration statement pursuant to Section 12 of the Securities Exchange Act of 1934

or

þ Annual report pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934

For fiscal year ended: March 31, 2005 Commission File number: 1-31402

CAE INC.

(Exact name of Registrant as specified in its charter)

Canada	**3699**	**Not Applicable**
(Province or Other Jurisdiction of Incorporation or Organization)	*(Primary Standard Industrial Classification Code Number, if applicable)*	*(I.R.S. Employer Identification Number, if applicable)*

8585 Côte-de-Liesse, Saint-Laurent, Québec, H4T 1G6

514-341-6780

(*Address and Telephone Number of Registrant's principal executive office)*

CT Corporation System, 111 Eighth Avenue, 13th Floor, New York, NY 10011 (212) 894-8700

(*Name, Address and Telephone Number of Agent for Service in the United States)*

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Common Shares, including associated Common Share purchase rights pursuant to the Registrant's Shareholder Rights Plan, which purchase rights will trade together with the Common Shares	**New York Stock Exchange** **Toronto Stock Exchange**

Securities registered or to be registered pursuant to Section 12(g) of the Act: none

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: none

For annual reports, indicate by check mark the information filed with this form:

þ Annual Information Form þ Audited Annual Financial Statements

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: **248,070,329**

Indicate by check mark whether the registrant by filing the information contained in this form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934 (the "Exchange Act"). If "Yes" is marked, indicate the file number assigned to the registrant in connection with such rule. Yes o No þ

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13(d) or 15(d) of the Exchange Act during the proceeding 12 months (or for such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements in the past 90 days.
Yes þ No o

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DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to ensure that information required to be disclosed by CAE in reports filed with securities regulatory agencies is recorded, processed, summarized and reported on a timely basis and is accumulated and communicated to CAE's management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Internal control over financial reporting are procedures designed to provide reasonable assurance that transactions are properly authorized, assets are safeguarded against unauthorized or improper use, and transactions are properly recorded and reported. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance with respect to the reliability of financial reporting and financial statement preparation. Accordingly, CAE's management, including our Chief Executive Officer and our Chief Financial Officer, does not expect that CAE's internal control over financial reporting will prevent or detect all error and all fraud.

There has been no change in CAE's internal control over financial reporting during the year ended March 31, 2005 that materially affected, or that is reasonably likely to materially affect, CAE's internal control over financial reporting.

CAE will continue to periodically review its disclosure controls and procedures and internal control over financial reporting and may make modifications from time to time as considered necessary or desirable. CAE is reviewing its existing internal control over financial reporting in preparation for the reporting and attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002 becoming effective. In connection with such review, modifications were made to CAE's disclosure controls and procedures and internal control over financial reporting and further modifications will, as appropriate, be made to CAE's disclosure controls and procedures or internal control over financial reporting in the future.

AUDIT COMMITTEE FINANCIAL EXPERT

CAE's board of directors has determined that it has at least one audit committee financial expert serving on its audit committee. The board of directors has determined that Mr. James F. Hankinson is an audit committee financial expert and is independent, as that term is defined by the New York Stock Exchange's corporate governance standards applicable to CAE.

The Securities and Exchange Commission has indicated that the designation of a person as an audit committee financial expert does not impose on such person any duties, obligations or liability that are greater than those imposed on such person as a member of the audit committee and the board of directors in the absence of such designation and does not affect the duties, obligations or liability of any other member of the audit committee or board of directors.

CODE OF ETHICS

CAE has adopted a code of ethics entitled, "Code of Business Conduct". The Code of Business Conduct applies to all officers and employees of CAE, including CAE's principal executive officer, principal financial officer, principal accounting officer, agents, representatives, contractors, suppliers and consultants. The Code of Business Conduct is available at CAE's Internet website, www.cae.com, in the Corporate Governance section. Amendments to the Code of Business Conduct and waivers, if any, for executive officers will be disclosed on CAE's website.

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PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following PricewaterhouseCoopers LLP aggregate fees were billed to CAE in each of the years ended March 31, 2005 and 2004 for professional services rendered to CAE:

Fees	2005 (amounts in CAD$ millions)	2004 (amounts in CAD$ millions)
Audit Fees [1]	$ 2.3	$ 2.0
Audit-Related Fees [2]	0.7	0.8
Tax Fees [3]	0.3	0.7
All Other Fees[4]	—	0.1
Total	**$ 3.3**	**$ 3.6**

1 Audit fees comprise professional services for the audit of CAE's annual financial statements, review of CAE's interim financial statements, and services normally provided in connection with CAE's statutory and regulatory filings.

2 Audit-Related Fees comprise amounts paid relating to the issuance of a prospectus and due diligence in connection with CAE's acquisitions and divestitures.

3 Tax Fees comprise professional services rendered for tax compliance and advice.

4 All Other Fees comprise amounts paid relating to certification services under certain government obligations, news services and software.

AUDIT COMMITTEE PRE-APPROVAL POLICIES AND PROCEDURES

CAE's Audit Committee has adopted a pre-approval policy with respect to permitted non-audit services. Under this policy, subject to certain conditions, specified audit-related services, tax compliance, audit services and tax services may be presented to the Audit Committee for pre-approval as a category of services on an annual or project basis. On a quarterly basis, management of CAE is required to update the Audit Committee in respect of the actual amount of fees in comparison to the pre-approved estimate. All non-audit services not otherwise pre-approved by the Audit Committee must be pre-approved by the Audit Committee on an individual basis. Non-audit services may be approved by the Chairman of the Audit Committee, provided that any such pre-approval is reported to the full Audit Committee at its next meeting. None of the services described above under the captions "Audit-Related Fees", "Tax Fees" or "All Other Fees" were approved pursuant by the Audit Committee pursuant to paragraph (c)(7)(i)(C) of Rule 2-01 of Regulation S-X.

OFF-BALANCE SHEET ARRANGEMENTS

The disclosure provided under "Off-Balance Sheet Arrangements" on page 36 of Exhibit 3, Management's Discussion and Analysis, is incorporated by reference herein.

CONTRACTUAL OBLIGATIONS

The disclosure provided under "Contractual Obligations" on page 35 of Exhibit 3, Management's Discussion and Analysis, is incorporated by reference herein.

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IDENTIFICATION OF THE AUDIT COMMITTEE

CAE's Audit Committee is comprised of the following directors: John A. Craig, Richard J. Currie, O.C., Paul Gagné, James F. Hankinson and James W. McCutcheon.

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UNDERTAKING AND CONSENT TO SERVICE OF PROCESS

A. Undertaking

CAE Inc. (the "Registrant") undertakes to make available, in person or by telephone, representatives to respond to inquiries made by the staff of the Securities and Exchange Commission ("SEC"), and to furnish promptly, when requested to do so by the SEC staff, information relating to the securities in relation to the obligation to file an annual report on Form 40-F arises or transactions in said securities.

B. Consent to Service of Process

The Registrant has previously filed with the SEC a Form F-X in connection with the Common Shares, including the associated Common Share purchase rights pursuant to the Registrant's Shareholder Rights Plan, which purchase rights trade together with the Common Shares.

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SIGNATURES

Pursuant to the requirements of the Exchange Act, the Registrant certifies that it meets all of the requirements for filing on Form 40-F and has duly caused this annual report to be signed on its behalf by the undersigned, thereto duly authorized.

Date: June 28, 2005

CAE INC.

By: /s/ Hartland Paterson
Name: Hartland J. A. Paterson
Title: Vice President, Legal, General Counsel and Corporate Secretary

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EXHIBIT INDEX

Exhibit No.	Description
1	Annual Information Form dated June 28, 2005
2	Audited annual financial statements for the fiscal year ended March 31, 2005
3	Management's Discussion and Analysis for the year ended March 31, 2005
4	Consent of PricewaterhouseCoopers LLP
5	Certificate of Robert E. Brown required by Rule 13a-14(a) or Rule 15d-14(a), pursuant to Section 302 of Sarbanes-Oxley Act of 2002
6	Certificate of Alain Raquepas required by Rule 13a-14(a) or Rule 15d-14(a), pursuant to Section 302 of Sarbanes-Oxley Act of 2002
7	Certificate of Robert E. Brown pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of Sarbanes-Oxley Act of 2002
8	Certificate of Alain Raquepas pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of Sarbanes-Oxley Act of 2002
9	Notice and Proxy Informational Circular dated May 12, 2005, other than the sections entitled "Report on Executive Compensation" and "Performance Graph" (incorporated by reference to Exhibit 99.1 of the Registrant's Form 6-K (Commission file No. 1-31402), excluding such sections, furnished to the Commission on June 1, 2005)

EXHIBIT 1

June 28, 2005



ANNUAL INFORMATION FORM
2005

June 28, 2005

CORPORATE OFFICE
8585 Côte-de-Liesse
Saint-Laurent, Québec
Canada H4T 1G6

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INFORMATION INCORPORATED BY REFERENCE

The Company's Review of Operations and Management's Discussion and Analysis and its consolidated financial statements for the year ended March 31, 2005, and the notes thereto (the "Consolidated Financial Statements") appear on pages 16 to 41 and pages 43 to 86 respectively in the Annual Report to Shareholders for the year ended March 31, 2005 (the "Annual Report"). The Consolidated Financial Statements were prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP"). For a discussion of the principal difference between Canadian GAAP and the accounting principles generally accepted in the United States, see note 27 to the Consolidated Financial Statements. The information contained therein is specifically incorporated by reference into this Annual Information Form (AIF). Any parts of the Annual Report not specifically incorporated by reference do not form part of this AIF.

Unless otherwise noted, all dollar references in this Annual Information Form are expressed in Canadian dollars.

References to fiscal 2005 refer to the period from April 1, 2004 to March 31, 2005, references to fiscal 2004 refer to the period from April 1, 2003 to March 31, 2004, and references to fiscal 2003 refer to the period from April 1, 2002 to March 31, 2003.

This Annual Information Form contains forward-looking statements with respect to CAE and its subsidiaries based on assumptions which CAE considered reasonable at the time they were prepared and may include information concerning the Company's future financial performance, business strategy, plans, goals and objectives. These forward-looking statements, by their nature, necessarily involve risks and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking statements. Statements preceded by the word "believe", "expect", "anticipate", "intend", "continue", "estimate", "may", "will", "should" and similar expressions are forward-looking statements. CAE cautions the reader that the assumptions regarding future events, many of which are beyond the control of CAE, may affect the extent to which a particular projection materializes and/or could ultimately prove to be incorrect. Factors that could cause actual results or events to differ materially from current expectations are discussed on pages 36 and 37 of the Annual Report. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise. In particular, forward-looking statements do not reflect the potential impact of any merger, acquisition or other business combinations or divestitures that may be announced or completed after such statements are made.

ITEM 3 — CORPORATE STRUCTURE OF CAE

3.1 Name, Address and Incorporation

March 17, 1947:	CAE Inc. (the "Company" or "CAE") was incorporated under the name Canadian Aviation Electronics Ltd. under the laws of Canada by letters patent.
July 5, 1965:	The name of the Company was changed to CAE Industries Ltd.

August 3, 1977:	The Company was continued under the Canada Business Corporations Act (the “CBCA”) by certificate of continuance.
June 10, 1993:	The Company changed its name to its present one, CAE Inc.

In 1979, the articles of the Company were amended to change its authorized share capital to an unlimited number of common shares. Each issued and outstanding Class A and Class B share was redesignated and changed into three common shares.

In 1981, the Company’s articles were again amended to subdivide the issued and outstanding common shares on a three-for-one basis, and to authorize an unlimited number of preferred shares, issuable in series, with such rights, privileges, restrictions and conditions as the directors of the Company may determine by resolution. The articles were amended further in 1984 and 1986, in each case to subdivide the issued and outstanding common shares on a two-for-one basis.

On June 9, 1995, the Company’s articles were amended to authorize the directors to appoint additional directors in accordance with the provisions of the CBCA.

On April 1, 2001, the Company was amalgamated with CAE Electronics Ltd., its wholly-owned subsidiary.

The Company’s registered office is located at 8585 Côte-de-Liesse, Saint-Laurent, Québec **,** Canada H4T 1G6, telephone: (514) 341-6780, fax: (514) 341-7699.

3.2 Inter-corporate Relationships

The direct and indirect subsidiaries and other ownership interests of the Company are set out in Schedule “A” hereto.

ITEM 4 – GENERAL DEVELOPMENT OF THE BUSINESS

4.1(a) General

Following incorporation in 1947, CAE’s primary business focused on the repair and overhaul of electronic and electro-mechanical equipment, as well as the design and installation of telecommunication and navigational systems. By the early 1950s, the Company had started to pursue new areas of opportunity in the design, development and manufacture of flight, radar and weapons simulators for Canadian defence requirements. A few years later, CAE began its commercial flight simulation activities.

From the 1960s to the turn of the century, the Company embarked on a program of growth and diversification. CAE acquired several new businesses, both in its traditional aerospace and electronics market segment and in several industrial technology segments. The industrial technology businesses provided a number of diverse engineered products and services for industries worldwide, chiefly those involved in fiber processing technologies (forest products,

pulp and paper), cleaning technologies (automotive parts, medical equipment and electronic food processing), and railway technologies and services.

The strategy was significantly changed in fiscal 2000, with the focus turned to the Company's core strengths and key opportunities. Over the last five years, CAE executed this strategy, divesting itself of its non-core businesses and transforming from being primarily a manufacturer of simulation equipment to also being a provider of fully integrated training in its core businesses: Civil Simulation and Training (CS&T) and Military Simulation and Training (MS&T).

CAE's strategy going forward revolves around taking the necessary steps to restore shareholder value. It will do this by leveraging its extensive experience in modeling and simulation to expand both vertically into other products and services within the aerospace and defence industry, as well as horizontally to pursue opportunities presented by emerging markets such as homeland defence and urban simulation. In order to be able to respond to growth opportunities, CAE must continue to invest in new and innovative technologies. See section 5.1 (2) "Reorganization" of this AIF for further details.

4.1(b) History

Over the past three fiscal years, CAE completed the following divestitures to better focus on its core businesses:

On June 28, 2002, CAE sold CAE Cleaning Technologies plc, one of CAE's Cleaning Technologies operations, to the same former management group which previously purchased CAE Ransohoff Inc. and CAE Ultrasonics, Inc. earlier that year.

On August 16, 2002, CAE sold its sawmill businesses to COE Manufacturing Company.

On April 30, 2003, CAE sold the operations of CAE Beyss GmbH, another of CAE's Cleaning Technologies businesses, to Bavaria Industriekapital AG.

On May 2, 2003, CAE sold its wood products business to Carmanah Design and Manufacturing Inc., a TD Capital company.

On July 31, 2003, CAE sold substantially all the assets of its last remaining Cleaning Technologies business, Alpheus Inc. to Cold Jet Inc. of Cincinnati, Ohio.

CAE completed the divestiture of substantially the entire Marine Controls segment to L-3 Communications ("L-3") of New York, New York during the fourth quarter of fiscal 2005 in a transaction valued at $239 million, resulting in an after-tax gain of approximately $104 million. In accordance with the purchase agreement, L-3 will also acquire two other components of the Marine Controls segment, including the assumption of the CAE's guarantee of £23.0 million of project-finance related debt for the UK Astute Class submarine training program, following all required approvals being obtained.

Through a combination of divestments and consolidations, the Company reduced the number of profit centers from 21 to 3.

April 1, 2005 CAE formed the Simulation Products Group to consolidate all manufacturing activities as well as engineering, program management, global procurement, and sales and marketing of civil simulation equipment. Its most important priorities are lowering costs across the board and shortening manufacturing cycle times.

CAE is investing in software and hardware innovations that will sustain its leading-edge technologies as well as complement its training services for CAE training centers and other customers. Examples of such innovation are the Company's SimFinity™ leading-edge simulation-based courseware, its Tropos™ and Medallion-S™ image generators and its STRIVE™ software development framework to test, model and design military systems during their planning and acquisition phases.

CAE has continued its investment in pilot training, and its increased access to the US and European military markets, during the past three years. In addition to acquisitions, CAE's move into civil aviation and training was further accelerated during that period with the following training center initiatives:

- In May 2004, CAE acquired LAN's training facility in Santiago, Chile and commenced providing flight training to LAN's pilots under a 10-year services agreement. CAE added an Airbus A320 full flight simulator ("FFS") in January 2005 to the existing Boeing 737-200 FFS already in operation in the center. A Boeing 767-300ER FFS will be added later in 2005. The A320 device is part of the CAE-Airbus training cooperation.

- CAE and Iberia Lineas Aereas de Espana, SA ("Iberia") formed an aviation training joint venture, consolidating the assets of their respective Spanish training centres – CAE's in Alcala and Iberia's at the Barajas airport. CAE contributed its Alcala assets and Iberia its Barajas assets and related debt to form a new company, in which Iberia is now training its nearly 2,000 pilots. CAE and Iberia have an 80-20 equity split, respectively.

- In August 2002, CAE and Airbus entered into a ten-year renewable co-operation agreement to develop a global network of training centers with the largest fleet of Airbus FFS in the world and offering a very high quality of Airbus flight crew training. Under this agreement, CAE is providing equipment, facilities and advanced training technologies while Airbus is providing its courseware and training expertise. The result is a worldwide global network of training centers combining the Miami and Toulouse Airbus facilities with those of CAE in Denver, Toronto, Madrid, Brussels, Rome, Dubai, Singapore and Sao Paulo. CAE is responsible for adding FFS and related training technologies in line with Airbus standards and expanding the global network according to market demand. This network is offering the whole range of integrated training solutions, from simulator availability to complete training for initial, recurrent, transition and specialty training.

- The Denver, Colorado facility became operational in July 2002. The four-bay center is currently operating four simulators: an Airbus A320, two Bombardier CRJ200/700 and a

CRJ200. The Denver center is strategically located close to the country's sixth busiest airport and is the first independent training center in the US for Bombardier CRJ700 regional jets. Two airlines are the anchor tenants in the new facility: Frontier Airlines and Air Wisconsin. The two carriers have committed to long-term training agreements of 5 years and 15 years, respectively. Other current customers include Horizon Air and over-flow training from Mesa Air Group.

- CAE's training facility located in an Arizona State University building near Phoenix, Arizona became operational in March 2003, and the Company signed a 10-year training contract with Mesa Air Group ("Mesa") for services at that center. CAE is providing training solutions to Mesa, primarily in support of the airline's fleet of Bombardier CRJ and Embraer ERJ-145 aircraft. CAE has installed a Bombardier CRJ200/700/900 FFS and an Embraer ERJ-145 FFS in the two-bay facility. With this new facility, CAE became the first independent training provider for the new CRJ900 regional jet. The contract with Mesa also includes CAE's SimFinity™ CRJ200/700/900 Integrated Procedure Trainer, the latest high-fidelity SimFinity™ three-dimensional training solution.

- CAE and China Southern Airlines ("China Southern") announced in November 2002 the formation of a joint venture to provide aviation-training solutions for Asian carriers. The joint venture company, Zhuhai Xiang Yi Aviation Technology Company Limited, is owned 51% by China Southern and 49% by CAE and is operating from China Southern's training facility at its Zhuhai flight base in Guangdong province. It is focused on developing and delivering high technology training solutions for aviation, initially offering simulation-based pilot training and other technical services for carriers operating Boeing 737NG, 737-300, 777, 757-200 and Airbus A320 and A321 aircraft.

- In operation since June 2002, Emirates-CAE Flight Training Center resulted from a July 2001 teaming agreement between Emirates Airlines and CAE. Located in a new 14 bay-facility, the center includes Airbus A319/A320/A321, Airbus A330/340, Boeing 737 NG/BBJ, Gulfstream IV and Gulfstream V FFS and a convertible Hawker 800/800XP FFS. The Dubai center is offering the highest standard in aviation training and facilities in the region for both airlines and corporate aircraft operators. It trains pilots to European Joint Aviation Authorities ("JAA"), UAE GCAA and US Federal Aviation Administration ("FAA") standards on CAE-designed FFS. Emirates-CAE Flight Training is equipped with the industry's latest integrated training technologies including CAE's SimFinity™ classroom trainer and convertible A320/B737 Integrated Procedures Trainer ("IPT").

CAE has experienced significant successes in military simulation and training in recent fiscal years:

- CAE-led Landmark Training Ltd. ("Landmark") was selected in 2004 as the intended preferred bidder for the British Army's Armoured Vehicles Training Service (AVTS) program. The AVTS program was to have been a private finance initiative designed to provide turnkey driver, gunnery and command information systems training to crews of armoured fighting vehicles. Landmark was notified on June 15, 2005 by the UK Ministry

of Defence of a change of approach to the program as it now intends to proceed with a conventional procurement strategy.

- In June 2003, CAE announced the creation of a consortium named “Rotorsim”, owned equally by CAE and Agusta S.p.A., to operate a new helicopter training facility in Sesto Calende, Italy and to provide integrated training solutions for AgustaWestland helicopters. The Rotorsim facility will open in early 2006 with the delivery of a CAE-built A109 full mission simulator (“FMS”). Later in 2006, Rotorsim will add a CAE-built AB139 FMS to the training centre. CAE subsequently signed a $7.8 million contract with Agusta S.p.A. for an upgrade to the Italian army’s A129 helicopter flight simulator located at the army-training base in Viterbo, Italy. CAE will provide its CAE Medallion-S™ image generator as part of the upgrade program.

- CAE’s Medium Support Helicopter Aircrew Training Facility (MSHATF) opened at Royal Air Force (RAF) Base Benson in Oxfordshire in 2000. The facility is the product of a highly innovative, 20 year, private finance initiative contract with the UK MoD. Payment is based on a guaranteed minimum usage and also allows for third party usage. Currently third party training is being provided to the Air Forces of The Netherlands, Republic of Singapore, Canada and others. The facility provides training to the RAF and third party customers on the Eurocopter Puma, Boeing CH-47 Chinook, and AgustaWestland EH-101 Merlin helicopters. The MSHATF is equipped with six CAE-built FMS (three Chinook, two Merlin, one Puma), four computer-based training classrooms, and a state-of-the-art tactical control center to plan and monitor training missions. It is staffed with a team of highly experienced former military instructors.

- Over the past several fiscal years, CAE USA has played a key role in establishing CAE’s presence in the critical US defence market. CAE USA is qualified as a prime contractor for each of the major US services (Air Force, Army, Navy), thus affording CAE USA the opportunity to pursue key US defence training and simulation programs. CAE USA is qualified as a prime contractor on the US Air Force Training Systems Acquisition II contract, US Army STRICOM Omnibus Contract, and US Navy Training Systems Contract. Recently, CAE USA qualified as a prime contractor for the first time on the US Navy’s Fielded Training Systems Support contract.

- The past three fiscal years have seen CAE USA establish a growing relationship with the US Army’s 160th Special Operations Aviation Regiment, an elite unit known as the “Night Stalkers”. CAE USA has been awarded contracts valued at more than $150 million over the past three years to design and develop a range of mission rehearsal and training systems for this customer. Included in CAE’s development has been the world’s first A/MH-6 Little Bird combat mission simulator, which is being delivered to the 160th during the summer of 2005. CAE is working on a range of innovative developments for the Special Operations Forces.

- In fiscal 2005, CAE USA secured a significant program win with the US Navy to develop a range of training systems for the new MH-60S Knighthawk helicopter. CAE USA is under contract to design and manufacture three MH-60S tactical operational flight trainers and four MH-60S weapons tactics trainers in a program valued at more than $80

million.

These last few examples underscore the close relationship that CAE has established in the US military market over the past several years.

4.1(c) Industry Overview and Trends

The civil and military markets CAE serves are driven by factors particular to each market. CAE believes the civil market is most affected by the nature and composition of aircraft fleets, pilot demographics, certification requirements and market demand for commercial and business air travel. The Company believes the military market is most influenced by a combination of defence spending and the nature of military activity.

4.1(d) Civil Simulation and Training

The use of flight simulators in pilot and crew training is well established within the commercial and business markets. Increased use of simulators has occurred as a result of the growth in commercial and business air travel which, in turn, has driven fleet expansion and increased demand for pilot training. Civil simulator usage has also increased due to advances in technology that enable increased realism and the significant cost savings provided by flight simulation training compared to actual flight time. The use of synthetically-generated reproductions of airport configurations and use of satellite terrain imagery incorporated into the simulation further enhance the effectiveness of simulation training. Simulators are also utilized by pilots to supplement actual flying time to maintain their certification. Today's most sophisticated civil flight simulators are rated Level D by the FAA or receive similar ratings from regulatory authorities in other countries, indicating that a pilot can be certified to fly an aircraft type based solely on simulator training. Flight simulators also allow pilots to experience and learn emergency procedures that cannot be practiced safely aboard the actual aircraft.

Flight simulation equipment is purchased by major and regional airlines, aircraft manufacturers and independent training providers. Simulators are manufactured by a limited number of companies and are sold based on the criteria of product quality, service, delivery, supplier reputation, price and life cycle costs. In fiscal 2005, 17 FFS were sold to third parties in the global competed market, in which contracts are awarded on the basis of a competitive bidding process. Average prices for civil flight simulation equipment can range from up to US$1 million for sophisticated procedure trainers, from US$2 to US$6 million for a flight training device (FTD) to US$11 to US$15 million for an FFS, assuming that OEM-supplied data, parts and equipment are included.

Within the flight simulation industry, training services is the largest and fastest growing market segment. The training services market consists of sales of training equipment, facilities, tools, programs, and instructors designed to enable pilots to obtain and retain the necessary qualifications to pilot a particular aircraft, and to enable maintenance workers to inspect, maintain and repair aircraft. Training is carried out by airlines as well as independent training providers. Currently, approximately half of the FFS in use around the world are owned and operated by commercial airlines to provide training to their pilots, with the vast majority owned by large commercial airlines. These large commercial airlines also use independent training

facilities to supplement their training programs. Ownership of simulators by regional airlines is considerably less common and virtually not the case for business aircraft operators. As a result these companies primarily use independent training providers.

CAE believes the following trends and developments will continue to drive the civil simulation and training industry:

Effectiveness and Cost Advantages of Simulation-Based Training

Simulation-based training is an essential element in civil pilot and crew training. The realism of the simulated flight experience has made procedure trainers, fixed training devices and FFS effective tools for training pilots and crew. Pilots and crew can be trained for a variety of aircraft, using visualizations of most of the civil airports around the world, and in varying environmental conditions. The cost savings to aircraft operators are substantial as it is 5 to 10 times cheaper to train in a simulator than in a civil aircraft. In addition, simulator training minimizes the risk of accidents and resulting injury to personnel and damage to equipment. FFS training users are also accorded more favorable liability insurance premiums. Simulator-based training also offers considerable flexibility with respect to the timing and duration of training sessions. In the past, the use of independent training services was limited by the availability of convenient training centers. With the development of additional independent training centers around the world, CAE believes that this historical deterrent will be addressed. CAE believes that the costs of acquiring and maintaining FFS will encourage additional usage of independent training providers by commercial airlines.

Pilot Certification and License Requirements

Piloting an aircraft is a regulated activity requiring both initial and recurring training to achieve defined levels of competence and experience. To keep a license to fly an aircraft weighing over 12,500 pounds, certain regulations require pilots to demonstrate proficiency for that aircraft type at least once a year. Certification and license requirements can be satisfied through simulated flight and many pilots elect to do so.

Expansion and Diversification of Aircraft Fleets

The introduction of new aircraft and expansion and diversification of fleets creates incremental pilot training requirements. Simulation training is now considered an essential element in pilot and crew training for the large commercial, regional and business segments of the market. An experienced pilot typically needs between 15 and 40 hours on a simulator to learn the intricacies of a new aircraft. CAE estimates that approximately one simulator is required to support every 20 wide-bodied commercial aircraft in operation, with that ratio changing to one for 40 regional jets and one for 80 business aircrafts.

New aircraft deliveries are a major driver for this market. In ‘‘The World Market for Large Commercial Jet Transports’’, Forecast International/DMS Inc. projects that 6,075 large commercial jet transports will be produced from 2005 to 2014.

Demand in recent years for civil air travel and the timing of delivery of new aircraft were adversely affected by the September 11, 2001 terrorist attacks, the ensuing war in Afghanistan, the SARS epidemic and the war on Iraq. As a result, aircraft orders suffered and CAE experienced a reduction in new third party orders for FFS. The market uncertainty caused by these events had a very negative effect on commercial airlines, aircraft manufacturers and, by extension, CAE, the Civil simulation division of which is somewhat dependent on the health and success of those industries. However, the impact of these events has been less severe on the demand for flight training services as pilots still need to be trained.

Virtually every business aircraft transaction, whether a new or after-market transaction, triggers the need for pilot training. Business aircraft simulation training is provided by independent training providers. CAE believes that additional demand for business aircraft simulation training will be driven by growth in new business aircraft sales – 11,036 are forecast to be produced between 2005 and 2014 — and the increase in fractional ownership and unscheduled charter flights. Long-term growth in civil air travel will drive increased aircraft deliveries across the spectrum of aviation service providers and, in turn, the demand for simulation technology and training.

Pilot Demographics

According to AIR Inc., US pilot hiring in 2004 doubled from 2003. In 2004, 9,382 were hired and more than 10,800 are expected to be hired in 2005. The most active airlines in the hiring are the low-cost, nationals and regional airlines. As pilots retire, other pilots must be trained to fly the aircraft. Historically, the major commercial airlines hired a substantial number of pilots from the military as these pilots retired or otherwise left military service. In recent years, there have been fewer available military pilots. The relative lack of available military pilots has caused increased demand for qualified pilots throughout the industry. As a result, the major airlines have begun to more actively promote pilots to larger aircraft from within their existing ranks or from regional airlines operating smaller aircraft. This increased mobility within a fleet results in more pilots needing to be certified on different aircraft and a corresponding increase in training requirements. The number of pilots on furlough in the US declined by 6% in 2004.

Other Factors

The September 11, 2001 terrorist attacks had an immediate and severe adverse impact on the passenger traffic and yields of CAE's customers in the civil airline industry. Even as the after-effect on the industry of the shock of that event and the subsequent war in Afghanistan were receding, the SARS epidemic and Iraqi war again caused a sharp drop-off in commercial travel coupled with higher fuel and other costs. Civil airline operators have continued to experience significantly lower revenue and have incurred additional costs for increased security, higher insurance premiums and jet fuel. Despite increased passenger traffic, the market is still fragile. Because of these events, resulting airline bankruptcies and funding problems and continuing weak domestic and international economic conditions, CAE expects that the delivery of new aircraft will be slightly higher than in 2004.

4.1(e) Military Simulation and Training

Military forces increasingly rely on sophisticated and interrelated weapons systems and equipment, computer systems, visual systems and other advanced technologies to operate in a broadening range of conditions and scenarios. Achieving a high state of operational readiness is a constant goal and challenge for militaries. Simulators enable military organizations to achieve their training goals while minimizing the physical use of expensive systems and equipment. In addition, the use of simulators helps to avoid injuries to personnel and the loss of equipment due to training accidents. Simulators allow for the training of tasks and missions that cannot be practiced in the real world.

Flight simulators are used to train pilots to operate a variety of military aircraft including fighter jets, helicopters and transport aircraft. Flight simulators permit the crews of military aircraft to coordinate and improve their essential combat skills in a safe, cost-effective and realistic range of environments. It is 15 to 25 times cheaper to train in a simulator than in a military aircraft. The simulators enable pilots to realistically practice both offensive and defensive tactics, such as firing aircraft weapons systems and avoiding attack from enemy surface and air threats. The immersive environment provided by simulators allows pilots to train for highly demanding maneuvers and life threatening scenarios, such as rotor failure, missile impact or the effects of exceptional turbulence.

Simulators for land systems provide similar advantages. Though land systems equipment is generally less complex than that found in aircraft, the systems often operate in conjunction with other equipment in environments involving many soldiers and various weapons systems.

CAE believes the following trends will influence the development of the military simulation and training market:

Increasing Defence Spending

Following the September 11, 2001 terrorist attacks, the US government increased its defence spending. The fiscal 2005 national defence budget in the US was more than US$455 billion, which does not include additional funding requested to support the war effort in Iraq. In fiscal 2006, according to the US Office of Management and Budget the US defence budget is expected to be about US$420 billion plus an anticipated $50 billion to $75 billion in supplemental funding expected for the war on terror. The US government's defence spending has recently represented close to 50% of the world's total defence spending and this is expected to continue through this decade. Apart from spending on defence, there is an increased emphasis on security in most Western nations in the face of increased terrorist threats. CAE expects that some of this spending will address new technologies and training for counter-terrorism activities.

Rapid Evolution of Technology and Warfare

Technological advances and the changing nature of warfare have resulted in a rapid evolution of weapons systems and equipment. This has been illustrated by recent events in Afghanistan and Iraq, where the coalition forces faced asymmetric threats and where extensive use was made of unmanned air vehicles ("UAV") such as the Predator and Global Hawk. Military forces face a

wide range of operations which are increasingly likely to be asymmetric or involve operations in urban terrain. In light of these changing circumstances, the key focus of military forces has evolved towards information dominance linked with networked weapons systems. These highly technical networked systems lend themselves to modeling, simulation, and simulation-based training.

Accelerated developments in computer and visual technologies enable devices of greater fidelity and promote the proliferation of simulation technologies. In particular, the rapid evolution of commodity graphics technologies of recent years has substantially redefined the price/performance envelope of visual equipment. Visual systems provide simulator-correlated, geo-specific representations of the synthetically generated environment under a broad range of weather, illumination and other conditions. Visual database representations can be rapidly synthesized from the Geographical Information System, including satellite data, and applied to military mission rehearsal exercises.

The introduction of new aircraft and weapons platforms, as well as upgrades and life extensions to existing aircraft and weapons platforms will necessitate new training requirements for military operators. For example, CAE expects programs in Europe such as the Eurofighter 2000, the A400M military airlifter and the NH90 helicopters to provide significant simulation and training opportunities. In addition, upgrades to aircraft such as the German Tornado tactical aircraft and the UK Lynx helicopter fleets will create additional flight simulation requirements. In North America, the US Air Force's upgrade of its C-130 fleet under the C-130 Avionics Modernization Program will also require corresponding upgrades and new simulators to train aircrews on upgraded aircraft. Other aircraft programs such as the F-35 (Joint Strike Fighter), the US Navy's Multi-mission Maritime Aircraft and the US Army's Armed Reconnaissance Helicopter will also enter service in the US over the next decade and produce opportunities for training systems. CAE is actively pursuing these opportunities.

Evolving Role of Simulation Training

CAE believes that the military will continue to make greater use of simulation as an effective solution for more frequent and sophisticated training requirements for several reasons. First, advances in technology have enhanced the realism that can be achieved in simulation training. As a result, militaries are more receptive to utilizing this technology. The achieved realism combined with the development of extensive environment databases offer militaries the ability to train in situations and conditions either difficult or impossible to consistently replicate in a physical setting. Second, simulation training also is more cost effective than training personnel on actual equipment. Third, simulation training involves less potential for accidents and resulting injury to personnel and damage to equipment. Finally, CAE believes simulation will increasingly be used in areas consistent with the Simulation Based Acquisition initiatives of the US Department of Defense which seek to use simulation to evaluate competing system designs prior to commitment to full scale design and development.

Increasing Interest of Governments in Privately Financed Long-Term Training Models

The increasing sophistication of weapons systems has resulted in the need for more sophisticated training equipment and services. The development, construction and delivery of these training

resources require a high level of specialized technology and knowledge, and often involve significant expense. The UK government has increasingly turned to private sector companies to build, maintain and deliver training equipment and services under long-term private financed initiatives ("PFI") because these companies can deliver an integrated training solution more quickly and efficiently and at lower cost. CAE's MSHATF is already in full scale operation in the UK's first military training PFI. CAE-led Landmark Training Ltd. ("Landmark") was selected in 2004 as the intended preferred bidder for the British Army's Armoured Vehicles Training Service (AVTS) program. The AVTS program was to have been a private finance initiative designed to provide turnkey driver, gunnery and command information systems training to crews of armoured fighting vehicles. Landmark was notified on June 15, 2005 by the UK Ministry of Defence of a change of approach to the program as it now intends to proceed with a conventional procurement strategy. The government of Germany awarded a consortium that includes CAE, Eurocopter, Rheinmetall Defence Electronics GmbH and Thales a contract to provide NH90 helicopter training services to the German Armed Forces over 14.5 years beginning in 2008.

ITEM 5– NARRATIVE DESCRIPTION OF THE BUSINESS

5.1 General

CAE is a world leading designer and manufacturer of advanced simulation equipment and provider of integrated training solutions for the military and civil aviation markets. With nearly 60 years of experience, strong technical capabilities, a highly trained workforce and a global reach, CAE has built an excellent reputation and long-standing customer relationships.

CAE has delivered simulation products to the military forces of more than 30 countries. The Company is the world's leading supplier of civil flight simulators in the competed market and is the second largest independent provider of civil aviation training services based on the number of simulators in operations.

CAE has a global presence with about 4,800 employees at manufacturing operations and training facilities in 17 countries on five continents. CAE reported fiscal 2005 results based on two business segments: (i) Civil Simulation and Training; and (ii) Military Simulation and Training. The Company's consolidated revenue from continuing operations in fiscal 2004 and 2005 was $938.4 and $986.2 million, respectively, and is broken down as follows:

Revenue by Product Line (%)

	2005	2004
Civil Simulation and Training	53%	49%
Military Simulation and Training	47%	51%
	100	**100**

Geographic Distribution of Revenue (%)

	2005	2004
US	42%	32%
Germany	11%	14%
UK	9%	9%
Canada	8%	12%
Other European countries	14%	16%
Other countries	16%	17%
	100	**100**

The following sets out, by business segment, the locations of CAE's primary subsidiaries and divisions:

CIVIL SIMULATION AND TRAINING

Canada

§ Montreal, Quebec

§ Toronto, Ontario

United States

§ Dallas, Texas

§ Denver, Colorado

§ Fort Worth, Texas

Europe

§ Amsterdam, The Netherlands

§ Brussels, Belgium

§ Burgess Hill, United Kingdom (shared with MS&T)

§ Madrid, Spain

§ Maastricht, The Netherlands

§ Evora, Portugal

Other

§ Dubai, United Arab Emirates

§ Sao Paulo, Brazil

§ Santiago, Chile

§ Zhuhai Guangdong, China

MILITARY SIMULATION AND TRAINING

Canada

§ Montreal, Quebec

§ Ottawa (CAE Professional Services)

United States

§ Tampa, Florida

Europe

§ Burgess Hill, United Kingdom

§ Royal Air Force base, Oxfordshire, United Kingdom

§ Stolberg, Germany

Other

§ Silverwater, Australia

5.1 (a) Summary of Business Segments

Civil Simulation and Training

The Company builds civil simulators for all categories of aircraft including those built by Airbus, Boeing, Bombardier, Cessna, Dassault, Embraer, Fairchild/Dornier, Gulfstream and Raytheon. CAE also builds simulators for civil helicopters, including models by Bell Helicopter and Sikorsky. During fiscal 2005, CAE was awarded 17 of 22 FFS orders or 77% of the worldwide-competed market (fiscal 2004 — 16 of 19 FFS orders). CAE also captured 10 of 22 competed visual systems, or 45% of the worldwide competed visual systems market. Since its inception, CAE has taken

orders for more than 500 FFS and FTDs from over 110 commercial airlines, aircraft manufacturers and external training centers in 38 countries, and to date has delivered nearly 490. With half a century of experience in designing and manufacturing FFS, CAE has established long-standing relationships with leading commercial airlines throughout the world.

In 2001, CAE entered the civil flight training business by opening its first pilot training center in Sao Paulo, Brazil in April and launching its Toronto, Canada facility in December. During 2001,

the Company also acquired Schreiner Aviation Training BV (“Schreiner”) and SimuFlite Training International, Inc. (“Simuflite”), adding six new pilot training centers to its operations. CAE is the world’s second largest independent provider of training services, based on the number of simulators available for third party training. As at March 31, 2005, CAE had an installed base of 106 civil FFS in 23 locations on four continents.

CAE intends to continue to expand its global network of strategically located training centers. The Company’s practice is to endeavour to secure at least one long-term training agreement with a major or regional airline prior to establishing a new civil training center. CAE’s customers at the commercial aviation training centers include major, low-cost and regional airlines that elect to outsource some of the training of their pilots and other crew members using either the Company’s training instructors or their own. The third party aviation training centers are used by more than 3,000 customers who tend to use third party training centers as their primary source for simulation training. CAE will continue to execute its pilot training strategy, with the focus now on ramping up utilization and increasing yield (through enhanced service offerings) in the training centers owned or operated by CAE.

During fiscal year 2005, CAE and Dassault Aviation have signed a contract making CAE the exclusive provider of entitlement training for the new Falcon 7X aircraft. Entitlement training is the initial training provided by the aircraft manufacturer with the purchase of the aircraft. The agreement covers pilot, maintenance and cabin crew training. As part of this agreement, CAE is developing two Falcon 7X FFS and a comprehensive training program that will incorporate CAE Simfinity training technology. All the Falcon FFS will be deployed in North America and Europe. The North American location will be CAE’s new training center in Morris County, New Jersey (US). The European location will be in CAE’s existing facilities in Burgess Hill, UK.

In June 2004, CAE was awarded a contract to train easyJet pilots on the Airbus A320. The contract included the installation of two A320 FFS, two CAE Simfinity Maintenance/Flight Training Devices (M/FTD), classrooms and related support services as well as the establishment of a comprehensive training curriculum. EasyJet pilots started training in our Burgess Hill training facility in November 2004.

CAE also inaugurated the A320 FFS it operates in Aeroflot training facility in Moscow. The 8-year training agreement with Aeroflot was signed in 2003 and is expected to generate about C$2.6 million (US$2 million) per year in revenue over eight years.

CAE became a Bell Associated Training Facility for Middle East-based operators of the Bell 412. Emirates-CAE Flight Training is scheduled to install a Bell 412 FFS at its facility in Dubai early in 2006.

CAE expects to maintain a commanding leadership position in civil simulation and visual systems by anticipating future customer needs through both its own training experience and trusted relationships with equipment customers, commitment to innovation and technology, product quality, reliability and efficiency, and continuing efforts to shorten delivery cycles through process improvements. CAE expects to improve on its lead-time, cost, quality and reputation for performance through operational improvements and research and development programs.

In fiscal 2005, many FFS orders came from the growing Asian and Middle East markets. Two FFS orders came from Etihad (A330/340), three from Emirates (A380, A340-600), four from Chinese operators (A330, A330/340-600, EMB 170) and one business aircraft FFS order from Singapore Flying College (Learjet 45).

CAE signed a contract with Airbus in fiscal 2004 for the development of the world's first A380 FFS. The initial A380 FFS was shipped to Airbus in Toulouse in May 2005 to be ready for use at the end of June 2005. CAE is providing a complete range of training devices for the A380, including two FFS equipped with the CAE Tropos™ visual system and CAE Simfinity™ software licenses for desktop and laptop trainers for $55 million. In addition, CAE and Airbus have joined forces to offer Airbus Corporate Jetliner ("ACJ") enhanced training courses. ACJ customers have access to training at 10 sites worldwide, including for the first time ever, four sites in North America.

In fiscal 2005, CAE signed three more orders for A380. CAE and Qantas signed a contract for a suite of Airbus A380 integrated training solutions, including an FFS and a CAE Simfinity™ training device. The training equipment package is valued at about $25 million and delivery of the FFS is slated for summer 2006. CAE was also selected by Emirates to provide two A380 FFS. As part of this contract, CAE became Emirate's exclusive provider of FFS for 10 years.

CAE's capabilities in simulation-based interactive learning, including its leading-edge CAE SimFinity™ system, also complement its traditional strength in FFS and FTDs. In fiscal year 2005, CAE sold 18 3d CAE Simfinity devices (Integrated Procedures Trainers (IPT), Maintenance/Flight Training Devices (M/FTD), FTDs). These orders included Qantas A380 IPT, JetBlue EMB190 FTDs (3 units), Singapore Learjet 45 IPT, FAA 737NG IPT and others. Pilots using CAE's SimFinity™ training system are able to practice landing, takeoff and taxiing under different weather conditions in over 250 airports. Combined with a growing network of training centers, this complete suite of simulation-based equipment and training products permits CAE to offer airlines and business jet operators a range of training solutions.

Fiscal 2005 Asset Impairment and Restructuring Charges

The Company performs the annual testing for impairment of its goodwill and intangible assets as at December 31 of each year using the two-step method prescribed under Canadian GAAP. Based on the test performed as at December 31, 2004, CAE concluded that an impairment charge was required.

During the third quarter of fiscal 2005, CAE's Management initiated a comprehensive review of current performance and the strategic orientation of its business units. This strategic review revealed that several factors have emerged and or worsened over the course of the past year that severely affected the Civil business, including:

- the enduring adverse economic and financial environment of the airline industry creating a new market reality, including a decreased level of interest in pilot training outsourcing;

- the appreciation of the Canadian dollar ;

- the erosion of the less than 50-seat regional jet market; and
- the escalating cost of acquiring data, parts and avionics for the manufacturing of FFS and other training devices.

Most of these elements are outside the direct control of the Company and currently show only modest signs of abatement. These elements caused Management to recalibrate some key assumptions in Civil's strategic planning.

New Market Reality

The enduring adverse economic environment of the airline industry, first initiated in 2001 with the 9/11 terrorist attacks, then further impacted by the SARS outbreak in Asia and the Afghanistan and Iraq wars, was, in 2004, exacerbated by soaring fuel costs and declining yields. These factors continue to offset the extensive cost-cutting initiatives the airlines have undertaken to such a point that US airlines lost an estimated US$5 billion in 2004 when less than a year ago, analysts were forecasting a break-even year. This fourth consecutive year of important losses for US airlines shows that there are no immediate solutions underway. In addition, the four years of lost growth will not easily be made up as only in mid-2004 did traffic volume return to pre-9/11 levels. CAE is now in a new market reality where cost management is at the centre of all decisions. In addition, interest in training outsourcing, which could be a contributor to improving cost-effectiveness, is low on the airline industry's priority list, where the focus is mainly on reducing labour and fleet costs. This new reality has translated into continued price pressures on Civil's equipment and training businesses.

Appreciation of the Canadian Dollar

The vast majority of Civil equipment revenues are based in US dollars while Civil's manufacturing costs are primarily in Canadian dollars. Therefore, the appreciation of the Canadian dollar to over US$0.83 (or C$1.20) in calendar 2004 had a material adverse impact on the profitability of Civil's business.

Erosion of the Less Than 50-Seat Regional Jet Market

The latter part of calendar year 2004 saw a major shift in demand for regional jets from the sub 50-seat segment to newer, larger platforms (70-to-100+ seat range). The value proposition for smaller regional jets has been severely impacted by the new low-yield market environment. In addition, legacy airlines are relaxing scope clauses, which previously restricted their use of 70-seat jets. Bombardier and Embraer have both reduced their 20-year market forecast in the less than 50-seat range and Bombardier has severely reduced its planned production for CRJ200s as evidenced by significant workforce reductions in 2004. These factors also make it less likely that production of the Dornier 328JET, for which CAE was the exclusive entitlement training provider, will be restored.

Escalating Cost of Acquiring Data, Parts and Avionics for the Manufacturing of FFS

In 2002, CAE launched its next generation FFS design, which was intended to reduce manufacturing and life cycle costs. However, as the Company experienced reduced throughput in

its manufacturing facilities, the anticipated savings have not materialized, which has prompted Management to make this issue a key priority to address.

Furthermore, CAE has also incurred increased costs for acquiring data, parts and avionics in the past few years, with these costs representing a major component in its manufacturing of FFS.

Based on the preceding factors and the results of the strategic review previously mentioned, CAE concluded its annual testing for impairment of its goodwill and intangible assets and its impairment assessment for property, plant and equipment as well as certain other assets and deferred costs. The Company concluded that the carrying value of some of Civil's tangible and intangible assets (including goodwill) were impaired and, on this basis, recorded in the third quarter of fiscal 2005 a $443.3 million impairment charge detailed as follows:

Detailed Impairment Charge (amounts in millions)	**Impairment Amount**
Goodwill	$ 205.2
Customer relations	86.7
Trade names and other intangible assets	20.4
Other assets	19.3
Property, plant and equipment (simulators)	78.4
Inventories	33.3
Total before taxes	$ 443.3
Tax recovery	89.1
Total impairment charge, net of tax	**$ 354.2**

The 20% tax recovery rate associated with the impairment charge was a result of the non-deductibility, for tax purposes, of some of the goodwill and intangibles assets impairment charge. As indicated in the table above, the after-tax effect of this non-cash charge on CAE's consolidated net earnings in the third quarter of 2005 was $354.2 million or $1.43 per share.

Restructuring Charges

On February 11, 2005, CAE announced a comprehensive restructuring plan (the "Plan") that will materially change the manner in which CAE conducts its business, and is aimed at restoring the Company's profitability, cash flow and return on investment. This Plan, to be executed over the next 18 months, results from the extensive strategic review of CAE's markets, customers and other external stakeholders as well as its internal resources and capabilities undertaken by the Management under the leadership of the new CEO.

The Plan, geared towards the elimination of duplication and the achievement of a more competitive cost structure, includes actions such as:

- the rationalization of its Civil training centres footprint including the consolidation of training centres where duplication exists and reallocation of a number of FFS to maximize yield and streamlining of the management structure; and

- the consolidation, into the new Simulation Products division as of April 1, 2005, of all manufacturing activities including engineering, program management and global procurement. These functions had previously existed in various business units and regionally, resulting in duplication.

The Company is reducing headcount; 450 employees have already left the Company since the announcement of the Plan.

In addition, in conjunction with the Plan, the Company will be implementing a new enterprise resource planning system ("ERP"), a business management system that integrates all aspects of the business, including planning, manufacturing, and sales and marketing, in order to improve transparency, accountability and information flow. Finally, CAE's incentive compensation structure has been reoriented, with a specific emphasis on building shareholder value through focus on delivery of free cash flows and adequate return on capital invested.

During fiscal 2005, the Company has recorded a $24.5 million restructuring charge for workforce reduction and related expenses. In line with the Plan previously announced, an additional restructuring cost in the range of up to $30 to $40 million should be incurred by the Company in fiscal 2006.

CAE experienced considerable softening of near-term demand for civil simulators in the last two years but experienced increases in simulator orders in fiscal 2005 to exceed the prior year's level. The contracting market for civil simulators in fiscal 2003 and 2004 led to pricing pressure that is reflected in the margins of CAE's backlog. The growth expected from training operations and a continued focus on productivity savings through cycle time reductions and other cost containment initiatives should position CAE to benefit from the gradual recovery of the civil airline industry.

Military Simulation and Training

CAE is a world leader in the design and production of military flight simulation equipment. The Company develops simulation equipment and training for a variety of military aircraft, including fighter jets, helicopters and patrol/transport planes. Its military simulators provide full combat environments that include interactive enemy and friendly players, as well as weapons and military sensors. These simulators incorporate highly realistic visual scenes covering areas as large as whole countries that are able to show the effects and characteristics of a variety of battlefield features, including those seen through Infra Red and Low Light Level TV Sensors. CAE has also moved beyond the supply of simulation equipment into the provision of military training with the Company's MSHATF in the UK and its C-130 training facility in Tampa, Florida. In 2006, Rotorsim will open a helicopter training centre in Sesto Calende, Italy. Rotorsim is owned equally by CAE and Agusta S.p.A.

CAE provides simulation equipment and training to the military forces of more than 30 countries, including all the US services. CAE has provided simulators for a wide range of aircraft and has more rotary wing expertise than any other simulator manufacturer. The Company has established a leading position in Europe in the supply of army command team land-based training systems, by supplying such systems to the forces of Germany, Austria, Italy, Norway, Finland and Ireland. The selection of a CAE visual system for the prestigious

Eurofighter program solidly establishes CAE's Medallion-S™ visual system as a premier system for fast jet simulation applications. The Medallion-S™ visual system is also being used to upgrade the US Army's Apache combat mission simulators, the German Tornado simulators, and the US Army's 160th Special Operations Aviation Regiment's MH-47 and MH-60 combat mission simulators. CAE's Medallion-S image generator is also being installed on new-build simulators, including the Canadian Forces CP-140 Patrol Aircraft simulator and the A109 simulator for Rotorsim.

Military support services include the provision of contractor logistics support, maintenance services and simulator instruction at over 60 sites worldwide. CAE provides maintenance support for most of the Canadian Forces flight simulators at six bases and all but one of the installed flight simulators of the German Army, Air Force and Navy. In the US, CAE provides a range of services across a wide number of bases, including the instruction of UAV Predator operators. CAE also provides a range of support services to facilities in Australia, the UK, the Netherlands and Italy, as well as mission software support for Canada's CF-18 fighter aircraft.

CAE will focus on growing its business with military customers around the world, and particularly in the US. The Company believes it can capitalize on the experience, expertise and increased visibility with military customers that it has gained from winning and performing significant contracts. CAE will continue its commitment to customer service by focusing on anticipating and meeting the needs of its military clients for highly-customized equipment and training. CAE believes its ability, through CAE USA Inc., to be a prime contractor in the US, in addition to strong supplier relationships with leading US defence contractors, will enable it to further penetrate the US military simulation and training market. CAE intends to continue to foster partnerships with key original equipment manufacturers such as AgustaWestland (CAE's partner in the Rotorsim consortium**)** with whom CAE has entered into a joint venture to deliver training equipment and services in support of AgustaWestland aircraft sales worldwide, and Lockheed Martin, with whom CAE is teamed on the C-130J Maintenance and Aircrew Training System program for the USAF.

In July 2004, Eurofighter Simulation Systems GmbH awarded a contract to CAE to provide a range of engineering and on-site support services for the visual systems on the Eurofighter Aircrew Synthetic Training Aids program. The contract is valued at approximately $30 million over five years.

In June 2004, the United States Navy has awarded CAE USA a contract initially valued at US$38 million ($52 million) to develop two MH-60S tactical operational flight trainers ("TOFTs") and two MH-60S weapons tactics trainers ("WTTs"). This contract grew significantly in fiscal 2005 as the US Navy exercised some contract options ahead of schedule for an additional MH-60S TOFT and two additional MH-60S WTTs, bringing the total value in fiscal 2005 to more than US$60 million.

The majority of CAE's contract revenue in its military simulation and training business result from contracts with militaries or government bodies performed under predominantly fixed-price contracts with only a small number of cost-plus contracts.

In most instances, under government regulations, certain costs, including certain financial costs, portions of research and development costs, lobbying expenses, certain types of legal expenses and certain marketing expenses related to the preparation of bids and proposals, are not allowed for pricing purposes and calculation of contract reimbursement rates under flexibly-priced contracts. Governments also routinely regulate the methods under which costs are allocated to government contracts. CAE is subject to a variety of audits performed by government agencies. These include pre-award audits that are performed at the submission of a proposal to the government. The purpose of the pre-award audit is to determine the basis of the bid and provide the information required for the relevant government to effectively negotiate the contract. During the performance of a contract the government has the right to request and to examine any labor charges, any material purchase, and any overhead changes to any contract that is active. Upon a contract's completion, the government may perform a post award audit of all aspects of contract performance to insure that the Company has performed in accordance with the terms of the contract.

Government contracts are generally, by their terms, subject to termination by the government either for convenience or default by the contractor. Fixed-price contracts provide for payment upon termination for items delivered to and accepted by the government and, if the termination is for convenience, for payment of fair compensation of work performed plus the costs of settling and paying claims by terminated subcontractors, other settlement expenses and a reasonable profit on the costs incurred. Cost-plus contracts generally provide that, upon termination, the contractor is entitled to reimbursement of its allowable costs and, if the termination is for convenience, a total fee proportionate to the percentage of the work completed under the contract. If a contract termination is for default, however, typically,

- the contractor may be paid an amount agreed upon for completed and partially completed products and services accepted by the government;
- the government may not be liable for the contractor's costs with respect to unacceptable items, and may be entitled to repayment of advance payments and progress payments, if any, related to the termination portion of the contract; and
- the contractor may be liable for excess costs incurred by the government in procuring undelivered items from another source.

In addition to the right of the government to terminate, government contracts are often conditioned upon the continuing availability of appropriations. Consequently, at the outset of a major program, such contracts are usually partially funded and additional monies are normally committed to the contract by the procuring agency only as appropriations are made for future fiscal years. Failure to obtain such appropriations normally results in termination of the contract and compensation to the contractor at less than the full value of the contract.

The military simulation and training market is driven in part by the introduction of new aircraft platforms, upgrades and life extensions to existing aircraft and a shift to greater use of simulation in pilot training programs due to the high degree of realism and the significantly lower cost compared to live training. CAE expects to improve its lead-time, cost, quality and reputation for performance through continued operational improvements and research and development programs. In particular, CAE launched a research and development program to introduce CAE NeTTS™ (Networked Tactical Training Solutions), a new PC-based architecture to address the

requirement for scalable, re-configurable, cost effective training devices. With a leading-edge technology solution, CAE is well positioned to capitalize on upcoming international military programs in Canada, the US, Europe, the UK, Asia and Australia, as well as teaming and/or collaboration arrangements in other countries.

Discontinued Operations

In fiscal 2004, CAE completed the divestiture plan started in December 2001 of all its non-core operations. On April 30, 2003, CAE completed the sale of the operations of CAE Beyss GmbH, another of CAE's Cleaning Technologies businesses, to Bavaria Industriekapital AG. Because the business had not been profitable for some time, CAE received nominal consideration. Subsequent to completing the sale, CAE incurred post disposition costs with respect to the transfer of employees, resulting in additional charges recorded in the results of Discontinued Operations. On May 2, 2003, CAE completed the sale of its remaining wood products business to Carmanah Design & Manufacturing Inc., a TD Capital company, for proceeds of approximately $20 million, plus certain rights to further payment if future earning targets are attained by the wood products business. On July 31, 2003, CAE completed the sale of substantially all the assets of its last remaining Cleaning Technologies business, Alpheus Inc. to Cold Jet Inc. of Cincinnati, Ohio. The total consideration was approximately US$2.1 million. In addition, the Company is entitled to receive further consideration of US$1.0 million based on the future performance of the combined businesses over the 53-month period from closing.

In the second quarter of fiscal 2005, the Board of Directors approved a plan to divest its Marine business. The plan was consistent with the Company's strategic process of focusing on its core competency — the development and use of simulation and modeling technology to provide training solutions. On February 3, 2005, CAE completed with L-3 the sale of substantially all of its Marine Controls segment for cash consideration of $238.6 million. This amount is subject to completion of a net working capital audit of the Marine Controls segment. CAE does not believe this provision will result in a material adjustment to the cash consideration received. In accordance with the purchase agreement, L-3 will also acquire two other components of the Marine Controls segment, including the assumption of the CAE's guarantee of $53.0 million (£23.0 million) of project finance related debt for the UK Astute Class submarine training program. The sale of these components is subject to regulatory approvals and expected to be completed during fiscal 2006. The expected proceeds on the sale of these components are nominal.

The results of Marine have been reported as discontinued operations and previously reported statements have been reclassified. This transaction resulted in a gain of $103.9 million, net of taxes of $25.1 million.

Research and Development

CAE differentiates itself by providing superior products and services that rely on the latest, most advanced technology available. As a result, the Company has a long-standing commitment to research and development ("R&D"). Each business segment is encouraged to apply R&D across the whole spectrum of its operations, from product development to production processes and techniques.

An additional part of CAE's R&D development strategy is to participate with several universities and government agencies in North America and in Europe in specific research projects. While development is the first priority, applied research is also vitally important to the Company's future. In addition to the basic internal research and development, R&D may also be carried out within customer contracts. This involves the development of technology that is necessary to complete a contract requirement but is also useful and may be reapplied by the Company in a broader sense. Certain CAE initiatives also receive the support of the Canadian government through Technology Partnerships Canada.

Total R&D expenditures include basic R&D costs as well as program related development costs. Basic internal R&D expenditures were in excess of $23 million for fiscal 2005, the product portion of which was largely associated with the development of the CAE NeTTS™ training system, CAE's SimFinity™ training system, and CAE's Medallion-S™ visual system. In addition to these development activities, basic internal research and development funds a variety of product enhancement and process improvement initiatives. Basic research and development expenditure is expected to be about 20% lower in fiscal 2006 and will be primarily focused on further developing CAE NeTTs™ and SimFinity™ training systems.

5.1 (b) Production and Services

Production

CAE's manufacturing facilities are located in Montreal, Canada; Tampa, US; Burgess Hill, UK; and Stolberg, Germany.

The manufacturing process for CAE simulators is complex, involving the coordination of approximately 250,000 parts and millions of lines of software code. The manufacture of a civil simulator includes five major stages: design, manufacture and assembly, testing, pack and ship and final test on site. Military simulators are much more complex and unique than civil simulators, and therefore take more time to design, manufacture and test.

Manufacturing is organized into 12 manufacturing cells comprised of the following three major disciplines: electronics (printed circuit board assembly), electrical (cables and harnesses, cabinets and chassis, aircraft instruments and avionics), and mechanical (welding, sheet metal and machine shop, precision assembly and hydraulics, structural assembly and final assembly).

Services

CAE's flight training services are provided to customers as described in section 5.1(a), "Summary of Business Segment", of this AIF.

CAE provides a range of technical support services to civil and military simulator operators, including parts replacement and repairs, installations, relocations, upgrades and technical training. Customers use the Company's technical services to answer questions, trouble-shoot and receive advice. This extends to service visits by CAE's engineers to assist in customer maintenance and repair activities. Military and civil upgrade services are not restricted to CAE

products; the Company can upgrade most other manufacturers' simulators. CAE services are offered either in conjunction with a sale of a simulator, through maintenance contracts or individual purchase orders. CAE believes that its service business provides opportunities to influence the upgrade of installed FFS while providing valuable insights into customer training needs.

5.1 (c) Specialized Skill and Knowledge

CAE employs predominantly engineers and software development staff, as well as flight training experts. As an industry leader, CAE is able to train its staff in the technology and software required for simulation software and equipment. Flight trainers are typically recruited from the ranks of former airline or military pilots. CAE has not experienced material difficulty in recruiting appropriate staff to carry out its manufacturing, training and development work.

5.1 (d) Competition

The markets in which CAE sells its products are highly competitive. Certain competitors are also the Company's customers, partners and suppliers on specific programs. The extent of competition for any single project generally varies according to the complexity of the product and the dollar volume of the anticipated award. CAE believes that it competes on the basis of:

- the performance and flexibility of its products;
- reputation for prompt and responsive contract performance;
- accumulated technical knowledge, intellectual property and expertise;
- strong after sales support;
- breadth of product line; and
- price.

CAE's future success will depend in large part upon its ability to improve existing product lines, develop new products and technologies in the same or related fields, improve delivery intervals and reduce the costs it incurs in producing its products and services.

CAE's major competitors in the military simulation and training market include Lockheed Martin Corporation, L-3, Boeing, Rockwell Collins NLX Corporation, Indra Systemas, Alenia Marconi Systems, Thales Training Simulation, Flight Safety International, Inc. and Rheinmetall Defence Electronics GmbH. Some of these competitors are predominantly local (one country or region) competitors. CAE sometimes partners with these and other competitors to cooperate on program contracts.

CAE's major competitors in the civil simulation equipment market include Thales Training & Simulation and Rockwell Collins Simulation division. Evans & Sutherland Computer Corporation also competes for visual systems. The Company's major competitors in civil pilot training include FlightSafety International, Inc., Alteon Training L.L.C. (formerly FlightSafety Boeing Training International), GECAT and PanAm International Flight Academy Inc.

5.1 (e) Components

CAE deals with a variety of goods and services suppliers across its business segments. It is not dependent on any single supplier for any key manufacturing components or services. Significant shortages of goods and services are not expected, and have not been encountered in the past. However, CAE's products contain sophisticated computer systems that run on software and operating systems supplied to it by third parties. Such computer systems and software may not always be available to CAE to license or purchase.

The production of CAE simulators is often dependent upon receipt by CAE of data, including confidential or proprietary data, concerning the functions, design and performance characteristics of a product or system, the performance of which CAE's simulator is intended to simulate. The Company cannot guarantee that it will be able to obtain such data on reasonable terms, or at all. Original manufacturers of these products and systems could object to the simulation by CAE of components of, or the totality of their products or systems, or could request high license fees that could negatively impact the Company's profit margins.

Most of the raw materials used in manufacturing (such as sheet metal, wires, cables and electronic integrated circuits) are available off the shelf from multiple commercial sources. The unique parts are the aircraft parts. These are usually available from aircraft manufacturers, the resale market, as well as through simulated part manufacturers.

The availability of most parts in a timely manner facilitates a relatively smooth production flow. Aircraft parts, in some instances, may be an exception, especially on new aircraft types or those out of production. The timely delivery of these parts is often the responsibility of CAE's customers. CAE's contracts normally link these aircraft parts delivery dates to the simulator delivery schedules. In cases where such aircraft parts cannot be made available, CAE's customers rely on CAE's ability to make simulated parts.

5.1 (f) Intangible Properties

CAE owns certain patents and has filed applications in respect of additional patents. The Company enters into agreements containing non-disclosure and confidentiality clauses with third parties and has similar provisions in place with its employees to protect its proprietary information and trade secrets. CAE also has internal policies concerning both ethics and intellectual property which guide its employees in their dealings with CAE's intellectual property and that of third parties. CAE's Intellectual Property Committee is mandated to oversee the protection, management and exploitation of the Company's inventions, trade secrets and other intellectual property.

Given the lengthy delay in obtaining patents (during which some technology may evolve into newer generations), the required detailed patent application disclosure which may permit competitors to reverse-engineer an invention, and the cost of maintaining and defending patents, CAE believes that certain intellectual property is adequately protected by either maintaining it as a trade secret or selectively disclosing enough of it to forestall anyone else from subsequently claiming it as their own original innovation.

CAE's agreements with Technology Partnerships Canada restrict CAE's ability to license (other than to customers) or transfer ownership of intellectual property developed with the program's

support until all funding has been repaid or Technology Partnerships Canada's consent has been obtained.

Given CAE's many decades of success in the field of aviation simulation, the Company believes that the CAE brand and some of its trademarked products have value in the markets it addresses.

5.1 (g) Cycles

There is a very limited cyclicality or seasonality to CAE's businesses. The MS&T division sells to government customers such that there is no evident cycle to the intake of orders. The same largely applies to the CS&T division's equipment sales to airlines, though to the extent that the entire commercial airline industry is affected by cycles of expansion and contraction, the Company will be affected by such cycles. The CS&T division's flight training services do experience an element of seasonality; in times of peak travel (holiday periods, etc.) airline and business jet pilots are often too busy flying aircraft to attend training sessions.

5.1 (h) Environmental Protection

CAE believes its current operations are in compliance in all material respects with environmental laws and regulations. Environmental protection requirements do not have material financial or operational effects on the Company's capital expenditures, earnings or competitive position.

CAE operations include, and past operations and those of some past operators at some of the Company's sites have included, the use, generation, storage, handling and disposal of hazardous materials which are subject to health and safety and environmental laws and regulations in the various countries in which CAE operates or has operated. Examples of claims in respect of former CAE operations include two claims against CAE in respect of the former CAE Electronics facility at the Edmonton International Airport, both of which CAE is contesting.

Separately, the New York State Department of Environmental Conservation (DEC) is studying whether Trichloroethene (TCE), allegedly present in ground water at or near CAE-USA's former Link Hillcrest New York facility site, could be evaporating and following soil vapors into homes. If it is, the DEC is trying to determine whether chemical oxidation of the affected land, or an air pump system installed in affected homes, would be the better remedy; as well as which properties, and parties, may have contributed to the alleged contamination. CAE is in discussions with the DEC, a neighbouring company and local officials to examine ways of resolving these concerns; no order has been issued against CAE in this regard.

5.1 (i) Employees

CAE currently employs approximately 4,800 employees of which approximately 750 are unionized and covered by 12 collective agreements. Three labor contracts were ratified in fiscal 2005. During fiscal 2006, CAE will enter into negotiations for the renewal of four collective agreements. The collective agreement for 575 employees in Montreal will remain in force until June 2008. There are no indications that negotiations on upcoming contract renewals will result in work stoppages. CAE considers employee relations to be satisfactory.

5.1 (j) Foreign Operations

For the fiscal year ended March 31, 2005, sales to customers outside Canada accounted for approximately 92% of CAE's revenue such that CAE is very dependent upon foreign sales and operations. The Company expects that sales outside Canada will continue to account for most of its revenue for the foreseeable future.

The Company believes that its physical presence in countries such as the US, Germany and the UK has enabled it to develop strong relationships and a good reputation with governments and other defence contractors who are important decision makers regarding defence contracts. In fiscal 2005 Military was awarded contracts by the Naval Air Systems Command to provide the U.S. Navy a range of MH-60S training systems and upgrade the U.S. Navy's P-3C operational flight trainers. Germany's Bundesamt fur Wehrtechnik und Beschaffung (BWB – procurement agency for Germany's military forces), Canada's Department of National Defence (DND), Lockheed Martin, and the U.S. Army's Program Executive Office – Simulation, Training and Instrumentation (PEO-STRI) also awarded contracts to CAE. Following the acquisition of BAE SYSTEMS Flight Simulation and Training in Tampa in fiscal 2002 and the subsequent creation of CAE USA Inc., CAE's ability to win contracts with the US military has been significantly enhanced with the awarding of prime contractor status under several omnibus procurement programs.

As a result, CAE is also subject to risks of doing business internationally, including:

- changes to regulatory requirements;
- changes to domestic and foreign government policies, including requirements to expend a portion of program funds locally and governmental industrial cooperation requirements;
- the complexity and necessity of using foreign representatives and consultants;
- imposition of tariffs or embargoes, export controls, including US, Canadian and foreign arms export controls, currency exchange controls and restrictions, and other trade restrictions affecting countries in which CAE sells its products or services;
- the difficulty of managing and operating an enterprise spread over various countries;
- compliance with a variety of foreign laws; and
- general economic and geopolitical conditions, including international hostilities, inflation, trade relationships and military and political alliances.

The impact of these factors is difficult to predict and any one or more of these factors could adversely affect the Company's operations in the future.

5.1 (2) Reorganization

Following Robert E. Brown's arrival as Chief Executive Officer in August 2004, an in-depth strategic review of CAE's markets, customers and other stakeholders as well as the Company's internal resources and capabilities was conducted. As a result of this review, the Company has reconfirmed its strategic direction. It adopted a plan intended to protect its technological leadership while at the same time fostering synergies between its various operating units, and implementing sound business practices. The plan maintains the existing Civil and Military

Groups, and adds a third: Simulation Products. The reorganization, which became effective April 1, 2005, is expected to result in significant savings to the Company and to position it well to face new market realities.

The major priorities of the newly formed Civil Training & Services Group ("CT&S") are to increase revenue per simulator in the Company's global network of training centres, and to deliver the most cost-effective and competitive training service in the marketplace. To this end, CT&S is expected to consolidate training centres where duplication exists, and to reallocate a number of simulators to maximize yield.

The Military Simulation & Training ("MS&T") Group's main goals are to service the defence market with technological excellence in modeling and simulation; to increase the Company's market share of the military training market, and to explore opportunities in non-traditional areas of the defence market, including such areas as analysis and planning.

The newly formed Simulation Products Group consolidates all manufacturing activities and includes engineering, program management, global procurement, and the marketing and sales of civil equipment. Its immediate focus is to substantially reduce the costs associated with manufacturing simulation equipment intended both for sale to third parties as well as for installation in the Company's own global network of training centres.

Fiscal year 2006 will be a transitional year for CAE while the Company addresses its business processes and cost structure, with the goal of ending the year with a restructured and solid earnings base.

5.2 Risk Factors

Execution of Restructuring

CAE's future success depends in part on the ability of its current management team to timely deploy the restructuring plan described in Section 5.1(1) (a) hereof, "Restructuring Charges" and ensure that the Company will fully benefit from that plan.

CAE's sales cycle is often lengthy and unpredictable, which could result in volatility in its operating results and the price of its common shares.

The sales cycle of CAE's products and services is lengthy and unpredictable, ranging from 6 to 18 months for civil aviation applications and from 6 to 24 months or longer for military applications. While customers are evaluating CAE's products and services, the Company may incur expenses and expend management effort. The result of making these expenditures, with no corresponding revenue in any given quarter, could further exacerbate fluctuations of its quarterly operating results and share price volatility.

CAE's success depends on the reliability of its products, the quality of its services and its ability to adapt to changing customer needs in a timely manner.

The civil aviation and military markets in which CAE operates are characterized by changes in customer requirements, new aircraft models and evolving industry standards. CAE's failure to

predict accurately the future needs of its customers and prospective customers and to develop product enhancements that address evolving standards and technologies may result in the loss of current customers or negatively affect its revenue and its ability to secure new customers.

A reduction in defence spending could result in a decrease in CAE's revenue.

CAE relies on sales to military customers around the world to generate a significant portion of its revenue. In fiscal 2005, such sales by Military Simulation and Training accounted for a significant portion of its revenues. CAE acts as prime contractor or major subcontractor for various US, European, Canadian and other foreign government programs. The termination of funding for a government program would result in a loss of anticipated future revenue attributable to that program which could have a negative impact on CAE's operations. A significant reduction in military expenditures by countries with which CAE has contracts could materially adversely affect its sales and earnings.

CAE operates in the civil simulation equipment and training services markets, both of which are heavily dependent on the airline industry.

CAE derives a material portion of its revenue from the supply of equipment and services to the commercial and business airline industry. The continued unprofitability generally of the major airlines has lead to a reduction or delay of new aircraft purchases which has resulted in reduced simulator orders and pricing constraints.

Intense competition in CAE's target markets could limit its ability to attract and retain customers.

The markets in which CAE sells its simulation and control equipment and training services are highly competitive. Some of the Company's competitors are larger than CAE and have greater financial, technical, marketing, manufacturing and distribution resources. In addition, some competitors have well-established relationships with aircraft manufacturers, airlines and governments which may give them an advantage over CAE in winning contracts with these organizations. CAE obtains most of its contracts through competitive bidding processes that subject the Company to the risk that it will expend substantial time and effort on proposals for contracts that may not be awarded to the Company. CAE cannot assure that it will continue to win competitively awarded contracts at the same rate as in the past.

CAE is subject to the risks of doing business abroad and currency fluctuations.

CAE has operations in numerous countries and sells its products and services to customers around the world. For the fiscal year ended March 31, 2005, sales to customers outside the US and Canada accounted for approximately 50% of revenue. CAE expects that sales outside the US and Canada will continue to account for a significant portion of revenue for the foreseeable future. As a result, CAE is subject to risks of doing business internationally. The majority of CAE's revenue is not currently denominated in Canadian dollars, and the Company expects that its revenue will continue to be generated in currencies other than the Canadian dollar. A substantial portion of operating expenses are payable in Canadian dollars. Fluctuations in the Canadian dollar exchange rate will impact results of operations and financial condition from

period to period. CAE is also subject to the risks of changes to laws and regulations in host countries; the cost and complexity of using foreign representatives and consultants; the imposition of tariffs, embargoes, controls and other restrictions impeding the free flow of goods, information and capital; the difficulties of managing and operating an enterprise and complying with laws in multiple jurisdictions; and general changes in economic and geopolitical conditions. CAE's currency hedging activities may not be successful.

CAE's use of fixed-price and long-term supply contracts could subject the Company to losses if there are cost overruns.

CAE provides its products and services primarily through fixed-price contracts that require the absorption of cost overruns, notwithstanding the difficulty of estimating all of the costs incurred in performing these contracts and in projecting the ultimate level of sales that the Company may achieve. In addition, a number of CAE's contracts to supply simulators to commercial airlines are long-term agreements for up to 20 years. These agreements establish the prices for the simulators to be delivered, subject to adjustments for inflation and cost increases. If these adjustments do not fully offset inflation or cost increases, CAE's results of operations could be adversely affected. CAE's business could be harmed if its products do not successfully integrate or operate with other sophisticated and continually evolving software, computing and communications systems. If CAE experiences difficulties or does not meet project milestones in a timely manner, the Company could be obligated to devote more engineering and other resources to a particular project than originally anticipated. While CAE believes it has recorded adequate provisions for losses on fixed-price contracts, obligations under fixed-price and long-term supply contracts could subject the Company to contract losses in excess of provisions.

CAE's government-funded military programs are regulated and subject to audit.

Like most suppliers of products and services to governments, CAE may be audited and reviewed periodically on some projects. Adjustments arising from government audits and reviews may have an adverse effect on results of operations. In addition, some costs may not be reimbursable or allowed in negotiation of fixed-price contracts. Further, as a government contractor, CAE may be subject to an increased risk of legal actions and liabilities which purely private sector companies are not subject to, the results of which could have a material adverse effect on operations. Failure to comply with applicable government regulations and requirements could lead to suspension or being barred from government contracting or subcontracting for a period of time, which would have a negative impact on CAE's operations and could have a negative effect on its reputation and ability to procure other government contracts in the future.

In the future, CAE may not be able to obtain financial support for research and development activities.

Some of CAE's research and development initiatives have been carried out with the financial support of governmental agencies including amounts from the government of Canada through Technology Partnerships Canada. If such financial assistance is not available to the Company in the future, CAE may have to find other financing, which may not be available.

CAE may experience contract cancellations within its existing backlog of orders.

At March 31, 2005, CAE had several hundred active contracts representing a total order backlog of $2.5 billion. Approximately 60% of the backlog is comprised of long-term contracts where revenues are guaranteed or expected based on current customer requirements. If certain of the Company's customers become insolvent or experience other financial difficulties, CAE's revenue would be adversely affected. In addition, contracting customers may terminate these contracts, unilaterally in some cases, if they desire. CAE cannot assure that its existing backlog will result in sales or that any such sales will be profitable.

CAE's ability to protect its intellectual property is limited, and competitors may use CAE's technology which could weaken the Company's competitive position.

CAE relies in part on trade secrets and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect its proprietary rights. Such reliance may be insufficient to prevent misappropriation of CAE's technology or deter others from developing similar technologies. Enforcement of CAE's intellectual property rights or its ability to acquire them may be unavailable or limited in some countries.

Reliance on the intellectual property of others could prevent or delay CAE's performance of contracts or negatively impact margins.

CAE's products contain sophisticated computer systems supplied to the Company by third parties. Such computer systems and software may not always be available to CAE. The production of CAE's simulators is often dependent upon receipt of data, including confidential or proprietary data, concerning the functions, design and performance characteristics of a product or system, the performance of which the Company's simulator is intended to simulate. CAE cannot assure that it will be able to obtain such data on reasonable terms, or at all.

Claims by other companies that CAE's products infringe their proprietary rights could adversely affect the Company's ability to sell its products and increase its costs.

Infringement claims may be brought against CAE or its customers in the future. CAE may not be successful in the defence of such claims and may not be able to develop processes that do not infringe on the rights of third parties or obtain licenses on commercially acceptable terms, if at all. In addition, any litigation related to CAE's intellectual property rights could be lengthy and costly and could adversely affect operations or financial results, whether or not CAE is successful.

CAE's union agreements are subject to renewal, and the Company may be unable to retain qualified personnel which would harm the ability to carry out its business strategy.

CAE is party to 12 collective bargaining agreements throughout its business units which are subject to expiration at various times in the future. If CAE is unable to renew these agreements, or others as they become subject to renegotiation from time to time, it could result in work stoppages and other labor disturbances which could have a material adverse effect on CAE's business. CAE's success depends to a significant degree upon the continued contributions of its qualified technical personnel and its future ability to attract and retain highly skilled personnel.

Any inability to attract and retain qualified personnel in the future may seriously harm CAE's business and results of operations.

CAE's debt agreements may restrict its ability to finance future operations and, if the Company is unable to meet its financial covenants, could cause CAE's debt to be accelerated.

Both the indenture governing CAE's senior notes and the terms of CAE's credit facilities contain restrictive covenants. These restrictions could hurt the Company's ability to finance future operations or capital needs, or to engage in other business activities that may be in CAE's interest. In addition, CAE is also required to comply with specified ratios and tests, including leverage, interest coverage ratios and a consolidated net worth test. A breach of any of these agreements or inability to comply with the required financial ratios or limits could result in a default, which would permit CAE's lenders to declare amounts owed to them due and immediately payable.

CAE's level of debt may adversely affect its financial and operating activity, and it may encounter difficulties in refinancing its debt.

CAE incurred indebtedness in connection with fiscal 2002-2003 acquisitions and CAE's capital expenditures were greater during the last two years than historical levels as the Company executed its business plan. In the future, CAE may borrow more money, subject to the limitations imposed by senior notes and credit facilities. CAE's indebtedness may affect the way it conducts business. A material element of CAE's debt matures in fiscal 2007 and if CAE is not able to refinance that debt on acceptable terms and conditions CAE may be adversely affected.

CAE may be subject to significant environmental liabilities imposed by environmental laws and regulations or contractual indemnities.

CAE's operations include, and its past operations and those of some past operators at some of its sites have included, the use, generation, storage, handling and disposal of hazardous materials. New laws and regulations, stricter enforcement of existing laws and regulations, the discovery of previously unknown contamination, the imposition of new clean-up requirements or claims on indemnities CAE has been given may require the Company to incur substantial costs in the future which could have a material adverse effect on its financial condition and results of operations.

CAE may be subject to liability claims arising from casualty losses.

Due to the nature of CAE's business, the Company may be subject to liability claims arising out of accidents or disasters involving aircraft for which CAE has provided training equipment or services, including claims for serious personal injury or death. CAE may also be subject to product liability claims in connection with past equipment and service sales by businesses comprising CAE's Discontinued Operations. CAE cannot be certain that its insurance coverage will be sufficient to cover one or more substantial claims.

The products CAE manufactures may be subject to warranty or other claims.

The simulators CAE manufactures are highly complex and sophisticated and may contain defects

that are difficult to detect and correct. The occurrence of errors and failures in CAE's products could result in warranty claims or the loss of customers. Correcting such defects could require significant capital investment. When defective products are integrated in the customers' equipment, CAE may face product liability claims based on damages to such equipment. Any claims, errors or failures could have an adverse effect on operating results and business. CAE cannot be certain that its insurance coverage will be sufficient to cover one or more substantial claims.

CAE is subject to compliance with regulatory rules imposed by aviation authorities that may change without notice, resulting in disruptions to its sales and operations.

CAE is subject to compliance with regulatory rules imposed by aviation authorities that may change without notice, resulting in disruptions to its sales and operations. Any changes imposed by a regulatory agency, including changes imposed by aviation authorities such as the US Federal Aviation Administration to safety standards, could require CAE to make unplanned modifications to its products and services, or may result in delays or cancellations of sales. CAE cannot predict the future impact of changing law or regulation on its operations and any changes could have a material adverse effect on its results of operations or financial condition.

Sales or licenses of certain CAE products require regulatory approvals.

The sale or license of virtually all of CAE's products is subject to regulatory controls, including the prohibition of sales to certain countries, or of certain technology such as military-related simulators or other training equipment including military data or parts, without an export license or other approvals. These regulations change with some frequency. CAE cannot assure that it will be permitted to sell or license certain products to customers and the Company may lose potential revenue as a result of the application of such regulations. Failure to comply with any of these regulations in the countries in which CAE operates could subject the Company to fines and other material sanctions.

CAE's ability to retain and attract key personnel.

CAE's continued success will depend in part on the ability to retain and attract key personnel with the relevant skills, expertise and experience. The Company applies a compensation policy designed to mitigate this risk.

ITEM 6 — DIVIDENDS

CAE paid a quarterly dividend of $0.03 per common share during the period of April 1, 2002 to December 31, 2004. CAE reduced the quarterly dividend to $0.01 per common share with effect as of February 11, 2005. The Company currently intends to maintain the quarterly dividend of $0.01 per common share. However, any decision to declare and pay dividends in the future will be made at the discretion of the Board of Directors, after taking into account the financial results, capital requirements and other factors the directors may deem relevant. The Company's contracts with Technology Partnerships Canada prohibit the payment of a dividend if such payment would prevent payment to Technology Partnerships Canada of a royalty owed under the contract.

The Company's Dividend Reinvestment Plan (DRIP) provides that Canadian resident eligible shareholders can elect to receive common stock dividends in lieu of cash dividends. During fiscal 2003, 2004 and 2005, CAE issued 54,622, 106,002 and 126,901 common shares, respectively, as share dividends.

ITEM 7 – DESCRIPTION OF CAPITAL STRUCTURE

Our authorized capital consists of an unlimited number of common shares without par value and an unlimited number of preferred shares without par value, issuable in series.

Each common share entitles the holder thereof to dividends if, as and when declared by our directors, to one vote at all meetings of holders of common shares and to participate, pro rata, with the holders of common shares, in any distribution of our assets upon liquidation, dissolution or winding-up, subject to the prior rights of holders of shares ranking in priority to common shares.

As at the close of business on March 31, 2005, 248,070,329 common shares were issued and outstanding. There are no preferred shares issued and outstanding.

ITEM 8 — MARKET FOR SECURITIES

The outstanding common shares of the Company are listed and posted for trading on The Toronto Stock Exchange under the symbol "CAE" and on the New York Stock Exchange under the symbol "CGT".

8.1 Trading Price and Volume

CAE Inc.
TSX Share Price Information
FY 2005

Month	Max	Min	Total Volume
April-04	$6.24	$5.56	19,904,111
May-04	$5.89	$5.16	17,831,500
June-04	$6.18	$5.33	14,989,226
July-04	$6.39	$5.74	13,109,001

Month	Max	Min	Total Volume
August-04	$6.55	$5.26	17,045,510
September-04	$5.85	$5.48	12,973,167
October-04	$5.71	$4.66	15,494,401
November-04	$5.07	$4.40	18,164,028
December-04	$5.10	$4.41	14,864,185
January-05	$5.22	$4.67	34,231,351
February-05	$5.88	$4.90	36,854,729
March-05	$6.04	$5.22	17,246,110

CAE Inc.
NYSE Share Price Information
FY 2005

Month	Max	Min	Total Volume
April-04	$4.77	$4.08	572,900
May-04	$4.29	$3.72	376,800
June-04	$4.59	$3.87	464,900
July-04	$4.82	$4.34	326,000
August-04	$4.99	$4.00	394,100
September-04	$4.51	$4.22	524,600
October-04	$4.51	$3.85	334,500
November-04	$4.13	$3.77	697,900
December-04	$4.25	$3.59	2,240,500
January-05	$4.27	$3.87	754,700
February-05	$4.76	$3.96	561,100
March-05	$4.99	$4.19	1,201,400

ITEM 9 — DIRECTORS AND OFFICERS

The directors of the Company are elected at each annual meeting of shareholders and hold office until the next annual meeting of shareholders or until their successors are elected or appointed. The names and municipalities of residence of the directors and officers of the Company, the positions and offices held by them in the Company, their respective principal occupations for the last five years, and the year in which they became a director are set forth below. In addition to fulfilling all statutory requirements, the Board of Directors oversees and reviews: (i) the strategic and operating plans and financial budgets and the performance against these objectives; (ii) the principal risks and the adequacy of the systems and procedures to manage these risks; (iii) the compensation and benefit policies; (iv) management development and succession planning; (v) business development initiatives; (vi) the communications policies and activities, including shareholder communications; (vii) the integrity of internal controls and management information systems; (viii) the monitoring of the corporate governance system; and (ix) the performance of the President and Chief Executive Officer.

The Committees of the Board of Directors are the Audit Committee, the Governance Committee, the Compensation Committee and the Executive Committee.

9.1 Name and Occupation

DIRECTORS

Name and Municipality of Residence and Year first became a director	Principal Occupation
BRIAN E. BARENTS Andover, Kansas, USA (2005)	Director of Kaman Corporation, Eclipse Aviation Corporation, the Nordam Group and Aerion Corporation, as well as a board member of the Flight Safety Foundation and a member of the Board of Trustees of Embry-Riddle Aeronautical University. A former Air National Guard Brigadier General and still an active pilot, Mr. Barents was the President, CEO and co-founder of Galaxy Aerospace Company, LP from 1997-2001 and before that Chairman, President and CEO of Learjet, Inc. from 1989-1996. Mr. Barents is a member of the Compensation Committee.
ROBERT E. BROWN Westmount, Quebec, Canada (2004)	President and Chief Executive Officer of the Company and a member of the Executive Committee. Mr. Brown was Chairman of the Board of Air Canada from May, 2003 to October, 2004, and before this, Mr. Brown was President and Chief Executive Officer of Bombardier Inc. from February 1999 to December 2002. Mr. Brown is a Director of Nortel Networks Corporation, Allen-Vanguard Corporation, ACE Aviation Holdings Inc. and several listed venture capital companies.
JOHN A. (IAN) CRAIG Ottawa, Ontario, Canada (2000)	Business consultant. Mr. Craig is also a director of Bell Canada International Inc., Arris International, XPU Capital and the Ottawa Heart Institute. Mr. Craig is a member of the Audit Committee.
RICHARD J. CURRIE, O.C. Toronto, Ontario, Canada (2001)	Non-executive Chairman of Bell Canada Enterprises Inc. and of Telesat. He is a Director of Staples, Inc. and Petro-Canada and Chancellor of the University of New Brunswick. Mr. Currie is a member of the Audit Committee.

Name and Municipality of Residence and Year first became a director	Principal Occupation
H. Garfield Emerson, Q.C. Toronto, Ontario, Canada (1992)	National Chairman and a senior partner of the national law firm of Fasken Martineau DuMoulin LLP. Mr. Emerson is also the Chairman of the Board of Rogers Communications Inc. and the Vice-Chairman of the Board of Rogers Wireless Communications Inc. He is also a Director of Canada Deposit Insurance Corporation, Rogers Cable Inc., Rogers Media Inc., Wittington Investments, Limited and Sunnybrook & Women's Health Sciences Centre. Mr. Emerson is a member of the Governance Committee.
Anthony S. Fell, O.C. Toronto, Ontario, Canada (2000)	Chairman of RBC Dominion Securities Inc. Mr. Fell is also Chairman of Munich Reinsurance Company of Canada, a Director of BCE Inc., Bell Canada, Loblaw Companies Limited and Telesat, and Chairman of the Board of Trustees of University Health Network. Mr. Fell is the Chairman of the Governance Committee.
Paul Gagné, CA, Montreal, Quebec, Canada (2005)	Director of Textron Inc., Inmet Mining Corporation, Wajax Limited, Fraser Papers Inc. and several private companies. Between 1998 and 2002, Mr. Gagné served as a consultant to Kruger Inc. and a Director of its UK Tissues Group. Prior to that, he was sequentially the Vice President Finance, Chief Operating Officer, Chief Executive Officer and Chairman of Canadian Pacific Forest Products Limited and Avenor Inc. Mr. Gagné is a member of the Audit Committee.
The Honourable James A. Grant, P.C., C.M., Q.C. Montreal, Quebec, Canada (1991)	Partner in the legal firm of Stikeman Elliott LLP (Montreal). Mr. Grant is a Director of Canadian Imperial Bank of Commerce, Shire Pharmaceuticals Group plc and various charitable and social organizations. Mr. Grant is a member of the Compensation and Executive Committees.

Name and Municipality of Residence and Year first became a director	Principal Occupation
JAMES F. HANKINSON Toronto, Ontario, Canada (1995)	President and Chief Executive Officer of Ontario Power Generation Inc. He is also a Director of Maple Leaf Foods Inc., Ontario Power Generation Inc. and Chair of the Board of Trustees of ROW Entertainment Income Fund. Mr. Hankinson is the Chairman of the Audit Committee and a member of the Governance Committee.
E. RANDOLPH (RANDY) JAYNE II Tysons Corner, Virginia (2001)	Senior Partner in Heidrick & Struggles International, Inc., an executive search firm (1996–present) and is currently the Office Managing Partner of the firm's Tysons Corner, VA office. Mr. Jayne is a member of the Compensation Committee.
JAMES W. MCCUTCHEON, Q.C. Toronto, Ontario, Canada (1979)	Counsel to the law firm of McCarthy Tétrault LLP. Mr. McCutcheon is a Director of Dominion of Canada General Insurance Company, Empire Life Insurance Company (Chairman 1991–1997), Guardian Capital Group Limited and Noranda Inc. Mr. McCutcheon is a member of the Audit Committee.
LAWRENCE N. STEVENSON Philadelphia, Pennsylvania, USA (1998)	Chief Executive Officer of Pep Boys, a NYSE-listed U.S. automotive services company. Mr. Stevenson is also a Director of SNC-Lavalin Group Inc. Mr. Stevenson is Chairman of the Compensation Committee.
LYNTON R. WILSON, O.C. Oakville, Ontario, Canada (1997)	Chairman of the Board of the Company. Mr. Wilson is the Chairman of Nortel Networks Corporation and of Allergen NCE Inc., and is also a Director of DaimlerChrysler AG, Mercedes-Benz Canada Inc., and DaimlerChrysler Canada Inc. He is the Chairman of the Executive Committee and is a member of the Compensation and Governance Committees.

OFFICERS WHO ARE NOT DIRECTORS

Name and Municipality of Residence	Office held with CAE and Principal Occupation[1]

Name and Municipality of Residence	Office held with CAE and Principal Occupation[1]
DONALD W. CAMPBELL Ottawa, Ontario, Canada	Group President, Military Simulation and Training; formerly Executive Vice President, Military Simulation and Training 2000 to 2002; Deputy Minister of Foreign Affairs (Canada) and Prime Minister's Personal Representative for Economic Summits, 1997 to 2000; Canadian Ambassador to Japan, 1993-1997.
MARC PARENT Blainville, Quebec, Canada	Group President, CAE Simulation Products: formerly Vice President and General Manager, Challenger Programs and Dorval Plants at Bombardier Aerospace 2004 to 2005; Vice President and General Manager at Bombardier Aerospace US operations, from 2003 to 2004; Vice President and General Manager, at Bombardier Aerospace, Toronto Site (former deHavilland) from 2001 to 2003.
JEFFREY G. ROBERTS Hudson, Quebec, Canada	Group President, Civil Training and Services of CAE Inc. appointed in February 2004 prior to this nomination he had joined CAE team in 2001, formerly Chief Executive Officer SimuFlite Training International Inc. 1999 to 2001.
ALAIN RAQUEPAS, CA, BCC St. Lambert, Quebec, Canada	Chief Financial Officer; formerly Vice President Finance, Military Simulation and Training, 2000 to 2005.
HARTLAND J.A. PATERSON Westmount, Quebec, Canada	Vice President, Legal, General Counsel and Corporate Secretary, 2001 to present; formerly Vice President, Legal and Regulatory of Cable & Wireless PLC (Japan), 1999 to 2001.
ERIC GEMME, CA, CPA, CBV St. Hubert, Quebec, Canada	Vice President and Corporate Controller, 2005; formerly Director Finance, Civil Simulation and Training. From 2001 to 2003 he occupied the function of Director, Mergers & Acquisitions and subsequently Vice President, Finance and Treasurer of Cognicase Inc. Prior to 2001, he was with PricewaterhouseCoopers LLP where he held various positions in their audit and corporate finance services.

Name and Municipality of Residence	Office held with CAE and Principal Occupation(1)
GUY BLANCHETTE, CA, CMA St-Bruno, Quebec, Canada	Vice President, and Treasurer, 2004 to present; formerly Chief Financial Officer Alstom Canada Inc.; Vice President Finance and Strategic Planning with SNC Industrial Technologies Inc. before he became Vice President, Treasurer and General Manager with SNC-Equity.

(1) Where the date 2000 appears, it signifies the beginning of the last five years and not necessarily the date upon which the individual commenced the relevant position or occupation.

The directors and senior officers of the Company as a group as at the date hereof beneficially own, directly or indirectly, or exercise control or direction over common shares, which represent 1.5 % of the Company's outstanding common shares.

9.2 Cease, Trade Orders, Bankruptcies, Penalties or Sanctions

None of the proposed directors of CAE is, or within ten years prior hereto has been, subject to a cease trade or similar order except that Messrs. Wilson and Brown were subject to cease trade orders of the Ontario Securities Commission and two other Canadian securities regulators prohibiting them, as directors of Nortel Networks Corporation and Nortel Networks Limited (collectively, "Nortel"), from trading in securities of Nortel. The orders were lifted after the receipt by the regulators of filings Nortel was required to make.

Mr. Brown joined the board of Air Canada two weeks before it filed for protection under the Companies' Creditors Arrangement Act on April 1, 2003 to help manage the financial crisis in which that company found itself.

9.3 Conflicts of Interest

The law firm Stikeman Elliott LLP, of which Mr. Grant is a partner, provided legal services to the Company in fiscal 2005 and continues to provide such services to the Company. The law firm's fees to the Company are less than 2% of the law firm's annual consolidated gross revenues.

ITEM 10 – TRANSFER AGENTS AND REGISTRARS

The Company only has common shares issued. The Company's transfer agent is Computershare Trust Company of Canada located at 100 University Avenue, Toronto, Ontario, M5J 2Y1.

ITEM 11 – MATERIAL CONTRACTS

In fiscal 2005, CAE entered into one non-ordinary course material contract, being the sale agreement in respect of the divestiture by the Company of its Marine Controls division. For further particulars of this contract, please refer to section 5.1(a) "Discontinued Operations" of this AIF.

ITEM 12 – AUDIT COMMITTEE

12.1 Mandate

The mandate of CAE's Audit Committee is as follows:

"ROLE AND MEMBERSHIP

The Audit Committee ("the Committee") shall be a committee to the Board of Directors.

The Committee shall consist of not fewer than four (4) such directors, one of whom shall be the Chairman of the Committee. All members of the Committee shall be independent directors, as determined by the Board taking into consideration applicable laws, regulations and other requirements applicable to such determination. Each member shall annually certify to CAE as to his or her independence, in form compliant with the standards of independence set out by regulatory authorities, stock exchanges and other applicable laws, regulations and requirements. Each member shall be able to read and understand financial statements (balance sheet, income statement, cash flow statement) that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by CAE's financial statements, or shall become able to do so within a reasonable period of time after joining the audit committee. One member shall have past employment in finance, accounting or any other comparable experience or background providing financial expertise. The Committee composition, including the qualifications of its members, shall comply with the requirements of regulatory authorities, stock exchanges and other applicable laws, regulations and requirements, as such requirements may be amended from time to time.

The Chairman of the Committee and its members shall be elected annually by the Board of Directors following recommendation of the Governance Committee and the Chairman of the Board. If the designated Chairman of the Committee is unable to attend a Committee meeting, the other Committee members present may elect a replacement Chairman for that meeting.

A majority of members of the Committee shall constitute a quorum.

RESPONSIBILITIES

Work closely and cooperatively with such officers and employees of CAE, its auditors, and/or other appropriate advisors and with access to such information as the Committee considers to be necessary or advisable in order to perform its duties and responsibilities, as assigned by the Board of Directors, in the following areas:

REVIEW OF AUDITED FINANCIAL STATEMENTS

1. Review the annual audited consolidated financial statements and make specific recommendations to the Board of Directors. As part of this process the Committee should:

- Review the appropriateness of and any changes to the underlying accounting principles and practices.
- Review the appropriateness of estimates, judgments of choice and level of conservatism of accounting alternatives.
- Review financial risks, uncertainties, commitments and contingent liabilities and discuss policies with respect to financial risk assessment and risk management.

ENGAGEMENT OF EXTERNAL AUDITORS

2. Recommend to the Board of Directors the appointment of the external auditor, which shall be accountable to the Board and the audit committee as representatives of the shareholders.

3. Review and approval of engagement letter. As part of this review the committee reviews and recommends to the Board of Directors for their approval the auditors' fees for the annual audit. The Committee is responsible for the oversight of the work of the company's auditor for the purpose of preparing or issuing an audit report or related work, and the auditor shall report directly to the Committee. The Committee shall approve the engagement of the external auditors for the audit, any audit-related services, advice with respect to taxation matters and other permitted services and fees for such services, including approval processes for any such service that comply with the requirements of regulatory authorities, stock exchanges and other applicable laws, regulations and requirements, as such requirements may be amended from time to time in accordance with the policy and procedures attached hereto.

4. Receipt of a written statement not less than annually from the external auditor describing in detail all relationships between the auditor and CAE that may impact the objectivity and independence of the auditor. Review annually with the Board of Directors the independence of the external auditors and either confirm to the Board of Directors that the external auditors are independent in accordance with applicable listing requirements, laws, regulations and other rules, or recommend that the Board of Directors take appropriate action to satisfy itself of the external auditors' independence. Review and approve CAE's hiring policies regarding partners, employees and former partners and employees of the present and former external auditor of CAE.

REVIEW AND DISCUSSION WITH EXTERNAL AUDITORS

5. Review with the external auditors and management the annual external audit plans which would include objectives, scope, timing, materiality level and fee estimate.

6. Request and review an annual report prepared by the external auditors of any significant recommendations to improve internal control and corresponding management responses. Request and review an annual report prepared by the external auditors regarding the auditor's internal quality-control procedures, material issues raised by the most recent internal quality-control review of the auditors, or by any inquiry or investigation by

governmental or professional authorities, within the preceding 5 years, respecting one or more audits carried out by the auditors, and any steps taken to deal with any such issues. Meet separately, periodically, with external auditors.

7. Make specific and direct inquiry of the external auditors relating to:

- Performance of management involved in the preparation of financial statements.
- Any restrictions on the scope of audit work.
- The level of cooperation received in the performance of the audit.
- The effectiveness of the work of internal audit.
- Any unresolved material differences of opinion or disputes between management and the external auditors.
- Any transactions or activities which may be illegal or unethical.
- Independence of the external auditor including the nature and fees of non-audit services performed by external audit firm and its affiliates.
- Any other matter so desired.

REVIEW AND DISCUSSION WITH INTERNAL AUDITORS

8. Review the annual internal audit plan including assessment of audit risk, planned activities, level and nature of reporting, audit organization and annual budget. Meet separately, periodically, with internal auditors.

9. Make specific and direct inquiry of the internal auditors relating to:

- Any significant recommendations to improve internal control and corresponding management responses.
- The level of independence of internal audit.
- Any material disagreement with management.
- Any other matter so desired.

REVIEW AND DISCUSSION WITH MANAGEMENT

10. Review and assess the adequacy and quality of organization and staffing for accounting and financial responsibilities as well as discuss with management the annual audited financial statements and quarterly financial statements and the independent auditor,

including CAE's disclosures under Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A).

11. Review with management the annual performance of external and internal audit.

REVIEW OF OTHER PUBLIC DOCUMENTS

12. Ensure the Committee reviews all material public documents relating to CAE's financial performance, financial position or analyses thereon, including financial statements, MD&A, annual and interim earnings press releases and the Annual Information Form (AIF). In certain cases which involve severe timing considerations, the Committee may designate the responsibility for review to any two members of the Committee. Review and monitor practices and procedures adopted by the company to assure compliance with applicable listing requirements, laws, regulations and other rules, and where appropriate, make recommendations or reports thereon to the Board of Directors. Discuss CAE's financial information and earnings guidance, if any, provided to analysts and rating agencies.

13. Review significant changes in the accounting principles to be observed in the preparation of the accounts of the company and its subsidiaries, or in their application, and in financial disclosure presentation.

14. Prepare such reports of the Committee as may be required by any applicable securities regulatory authority to be included in the company's information circular or any other disclosure document of the company.

15. The Committee shall review and approve the procedures set out in the company's Corporate Communications & Disclosure Policy and will annually verify that adequate procedures exist within the company for the review of its disclosure of financial information derived from its financial statements.

OTHER RESPONSIBILITIES

16. The Board may refer from time to time such matters relating to the financial affairs of the company as the Board may deem appropriate.

MEETINGS

17. The Committee shall meet at such times as deemed necessary by the Board or the Committee and shall report regularly to the Board.

ENGAGEMENT OF PROFESSIONAL SERVICES

18. The Committee is authorized to engage independent counsel, and other advisers, as it determines necessary to carry out its duties. The company shall provide for appropriate funding, as determined by the Committee, for such services.

HANDLING OF COMPLAINTS

19. The Committee shall maintain procedures for the receipt, retention and treatment of complaints received by the company regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submission by employees of the company of concerns regarding questionable accounting or auditing matters.

ANNUAL REVIEW

20. The Committee shall review and assess the adequacy of its mandate annually, report to the Board of Directors thereon and recommend any proposed changes to the Board of Directors for approval. The Committee shall also perform an annual evaluation of the performance of the Committee and shall report to the Chairman of the Governance Committee of the CAE Board of Directors thereon."

12.2 Membership

The members of CAE's Board of Director Audit Committee are:

Mr. James F. Hankinson (chair)
Mr. James W. McCutcheon, Q.C.
Mr. John A. (Ian) Craig
Mr. Richard J. Currie
Mr. Paul Gagné

Each of these members is independent and financially literate.

Mr. Hankinson is a chartered accountant and has a Master of Business Administration from McMaster University. He served as President and Chief Executive Officer of New Brunswick Power Corporation from 1996 to 2002. In 1973, he joined Canadian Pacific Limited, and served as chief operating officer from 1990 to 1995. Mr. Hankinson is also a member of the Audit Committee of the board of directors of Maple Leaf Foods Inc.

Mr. McCutcheon has extensive board experience. He is also member of the Audit Committees of the boards of directors of Noranda Inc. and of The Empire Life Insurance Company.

Mr. Craig has extensive board experience. He is also member of the Audit Committees of the boards of directors of Bell Canada International Inc. and ARRIS Group Inc.

Mr. Currie has extensive board experience and is a graduate of the Harvard Business School. In 2001 Mr. Currie was elected CANADA'S OUTSTANDING CEO OF THE YEAR.™ In 2003 he was elected to the Canadian Business Hall of Fame. In February, 2004 he was the recipient of the McGill Management Achievement Award, and in May, 2004 he was inducted as a Fellow of the Institute of Corporate Directors.

Mr. Gagné is a chartered accountant. He was sequentially the Vice-President Finance, Chief Operating Officer, Chief Executive Officer and Chairman of Canadian Pacific Forest Products

Limited and Avenor Inc. Mr. Gagné is chairman of the Audit Committees of the boards of directors of Fraser Papers Inc., Textron Inc. and Inmet Mining Corporation

12.3 Approval of Services

The Audit Committee is responsible for the appointment, compensation, retention and oversight of the work of its independent auditor. The Audit Committee must pre-approve any audit and non-audit services performed by PricewaterhouseCoopers LLP ("PwC"), the auditor of the Company, or such services must be entered into pursuant to the policies and procedures established by the Committee. Pursuant to such policies the Audit Committee annually authorizes CAE and its affiliates to engage the auditor for specified permitted tax, financial advisory and other audit-related services up to specified fee levels. The Audit Committee has considered and concluded that the provision of these services by PwC is compatible with maintaining PwC's independence. The Audit Committee's policy also identifies prohibited services that PwC is not to provide the Company.

The following chart shows all fees paid to PwC by the Company and its subsidiaries in the most recent and prior fiscal years for the various categories of services (generic description only).

Fee Type	Fiscal 2005 (Millions $)	Fiscal 2004 (Millions $)
Audit Services: Annual audit of the consolidated financial statements, including quarterly reviews, statutory audits or financial audits for subsidiaries and affiliates of the Company; services associated with documents filed with regulatory authorities.	2.3	2.0
Audit-related Services*: Translation service for financial results; due diligence services pertaining to potential acquisitions/dispositions; audit procedures related to accounting and/or billing records; consultations as to the accounting or disclosure treatment of transactions or events and/or the actual or potential impact of final or proposed rules, standards or interpretations by any regulatory or standard setting bodies; audit of closing balance sheet, working capital statement and/or any similar statements pertaining to business dispositions; and assistance re implementation of the requirements of laws, regulations or listing standards including assistance with the implementation of Section 404 of the Sarbanes-Oxley Act of 2002.	0.7	0.8

Fee Type	Fiscal 2005 (Millions $)	Fiscal 2004 (Millions $)
Tax Services: Federal, provincial, state and local tax compliance and advice; assistance with tax audits and appeals before governmental agencies; tax-related valuation services, including transfer pricing and cost segregation studies.	0.3	0.7
Other Services: Software and news services.	—	0.1
Total:	3.3	3.6

* Audit-related fees include fees relating to the issuance of a prospectus and due diligence in connection with the Company's acquisitions and divestitures.

ITEM 13 — ADDITIONAL INFORMATION

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of the Company's securities, options to purchase securities and interests of insiders in material transactions, where applicable, is contained in the Proxy Information Circular dated May 12, 2005, in connection with the Company's Annual and Special Meeting of Shareholders held on June 22, 2005. Additional financial information, including comparative consolidated audited financial statements and MD&A, are provided in the Company's Annual Report to the shareholders for the financial year ended March 31, 2005. A copy of such documents may be obtained from the Vice President, Global Communications or the Secretary of the Company upon request, or available online at www.sedar.com, as well as the Company's website at www.cae.com.

In addition, the Company will provide to any person or company, upon request to the Vice President, Global Communications or the Secretary of the Company, the documents specified below:

(a) When the securities of the Company are in the course of a distribution under a preliminary short form prospectus or a short form prospectus:

(i) one copy of the annual information form of the Company together with one copy of any document, or the pertinent pages of any document, incorporated by reference in such annual information form;

(ii) one copy of the comparative financial statements of the Company for its most recently completed financial year together with the accompanying report of the auditors and one

copy of the most recent interim financial statements of the Company for any period after the end of its most recently completed financial year;

(iii) one copy of the information circular in respect of its most recent annual meeting of shareholders that involved the election of directors; and

(iv) one copy of any other documents which are incorporated by reference into the preliminary short form prospectus or the short form prospectus and are not required to be provided under (i) to (iii) above; or

(b) At any other time, one copy of any other document referred to in clauses (i), (ii) and (iii) of paragraph (a) above, provided that the Company may require the payment of a reasonable charge if the request is made by a person or company who is not a security holder of the Company.

SCHEDULE "A" — SUBSIDIARIES

Set forth below are the names of all the direct and indirect subsidiaries of the Company. All companies are wholly owned except as noted.

Name of Subsidiary	Jurisdiction of Incorporation
Canada	
3985954 Canada Inc.	Canada
4025164 Canada Inc.	Canada
CAE International Holdings Limited	Canada
CAE Railway Ltd.	Canada
CAE Machinery Ltd.	British Columbia
CAE Simulator Services Inc.	Quebec
Greenley & Associates Incorporated	Canada
United States	
CAE (US) Inc.	Delaware
CAE (US) LLC	Delaware
CAE Railway Inc.	Delaware
CAE USA Inc.	Delaware
Civil Aviation Training Solutions Inc.	Florida
CAE SimuFlite Inc.	Texas
Europe	
CAE Center Brussels N.V	Belgium
Simubel N.V. (a CAE Aviation Training Company).	Belgium
CAE Beyss Grundstücksgesellschaft GmbH	Germany
CAE Elektronik GmbH	Germany
CAE Verwaltungsgesellschaft mbH.	Germany
CityLine Canadair Simulator und Training GmbH (15%)	Germany
Helicopter Training Media International GmbH	Germany
HFTS Helicopter Flight Training Services GmbH	Germany
SAGO Grünstucks-Verwaltungsgesellschaft mbH (51%)	Germany
SAGO Grünstucks-Verwaltungsgesellschaft mbH & Co. KG (95%)	Germany
ZFB Zentrum für Flugsimulation Berlin GmbH (17%)	Germany
CAE International Capital Management Hungary LLC	Hungary
CAE Visual Software Private Limited	India
Rotorsim (Consortium) (50%)[1]	Italy
CAE Investments S.à r.l.	Luxembourg
B.V. Nationale Luchtvaartschool	Netherlands
CAE Aviation Training B.V.	Netherlands

[1] Partnership

Name of Subsidiary	Jurisdiction of Incorporation
CAE Center Amsterdam B.V.	Netherlands
CAE Center Maastricht B.V.	Netherlands
CAE Flight Crew Training B.V.	Netherlands
CAE Holdings BV	Netherlands
CAE Investments BV	Netherlands
CAE Training Aircraft B.V.	Netherlands
CAE Training B.V.	Netherlands
NLS Amsterdam B.V.	Netherlands
Academia Aeronautica De Evora S.A.(56%)	Portugal
CAE Euroco S.à.r.l.	Portugal
CAE Servicios Globales de Instrucción de Vuelo (España), S.L.	Spain
Servicios de Instrucción de Vuelo, S.L. (80%)	Spain
CAE Holdings Limited	United Kingdom
Invertron Simulators plc	United Kingdom
CAE (UK) plc	United Kingdom
CAE Aircrew Training Services plc (78%)	United Kingdom
CVS Leasing Limited (13.39%)	United Kingdom
Fast Holdings Limited (47.5%)	United Kingdom
Fast Training Services Limited	United Kingdom
Landmark Operations Limited	United Kingdom
Landmark Training Limited	United Kingdom
Other	
CAE Australia Pty Ltd	Australia
CAE South America Flight Training do Brasil Ltda	Brazil
CAE Aviation Training Chile Limitada[2]	Chile
Qindao Fei Sheng International Aviation Training Technology Development Co. Ltd. (33%)	China
Zhuhai Xiang Yi Aviation Technology Company Limited (49%)	China
CAE Dubai LLC (49%)	Dubai
CAE Electronics Private Ltd	India
CAE Electronics SDN BHD	Malaysia
CAE Labuan Inc	Malaysia
CAE Aviation Training International Ltd	Mauritius
Flight Training Device (Mauritius) Limited	Mauritius

2 Partnership

DISCONTINUED OR INACTIVE

Name of Subsidiary	Jurisdiction of Incorporation
Canada	
CAE Pederson Ltd. (49%)	British Columbia
United States	
CAE CT Inc.	California
Europe	
CAE Screenplates SA	France
CAE Beteiligungsgesellschaft mbH	Germany
CAE Screenplates AB	Sweden
Other	
CAE Simco (Barbados) Ltd.	Barbados
CAE MRAD Pty Ltd.	Australia
ISDAT Simulation SDN BHD (20%)	Malaysia

SELECTED FINANCIAL INFORMATION

SELECTED ANNUAL INFORMATION FOR THE PAST FIVE YEARS

(Unaudited— amounts in millions except per share amounts)	**2005**	2004	2003	2002	2001
Revenue	**$ 986.2**	$ 938.4	$ 976.8	$1,010.7	$ 820.3
(Loss) earnings from continuing operations	**(304.7)**	47.4	113.9	133.0	99.3
Net (loss) earnings	**(199.9)**	64.0	117.2	149.5	106.1
Financial position:					
Total assets	**$1,699.7**	$2,308.7	$2,356.5	$2,378.4	$1,366.8
Total net debt	**285.8**	529.6	757.1	822.2	108.7
Per share:					
(Loss) earnings from continuing operations	**$ (1.23)**	$ 0.20	$ 0.52	$ 0.61	$ 0.46
Net (loss) earnings	**(0.81)**	0.27	0.53	0.69	0.49
Dividends	**0.10**	0.12	0.12	0.11	0.10
Shareholders' equity	**2.64**	3.94	3.42	2.81	2.13

SELECTED QUARTERLY FINANCIAL INFORMATION

(Unaudited— amounts in millions, except share amounts and per share amounts)	Q1	Q2	Q3	Q4
Fiscal 2003				
Revenue	$ 244.7	214.7	246.9	270.5
Earnings from continuing operations	$ 33.2	18.2	27.9	34.6
Basic earnings per share from continuing operations	$ 0.15	0.08	0.13	0.16
Diluted earnings per share from continuing operations	$ 0.15	0.08	0.13	0.16
Net earnings	$ 37.4	23.3	31.5	25.0
Basic earnings per share	$ 0.17	0.11	0.14	0.11
Diluted earnings per share	$ 0.17	0.11	0.14	0.11
Average number of shares outstanding, in millions	219.3	219.4	219.4	219.4
Average exchange rate, 1 US dollar to Canadian dollar	$ 1.56	1.56	1.57	1.51
Fiscal 2004				
Revenue	$ 208.9	213.2	255.2	261.1
Earnings from continuing operations	$ 12.2	11.0	14.5	9.7
Basic earnings per share from continuing operations	$ 0.06	0.05	0.05	0.04
Diluted earnings per share from continuing operations	$ 0.06	0.05	0.05	0.04
Net earnings	$ 13.2	15.1	21.4	14.3
Basic earnings per share	$ 0.06	0.07	0.09	0.05
Diluted earnings per share	$ 0.06	0.07	0.09	0.05
Average number of shares outstanding, in millions	219.7	220.0	246.5	246.6
Average exchange rate, 1 US dollar to Canadian dollar	$ 1.40	1.38	1.32	1.32
Fiscal 2005				
Revenue	**$ 230.9**	**235.1**	**257.5**	**262.7**
Earnings (loss) from continuing operations	**$ 18.9**	**12.8**	**(345.7)**	**9.3**
Basic earnings (loss) per share from continuing operations	**$ 0.08**	**0.05**	**(1.40)**	**0.04**
Diluted earnings (loss) per share from continuing operations	**$ 0.08**	**0.05**	**(1.40)**	**0.04**
Net earnings (loss)	**$ 24.3**	**14.0**	**(347.0)**	**108.8**
Basic earnings (loss) per share	**$ 0.10**	**0.06**	**(1.40)**	**0.44**
Diluted earnings (loss) per share	**$ 0.10**	**0.05**	**(1.40)**	**0.44**
Average number of shares outstanding, in millions	**246.7**	**246.8**	**247.0**	**247.8**
Average exchange rate, 1 US dollar to Canadian dollar	**$ 1.36**	**1.31**	**1.22**	**1.23**

MANAGEMENT AND AUDITORS' REPORTS

MANAGEMENT'S STATEMENT OF RESPONSIBILITY

The consolidated financial statements contained in this Annual Report are the responsibility of management, and have been prepared in accordance with Canadian generally accepted accounting principles and include when necessary some estimates based on management best judgment. Financial information presented elsewhere in the Annual Report is under management responsibilities and consistent with that contained in the accompanying financial statements.

CAE's policy is to maintain internal accounting and administrative systems, combined with disclosure control of high quality consistent with reasonable cost. Such systems are designed to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets.

The Board of Directors is responsible for ensuring that Management fulfils its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements through its Audit Committee, consisting solely of outside directors, which reviews the consolidated financial statements and reports thereon to the Board. The Committee meets periodically with the external auditors, internal auditors and management to review their respective activities and to satisfy itself that each party is properly discharging its responsibilities. Both external auditors and internal auditors have free access to the Committee, with or without management, to discuss the scope of their audits, the adequacy of the system of internal controls and financial reporting.

The financial statements have been reviewed by the Audit Committee and, together with the other required information in the Annual Report, approved by the Board of Directors. In addition, the consolidated financial statements have been audited by PricewaterhouseCooper LLP, whose report is provided below.

(Signed)
R.E. Brown
President and Chief Executive Officer

(Signed)
A. Raquepas
Vice President, Finance and Chief Financial Officer

Montreal, Canada
May 10, 2005

AUDITORS' REPORT

To the Shareholders of CAE Inc.

We have audited the consolidated balance sheets of CAE Inc. as at March 31, 2005 and 2004, and the consolidated statements of earnings, retained earnings and cash flows for each of the years in the three-year period ended March 31,2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 2005 and 2004, and the results of its operations and cash flows for each of the years in the three-year period ended March 31, 2005 in accordance with Canadian generally accepted accounting principles.

(Signed)
Chartered Accountants, Montreal, Canada
May 10, 2005

Comments by Auditors for U.S. Readers on Canada-U.S. Reporting Difference

In the United States, reporting standards for auditors require the addition of an explanatory paragraph (following the opinion paragraph) when there is a change in accounting principles that has a material effect on the comparability of the company's financial statements, such as the changes described in Note 1 to the consolidated financial statements. Our report to the shareholders dated May 10, 2005 is expressed in accordance with Canadian reporting standards which do not require a reference to such a change in accounting principles in the auditors' report when the change is properly accounted for and adequately disclosed in the financial statements.

(Signed)
Chartered Accountants, Montreal, Canada
May 10, 2005

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS

As at March 31 (amounts in millions of Canadian dollars)	**2005**	2004
Assets		
Current assets		
Cash and cash equivalents	**$ 57.1**	$ 54.7
Accounts receivable (Note 5)	**255.7**	316.5
Inventories (Note 6)	**101.0**	147.7
Prepaid expenses	**17.8**	19.6
Income taxes recoverable	**58.5**	52.0
Future income taxes (Note 15)	**2.5**	1.8
Current assets held for sale (Note 3)	**5.8**	89.8
	498.4	682.1
Restricted cash	**0.9**	7.0
Property, plant and equipment, net (Note 7)	**792.2**	780.0
Future income taxes (Note 15)	**101.0**	89.0
Intangible assets (Note 8)	**20.2**	129.2
Goodwill (Note 9)	**92.1**	300.7
Other assets (Note 10)	**137.4**	180.8
Long-term assets held for sale (Note 3)	**57.5**	139.9
	$1,699.7	$2,308.7
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	**$ 312.8**	$ 322.0
Deposits on contracts	**93.5**	69.3
Long-term debt due within one year (Note 11)	**35.3**	8.8
Future income taxes (Note 15)	**19.6**	51.1
Current liabilities related to assets held for sale (Note 3)	**7.8**	54.5
	469.0	505.7
Long-term debt (Note 11)	**307.6**	575.5
Deferred gains and other long-term liabilities (Note 16)	**179.8**	171.0
Future income taxes (Note 15)	**38.3**	77.5
Long-term liabilities related to assets held for sale (Note 3)	**53.4**	60.2
	1,048.1	1,389.9
Shareholders' Equity		
Capital stock (Note 12)	**373.8**	367.5
Contributed surplus (Note 13)	**3.3**	1.3
Retained earnings	**340.8**	562.1
Currency translation adjustment (Note 22)	**(66.3)**	(12.1)
	651.6	918.8
	$1,699.7	$2,308.7

Contingencies and commitments (Notes 18 and 20)

The accompanying notes form an integral part of these consolidated financial statements.

Approved by the Board:

(Signed)	(Signed)
R.E. Brown	L.R. Wilson
Director	Director

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF EARNINGS

Years ended March 31 (amounts in millions of Canadian dollars, except per share amounts)	**2005**	2004	2003
Revenue			
Civil Simulation and Training	**$ 520.2**	$ 461.8	$ 517.2
Military Simulation and Training	**466.0**	476.6	459.6
	$ 986.2	$ 938.4	$ 976.8
Earnings from continuing operations before interest and income taxes			
Civil Simulation and Training (Note 23)	**$ 47.6**	$ 39.0	$ 115.6
Military Simulation and Training (Note 23)	**47.2**	51.6	78.8
Impairment of goodwill, tangible and intangible assets (Note 4)	**(443.3)**	—	—
Restructuring Costs (Note 24)	**(24.5)**	(9.3)	—
(Loss) earnings from continuing operations before interest and income taxes	**$ (373.0)**	$ 81.3	$ 194.4
Interest on long-term debt (Note 11A(ix))	**37.8**	28.0	31.6
Other interest expense (income), net (Note 11A(ix))	**(5.7)**	(5.6)	(3.5)
(Loss) earnings from continuing operations before income taxes	**$ (405.1)**	$ 58.9	$ 166.3
Income tax (recovery) expense (Note 15)	**(100.4)**	11.5	52.4
(Loss) earnings from continuing operations	**$ (304.7)**	$ 47.4	$ 113.9
Results of discontinued operations (Note 3)	**104.8**	16.6	3.3
Net (loss) earnings	**$ (199.9)**	$ 64.0	$ 117.2
Basic (loss) earnings per share from continuing operations	**$ (1.23)**	$ 0.20	$ 0.52
Diluted (loss) earnings per share from continuing operations	**$ (1.23)**	$ 0.20	$ 0.52
Basic (loss) earnings per share	**$ (0.81)**	$ 0.27	$ 0.53
Diluted (loss) earnings per share	**$ (0.81)**	$ 0.27	$ 0.53
Weighted average number of common shares outstanding	**247.1**	233.2	219.4

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

Years ended March 31 (amounts in millions of Canadian dollars)	**2005**	2004	2003
Retained earnings at beginning of year as previously reported	**$ 562.1**	$ 531.2	$ 440.4
Change in accounting policy (Note 1)	**3.3**	—	—
Retained earnings at beginning of year	**565.4**	531.2	440.4
Share issue costs (2004-net of taxes of $2.4 million)	**—**	(5.1)	—
Net (loss) earnings	**(199.9)**	64.0	117.2
Dividends	**(24.7)**	(28.0)	(26.4)
Retained earnings at end of year	**$ 340.8**	$ 562.1	$ 531.2

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CASH FLOW

Years ended March 31 (amounts in millions of Canadian dollars)	**2005**	2004	2003
Operating activities			
Net (loss) earnings	**$ (199.9)**	$ 64.0	$ 117.2
Results of discontinued operations	**(104.8)**	(16.6)	(3.3)
(Loss) earnings from continuing operations	**(304.7)**	47.4	113.9
Adjustments to reconcile earnings to cash flows from operating activities:			
Impairment of goodwill, tangible and intangible assets (Note 4)	**443.3**	—	—
Amortization	**82.0**	71.4	65.1
Future income taxes	**(113.9)**	(2.9)	16.2
Investment tax credits	**(29.2)**	(9.2)	28.2
Stock based compensation (Note 13)	**2.0**	1.3	—
Other	**20.9**	(6.3)	(18.4)
Decrease (increase) in non-cash working capital (Note 17)	**85.6**	(100.2)	(64.7)
Net cash provided by continuing operating activities	**186.0**	1.5	140.3
Net cash provided by discontinued operating activities	**21.6**	4.2	14.6
Net cash provided by operating activities	**207.6**	5.7	154.9
Investing activities			
Purchase of businesses (Note 2)	**(13.8)**	—	—
Proceeds from disposal of discontinued operations (Note 3)	**239.4**	22.3	25.0
Short-term investments, net	**—**	2.6	18.8
Capital expenditures	**(118.0)**	(86.8)	(224.2)
Proceeds from sale and leaseback of assets	**43.8**	122.5	127.0
Deferred development costs	**(9.9)**	(12.7)	(13.3)
Deferred pre-operating costs	**(1.7)**	(6.6)	(7.6)
Other assets	**(2.4)**	(4.8)	(27.5)
Net cash provided by (used in) continuing investing activities	**137.4**	36.5	(101.8)
Net cash used in discontinued investing activities	**(5.8)**	(12.0)	(32.6)
Net cash provided by (used in) investing activities	**131.6**	24.5	(134.4)
Financing activities			
Proceeds of long-term debt	**267.7**	514.9	250.0
Repayments of long-term debt	**(588.5)**	(650.4)	(326.3)
Dividends paid	**(24.0)**	(27.4)	(26.2)
Capital stock issuances (Note 12)	**3.6**	176.4	3.5
Share issue costs	**—**	(7.5)	—
Other	**0.7**	1.4	(14.1)
Net cash (used in) provided by continuing financing activities	**(340.5)**	7.4	(113.1)
Net cash provided by discontinued financing activities	**3.2**	10.4	18.7
Net cash (used in) provided by financing activities	**(337.3)**	17.8	(94.4)
Effect of foreign exchange rate changes on cash and cash equivalents	**(2.3)**	(3.2)	2.2
Net (decrease) increase in cash and cash equivalents	**(0.4)**	44.8	(71.7)
Cash and cash equivalents at beginning of year	**61.9**	17.1	88.8
Cash and cash equivalents at end of year	**$ 61.5**	$ 61.9	$ 17.1
Cash and cash equivalents related to:			
Continuing operations	**$ 57.1**	$ 54.7	$ 13.5
Discontinued operations	**4.4**	7.2	3.6
	$ 61.5	$ 61.9	$ 17.1

Supplementary Cash Flow Information (Note 17)

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended March 31, 2005, 2004 and 2003 (amounts in millions of Canadian dollars)

NOTE 01.
NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

CAE Inc designs and provides simulation equipment and services and develops integrated training solutions for the military, commercial airlines, business aircraft operators and aircraft manufacturers.

CAE's flight simulators replicate aircraft performance in normal and abnormal operations and a comprehensive set of environmental conditions, utilizing visual systems with an extensive database of airports, other landing areas and flying environments and motion and sound cues to create a fully immersive training environment. The Company offers a full range of flight training devices based on the same software used in its simulators. CAE also operates a global network of training centres in locations around the world.

CAE's operations are broken down into two operating segments; Military Simulation and Training ("Military") and Civil Simulation and Training ("Civil").

Prior to the sale of its Marine Controls division in the fourth quarter of fiscal 2005 the Company also provided simulators and training services for sea and land-based activities and supplied marine automation systems for military and civil applications.

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES AND FINANCIAL STATEMENT PRESENTATION

The accounting policies of CAE Inc. and its subsidiaries ("CAE" or "the Company") conform, in all material respect, to Canadian generally accepted accounting principles ("GAAP") as defined by the Canadian Institute of Chartered Accountants ("CICA"). These accounting principles are different in some respects from United States generally accepted accounting principles ("U.S. GAAP"). The significant differences are described in Note 27.

On April 1, 2004, the Company adopted CICA Handbook Sections 1100, *Generally Accepted Accounting Principles and* 1400, *General Standards of Financial Statement Presentation*. Section 1100 describes what constitutes Canadian GAAP and its sources, and provides guidance on sources to consult when selecting accounting policies and appropriate disclosure when a matter is not dealt with explicitly in the primary sources of GAAP, thereby recodifying GAAP hierarchy. Section 1400 clarifies what is fair presentation in accordance with GAAP and provides general guidance on financial presentation. The adoption of these standards did not have any material effect on consolidated financial statements.

Except where otherwise noted, all amounts in these financial statements are expressed in Canadian dollars.

USE OF ESTIMATES

The preparation of financial statements in conformity with GAAP requires CAE's management ("Management") to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the period reported. On a ongoing basis, Management reviews its estimates, particularly as they relate to accounting on long-term contracts, useful lives, employee future benefits, income taxes, impairment of long-lived assets and goodwill, based on Management's best knowledge of current events and actions that the Company may undertake in the future. Actual results could differ from those estimates, significant changes in estimates and/or assumptions could result in impairment of certain assets.

CONSOLIDATION

The consolidated financial statements include the accounts of CAE Inc. and of all majority owned subsidiaries. They also include the Company's proportionate share of assets, liabilities and earnings of joint ventures in which the Company has an interest. All significant intercompany accounts and transactions have been eliminated. Investments over which CAE exercises significant influence are accounted for using the equity method and portfolio investments are accounted for using the cost method.

CONSOLIDATION OF VARIABLE INTEREST ENTITIES

On January 1st, 2005, the Company adopted Accounting Guideline "Consolidation of Variable Interest Entities" ("AcG-15") on a retroactive basis without restatement of prior periods. AcG-15 provides a framework for identifying variable interest entities ("VIEs") and determining when an entity should include the assets, liabilities and results of operations of a VIE in its consolidated financial statements.

In general, a VIE is a corporation, partnership, limited-liability corporation, trust, or any other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has a group of equity owners that are unable to make significant decisions about its activities, or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 01. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

AcG-15 requires a VIE to be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a variable interest holder) is exposed to a majority of the risk of loss from the VIE's activities, is entitled to receive a majority of the VIE's residual returns (if no party is exposed to a majority of the VIE's losses), or both (the primary beneficiary). Upon consolidation, the primary beneficiary generally must initially record all of the VIE's assets, liabilities and non-controlling interests at fair value at the date the enterprise became the primary beneficiary. However, for variable interest entities created prior to the initial adoption of AcG-15, the assets, liabilities and non-controlling interest of these entities must be initially consolidated as if the entities were always consolidated based on majority voting interest. AcG-15 also requires disclosures about VIEs that the variable interest holder is not required to consolidate, but in which it has a significant variable interest.

The adoption of AcG-15 on January 1, 2005 resulted in an increase in total assets, total liability, and retained earnings of $46.4 million, $43.2 million, and $3.3 million, respectively and a decrease in the currency translation adjustment of $0.1 million.

FOREIGN CURRENCY TRANSLATION

SELF-SUSTAINING FOREIGN OPERATIONS

Foreign operations of the Company classified as self-sustaining operations are translated to Canadian dollars using the current rate method. Under this method assets and liabilities are translated at exchange rates in effect at the balance sheet date and revenues and expenses are translated at the average exchange rates for the period. Gains or losses on translation of foreign operations into Canadian dollars are included in the currency translation adjustment account, a separate component of shareholders' equity.

Accumulated amounts in the currency translation adjustment account are released to the statement of earnings when the Company reduces its net investment in foreign operations by way of capital reduction or through the settlement of long-term inter-company balances which had been considered part of CAE's net investment.

FOREIGN CURRENCY TRANSACTIONS

Monetary assets and liabilities denominated in currencies other than the functional currency are translated at the prevailing exchange rate at the balance sheet date. Non-monetary assets and liabilities denominated in currencies other than the functional currency and revenue and expense items are translated into the functional currency using the exchange rate prevailing at the dates of the respective transactions. Translation gains or losses are included in the determination of earnings, except those related to long-term intercompany account balances, that form part of the net investment in foreign operations, and those arising from the translation of foreign currency debt that has been designated as a hedge of the net investment in subsidiaries, which are included in the currency translation adjustment account, a separate component of shareholders' equity.

REVENUE RECOGNITION

Revenue from long-term contracts for the design, engineering and manufacturing of flight simulators is recognized, when persuasive evidence of an arrangement exists, the fee is fixed or determinable and recovery is reasonably certain, using the percentage-of-completion method. Under this method, revenue and earnings are recorded as related costs are incurred, on the basis of the percentage of actual costs incurred to date, relative to the estimated total costs to complete the contract. The cumulative impact of any revisions in cost and earnings estimates are reflected in the period in which the need for a revision becomes known. Losses, if any, are recognized fully when first anticipated. Warranty provisions are recorded at the time revenue is recognized, based on past experience. No right of return or complementary upgrades is provided to customers. Post-delivery customer support is billed separately and revenue is recognized over the support period.

Long-term contracts provide for progress billings based on completion of certain phases of work. Unbilled receivables represent excess of work performed over customer billings. Deposits on contract represent customer payments in excess of work performed.

Training services and other revenue are recognized when persuasive evidence of an arrangement exists, the fee is fixed or determinable, recovery is reasonably certain and, when applicable, products have been delivered, or services have been rendered.

INCOME TAXES AND INVESTMENT TAX CREDITS

The Company uses the tax liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined according to differences between the carrying value and the tax bases of assets and liabilities. This method also requires the recognition of future tax benefits, such as net operating loss carryforwards, to the extent that realization of such benefits is more likely than not. Future tax assets and liabilities are measured by applying enacted or substantively enacted rates and laws at the date of the financial statements for the year for which the temporary differences are expected to reverse. CAE does not provide for income taxes on undistributed earnings of foreign subsidiaries that are not expected to be repatriated in the foreseeable future.

A valuation allowance is recognized to the extent that, in the opinion of Management, it is more likely than not that the future income tax assets will not be realized. (Refer to Note 15)

Investment tax credits ("ITC") arising from research and development ("R&D") activities are deducted from the related costs and are accordingly included in the determination of earnings when there is reasonable assurance that the credits will be realized. ITC arising from the acquisition of property, plant and equipment and deferred development costs are deducted from the cost of those assets with amortization calculated on the net amount.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company is subject to examination by taxation authorities in various jurisdictions. The determination of tax liabilities and ITC recoverable involve certain uncertainties in the interpretation of complex tax regulations. Therefore, the Company provides for potential tax liabilities and ITC recoverable based on Management's best estimates. Differences between the estimates and the ultimate amounts of taxes and ITC are recorded in earnings at the time they can be determined. (Refer to Note 23)

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of highly liquid investments with original terms to maturity of 90 days or less.

RESTRICTED CASH

During fiscal 2004, under the terms of subsidiaries external bank financing and some government-related sales contracts, the Company was required to hold a defined amount of cash as collateral. In fiscal 2005, the subsidiaries' external bank financing agreements which required the holding of cash as collateral as well as the government-related contracts were settled and effectively released a large portion of the restricted cash.

ACCOUNTS RECEIVABLE

Receivables are recorded at cost, net of a provision for doubtful accounts, based on expected recoverability. In fiscal 2005, the Company entered into a program under which it sells certain of its accounts receivable to a third party for cash consideration without recourse to the Company. These transactions are accounted for when the Company is considered to have surrendered control over the transferred accounts receivable. Losses and gains on these transactions are recognized as other expense or income. (Refer to Note 5)

INVENTORIES

Raw materials are valued at the lower of cost and replacement cost. Work in process is stated at the lower of average cost and net realizable value. The cost of work in process includes material, labour and an allocation of manufacturing overhead. (Refer to Note 6)

LONG-LIVED ASSETS

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at amortized cost, net of any impairment charges. The declining balance and straight-line methods are used in computing amortization over the estimated useful lives of the assets. Useful lives are estimated as follows:

	METHOD	RATES/YEARS
Building and improvements	Declining balance	5% -10%
Simulators	Straight-line (10% residual)	5 to 25 years
Machinery and equipment	Declining balance	20% -35%

LEASES

Leases entered into by the Company in which substantially all the benefits and risks of ownership are transferred to the Company are recorded as capital leases and classified as property, plant and equipment and long-term borrowings. All other leases are classified as operating leases under which leasing costs are expensed in the period in which they are incurred. Gains, net of transaction costs, related to the sale and leaseback of simulators are deferred and the gains in excess of the residual value guarantees are amortized over the term of the lease. The residual value guarantees are to be ultimately recognized in the Company's earnings upon expiry of the related sale and leaseback agreement.

INTEREST CAPITALIZATION

Interest costs relating to the construction of simulators and buildings for training centres are capitalized as part of the cost of property, plant and equipment. Capitalization of interest ceases when the simulator and training centre are completed and ready for productive use.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 01. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

INTANGIBLE ASSETS WITH DEFINITE USEFUL LIVES

Intangible assets with definite useful lives are recorded at their fair value at the date of acquisition of the related acquired enterprise. Amortization is provided for all intangible assets on a straight-line basis over their estimated useful lives as follows:

	AMORTIZATION PERIOD	WEIGHTED AVERAGE AMORTIZATION PERIOD
Trade names	10 to 25 years	20
Backlog and contractual agreements	1 to 20 years	15
Customer relationships	10 to 25 years	10
Other	12 to 20 years	12

***IMPAIRMENT OF LONG-LIVED* ASSETS**

The Company recognizes impairment losses for a long-lived asset to be held and used when events or changes in circumstances cause its carrying value to exceed the total undiscounted cash flows expected from its use and eventual disposition. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its fair value.

BUSINESS COMBINATIONS AND GOODWILL

Acquisitions are accounted for using the purchase method and, accordingly, the results of operations of the acquired enterprise are included in the consolidated statement of earnings (losses) from the respective dates of acquisition.

Goodwill represents the excess of the cost of acquired enterprises over the net of the amounts assigned to identifiable assets acquired and liabilities assumed. Goodwill is tested for impairment, at least annually or more frequently if events or changes in circumstances indicate that it might be impaired.

The impairment test consists of a comparison of the fair value of the Company's reporting units with their carrying amount. When the carrying amount of the reporting unit exceeds the fair value, the Company compares, in a second step, the fair value of goodwill related to the reporting unit to its carrying value and recognizes if required an impairment loss equal to the excess. The fair value of a reporting unit is calculated based on one or more fair value measures, including present value techniques of estimated future cash flows and estimated amounts at which the unit as a whole could be bought or sold in a current transaction between willing parties. If the carrying amount of the reporting unit exceeds the fair value, step two requires the fair value of the reporting unit to be allocated to the underlying assets and liabilities of that reporting unit, resulting in an implied fair value of goodwill. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss equal to the excess is recorded in net earnings (loss). (Refer to Note 9)

OTHER ASSETS

RESEARCH AND DEVELOPMENT COSTS

Research costs are charged to earnings in the periods in which they are incurred. Development costs are also charged to earnings in the period incurred unless they meet all the criteria for deferral as per the CICA Handbook Section 3450, Research and Development Costs and their recovery is reasonably assured. Government assistance arising from research and development activities is deducted from the related costs or assets if deferred. Amortization of development costs deferred to future periods commences with the commercial production of the product and is charged to earnings based on anticipated sales of the product, over a period not exceeding five years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PRE-OPERATING COSTS

The Company defers costs incurred during the pre-operating period for all new training centres. Pre-operating costs are incremental in nature and are considered by Management to be recoverable from the future operations of the new training centre. Capitalization ceases at the opening of the training centre. Amortization of the deferred pre-operating costs is taken over five years in respect to civil training operations.

DEFERRED FINANCING COSTS

Costs incurred relating to the issuance of long-term debt are deferred and amortized on a straight-line basis over the term of the related debt. Costs related to sale and leaseback agreements are amortized on a straight-line basis over the term of the lease. (Refer to Note 10)

EMPLOYEE FUTURE BENEFITS

The Company maintains defined benefit pension plans that provide benefits based on length of service and final average earnings. The service costs and the pension obligations are actuarially determined using the projected benefit method prorated on employee service and Management's best estimate of expected plan investment performance, salary escalation and retirement ages of employees. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the remaining service period of active employees. Past service costs, arising from plan amendments, are deferred and amortized on a straight-line basis over the average remaining service period of active employees at the date of amendment.

When a curtailment arises, any unamortized past service cost associated with the reduction of future services is recognized immediately. Also, the increase or decrease in benefit obligation is recognized as a loss or a gain net of unrecognized actuarial gains or losses. Finally, when the restructuring of a benefit plan gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to the settlement.

On April 1, 2004, CAE adopted new disclosure requirements for employee future benefits of CICA Handbook Section 3461, *Employee Future Benefits.* Section 3461 requires additional disclosures about the assets, cash flow and net periodic benefit costs of defined benefits pension plans and other future employee benefit plans. (Refer to Note 21)

STOCK-BASED COMPENSATION PLANS

The Company's stock-based compensation plans consist of five plans; an Employee Stock Option Plan ("ESOP"), an Employee Stock Purchase Plan ("ESPP"), a Deferred Share Unit ("DSU") plan for executives, a Long-Term Incentive Deferred Share Unit ("LTI-DSU") Plan and on April 1, 2004, the Company adopted a Long-Term Incentive Restricted Share Unit ("LTI-RSU") Plan. All plans are described in Note 13.

Since fiscal 2004, net earnings include compensation costs for CAE's stock options. Using the fair value method, compensation expense is measured at the grant date and recognized over the service period with a corresponding increase to contributed surplus in shareholders' equity. The Company estimates the fair value of options using the Black-Scholes pricing model.

The Black-Scholes pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, valuation models generally require the input of highly subjective assumptions including the expected stock price volatility.

In Note 13, pro forma net earnings and pro forma basic and diluted net earnings per share figures are presented as if the fair value based method of accounting had been used to account for stock options granted to employees during fiscal 2003.

A compensation expense is also recognized for the Company's portion of the contributions made under the ESPP and for the grant date amount of vested units under the DSU, LTI-DSU and LTI-RSU plans. Any subsequent changes in CAE's stock price affects the compensation expense. In March 2004, the Company entered into an equity swap agreement with a major Canadian institution to reduce its cash and earnings exposure to fluctuation in the Company's share price relating to the DSU, LTI-DSU and LTI-RSU programs.

CAE's practice is to issue options in May of each fiscal year or at the time of hiring of new employees or new appointments. In both instances these options vest equally over four years. Any consideration paid by plan participants on the exercise of share options or the purchase of shares is credited to share capital together with any related stock-based compensation expense.

HEDGING RELATIONSHIPS AND DERIVATIVE FINANCIAL INSTRUMENTS

The Company enters into forward, swap and option contracts to reduce financial risk related to its exposure to fluctuations in interest rates and foreign exchange rates. The interest rate risk associated with certain long-term debt is hedged through interest rate swaps. The foreign currency risk associated with certain purchase and sale commitments denominated in a foreign currency is hedged through a combination of forward contracts and options. The Company does not use any derivative financial instruments for trading or speculative purposes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 01. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Effective April 1, 2004, the Company adopted prospectively CICA Accounting Guideline ("AcG-13"), *Hedging Relationships* and CICA Emerging Issues Committee Abstract 128 ("EIC-128"), *Accounting for Trading, Speculative or Non-Hedging Derivative Financial Instruments.* This guideline addresses identification, designation, documentation and effectiveness of hedging relationships for the purpose of applying hedge accounting, and the discontinuance of hedge accounting. Under this guideline, complete documentation of the information related to hedging relationships is required and the effectiveness of the hedges must be demonstrated and documented. The adoption of these guidelines did not have a material impact on the Company's financial statements.

Gains and losses on foreign currency contracts designated and effective as hedges are recognized in the consolidated statement of earnings during the same period as the underlying revenues and expenses. For interest rate swaps, the difference between the swap rate and the actual rate is reflected in earnings against the related interest expense. CAE assesses on an ongoing basis whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items.

Realized and unrealized gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, are deferred under other current, or non-current, assets or liabilities on the balance sheet and recognized in income in the period in which the underlying hedged transaction is recognized. In the event a designated hedged item is sold, extinguished or matured prior to the termination of the related derivative instrument, any realized or unrealized gain or loss on such derivative instrument is recognized in earnings. The interest payments relating to swap contracts are recorded in net earnings over the life of the underlying transaction based on the accrual method as an adjustment to interest income or interest expense. (Refer to Note 14)

DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS

Long-lived assets to be disposed of by sale are measured at the lower of their carrying amount or fair value less cost to sell, and are not depreciated while classified as held for sale.

Results of operations of components of the Company that have been disposed of by sale or are classified as held for sale are reported as discontinued operations if the operations and cash flows of those components have been, or will be, eliminated from the ongoing operations as a result of the disposal transaction and if the Company will not have any significant continuing involvement in the operations of the component after the disposal transaction. A component of an enterprise comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the Company's operations and cash flows. (Refer to Note 3)

SEVERANCE, TERMINATION BENEFITS AND COSTS ASSOCIATED WITH EXIT AND DISPOSAL ACTIVITIES

In accordance with EIC-134, *Accounting for Severance and Termination Benefits* and EIC-135, *Accounting for Costs Associated with Exit and Disposal Activities (Including Costs Incurred in a Restructuring),* the Company recognizes severance benefits that do not vest when the decision is made to terminate the employee. Special termination benefits are accounted for when Management commits to a plan that specifically identifies all significant actions to be taken and commits the entity to the event that obligates it under the terms of the contract with its employees to pay such termination benefits. Such termination benefits and the benefit arrangement is communicated to the employees in sufficient detail to enable them to determine the type and amount of benefits they will receive when their employment is terminated.

All other costs associated with restructuring, exit and disposal activities are recognized in the period when they are incurred and measured at their fair value.

CAE applied these guidelines for severance termination benefits and other restructuring costs as described in Note 24.

DISCLOSURE OF GUARANTEES

The Company discloses all information concerning certain types of guarantees that may require payments, contingent on specified types of future events. In the normal course of business, CAE issues letters of credit and performance guarantees. (Refer to Note 14)

EARNINGS PER SHARE

Earnings per share are calculated by dividing net earnings available for common shareholders by the weighted average number of common shares outstanding during the year. The diluted weighted average number of common shares outstanding is calculated by taking into account the dilution that would occur if the securities or other agreements for the issuance of common shares were exercised or converted into common shares at the later of the beginning of the period or the issuance date. The treasury stock method is used to determine the dilutive effect of the stock options. The treasury stock method is a method of recognizing the use of proceeds that could be obtained upon the exercise of options and warrants in computing diluted earnings per share. It assumes that any proceeds would be used to purchase common shares at the average market price during the period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FUTURE CHANGES TO ACCOUNTING STANDARDS

FINANCIAL INSTRUMENTS – RECOGNITION AND MEASUREMENT, HEDGES AND COMPREHENSIVE INCOME

In January 2005, the ASB issued three new standards dealing with financial instruments; (i) Financial Instruments-Recognition and Measurement; (ii) Hedges; and (iii) Comprehensive Income. The new standards are based on the U.S. FASB Statement 133, *Accounting for Derivative Instruments and Hedging Activities,* and on the International Accounting Standards ("IAS") Board's new standard, IAS 39, *Financial Instruments-Recognition and Measurement.* These requirements will be applicable for CAE in the first quarter of fiscal 2007. The Company is currently evaluating the impact of these new Handbook Sections on its financial statements.

The Handbook Section 3855, *Financial instruments-Recognition And Measurement prescribes* when a financial instrument is to be recognized on the balance sheet and the measurement method, using fair value or using cost-based measures. It also specifies how financial instrument gains and losses are to be presented.

New Handbook Section 3865, *Hedges* allows optional treatment providing that hedges be designated as either fair value hedges, cash flow hedges or hedges of a net investment in a self-sustaining foreign operation. For a fair value hedge, the gain or loss attributable to the hedged risk is recognized in net income in the period of change together with the offsetting loss or gain on the hedged item attributable to the hedged risk. The carrying amount of the hedged item is adjusted for the hedged risk. For a cash flow hedge or for a hedge of a net investment in a self-sustaining foreign operation, the effective portion of the hedging item's gain or loss is initially reported in other comprehensive income and subsequently reclassified to net income when the hedged item affects net income.

The ASB has issued new Handbook Section 1530, *Comprehensive Income,* and amended *Surplus,* Section 3250 to be renamed *Equity,* Section 3251. These standards require that an enterprise present comprehensive income and its components, as well as net income in its financial statements; and that an enterprise present separately changes in equity during the period, as well as components of equity at the end of the period, including comprehensive income.

NOTE 02.
BUSINESS ACQUISITIONS AND COMBINATIONS

GREENLEY & ASSOCIATES INC.

On November 30, 2004, the Company acquired all the issued and outstanding shares of Greenley & Associates Inc. ("G&A"), which provides services in the areas of project management, human factors, modelling and simulation. Total consideration for this acquisition amounted to $4.4 million payable in equivalent common shares issued by CAE in four installments as follows; 424,628 shares (representing $2.0 million) at the closing date, $0.8 million on November 30, 2005, $0.8 million on November 30, 2006, and 169,851 shares (representing $0.8 million) to be issued on November 30, 2007. The number of shares issued (to be issued) to satisfy the first and the fourth payments was calculated based on the average closing share price ($4.71 per share) of CAE common shares on the Toronto Stock Exchange ("TSX") for the 20-day period ending two days prior November 30, 2004. The number of shares to be issued to satisfy the second and the third payments will be based on the average closing share price of CAE common shares on the TSX for the 20-day period ending two days before their respective date of issuance. The purchase price is subject to an adjustment based on performance of the business for the twelve-month period following the acquisition. Any changes in the total consideration will be accounted for as a change in goodwill.

SERVICIOS DE INSTRUCCION DE VUELO, S.L.

In February 2004, CAE and Iberia Lineas Aereas de Espana, SA ("Iberia") agreed to combine their aviation training operations in Spain after receiving regulatory clearance from the Spanish authorities to commence operations, under an agreement entered into in October 2003.

On May 27, 2004, in connection with the financing of the combined operation, CAE Servicios Globales de Instruccion de Vuelo (Espana), S.L. ("SGIV"), a wholly-owned subsidiary of CAE, and Iberia contributed the net assets of their respective training centre facilities to Servicios de Instruccion de Vuelo, S.L. ("SIV"), with SGIV obtaining ownership of 80% of SIV. SIV financed the acquisition of the assets from SGIV and Iberia through an asset-backed financing transaction. (Refer to Note 11)

As part of this transaction, should the October 2003 agreement be terminated, SGIV and Iberia will be obliged to repurchase the assets they contributed, in proportion to the fair market value of the assets, for a total amount equal to the outstanding balance under the financing transaction.

FLIGHT TRAINING CENTRE CHILE S.A.

On April 22, 2004, the Company acquired from LAN Chile S.A. all the issued and outstanding shares of Flight Training Centre Chile S.A. ("FTC Chile") located in Santiago, Chile, for a total cash consideration of $0.9 million (US$ 0.7 million). This acquisition expands the Company's pilot-training operations into the South American market.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 02. BUSINESS ACQUISITIONS AND COMBINATIONS (CONT'D)

For the years ended March 31, 2004 and 2003, there were no acquisitions for the continuing operations. The net assets contributed by Iberia to SIV and net assets acquired from FTC Chile and G&A are summarized as follows:

(amounts in millions)	SIV	FTC CHILE	G&A	TOTAL
Current assets	$ 4.6	$ 0.2	$ 2.1	$ 6.9
Current liabilities	(0.1)	(0.1)	(1.2)	(1.4)
Property, plant and equipment	73.1	2.2	0.3	75.6
Other assets	—	—	0.5	0.5
Intangible assets				
Trade names	—	—	0.3	0.3
Customer relations	7.2	—	0.5	7.7
Other intangibles	—	—	0.1	0.1
Goodwill	6.9	—	2.5	9.4
Future income taxes	—	0.4	(0.5)	(0.1)
Long-term debt	(61.8)	—	(0.2)	(62.0)
Long-term liabilities	(2.4)	(0.3)	—	(2.7)
Total cost of the purchase:	27.5	2.4	4.4	34.3
Less: Balance of purchase price	—	(1.5)	—	(1.5)
Issuance of 424,628 shares (Note 12)	—	—	(2.0)	(2.0)
Common shares to be issued	—	—	(2.4)	(2.4)
Minority interest	(14.6)	—	—	(14.6)
Total cash consideration	$ 12.9	$ 0.9	$ —	$ 13.8

The net assets of SIV and FTC are included in the Civil Simulation and Training segment. The net assets of G&A are included in the Military Simulation and Training segment.

As part of the May 27, 2004 agreement (the "Agreement"), Iberia was to subsequently transfer a simulator that it was leasing from a third party, to SIV in exchange for a cash consideration of $5.7 million (€3.5 million). This transaction was accounted for as an increased contribution of property, plant and equipment and in long-term debt with a cash consideration equivalent to the net asset value.

During the year the Company reviewed its initial purchase price allocation of SIV, whereby property, plant and equipment were reduced by $4.5 million, customer relationship was increased by $7.2 million, goodwill increased by $4.5 million and cash consideration increased by $7.2 million.

In addition, as part of the Agreement, SIV has agreed to fund an amount up to a maximum of $2.4 million (€1.5 million) to cover any payments made by Iberia to former employees in order to indemnify Iberia for potential costs to be incurred due to certain employment matters. Based on Management's best estimate of SIV's potential liability, an amount of $2.4 million (€1.5 million) has been accrued as part of the purchase price and accounted for as goodwill.

NOTE 03.
DISCONTINUED OPERATIONS AND ASSETS HELD FOR SALE

DISCONTINUED OPERATIONS

CLEANING TECHNOLOGIES

On April 30, 2003, the Company completed the sale of certain assets of its German Cleaning Technologies operations to Bavaria AG for a nominal cash consideration approximating book value. Subsequent to completing the sale, CAE incurred post disposition costs with respect to the transfer of employees, resulting in a net charge of $2.6 million recorded in its results of discontinued operations. At the time of the sale, CAE and the buyer also entered into agreements by which CAE was to finance pension costs which would be compensated by the buyer. During fiscal 2005, CAE recorded in its results from discontinued operations a charge of $4.4 million (€2.8 million) relating to cover potential bad debts.

On July 31, 2003, CAE completed the sale of substantially all the assets of its last remaining Cleaning Technology business, Alpheus Inc. to Cold Jet Inc. of Cincinnati, Ohio. The total consideration, received was $2.8 million (US$2.1 million) of which $2.0 million (US$1.5 million) was received in fiscal 2004 and $0.8 million (US$0.6 million) received during the current fiscal year. In addition, the Company is entitled to receive further consideration of US$1.0 million based on the future performance of the combined businesses over the 53-month period from closing. No value has been ascribed in these financial statements to this additional consideration.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FORESTRY SYSTEMS

On August 16, 2002, CAE sold substantially all the assets of the sawmill division of its Forestry Systems segment for cash consideration of $25.0 million and a further estimated payment at $10.0 million, included in other assets, based on the operating performance of the disposed business in the three-year period following the closing date.

On May 2, 2003, CAE completed the sale of its remaining Forestry Systems business to Carmanah Design and Manufacturing Inc. for a total cash consideration of $20.3 million ($19.8 million received on closing, $0.5 million received during the second quarter of fiscal 2004). The Company is entitled to receive further consideration based on the performance of the business over the 30-month period following the closing. No value has been ascribed to this additional consideration in these financial statements.

MARINE CONTROLS

In the second quarter of fiscal 2005, the Board of Directors approved a plan to divest its Marine Controls business. The plan was consistent with the Company's strategic process of focusing on its core competency–the development and use of simulation and modelling technology to provide training solutions. On February 3, 2005, CAE completed with L-3 Communications Corporation ("L-3") the sale of the substantial components of its Marine Controls segment for cash consideration of $238.6 million. This amount is subject to completion of a net working capital audit of the Marine Controls segment. CAE does not believe this provision will result in a material adjustment to the cash consideration received. In accordance with the purchase agreement, L-3 will also acquire two other components of the Marine Controls segment, including the assumption of the CAE's guarantee of $53.0 million (£23 million) of project financed related debt for the U.K. Astute Class submarine training program. The sale of these components is subject to regulatory approvals and expected to be completed by the end of fiscal 2006. The expected proceeds on the sale of these components are nominal. The results of Marine Controls have been reported as discontinued operations and previously reported statements have been reclassified. Interest expense relating to debt not directly attributable to the continuing operations and expected to be paid with the proceeds of the sale of the Marine Controls business has been allocated to the discontinued operations based on their share of net assets (refer to Note 11A (ix)). This transaction resulted in a gain of $103.9 million, net of taxes of $25.1 million. The gain takes into account $43.7 million of goodwill and $7.0 million relating to the release of currency translation adjustment on CAE's Marine entities.

ASSETS HELD FOR SALE

CIVIL SIMULATION AND TRAINING

In the third quarter of fiscal 2005, CAE as part of is global expansion, announced that it will be opening a new business aviation-training centre in Morris County, New Jersey. The new training centre is expected to be operational in fiscal 2006. As a result, two redundant training centre buildings, one located in Dallas, Texas and a second located in Marietta, Georgia were adjusted to their fair value in fiscal 2005 and reclassified to assets held for sale in December 2004 and previously reported statements have been restated.

Summarized financial information for the discontinued operations is as follows:

OPERATION SUMMARY OF DISCONTINUED OPERATIONS

(amounts in millions, except per share amounts)	**2005**	2004	2003
Revenue			
Cleaning Technologies	**$**	$ 1.7	$ 72.0
Forestry Systems	**—**	3.1	20.8
Marine Controls	**109.6**	154.8	153.8
	$ 109.6	$ 159.6	$ 246.6
Net loss from Cleaning Technologies net of tax recovery (2005 –Nil; 2004–$1.7; 2003–$7.7)	**$ (4.4)**	$ (2.6)	$ (6.6)
Net loss from Forestry Systems net of tax recovery (2005 –Nil; 2004–$0.2; 2003–$3.0)	**—**	(0.5)	(7.2)
Net loss from Civil Simulation and Training net of tax recovery (2005–$0.1; 2004–$0.2; 2003–$0.2)	**(0.2)**	(0.3)	(0.4)
Net earnings from Marine Controls net of tax expense (2005 –$3.8; 2004 –$9.2; 2003 –$8.0)	**5.5**	20.0	17.5
Gain on sale of Marine Controls net of $25.1 million tax expense	**103.9**	—	—
Net earnings from discontinued operations	**$ 104.8**	$ 16.6	$ 3.3
Basic net earnings per share	**$ 0.42**	$ 0.07	$ 0.01
Diluted net earnings per share	**$ 0.42**	$ 0.07	$ 0.01

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 03. DISCONTINUED OPERATIONS AND ASSETS HELD FOR SALE (CONT'D)

NET ASSETS OF DISCONTINUED OPERATIONS AND ASSETS HELD FOR SALE

(amounts in millions)	AS AT MARCH 31, 2005		AS AT MARCH 31, 2004	
	MARINE CONTROLS	CIVIL	MARINE CONTROLS	CIVIL
Current assets held for sale				
Cash and cash equivalents	$ 4.4	$ —	$ 7.2	$ —
Accounts receivable	1.2	—	74.4	—
Inventories	—	—	7.1	—
Prepaid expenses	0.2	—	1.1	—
	$ 5.8	$ —	$ 89.8	$ —
Long-term assets held for sale				
Property, plant and equipment, net	$ 50.8	$ 4.2	$ 51.3	$ 11.7
Future income taxes	—	—	4.8	—
Intangible assets	—	—	26.0	—
Goodwill	—	—	43.1	—
Other assets	2.5	—	3.0	—
	$ 53.3	$ 4.2	$ 128.2	$ 11.7
Current liabilities related to assets held for sale				
Accounts payable and accrued liabilities	$ 7.8	$ —	$ 28.0	$ —
Deposits on contracts	—	—	21.8	—
Long-term debt due within one year	—	—	4.7	—
	$ 7.8	$ —	$ 54.5	$ —
Long-term liabilities related to assets held for sale				
Long-term debt	$ 53.0	$ —	$ 47.9	$ —
Future income taxes	0.4	—	12.3	—
	$ 53.4	$ —	$ 60.2	$ —

NOTE 04.
IMPAIRMENT OF GOODWILL, TANGIBLE AND INTANGIBLE ASSETS

During the third quarter of fiscal 2005, Management performed a comprehensive review of current performance and strategic orientation of its reporting units. This strategic review revealed that, several factors have severely affected mainly the Civil business, including; the enduring adverse economic environment of the airline industry creating a new market reality, slower than anticipated training outsourcing opportunities (due to pilot-related restructuring efforts at some major airlines), the escalating cost of manufacturing full-flight simulators, the erosion of the less than 50-seat regional jet market and the recent and rapid appreciation of the Canadian dollar versus its US counterpart. These elements have caused the recalibration of some key assumptions in Civil's strategic planning, which led to the review of the carrying amount of certain assets including; goodwill, intangible assets acquired in previous acquisitions, inventory levels, non-performing training equipment and certain other assets.

In testing for impairment of long-lived assets, the Company assessed recoverability of the carrying amounts by reference to expected undiscounted cash flows. An impairment charge is recognized when the carrying amount is not fully recoverable and when it exceeds the fair values determined by reference to recognized valuation methods, including discounted cash flows and independent appraisals.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Therefore, based on this review, the Company recorded a $443.3 million impairment charge, virtually all related to its Civil business, detailed as follows:

(amounts in millions)	2005
Goodwill	**$ 205.2**
Customer relations	**86.7**
Trades names	**20.4**
Property, plant and equipment (simulators)	**78.4**
Inventories	**33.3**
Other assets	**19.3**
	$ 443.3

NOTE 05.
ACCOUNTS RECEIVABLE

(amounts in millions)	2005	2004
Trade	**$ 99.9**	$ 130.0
Allowance for doubtful accounts	**(3.5)**	(7.9)
Unbilled receivables	**122.0**	148.7
Other receivables	**37.3**	45.7
	$ 255.7	$ 316.5

Approximately $10.4 million of the March 2005 unbilled receivables are not expected to be recovered within one year (2004–$5.9 million).

Under an agreement dated March 24, 2005, on an ongoing basis, the Company will sell third party receivables to a financial institution for an amount of up to $25.0 million. Under the terms of the agreement, the Company will continue to act as collection agent. The selected accounts receivable will be sold to a third party for cash consideration on a non-recourse basis to the Company. As at March 31, 2005, $16.5 million of specific accounts receivable were sold to the financial institution pursuant to this agreement. Net proceeds of the sale were used to repay borrowings under the Company's committed credit facilities.

NOTE 06.
INVENTORIES

(amounts in millions)	2005	2004
Work-in-progress	**$ 61.6**	$ 110.8
Raw materials, supplies and manufactured products	**39.4**	36.9
	$ 101.0	$ 147.7

As indicated in Note 4, the Company recognized an impairment charge of $33.3 million related to certain inventory, during the third quarter of fiscal 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 07.
PROPERTY, PLANT AND EQUIPMENT

(amounts in millions)	2005			2004		
	COST	ACCUMULATED DEPRECIATION	NET BOOK VALUE	COST	ACCUMULATED DEPRECIATION	NET BOOK VALUE
Land	**$ 18.8**	**$ —**	**$ 18.8**	$ 19.7	$ —	$ 19.7
Buildings and improvements	**233.9**	**66.9**	**167.0**	240.4	58.3	182.1
Simulators	**396.3**	**43.0**	**353.3**	403.2	36.1	367.1
Machinery and equipment	**185.3**	**100.3**	**85.0**	214.4	102.6	111.8
Assets under capital lease	**137.0**	**27.8**	**109.2**	38.2	24.3	13.9
Assets under construction						
Simulators	**58.9**	**—**	**58.9**	85.4	—	85.4
	$1,030.2	**$ 238.0**	**$ 792.2**	$1,001.3	$ 221.3	$ 780.0

As indicated in Note 4, during the third quarter of fiscal 2005, the Company recognized an impairment charge of $78.4 million related to non performing simulators.

Depreciation of property, plant and equipment was $55.1 million in 2005 (2004—$51.3 million, 2003–$48.5 million).

NOTE 08.
INTANGIBLE ASSETS

(amounts in millions)	2005			2004		
	COST	ACCUMULATED DEPRECIATION	NET BOOK VALUE	COST	ACCUMULATED DEPRECIATION	NET BOOK VALUE
Trade names	**$ 12.3**	**$ 0.2**	**$ 12.1**	$ 30.5	$ 3.3	$ 27.2
Customer relations	**0.5**	**—**	**0.5**	101.7	10.6	91.1
Customer contractual agreements	**8.5**	**2.5**	**6.0**	11.5	2.3	9.2
Other intangible assets	**2.1**	**0.5**	**1.6**	2.4	0.7	1.7
	$ 23.4	**$ 3.2**	**$ 20.2**	$ 146.1	$ 16.9	$ 129.2

As indicated in Note 4, during the third quarter of fiscal 2005, the Company recognized an impairment charge of $86.7 million and $20.4 million related to customer relations and trade names, respectively, originating from Civil's acquisitions in fiscal 2002.

The continuity of intangible assets is as follows:

(amounts in millions)	2005			2004		
	CIVIL	MILITARY	TOTAL	CIVIL	MILITARY	TOTAL
Beginning balance	**$ 127.4**	**$ 1.8**	**$ 129.2**	$ 140.1	$ 2.1	$ 142.2
Additions (Note 2)	**7.2**	**0.9**	**8.1**	0.6	—	0.6
Amortization	**(6.3)**	**(0.1)**	**(6.4)**	(6.8)	(0.1)	(6.9)
Impairment	**(107.1)**	**—**	**(107.1)**	—	—	—
Foreign exchange	**(3.5)**	**(0.1)**	**(3.6)**	(6.5)	(0.2)	(6.7)
Ending balance	**$ 17.7**	**$ 2.5**	**$ 20.2**	$ 127.4	$ 1.8	$ 129.2

The yearly amortization expense for the five following years will be approximately $1.8 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 09.
GOODWILL

The continuity of goodwill by reportable segment is as follows:

(amounts in millions)	2005			2004		
	CIVIL	MILITARY	TOTAL	CIVIL	MILITARY	TOTAL
Beginning balance	**$ 204.1**	**$ 96.6**	**$ 300.7**	$ 216.5	$ 104.0	$ 320.5
Additions (Note 2)	**6.9**	**2.5**	**9.4**	—	—	—
Impairment	**(205.2)**	**—**	**(205.2)**	—	—	—
Foreign exchange	**(5.8)**	**(7.0)**	**(12.8)**	(12.4)	(7.4)	(19.8)
Ending balance	**$ —**	**$ 92.1**	**$ 92.1**	$ 204.1	$ 96.6	$ 300.7

As indicated in Note 4, a goodwill impairment charge of $205.2 million was recorded in the third quarter of fiscal 2005, which represented all the goodwill related to the Civil segment.

NOTE 10.
OTHER ASSETS

(amounts in millions)	2005	2004
Investment in and advances to CVS Leasing Ltd. (1)	**$ 41.2**	$ 49.1
Deferred development costs net of $10.7 million accumulated amortization (2004– $5.6 million) (ii) (iv)	**33.7**	41.3
Deferred pre-operating costs net of $14.6 million accumulated amortization (2004– $8.5 million)	**13.5**	25.2
Long-term receivables (iii)	**10.6**	18.4
Deferred financing costs net of $14.7 million accumulated amortization (2004– $5.7 million)	**5.6**	11.5
Other net of $0.3 million accumulated amortization (2004– Nil) (Note 21)	**32.8**	35.3
	$ 137.4	$ 180.8

(i) The Company led a consortium which was contracted by the U.K. Ministry of Defence (MoD) to design, construct, manage, finance and operate an integrated simulator-based aircrew training facility for the Medium Support Helicopter ("MSH") fleet of the Royal Air Force. The contract covers a 40-year period, which can be terminated by the MoD after 20 years, in 2018.

In connection with the contract, the Company has established a subsidiary, CAE Aircrew Training Pic ("Aircrew"), of which it owns 78% with the balance held by the other consortium partners. This subsidiary has leased the land from the MoD, built the facility and operates the training centre. Aircrew has been consolidated with the accounts of the Company.

In addition, the Company has a minority shareholding of 14% in, and has advanced funds to, CVS Leasing Ltd. ("CVS"), an entity established to acquire the simulators and other equipment that are leased to Aircrew. CVS obtained project financing which amounts to £70.6 million at March 31, 2005 and expires in October 2016. This financing is secured solely by the assets of CVS with no recourse to CAE.

(ii) R&D expenditures aggregated $93.5 million during the year (2004–$81.0 million, 2003–$102.0 million), of which $9.9 million representing qualifying development costs pursuant to CICA requirements (2004–$12.7 million, 2003–$13.7 million) was deferred. The Company has received government assistance of $10.8 million related to R&D expenditures during the year (2004–$13.9 million, 2003–$32.5 million), of which $0.9 million (2004–$2.3 million, 2003–$2.3 million) was recorded against deferred costs incurred to develop new products and none was recorded against machinery and equipment (2004–$1.8 million, 2003-nil), with the balance being accounted for as a reduction of research and development expenses. (Refer to Note 19)

(iii) The Company has established secured subordinated promissory notes in connection with the sale of its various Cleaning Technologies businesses totaling $7.6 million. The notes bear interest at rates ranging from 3% to 7%.

(iv) As indicated in Note 4, during the third quarter of fiscal 2005, the Company recognized an impairment charge of $19.3 million related to deferred development charges.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11.
DEBT FACILITIES

A. LONG-TERM DEBT

(amounts in millions)	2005	2004
(i) Senior notes	**$ 150.6**	$ 161.5
(ii) Revolving unsecured term credit facilities,		
5 years maturing April 2006, US$350.0 (outstanding March 31, 2005–$30.4 and US$Nil, March 31, 2004–$18 1.4 and US$70.0)	**30.4**	273.1
5 years, maturing April 2006, €100.0 (outstanding March 31, 2005–€Nil, March 31, 2004–€20.0)	**—**	32.2
(iii) Term loan, maturing in April 2009 (outstanding March 31, 2005–US$Nil, March 31, 2004–US$28.2)	**—**	37.0
(iv) Term loans, maturing in May and June 2011 (outstanding March 31, 2005–€30.5 and €6.0, March 31, 2004–€Nil)	**57.3**	—
(v) Term loan of £12.7, secured, maturing in October 2016 (outstanding March 31, 2005–£6.0, March 31, 2004–£8.9)	**13.7**	21.4
(vi) Grapevine Industrial Development Corporation bonds, secured (US$27.0)	**32.7**	35.4
(vii) Amsterdam asset-backed financing maturing in December 2007 and August 2008 (outstanding March 31, 2005–€24.7, March 31, 2004–€Nil)	**38.8**	—
(viii) Obligations under capital lease commitments	**19.4**	23.7
	342.9	584.3
Less: Long-term debt due within one year	**35.3**	8.8
	$ 307.6	$ 575.5

(i) Pursuant to a private placement, the Company borrowed US$108.0 million and $20.0 million. These unsecured senior notes rank equally with term bank financings with fixed repayment amounts of $20.0 million in 2005, US$15.0 million in 2007, US$60.0 million in 2009 and US$33.0 million in 2012. Fixed interest is payable semi-annually in June and December at an average rate of 7.6% on the US amounts and 7.2% on the Canadian amount. The Company has entered into interest rate swap agreements converting the initial fixed interest rate into the equivalent of a three-month LIBOR borrowing plus 3.6% on US$33.0 million of the senior notes.

(ii) These revolving term credit facilities (US$350.0 million and €100.0 million) are unsecured and the interest rate payable is based on LIBOR, BAs or EURIBOR plus 0.6%. As at the end of March 31, 2004, an amount of $35.0 million had been fixed through a swap agreement until April 2006 at a rate of 5.0%. This swap was unwound in February 2005 as the Company repaid substantially all of the outstanding borrowings under the facilities. The average interest rate at March 31, 2005 is 3.1% (2004–3.4%).

(iii) The Company had arranged project financing for its training centre in São Paulo, Brazil. This term loan was carrying an interest rate of 7.7% and was supported by a letter of credit for an amount equal to the outstanding obligations. The loan was repaid prior to March 31, 2005 with the proceeds from the sale of the Marine division.

(iv) The Company, in association with Iberia Lineas de España, combined their aviation training operations in Spain. The operators financed the acquisition of the simulators from CAE and Iberia through asset-backed financing maturing in May and June 2011. As part of the lease agreements, should the October 2003 agreement be terminated, CAE and Iberia will be obliged to repurchase the simulators they contributed, in proportion to the fair value of the simulators, for a total amount equal to the outstanding balance under the financing agreement. Quarterly capital repayments are to be made for the term of the financing. The implicit interest rate is 4.60%. The net book value of the simulators being financed, as at March 31, 2005 is equal to approximately $90.2 million (€57.5 million).

(v) The Company arranged project financing for one of its subsidiaries to finance the Company's MSH program for the MoD in the United Kingdom. The credit facility includes a term loan that is secured by the project assets of the subsidiary and a bi-annual repayment is required until 2016. Interest on the loans is charged at a rate approximating LIBOR plus 0.85%. The Company has entered into an interest rate swap totaling £5.5 million fixing the interest rate at 6.31%. The value of the assets pledged as collateral for the credit facility as at March 31, 2005, is £26.1 million (2004–27.5 million).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(vi) Airport Improvement Revenue Bonds were issued by the Grapevine Industrial Development Corporation, Grapevine, Texas for amounts of US$8.0 million and US$19.0 million and maturing respectively in 2010 and 2013. Real property, improvements, fixtures and specified simulation equipment secure the bonds. The rates are set periodically by the remarketing agent based on market conditions. For the bonds maturing in 2010, the rate is set weekly. For the bonds maturing in 2013, the rate is set yearly and is subject to a maximum rate of 10% permissible under current applicable laws. As at March 31, 2005, the combined rate for both series was approximately 2.6%. The security is limited to an amount not exceeding the outstanding balance of the loans which represents US$27.0 million as at March 31, 2005. Also, a letter of credit has been issued to support the bonds for the outstanding amount of the loans.

(vii) Asset backed financing in the Company's Amsterdam Training centre represents financing for three different simulators expiring in December 2007 and August 2008. The average cost of the financing is equal to approximately 8.0%. The net book value of the simulators under the financing, as at March 31, 2005 is equal to approximately $44.7 million (€28.5 million).

(viii) These capital leases are related to the leasing of various simulators in CAE's subsidiaries. The effective interest rate on obligations under capital leases which mature have staggered maturities until March 2024 was approximately 5.0% (2004–5.0%).

(ix) Payments required in each of the next five fiscal years to meet the retirement provisions of the long-term debt are as follows:

(amounts in millions)	
2006	$ 35.3
2007	45.7
2008	47.8
2009	21.9
2010	84.3
Thereafter	107.9
	$ 342.9

Details of net interest expense (income) are as follows:

(amounts in millions)	**2005**	2004	2003
Long-term debt interest expense	**$ 35.3**	$ 30.2	$ 33.5
Amortization of deferred financing costs and other	**9.7**	5.7	6.7
Allocation of interest expense to discontinued operations	**(1.4)**	(1.5)	(2.4)
Interest capitalized	**(5.8)**	(6.4)	(6.2)
Interest on long-term debt	**$ 37.8**	$ 28.0	$ 31.6

(amounts in millions)	**2005**	2004	2003
Interest income	**$ (5.7)**	$ (6.1)	$ (3.7)
Other interest expense	**—**	0.5	0.2
Other interest income, net	**$ (5.7)**	$ (5.6)	$ (3.5)

Certain of the Company's debt instruments include customary positive and negative covenants, including interest coverage, leverage ratios, and restrictions on the sale of assets. In connection with the impairment charge taken during the third quarter of fiscal 2005, CAE obtained an amendment to certain definitions related to financial covenants from both its banking syndicate, with respect to the unsecured revolving credit facilities, and its senior note holders. CAE was able to obtain approval from both groups of senior lenders to amend the definitions, thus allowing the Company to be compliant with the financial covenants associated with each agreement. As at March 31, 2005, CAE is in full compliance with its financial covenants.

B. SHORT-TERM DEBT

The Company has unsecured bank lines of credit available in various currencies totaling $31.0 million (2004–$28.2 million, 2003–$89.0 million), of which $11.2 million was used as at March 31, 2005 (2004–$6.4 million, 2003–$41.3 million). The effective rate on the short-term borrowings was 4.25% (2004–4.0%, 2003–4.8%).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12.
CAPITAL STOCK

(i) The Company's articles of incorporation authorize the issuance of an unlimited number of preferred shares, issuable in series, and an unlimited number of common shares. To date, the Company has not issued any preferred shares.

(ii) A reconciliation of the issued and outstanding common shares of the Company is as follows:

(amounts in milions, except number of shares)	**2005**		2004		2003	
	NUMBER OF SHARES	**STATED VALUE**	NUMBER OF SHARES	STATED VALUE	NUMBER OF SHARES	STATED VALUE
Balance at beginning of year	**246,649,180**	**$ 367.5**	219,661,178	$ 190.5	218,955,780	$ 186.8
Shares issued (Note 2, (a) (b))	**424,628**	**2.0**	26,600,000	175.0	—	—
Stock options exercised	**869,620**	**3.6**	282,000	1.4	650,776	3.5
Stock dividends (c)	**126,901**	**0.7**	106,002	0.6	54,622	0.2
Balance at end of year	**248,070,329**	**$ 373.8**	246,649,180	$ 367.5	219,661,178	$ 190.5

(a) On November 30, 2004, the Company issued 424,628 common shares at a price of $4.71 per share, for the acquisition of Greenley & Associates Inc.

(b) On September 30, 2003, the Company issued 26,600,000 common shares at a price of $6.58 per share, for a cash proceeds of $175.0 million.

(c) Until February 29th, 2004, the Company's Dividend Reinvestment Plan ("DRIP") provided that eligible shareholders (which covered all shareholders living wherever the shares were distributed) could elect to receive common stock dividends in lieu of cash dividends. As of March 1, 2004, eligibility has been limited to Canadian resident shareholders only.

(iii) The following is a reconciliation of the denominators for the basic and diluted earnings per share computations:

	2005	2004	2003
Weighted average number of common shares outstanding –Basic	**247,060,580**	233,167,858	219,427,513
Effect of dilutive stock options	**812,273**	849,912	897,806
Weighted average number of common shares outstanding –Diluted	**247,872,853**	234,017,770	220,325,319

Options to acquire 4,635,100 common shares (2004–4,195,400, 2003–3,198,000) have been excluded from the above calculation since their inclusion would have an anti-dilutive effect.

NOTE 13.
STOCK-BASED COMPENSATION PLANS

EMPLOYEE STOCK OPTION PLAN

Under the long-term incentive program of the Company, options may be granted to officers and other key employees of the Company and its subsidiaries to purchase common shares of the Company at a subscription price of 100% of the market value at the date of the grant. Market value is determined as the closing price of the common shares on the Toronto Stock Exchange on the last day of trading prior to the effective date of the grant.

At March 31, 2005, a total of 10,660,426 common shares remained authorized for issuance under the Employee Stock Option Plan ("ESOP"). The options are exercisable during a period not to exceed six years and are not exercisable during the first 12 months after the date of the grant. The right to exercise all of the options accrues over a period of four years of continuous employment. However, if there is a change of control of the Company, the options become immediately exercisable. Options are adjusted proportionately for any stock dividends or stock splits attributed to the common shares of the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A reconciliation of the outstanding options is as follows:

For the years ended March 31	**2005**		2004		2003	
	NUMBER OF OPTIONS	**WEIGHTED AVERAGE EXERCISE PRICE**	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
Options outstanding at beginning of year	**8,128,370**	**$ 7.51**	5,692,750	$ 9.37	4,999,078	$ 7.70
Granted	**2,046,650**	**$ 5.68**	3,536,320	$ 4.14	1,767,000	$ 12.71
Exercised	**(869,620)**	**$ 4.15**	(282,000)	$ 4.88	(650,776)	$ 5.62
Forfeited	**(809,725)**	**$ 6.77**	(718,400)	$ 6.98	(325,400)	$ 9.38
Expired	**(287,000)**	**$ 6.43**	(100,300)	$ 5.70	(97,152)	$ 9.10
Options outstanding at end of year	**8,208,675**	**$ 7.52**	8,128,370	$ 7.51	5,692,750	$ 9.37
Options exercisable at end of year	**3,731,085**	**$ 8.76**	2,887,000	$ 8.07	2,000,975	$ 6.78

The following table summarizes information about the Company's ESOP as at March 31, 2005:

	OPTIONS OUTSTANDING			**OPTIONS EXERCISABLE**	
RANGE OF EXERCISE PRICES	**NUMBER OUTSTANDING**	**AVERAGE REMAINING CONTRACTUAL LIFE (YEARS)**	**WEIGHTED AVERAGE EXERCISE PRICE**	**NUMBER EXERCISABLE**	**WEIGHTED AVERAGE EXERCISE PRICE**
$4.08 to $5.20	**2,876,875**	**4.07**	**$ 4.21**	**916,185**	**$ 4.15**
$5.28 to $5.89	**1,206,700**	**5.15**	**$ 5.63**	**91,800**	**$ 5.45**
$6.03 to $9.20	**1,527,850**	**2.52**	**$ 6.72**	**1,021,225**	**$ 6.98**
$12.225 to $14.60	**2,597,250**	**3.65**	**$ 12.53**	**1,701,875**	**$ 12.48**
Total	**8,208,675**	**3.33**	**$ 7.52**	**3,731,085**	**$ 8.76**

For the year ended March 31, 2005, compensation cost for CAE's stock options was recognized in net earnings with a corresponding credit of $2.0 million (fiscal 2004-$1.3 million) to contributed surplus using the fair value method of accounting for awards that were granted in fiscal 2004 and 2005.

The assumptions used for purposes of the option calculations outlined in this note are presented below:

	2005	2004	2003
Assumptions used in Black-Scholes options pricing model:			
Dividend yield	**1.26%**	1.29%	1.06%
Expected volatility	**40.0%**	41.5%	46.5%
Risk-free interest rate	**5.75%**	5.75%	5.26%
Expected life (years)	**6**	6	6
Weighted average fair value of options granted	**$ 2.27**	$ 1.65	$ 5.84

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 13. STOCK-BASED COMPENSATION PLANS (CONT'D)

DISCLOSURE OF PRO FORMA INFORMATION REQUIRED UNDER CICA HANDBOOK SECTION 3870

During the year ended March 31, 2003, the Company granted 1,767,000 options to purchase common shares. The weighted average grant date fair value of options granted during this period amounted to $5.84 per option. To compute the pro forma compensation cost, the Black-Scholes valuation model was used to determine the fair value of the options granted. Pro forma net earnings and pro forma basic and diluted net earnings per share are presented below:

(amounts in millions, except per share amounts)	**2005**	2004	2003
Net (loss) earnings, as reported	**$ (199.9)**	$ 64.0	$ 117.2
Pro forma impact	**(2.1)**	(2.5)	(2.5)
Pro forma net (loss) earnings	**$ (202.0)**	$ 61.5	$ 114.7
Pro forma basic and diluted net earnings per share [1]	**$ (0.82)**	$ 0.26	$ 0.52

1 For fiscal 2005, the effect of stock options potentially exercisable on pro forma net loss per share was anti-dilutive; therefore, basic and diluted pro forma net loss per share are the same.

EMPLOYEE STOCK PURCHASE PLAN

The Company maintains an Employee Stock Purchase Plan ("ESPP") to enable employees of the Company and its participating subsidiaries to acquire CAE common shares through regular payroll deductions plus employer contributions. The Plan allows employees to contribute up to 10% of their annual base salary. The Company and its participating subsidiaries match the first $500 employee contribution and contribute $1 for every $3 on additional employee contributions, to a maximum of 2% of the employee's base salary. Matching contributions vest at the beginning of the third year following the year during which the employee contributions were made, provided employment has been continuous during that period. Common shares of the Company are purchased by the ESPP trustee on behalf of the participants on the open market, through the facilities of the Toronto Stock Exchange. The Company recorded compensation expense in the amount of $1.4 million (2004–$1.6 million, 2003–$1.9 million) in respect of employer contributions under the Plan.

DEFERRED SHARE UNIT PLAN

The Company maintains a Deferred Share Unit ("DSU") Plan for executives whereby an executive may elect to receive any cash incentive compensation in the form of deferred share units. The Plan is intended to enhance the Company's ability to promote a greater alignment of interests between executives and the shareholders of the Company. A deferred share unit is equal in value to one common share of the Company. The units are issued on the basis of the average closing board lot sale price per share of CAE common shares on the Toronto Stock Exchange during the last 10 days on which such shares traded prior to the date of issue. The units also accrue dividend equivalents payable in additional units in an amount equal to dividends paid on CAE common shares. Deferred share units mature upon termination of employment, whereupon an executive is entitled to receive the fair market value of the equivalent number of common shares, net of withholdings, in cash.

In fiscal 2000, the Company adopted a DSU Plan for Non-Employee Directors. A non-employee director holding less than 5,000 common shares of the Company receives the Board retainer and attendance fees in the form of deferred share units. A non-employee director holding at least 5,000 common shares may elect to participate in the Plan in respect of part or all of his or her retainer and attendance fees. The terms of the Plan are essentially identical to the key executive DSU Plan.

The Company records the cost of the DSU Plan as compensation expense. As at March 31, 2005, 343,116 units were outstanding at a value of $1.9 million (2004–403,071 units at a value of $2.3 million; 2003–362,498 units at a value of $1.0 million). A total number of 114,969 units were redeemed during the fiscal year ended March 31, 2005 under both DSU Plans in accordance with their respective plan text, for a total of $0.6 million. As at March 31, 2005 and March 31, 2004 no DSU were cancelled.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

LONG-TERM INCENTIVE-DEFERRED SHARE UNIT PLAN (MAY 2003 AND MAY 2004)

During the year ended March 31, 2005, the Company adopted, as an element of its long-term incentive compensation plan, a new long-term deferred share units ("LTI-DSU"). This new LTI-DSU does not replace the existing 2003 LTI-DSU Plan. Both plans are intended to enhance the Company's ability to promote a greater alignment of interests between executives and the shareholders of the Company. LTI-DSUs have been granted to executives and managers of the Company. A LTI-DSU is equal in value to one common share of the Company determined based on the closing quoted market value of the Company shares net of withholdings at a specific date, and subject to the Company plan. The LTI-DSU also accrued dividend equivalents payable in additional units in an amount equal to dividends paid on CAE common shares. The April 2003 LTI-DSU vest equally over four years and can be redeemed for cash upon retirement, death, disability or involuntary termination. In May 2003, the Company issued 1,441,011 LTI-DSU units. The expense recorded in fiscal 2005 with respect to these units was $1.2 million (2004–$1.4 million). The May 2004 LTI-DSU vest equally over five years and can be redeemed for value upon retirement, death, disability or involuntary termination. The vested shares in the account of the participant upon voluntary termination may be redeemed. The value is equal to the fair market value of the equivalent number of common shares of the Company, net of withholdings, in cash. In fiscal 2005, the Company issued 582,431 LTI-DSU units. The expense recorded in fiscal 2005 with respect to these units was $0.6 million. On March 15, 2004, the Company entered into a contract to reduce its earnings exposure to the fluctuations in the Company's share price (refer to Note 14).

LONG-TERM INCENTIVE-RESTRICTED SHARE UNIT PLAN

The long-term incentive–restricted share unit (LTI-RSU) is intended to enhance CAE Inc.'s ability to attract and retain talented individuals to serve as officers and executive of CAE and to promote a greater alignment of interests between such officers, executives and the shareholders of CAE. The LTI-RSU is set up as a stock based performance plan. Vesting of granted restricted shares is based on the performance of the stock on the third anniversary of the grant date. Vesting is conditional to the targets set out in the LTI-RSU plan and described hereafter:

(i) 100% of the units, if CAE shares have appreciated at least 33% (10% annual compounded growth) during that timeframe; or

(ii) 50% of the units, if CAE shares have appreciated at least 24% (7.5% annual compounded growth) but not as much as 33% during that timeframe.

No LTI-RSU vest if the market value of the Common Shares has appreciated less than 24% during the specified timeframe.

No pro-ration in the vesting percentage of LTI-RSU occurs for any appreciation of the market value of CAE shares of between 24% and 33% during the specified timeframe.

In order to determine if the maximum or minimum return has been reached, the plan uses the weighted value of the Common Share, based on the Fair Market value during the twenty trading days immediately preceding the date. If a participant is subjected to employment loss or other form of dismissal other than for cause subjected to conditional pro-rata. If a participant leaves voluntarily or is terminated for cause, both the vested and unvested portion of the Restricted Share Units are cancelled. If the above-mentioned criteria are satisfied, the amount of money to be paid to each participant is determined by the number of Restricted Share Units in the participant's account multiplied by the closing price of CAE's stock on the TSX. Therefore, the closing price on the particular date is used for the vesting determination date (i.e. third anniversary vesting date). The participants are paid within ten days of the vesting determination date. In fiscal 2005, the Company issued 788,167-RSU units. The expense recorded in fiscal 2005 with respect to these units was $1.0 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14.
FINANCIAL INSTRUMENTS

FOREIGN CURRENCY RISK

The Company entered into forward foreign exchange contracts totaling $305.0 million (buy contracts $42.4 million and sell contracts $262.6 million). The total net unrealized gain as of March 31, 2005, is $9.1 million (unrealized loss on buy contracts of $0.1 million and unrealized gain on sell contracts of $9.2 million).

CONSOLIDATED FOREIGN EXCHANGE TRANSACTIONS OUTSTANDING

(amounts in millions)	**2005**		2004	
CURRENCIES (SOLD/BOUGHT)	**NOTIONAL AMOUNT[1]**	**AVERAGE RATE**	NOTIONAL AMOUNT[1]	AVERAGE RATE
US/CA				
Less than 1 year	**$ 169.3**	**0.7964**	$ 96.4	0.7492
Between 1 and 3 years	**48.6**	**0.7989**	15.4	0.7410
Between 3 and 5 years	**0.4**	**0.8263**	—	—
CA/US				
Less than 1 year	**34.4**	**1.2125**	11.8	1.3141
US/EUR				
Less than 1 year	**—**	**—**	1.9	1.1383
CA/EUR				
Less than 1 year	**7.9**	**1.5796**	—	—
EUR/CA				
Less than 1 year	**22.2**	**0.6268**	—	—
Between 1 and 3 years	**8.9**	**0.6271**	—	—
Between 3 and 5 years	**7.8**	**0.6147**	—	—
GBP/CA				
Less than 1 year	**5.0**	**0.4251**	3.3	0.4122
Between 1 and 3 years	**—**	**—**	0.9	0.4135
CA/GBP				
Less than 1 year	**0.5**	**2.2126**	—	—
GBP/US				
Less than 1 year	**—**	**—**	51.7	0.5561
	$ 305.0		$ 181.4	

1 Exchange rates as at the end of the respective fiscal years were used to translate amounts in foreign currencies.

CREDIT RISK

The Company is exposed to credit risk on billed and unbilled accounts receivable. However, its customers are primarily established companies with publicly available credit ratings or government agencies, factors that facilitate monitoring the risk. In addition, the Company typically receives substantial non-refundable deposits on contracts. The Company closely monitors its exposure to major airlines in order to curtail it to the extent possible.

The Company is exposed to credit risk in the event of non-performance by counterparties to its derivative financial instruments. The Company minimizes this exposure by entering into contracts with counterparties that are of high credit quality. Collateral or other security to support financial instruments subject to credit risk is usually not obtained. The credit standing of counterparties is regularly monitored.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

INTEREST RATE EXPOSURE

The Company bears some interest rates fluctuation risk on its variable long-term debt and some fair value risk on its fixed interest long-term debt. As at March 31, 2005, the Company has entered into three interest rate swap agreements with three different financial institutions to mitigate these risks for a total notional value of $65.8 million. One agreement, with a notional value of $39.9 million (US$33.0 million), has converted fixed interest rate debt into floating whereby the Company pays the equivalent of a 3-month LIBOR borrowing rate plus 3.6% and receives a fixed interest rate of 7.8% up to June 2012. The remaining two contracts are converting floating interest rate debt into fixed for a notional value of $25.9 million whereby the Company will receive quarterly LIBOR and a weekly tax-exempt based floating rate and pay fixed interest payments as follows:

- until September 2005 on $13.3 million (US$11.0 million), the Company will pay monthly a fixed annual interest rate of 5.0%;
- until October 2016 on $12.6 million (£5.5 million), the Company will pay quarterly fixed annual interest rate of 6.3%.

After considering these swap agreements, as at March 31, 2005, 70% of the long-term debt bears fixed interest rates.

STOCK BASED COMPENSATION COST

In March 2004, the Company entered into an equity swap agreement with a major Canadian institution to reduce its cash and earnings exposure to fluctuation in the Company's share price relating to the DSU and LTI-DSU programs. Pursuant to the agreement, the Company receives the economic benefit of dividends and share price appreciation while providing payments to the financial institution for the institution's cost of funds and any share price depreciation. The net effect of the equity swap partly offsets movements in the Company's share price impacting the cost of the DSU and LTI-DSU programs. As at March 31, 2005, the equity swap agreement covered 600,000 shares of the Company.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions have been used to estimate the fair value of the financial instruments:

- cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities are valued at their carrying amounts on the balance sheet, which represent an appropriate estimate of their fair values due to their near-term maturities;
- capital leases are valued using the discounted cash flow method;
- long-term debt value is estimated based on discounted cash flows using current interest rates for debt with similar terms and remaining maturities;
- interest rate and currency swap contracts reflect the present value of the potential gain or loss if settlement were to take place at the balance sheet date;
- the forward foreign exchange contracts are represented by the estimated amounts that the Company would receive or pay to settle the contracts at the balance sheet date.

The fair value and the carrying amount of the financial instruments as at March 31 is as follows:

(amounts in millions)	**2005**		**2004**	
	FAIR VALUE	**CARRYING AMOUNT**	FAIR VALUE	CARRYING AMOUNT
Long-term debt	**$ 354.2**	**$ 342.9**	$ 612.0	$ 584.3
Net forward foreign exchange contracts	**9.1**	**—**	1.2	—
Interest rate swap contracts	**(1.8)**	**—**	(2.6)	—

LETTERS OF CREDIT AND GUARANTEES

As at March 31, 2005, CAE had outstanding letters of credit and performance guarantees in the amount of $73.3 million (2004–$168.6 million) issued in the normal course of business. These guarantees are issued under standby facilities available to the Company through various financial institutions.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14. FINANCIAL INSTRUMENTS (CONT'D)

The advance payment guarantees are related to progress/milestone payments made by our customers and are reduced or eliminated upon delivery of the product. The contract performance guarantees are linked to the completion of the intended product or service rendered by CAE and at the satisfaction of the customer. It represents 10% to 20% of the overall contract amount. The customer releases the Company from these guarantees at the signature of a certificate of completion. The letters of credit for the operating lease obligations provide credit support for the benefit of the owner participant in the September 30, 2003 sale and leaseback transaction and an operating lease for a simulator in another subsidiary.

(amounts in millions)	**2005**	2004
Advance payment	**$ 25.3**	$ 119.2
Contract performance	**7.8**	10.6
Operating lease obligations	**37.6**	31.1
Others	**2.6**	7.7
Total	**$ 73.3**	$ 168.6

RESIDUAL VALUE GUARANTEES-SALE AND LEASEBACK TRANSACTIONS

Following certain sale and leaseback transactions, the Company has agreed to guarantee the residual value of the underlying equipment in the event that the equipment is returned to the lessor and the net proceeds of any eventual sale do not cover the guaranteed amount. The maximum amount of exposure is $52.3 million of which $22.6 million matures in 2007, $12.3 million matures in 2008, $8.2 million in 2020 and $9.2 million in 2023. Of this amount, as at March 31, 2005, $33.1 million is recorded as deferred gain (2004–$33.1 million).

INDEMNIFICATIONS

In certain instances when CAE sells businesses, the Company may retain certain liabilities for known exposures and provide indemnification to the buyer with respect to future claims for certain unknown liabilities existing, or arising from events occurring, prior to the sale date, including liabilities for taxes, legal matters, environmental exposures, product liability, and other obligations. The terms of the indemnifications vary in duration, from one to two years for certain types of indemnities, terms for tax indemnifications that are generally aligned to the applicable statute of limitations for the jurisdiction in which the divestiture occurred, and terms for environmental liabilities that typically do not expire. The maximum potential future payments that the Company could be required to make under these indemnifications are either contractually limited to a specified amount or unlimited. The Company believes that other than the liabilities already accrued, the maximum potential future payments that the Company could be required to make under these indemnifications are not determinable at this time, as any future payments would be dependent on the type and extent of the related claims, and all available defenses, which are not estimable. However, costs incurred to settle claims related to these indemnifications have not been material to the Company's financial position, results of operations or cash flows.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15.
INCOME TAXES

A reconciliation of income taxes at Canadian statutory rates with the reported income taxes is as follows:

(amounts in millions)	**2005**	2004	2003
Earnings before income taxes and discontinued operations	**$ (405.1)**	$ 58.9	$ 166.3
Statutory income tax rates in Canada	**31.27%**	32.78%	34.70%
Income taxes at Canadian statutory rates	**$ (126.7)**	$ 19.3	$ 57.7
Difference between Canadian statutory rates and those applicable to foreign subsidiaries	**(12.2)**	(2.9)	1.4
Manufacturing and processing allowance	**—**	(0.5)	(3.5)
Goodwill impairment	**61.7**	—	—
Losses not tax effected	**2.7**	0.2	1.0
Tax benefit of operating losses not previously recognized	**(12.2)**	(5.2)	(1.1)
Tax benefit of capital losses not previously recognized	**(11.3)**	—	—
Non taxable capital gain	**(0.1)**	(0.2)	(0.7)
Non deductible items	**4.5**	3.3	(0.4)
Prior years' tax adjustments and assessments	**(3.6)**	(3.6)	(0.9)
Impact of change in income tax rates on future income taxes	**(1.0)**	0.7	(1.7)
Non taxable research and development tax credits	**(1.5)**	(0.5)	(0.4)
Other	**(0.7)**	0.9	1.0
Total income tax (recovery) expense	**$ (100.4)**	$ 11.5	$ 52.4

Significant components of the provision for income tax expense attributable to continuing operations are as follows:

(amounts in millions)	**2005**	2004	2003
Current income tax expense	**$ 13.5**	$ 14.4	$ 36.2
Future income tax (recovery) expense	**(113.9)**	(2.9)	16.2
Total income tax (recovery) expense	**$ (100.4)**	$ 11.5	$ 52.4

The tax effects of temporary differences that gave rise to future tax liabilities and assets are as follows:

(amounts in millions)	**2005**	2004
Non-capital loss carryforwards	**$ 71.4**	$ 73.6
Capital loss carryforwards	**4.6**	17.5
Investment tax credits	**(20.9)**	(14.3)
Property, plant and equipment	**(8.7)**	(32.7)
Intangibles	**(0.5)**	(22.3)
Amounts not currently deductible	**19.1**	13.7
Deferred revenues	**12.4**	4.7
Percentage of completion versus completed contract	**(6.9)**	(45.3)
Other	**6.2**	10.5
	76.7	5.4
Valuation allowance	**(31.1)**	(43.2)
Net future income tax assets (liabilities)	**$ 45.6**	$ (37.8)

As of March 31, 2005, the Company has accumulated non-capital losses carried forward relating to operations in the United States for approximately $122.6 million (US$101.3 million). For financial reporting purposes, a net future tax income asset of $33.6 million (US$27.8 million) has been recognized in respect of these loss carry forwards.

The Company has accumulated non-capital tax losses carried forward relating to its operations in other countries of approximately $66.8 million. For financial reporting purposes, a net future income tax asset of $10.6 million has been recognized.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15. INCOME TAXES (CONT'D)

The Company has also accumulated capital losses carried forward relating to operations in the United States for approximately $11.5 million (US$9.5 million). For financial reporting purposes, no future tax income asset was recognized, as a full valuation allowance was taken.

The non-capital losses for income tax purposes expire as follows:

(amounts in millions)	UNITED STATES (US$)	OTHER COUNTRIES (CA$)
Year of expiration:		
2006	$ —	$ —
2007	31.5	—
2008	27.2	0.4
2009	6.0	0.8
2010	—	0.1
2011-2023	36.6	0.6
No expiration	—	64.9
	$ 101.3	$ 66.8

The valuation allowance relates principally to loss carryforward benefits where realization is not likely due to a history of loss carryforwards and to the uncertainty of sufficient taxable earnings in the future, together with time limitations in the tax legislation giving rise to the potential benefit. In 2005, $22.3 million (2004–$5.7 million) of the valuation allowance balance was reversed when it became more likely than not that benefits would be realized.

NOTE 16.
DEFERRED GAINS AND OTHER LONG-TERM LIABILITIES

(amounts in millions)	**2005**	2004
Deferred gains on sale and leasebacks (i)	**$ 90.7**	$ 90.5
Deferred revenue and gains	**21.1**	33.9
Long-term portion of employee benefits obligation (Note 21)	**24.9**	26.3
Government cost sharing (Note 19)	**7.6**	7.2
Minority interest (ii)	**16.9**	1.6
Other	**18.6**	11.5
	$ 179.8	$ 171.0

(i) The related amortization for the year amounts to $3.5 million (2004–$3.2 million, 2003–$2.1 million).

(ii) In fiscal 2005 CAE acquired 80% of the training centre Servicios de Instruccion de Vuelo, S.L. in Spain.

NOTE 17.
SUPPLEMENTARY CASH FLOW INFORMATION

Cash provided (used in) by non-cash working capital is as follows:

(amounts in millions)	**2005**	2004	2003
Accounts receivable	**$ 53.9**	$ (16.1)	$ 28.7
Inventories	**18.7**	(21.6)	0.6
Prepaid expenses	**0.5**	(6.3)	(6.3)
Income taxes recoverable	**28.5**	(8.8)	(23.7)
Accounts payable and accrued liabilities	**(42.3)**	(49.7)	17.9
Deposits on contracts	**26.3**	2.3	(81.9)
Decrease (increase) in non-cash working capital	**$ 85.6**	$ (100.2)	$ (64.7)
Interest paid	**$ 38.2**	$ 41.1	$ 38.1
Income taxes paid	**$ —**	$ 8.2	$ 3.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Earnings from continuing operations include a net foreign exchange gain of $5.2 million in 2005 or $0.02 per share (2004–net foreign exchange gain of $10.2 million or $0.04 per share, 2003–net foreign exchange gain of $7.6 million or $0.03 per share).

NOTE 18.
CONTINGENCIES

Through the normal course of operations, the Company is party to a number of lawsuits, claims and contingencies. Accruals are made in instances where it is probable that liabilities will be incurred and where such liabilities can be reasonably estimated. Although it is possible that liabilities may be incurred in instances for which no accruals have been made, the Company has no reason to believe that the ultimate outcome of these matters will have a material impact on its financial position.

NOTE 19.
GOVERNMENT COST SHARING

The Company has signed agreements with the Government of Canada whereby the latter shares in the cost, based on expenditures incurred by the Company, of certain R&D programs for visual systems and advanced flight simulation technology for civil applications and networked simulation for military applications. Funding in the amount of $31.2 million related to the visual R&D programs was completed in 2001. There were no royalty payments for this program in fiscal 2005 (2004-$0.4 million). Funding in the amount of $41.4 million related to the civil flight simulation program was completed in 2004. Royalty payments for this program are estimated at $3.5 million in fiscal 2005 (2004-$3.2 million). In fiscal 2003, funding of $39.0 million was approved to develop a military network simulation. Royalty payments for this program are estimated at $2.4 million in fiscal 2005 (2004–nil). The amount of funding received in fiscal 2005 was $10.8 million (2004–$8.5 million, 2003-$12.3 million). The Company provided for $12.9 million of future repayments on the civil flight simulation program and the military network simulation program in fiscal 2005. These programs are repayable in the form of royalties to March 2013 based on future sales. The maximum amount of royalties payable under the visual program is $41.4 million. The maximum payment under the civil or military simulation programs, based on future sales, is $66.0 million and $53.6 million respectively.

NOTE 20.
OPERATING LEASE COMMITMENTS

Future minimum lease payments under operating leases are as follows:

(amounts in millions)	CIVIL	MILITARY	TOTAL
Years ending March 31,			
2006	$ 46. 1	$ 34.7	$ 80.8
2007	58.5	26.3	84.8
2008	48.4	24.3	72.7
2009	36.0	23.4	59.4
2010	33.6	21.8	55.4
Thereafter	284.9	76.6	361.5
	$ 507.5	$ 207.1	$ 714.6

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 21.
EMPLOYEE FUTURE BENEFITS

The Company has two Registered funded defined benefit pension plans in Canada (one for employees and one for designated executives) that provide benefits based on length of service and final average earnings. In addition, the Company maintains a Supplemental arrangement to provide defined benefits for designated executives. This Supplemental arrangement is solely the obligation of the Company and there is no requirement to fund it. The Company, however, is obligated to pay the benefits when they become due. Once the designated executive retires from the Company, the Company is required to secure the obligation for that executive. As at March 31, 2005, the Company has issued letters of credit totaling $19.2 million to secure the obligations under this Supplemental arrangement.

Contributions reflect actuarial assumptions concerning future investment returns, salary projections and future service benefits. Plan assets are represented primarily by Canadian and foreign equities and government and corporate bonds.

On February 3, 2005 the Company sold the Marine Controls division, resulting in a curtailment loss of $0.2 million which has been included in discontinued operations.

On January 1, 2005, the Company approved some pension plan improvements to the Registered pension plans resulting in increased pension obligations of $0.9 million.

The changes in the pension obligations and in the fair value of assets and the funded status of the Registered pension plans were as follows:

(amounts in millions)	**2005**	2004
Change in pension obligations		
Pension obligation, beginning of year	**$ 139.5**	$ 133.5
Current service cost	**3.6**	3.4
Interest cost	**9.0**	8.6
Curtailment of discontinued operations	**(4.2)**	(1.5)
Employee contributions	**2.6**	2.7
Plan amendments	**0.9**	1.2
Pension benefits paid	**(8.1)**	(8.4)
Actuarial loss	**15.4**	—
Pension obligation, end of year	**158.7**	139.5
Change in fair value of plan assets		
Fair value of plan assets, beginning of year	**$ 118.9**	$ 105.6
Actual return on plan assets	**12.6**	14.4
Pension benefits paid	**(8.1)**	(8.4)
Settlement of discontinued operations	**(4.2)**	(1.3)
Plan expenses	**(0.3)**	(0.3)
Employee contributions	**2.6**	2.7
Employer contributions	**6.7**	6.2
Fair value of plan assets, end of year	**128.2**	118.9
Funded status-plan deficit	**(30.5)**	(20.6)
Unrecognized net actuarial loss	**42.4**	34.4
Unamortized past service cost	**6.1**	5.8
Amount recognized as an asset, end of year	**$ 18.0**	$ 19.6

As at March 31, 2004 and March 31, 2005, all plans had pension obligations in excess of plan assets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CAE pension plan weighted-average asset allocations by asset category are as follows:

	ALLOCATION OF PLAN ASSETS AT MEASUREMENT DATES	
ASSET CATEGORY	DECEMBER 31, 2004	DECEMBER 31, 2003
Equity securities	63%	64%
Fixed income securities	37%	36%
Total	100%	100%

There is a target allocation percentage for equity securities of 63%, which includes a mix of Canadian, U.S. and international equities, and for the fixed income securities of 37%, which must be rated BBB or higher. Individual asset classes are allowed to fluctuate slightly, and are rebalanced regularly to the target mix. Fund managers are responsible for investing the assets so as to achieve return in line with underlying market indices.

The net pension cost for Registered pension plans for the years ended March 31 included the following components:

(amounts in millions)	**2005**	2004	2003
Current service cost	**$ 3.6**	$ 3.4	$ 3.8
Plan expenses	**0.3**	0.3	0.3
Interest cost on pension obligations	**9.0**	8.5	7.6
Actual return on plan assets	**(12.6)**	(14.4)	7.3
Net actuarial loss on benefit obligation	**15.4**	—	7.3
Past service cost arising from plan amendments in the period	**0.9**	1.2	2.8
Pension cost before adjustments to recognize the long-term nature of plans	**16.6**	(1.0)	29.1
Adjustments to recognize long-term nature of plans:			
Difference between expected return and actual return on plan assets	**4.8**	7.7	(14.5)
Difference between actuarial loss recognized for the year and actual actuarial loss on benefit obligation for the year	**(14.0)**	2.2	(6.5)
Difference between amortization of past service cost for the year and actual plan amendments for the year	**(0.4)**	(0.8)	(2.6)
Total adjustment	**(9.6)**	9.1	(23.6)
Net pension cost	**7.0**	8.1	5.5
Curtailment/settlement of discontinued operations	**1.3**	0.8	—
Net pension cost including curtailment/settlement of discontinued operations	**$ 8.3**	$ 8.9	$ 5.5

The following components must be disclosed under US GAAP and are combinations of elements presented above:

(amounts in millions)	**2005**	2004	2003
Expected return on plan assets	**$ (7.8)**	$ (6.7)	$ (7.2)
Amortization of net actuarial loss	**1.4**	2.2	0.8
Amortization of past service costs	**0.5**	0.4	0.2

With respect to the Supplemental arrangement, the net pension cost for 2005 was $1.4 million (2004–$1.7 million; 2003–$1.7 million). The net pension cost for 2005 is made up of $0.8 million of current service cost (2004–$0.8 million; 2003–$0.8 million), $1.0 million of interest cost on obligations (2004–$0.9 million; 2003–$0.9 million), $1.0 million of actuarial loss (2004–$0.1 million; 2003–$1.7 million), an adjustment to actuarial loss of ($1.0) million (2004–($0.1) million; 2003–($1.7 million) and ($0.4) million (2004–nil; 2003–nil) of settlement and other loss.

The pension obligations relative to the Supplemental arrangement was $16.1 million as at March 31,2005 (2004–$14.6 million; 2003 – $13.7 million). In fiscal year ending March 2005, the current service cost was $0.8 million, the interest cost on pension obligations was $0.9 million, the benefits paid were $0.8 million, the actuarial loss was $1.0 million, the special/contractual termination benefits was $0.2 million and the settlement of discontinued operations was $0.6 million. In fiscal year ending March 2004, the current service cost was $0.8 million, the interest cost on pension obligations was $0.9 million, the benefits paid were $0.9 million and the actuarial loss was $0.1 million. The total amount recognized as a liability, as at March 31, 2005, was $16.0 million (2004–$15.4 million). The difference between this obligation recognized by the Company and the pension obligation is the amount of unamortized actuarial (loss) gains of $(0.1) million (2004-$0.8 million).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 21. EMPLOYEE FUTURE BENEFITS (CONT'D)

Expected contributions and benefit payments:

In the fiscal year ending March 2005, CAE contributed $6.7 million (2004–$6.2 million) to its Registered pension plans and an additional $0.8 million (2004-0.9$ million) to the Supplemental arrangement.

In the next fiscal year, CAE expects to contribute $7.4 million to its Registered pension plans and an additional $0.8 million to the Supplemental arrangement.

The benefit payments expected to be paid in future years are as follows:

(amounts in millions)	REGISTERED PLANS	SUPPLEMENTAL ARRANGEMENT
Year:		
2006	$ 8.3	$ 0.9
2007	8.9	0.9
2008	9.5	0.9
2009	10.3	0.9
2010	11.1	1.0
2011-2015	70.0	6.5

Significant assumptions (weighted average):

	2005	2004
Pension obligations as of March 31:		
Discount rate	**6.0%**	6.5%
Compensation rate increases (i)	**4.5%**	4.25%
Net pension cost:		
Expected return on plan assets	**6.5%**	6.5%
Discount rate	**6.5%**	6.5%
Compensation rate increases (i)	**4.5%**	4.25%

(i) For the executive plans, the compensation rate increase is 3.25%.

For the purpose of calculating the expected return on plan assets, historical and expected future returns were considered separately for each class of asset based on the asset allocation.

The Company measures its benefit obligations and fair value of plan assets for accounting purposes as at December 31 of each year. The most recent actuarial valuation of the pension plans for funding purposes was as of March 28, 2002 for the employee Registered plan, and December 31, 2001 for the designated executive Registered plan. The next required valuation will be as of December 31, 2004 for both Registered plans.

The total net amount recognized for the Registered plans and the Supplemental arrangement is an asset of $2.0 million (2004–asset of $4.2 million) and is included in the Company's Consolidated Balance Sheet in other assets for $18.0 million (2004 – $19.6 million) and in deferred gains and other long-term liabilities for $16.0 million (2004–$15.4 million).

NOTE 22.
CURRENCY TRANSLATION ADJUSTMENT

The net change in the currency translation adjustment account is as follows:

(amounts in millions)	**2005**	2004
Balance at beginning of year	**$ (12.1)**	$ 28.5
Effect of changes in exchange rates during the year:		
On net investment in self-sustaining subsidiaries (net of taxes)	**(59.4)**	(62.2)
On certain long-term debt denominated in foreign currencies designated as a hedge of net investments in self-sustaining foreign subsidiaries	**12.2**	21.6
Portion included in income as a result of reductions in net investments in self-sustaining foreign operations	**(7.0)**	—
Balance at end of year	**$ (66.3)**	$ (12.1)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 23.
INVESTMENT TAX CREDITS

In the first quarter of fiscal 2005, an amount of $11.4 million, net of tax of $4.7 million of ITC was recognized in net earnings and $0.4 million was recorded against deferred development costs for expenses. These amounts related to the results of examinations by the taxation authorities for fiscal years 2000 to 2002, and to Management's reassessment of its best estimate of potential tax liabilities for the subsequent fiscal years. On a per segment and discontinued operations basis gross ITC were recognized as follows: Civil $9.8 million, Military $4.4 million and discontinued operations $1.9 million.

The following table provides the earnings from operations before interest and income taxes amounts by segment and discontinued operations, including and excluding ITC provisions reversed based on recent tax examinations:

(amounts in millions)	INCLUDING ITC PROVISIONS REVERSED	EXCLUDING ITC PROVISIONS REVERSED
Civil	$ 47.6	$ 37.8
Military	47.2	42.8
Discontinued operations	135.0	133.1
	$ 229.8	$ 213.7

NOTE 24.
RESTRUCTURING COSTS

In fiscal 2004 and fiscal 2005, the Company proceeded with three measures intended to restore the Company's profitability, cash flow and return on investment.

The first two initiatives were announced at the end of the fourth quarter of fiscal 2004 and carried-out during the first and second quarters of fiscal 2005.

The first initiative resulted in a restructuring charge of $8.2 million that was recorded in the results of the fourth quarter of fiscal 2004. An amount of $0.7 million related to the sale of its Marine Controls segment has been allocated to discontinued operations. The charge included severance and other involuntary termination costs that related mainly to the workforce reduction of approximately 250 employees in the Montreal plant, following the loss of a major simulation equipment contract to a competitor. The complete amount was disbursed during the first and second quarters of fiscal 2005.

The second initiative was designed to integrate a number of functions in some European training centres. A restructuring charge of $1.8 million, mainly for severances and other costs, was also recorded in the results of the fourth quarter of fiscal 2004. During fiscal 2005, an amount of $1.2 million was disbursed, leaving a provision of $0.6 million, expected to be paid by the end of the first quarter of fiscal 2006.

During the fourth quarter of 2005, following a comprehensive review of current performance and the strategic orientation of its operations, the Company announced a broad restructuring plan aimed at the elimination of existing duplications between the Civil and Military segments and the achievement of a more competitive cost structure. The plan, that includes a workforce reduction of approximately 450 employees and the closing of redundant facilities, has an important effect on the Company's operations in Montreal but also around the world, including some European and American training centres. Total amount to be incurred as a result of this measure is in the range of $55 to $65 million. A restructuring charge of $24.5 million, consisting mainly of severance and other related costs, was recorded in the results of the fourth quarter of fiscal year 2005 on a separate line of the statement of earnings. During the quarter, $13.9 million was paid, resulting in a balance of $10.6 million as at March 31, 2005, which is expected to be paid in fiscal year 2006.

RESTRUCTURING COSTS SUMMARY

(amounts in millions)	EMPLOYEE TERMINATION COSTS	OTHER COSTS	TOTAL
Costs charged to expense	$ 8.7	$ 0.6	$ 9.3
Payments made	(8.2)	(0.5)	(8.7)
Balance of provision as at March 31, 2004	0.5	0.1	0.6
Costs charged to expense	20.8	3.7	24.5
Payments made	(12.1)	(1.8)	(13.9)
Balance of provision as at March 31, 2005	$ 9.2	$ 2.0	$ 11.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 25.
VARIABLE INTEREST ENTITIES

The Company has entered into sale and leaseback arrangements with special purpose entities ("SPEs"). These arrangements relate to simulators used in the Company's training centres for the military and civil aviation. These leases expire in different periods up to 2023, with the exception of one in 2037. Typically, the Company has the option to purchase the equipment at a specific time during the lease terms at a specific purchase price. Some leases include renewal options at the end of the term. In some cases, the Company has provided guarantees for the residual value of the equipment at the expiry date of the leases or at the date the Company exercises its purchase option. These SPEs are financed by secured long-term debt and third-party equity investors who in certain cases benefit from tax incentives. The equipment serves as collateral for the SPEs' long-term debt.

The Company's variable interests in these SPEs are solely through residual value guarantees and fixed purchase price options, except for one case where it is in the form of equity and subordinated loan. In one case, the Company also provides administrative services to the SPE in return for a market fee.

Some of these SPEs are variable interest entities (VIEs) and the Company is the primary beneficiary for only one of them with assets and liabilities amounting to $44.1 million and $38.9 million respectively as at March 31, 2005. Accordingly, this entity was consolidated effective January 1, 2005 and the retroactive application, without restatement, of AcG-15 resulted in a $3.3 million increase in retained earnings as at March 31, 2005. For all of the other SPEs that are VIEs, the Company is not the primary beneficiary and consolidation is not appropriate under AcG-15. As at March 31, 2005, the Company's maximum potential exposure relating to these non-consolidated SPEs was $49.4 million. The non-consolidated SPEs' assets amounted to $183.8 million as at March 31, 2005.

The liabilities recognized as a result of consolidating this VIE do not represent additional claims on the Company's general assets; rather, they represent claims against the specific assets of the consolidated VIE. Conversely, assets recognized as a result of consolidating this VIE do not represent additional assets that could be used to satisfy claims against the Company's general assets. Additionally, the consolidation of this VIE did not result in any change in the underlying tax, legal or credit exposure of the Company.

NOTE 26.
OPERATING SEGMENTS AND GEOGRAPHIC INFORMATION

The Company's significant operating segments include:

(i) Civil Simulation and Training ("Civil") –a world-leading supplier of civil flight simulators and visual systems, and a provider of business and civil aviation training.

(ii) Military Simulation and Training ("Military") –a premier supplier of military flight and land-based simulators, visual and training systems.

Each operating segment is led by a senior executive and offers different products and uses different technology and marketing strategies. The Company evaluates performance based on earnings before interest, income taxes and discontinued operations and uses capital employed to assess resources allocated to each segment. Capital employed includes accounts receivable, inventories, prepaid expenses, property, plant and equipment, goodwill, intangible assets and other assets less accounts payable and accrued liabilities, deposits on contracts and deferred gains and other long-term liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Financial information on the Company's operating segments is shown in the following table:

OPERATING SEGMENTS

(amounts in millions)	**2005**	2004	2003
Capital employed			
Civil	**$ 621.5**	$1,030.1	$1,143.2
Military	**193.5**	303.6	251.9
Other	**15.3**	(21.5)	(35.9)
Total capital employed	**$ 830.3**	$1,312.2	$1,359.2
Cash and cash equivalents	**57.1**	54.7	13.5
Restricted cash	**0.9**	7.0	14.4
Short-term investments	**—**	—	2.5
Income taxes recoverable	**58.5**	52.0	25.7
Accounts payable and accrued liabilities	**312.8**	322.0	376.5
Deposits on contracts	**93.5**	69.3	68.5
Future income taxes— short-term	**2.5**	1.8	(13)
Future income taxes— long-term	**101.0**	89.0	85.7
Deferred gains and other long-term liabilities	**179.8**	171.0	139.6
Assets held for sale	**63.3**	229.7	272.2
Total assets	**$1,699.7**	$2,308.7	$2,356.5
Total assets by segment			
Civil	**$ 929.7**	$1,315.6	$1,460.6
Military	**418.5**	509.6	449.1
Assets held for sale	**63.3**	229.7	272.2
Other	**288.2**	253.8	174.6
	$1,699.7	$2,308.7	$2,356.5
Segmented revenues			
Civil	**$ 523.0**	$ 465.0	$ 518.1
Military	**467.6**	477.5	463.7
	$ 990.6	$ 942.5	$ 981.8
Intersegment revenues			
Civil	**$ 2.8**	$ 3.2	$ 0.9
Military	**1.6**	0.9	4.1
	$ 4.4	$ 4.1	$ 5.0
External revenues			
Civil	**$ 520.2**	$ 461.8	$ 517.2
Military	**466.0**	476.6	459.6
	$ 986.2	$ 938.4	$ 976.8
Amortization of property, plant and equipment			
Civil	**$ 41.8**	$ 37.7	$ 37.2
Military	**12.1**	12.7	11.0
Other	**1.2**	0.9	0.3
	$ 55.1	$ 51.3	$ 48.5
Amortization of intangible assets			
Civil	**$ 6.3**	$ 6.8	$ 7.5
Military	**0.1**	0.1	0.2
	$ 6.4	$ 6.9	$ 7.7
Amortization of other assets			
Civil	**$ 14.4**	$ 10.1	$ 5.3
Military	**4.5**	1.4	1.6
Other	**1.6**	1.7	2.0
	$ 20.5	$ 13.2	$ 8.9

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 26. OPERATING SEGMENTS AND GEOGRAPHIC INFORMATION (CONT'D)

OPERATING SEGMENTS

(amounts in millions)	**2005**	2004	2003
Capital expenditures			
Civil	**$ 111.5**	$ 81.7	$ 212.1
Military	**6.5**	5.1	12.1
	$ 118.0	$ 86.8	$ 224.2
Additions and adjustments to goodwill			
Civil	**$ 1.1**	$ (12.5)	$ (4.8)
Military	**(4.5)**	(7.4)	(7.1)
Impairment	**(205.2)**	—	—
	$ (208.6)	$ (19.9)	$ (11.9)
Additions and adjustments to intangible assets			
Civil	**$ 3.8**	$ (5.9)	$ 6.2
Military	**0.7**	(0.2)	(0.2)
Impairment	**(107.1)**	—	—
	$ (102.6)	$ (6.1)	$ 6.0

GEOGRAPHIC INFORMATION

(amounts in millions)	**2005**	2004	2003
Revenue from external customers based on their location			
Canada	**$ 81.4**	$ 109.8	$ 75.3
United States	**413.5**	302.2	292.0
United Kingdom	**85.3**	86.5	109.6
Germany	**110.2**	129.8	113.7
Other European countries	**137.9**	153.2	128.0
Other countries	**157.9**	156.9	258.2
	$ 986.2	$ 938.4	$ 976.8
Property, plant and equipment, goodwill and intangible assets			
Canada	**$ 195.7**	$ 224.1	$ 226.6
United States	**277.4**	430.6	563.1
European	**405.1**	500.9	466.4
Other countries	**26.3**	54.3	83.1
	$ 904.5	$1,209.9	$1,339.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 27.
DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP), which differ in certain respects from those principles that the Company would have followed had its financial statements been prepared in accordance with accounting principles generally accepted in the United States (US GAAP).

Additional disclosures required under US GAAP have been provided in the accompanying financial statements and notes.

The reconciliation of net earnings in accordance with Canadian GAAP to conform to US GAAP is as follows:

Years ended March 31 (amounts in millions, except per share amounts)	NOTE	**2005**	2004	2003
Net (loss) earnings in accordance with Canadian GAAP		**$ (199.9)**	$ 64.0	$ 117.2
Discontinued operations in accordance with Canadian GAAP		**104.8**	16.6	3.3
(Loss) Earnings from continuing operations for the year in accordance with Canadian GAAP		**$ (304.7)**	$ 47.4	$ 113.9
Deferred development costs, net of tax recovery of $2.2 (2004 - recovery-$1.2), (2003 - recovery — $2.7)	A	**9.5**	(2.5)	(5.8)
Deferred pre-operating costs, net of tax expense of $3.6 (2004 - $0.4), (2003 - recovery-$1.2)	B	**8.1**	(0.1)	(2.6)
Derivative instruments, net of tax recovery of $0.8 (2004 -$4.0) (2003 -$7.2)	C	**(4.0)**	(8.5)	(15.5)
Variable interest entities net of tax expense of $0.5 (2004 - $2.5) , (2003 - $0.9)	G	**0.6**	5.3	2.0
Foreign exchange gain on purchase of subsidiary in 2002, net of tax recovery of $3.7 million	E	**(7.9)**	—	—
(Loss) Earnings from continuing operations before cumulative effect of accounting change — US GAAP		**$ (298.4)**	$ 41.6	$ 92.0
Discontinued operations in accordance to US GAAP	A,B,C,H	**98.9**	15.9	3.9
Net (loss) earnings before cumulative effect of accounting change — US GAAP		**$ (199.5)**	$ 57.5	$ 95.9
Cumulative effect on prior years of accounting change	D,G	**(0.6)**	—	—
Net (loss) earnings for the year in accordance with US GAAP		**$ (200.1)**	$ 57.5	$ 95.9
Basic and diluted (loss) earnings per share from continuing operations in accordance with US GAAP		**$ (1.21)**	$ 0.18	$ 0.42
Basic and diluted results per share from discontinued operations in accordance with US GAAP		**$ 0.40**	$ 0.07	$ 0.02
Basic and diluted net (loss) earnings per share before cumulative effect of accounting change in accordance with US GAAP		**$ (0.81)**	$ 0.25	$ 0.44
Basic and diluted net (loss) earnings per share in accordance with US GAAP		**$ (0.81)**	$ 0.25	$ 0.44
Dividends per common share		**$ 0.10**	$ 0.12	$ 0.12
Weighted average number of common shares outstanding		**247.1**	233.2	219 .4

(amounts in millions)		**2005**	2004	2003
Comprehensive income				
Net (loss) earnings in accordance with US GAAP		**$ (200.1)**	$ 57.5	$ 95.9
Accumulated minimum pension liability, net of taxes of $1.7 (2004- $4.2) (2003 - $10.8)	J	**(4.2)**	9.1	(23.5)
Foreign currency translation adjustments		**(41.3)**	(40.1)	36.8
Comprehensive income		**$ (245.6)**	$ 26.5	$ 109.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 27. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (CONT'D)

ACCUMULATED OTHER COMPREHENSIVE LOSS IN ACCORDANCE WITH US GAAP

(amounts in millions)	FOREIGN CURRENCY TRANSLATION ADJUSTMENTS	CHANGE IN MINIMUM PENSION LIABILITY	TOTAL
Opening balance — 2003	$ (15.1)	$ —	$ (15.1)
Changes for the year — 2003	36.8	(23.5)	13.3
Closing balance — 2003	21.7	(23.5)	(1.8)
Changes for the year — 2004	(40.1)	9.1	(31.0)
Closing balance — 2004	(18.4)	(14.4)	(32.8)
Changes for the year — 2004	(41.3)	(4.2)	(45.5)
Ending balance — 2005	$ (59.7)	$ (18.6)	$ (78.3)

The cumulative effect of these adjustments on the shareholders' equity of the Company is as follows:

(amounts in millions)	NOTE	**2005**	2004
Shareholders' equity in accordance with Canadian GAAP		**$ 651.6**	$ 918.8
Deferred development costs, net of tax expense of $15.6 (2004 — $13.4)	A	**(18.4)**	(27.9)
Deferred pre-operating costs, net of tax expense of $5.2 (2004 — $8.8)	B	**(10.8)**	(18.9)
Derivative instruments, net of tax expense of $10.3 (2004 — $9.8)	C	**(22.5)**	(21.0)
Foreign currency translation adjustments	H	**—**	(6.6)
Variable interest entities net of tax recovery of nil (2004 — $3.0)	I	**—**	6.0
Foreign exchange gain on purchase of subsidiary, net of tax recovery of nil (2004 - $3.7)	E	**—**	7.9
Minimum pension liability, net of tax expense of $8.3 (2004 - $6.6)	J	**(18.6)**	(14.4)
Shareholders' equity in accordance with US GAAP		**$ 581.3**	$ 843.9

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The balance sheets in accordance with US GAAP as at March 31, 2005 and March 31, 2004 are as follows:

(amounts in millions)	NOTES	MARCH 31, 2005 CANADIAN GAAP	MARCH 31, 2005 US GAAP	MARCH 31,2005 CANADIAN GAAP	MARCH 31,2005 US GAAP
Assets					
Cash and cash equivalents		**$ 57.1**	**$ 57.1**	$ 54.7	$ 54.7
Accounts receivable		**255.7**	**255.7**	316.5	316.5
Derivative instruments	C	**—**	**9.1**		1.4
Inventories		**101.0**	**101.0**	147.7	147.7
Prepaid expenses		**17.8**	**17.8**	19.6	16.2
Income taxes recoverable		**58.5**	**58.5**	52.0	52.0
Future income taxes		**2.5**	**2.5**	1.8	1.8
Current assets held for sale		**5.8**	**3.4**	89.8	87.7
		$ 498.4	**$ 505.1**	$ 682.1	$ 678.0
Restricted cash		**0.9**	**0.9**	7.0	7.0
Property, plant and equipment, net		**792.2**	**792.2**	780.0	858.9
Future income taxes	A,B,C,E,G,J	**101.0**	**140.9**	89.0	120.7
Intangible assets	J	**20.2**	**26.3**	129.2	135.0
Goodwill		**92.1**	**92.1**	300.7	312.3
Other assets	A,B	**137.4**	**90.5**	180.8	114.2
Long-term assets held for sale		**57.5**	**56.9**	139.9	140.0
		$1,699.7	**$ 1,704.9**	$2,308.7	$ 2,366.1
Liabilities and shareholders' equity					
Current liabilities					
Accounts payable and accrued liabilities		**$ 312.8**	**$ 312.8**	$ 322.0	$ 321.3
Deposits on contracts		**93.5**	**93.5**	69.3	69.3
Derivative instruments	C	**—**	**42.3**	—	31.3
Long-term debt due within one year		**35.3**	**35.3**	8.8	21.1
Future income taxes		**19.6**	**19.6**	51.1	51.1
Current liabilities related to assets held for sale	J	**7.8**	**8.0**	54.5	55.8
		$ 469.0	**$ 511.5**	$ 505.7	$ 549.9
Long-term debt		**307.6**	**307.6**	575.5	669.1
Deferred gains and other long-term liabilities	J	**179.8**	**212.8**	171.0	165.5
Future income taxes		**38.3**	**38.3**	77.5	77.5
Long-term liabilities related to assets held for sale		**53.4**	**53.4**	60.2	60.2
		$1,048.1	**$ 1,123.6**	$1,389.9	$ 1,522.2
Shareholders' equity					
Capital stock	F,K	**$ 373.8**	**$ 618.0**	$ 367.5	$ 611.7
Contributed surplus		**3.3**	**3.3**	1.3	1.3
Retained earnings	A,B,C,D,E,F,G,H,K	**340.8**	**38.3**	562.1	263.7
Currency translation adjustment	H,I	**(66.3)**	**—**	(12.1)	—
Accumulated other comprehensive loss	H,J	**—**	**(78.3)**	—	(32.8)
		$ 651.6	**$ 581.3**	$ 918.8	$ 843.9
		$1,699.7	**$ 1,704.9**	$2,308.7	$ 2,366.1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 27. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (CONT'D)

CONSOLIDATED STATEMENT OF CASH FLOWS

Under US GAAP reporting, separate subtotals within operating, financing and investment activities would not be presented.

The reconciliation of cash flows under Canadian GAAP to conform to US GAAP is as follows:

Years ended March 31 (amounts in millions)	NOTE	**2005**	2004	2003
Cash flows from operating activities in accordance with Canadian GAAP		**$ 207.6**	$ 5.7	$ 154.9
Deferred development costs	A	**(9.9)**	(12.7)	(13.3)
Deferred pre-operating costs	B	**(1.7)**	(6.6)	(10.3)
Variable interest entities	G	**5.6**	13.7	10.9
Deferred pre-operating costs related to discontinued operations		**(0.4)**	(3.8)	2.7
Cash flows from operating activities in accordance with US GAAP		**$ 201.2**	$ (3.7)	$ 144.9
Cash flows from investing activities in accordance with Canadian GAAP		**$ 131.6**	$ 24.5	$ (134.4)
Deferred development costs	A	**9.9**	12.7	13.3
Deferred pre-operating costs	B	**1.7**	6.6	10.3
Deferred pre-operating costs related to discontinued operations		**0.4**	3.8	(2.7)
Cash flows from investing activities in accordance with US GAAP		**$ 143.6**	$ 47.6	$ (113.5)
Cash flows from financing activities in accordance with Canadian GAAP		**$ (337.3)**	$ 17.8	$ (94.4)
Variable interest entities	G	**(5.6)**	(13.7)	(10.9)
Cash flows from financing activities in accordance with US GAAP		**$ (342.9)**	$ 4.1	$ (105.3)

RECONCILIATION ITEMS

A) DEFERRED DEVELOPMENT COSTS

Under US GAAP, development costs are charged to expense in the period incurred. Under Canadian GAAP, certain development costs are capitalized and amortized over their estimated useful lives if they meet the criteria for deferral. The difference between US GAAP and Canadian GAAP represents the gross development costs capitalized in the respective year, net of the reversal of amortization expense recorded for Canadian GAAP relating to amounts previously capitalized.

B) DEFERRED PRE-OPERATING COSTS

Under US GAAP, pre-operating costs are charged to expense in the period incurred. Under Canadian GAAP, the amounts are deferred and amortized over 5 years based on the expected period and pattern of benefit of the deferred expenditures. The difference between US GAAP and Canadian GAAP represents the gross pre-operating costs capitalized in the respective year, net of the reversal of amortization expense recorded for Canadian GAAP relating to amounts previously capitalized.

C) DERIVATIVE FINANCIAL INSTRUMENTS

Under Canadian GAAP, the Company recognizes the gains and losses on forward contracts entered into for hedging purposes in income concurrently with the recognition of the transactions being hedged. The interest payments relating to swap contracts are recorded in net earnings over the life of the underlying transaction on an accrual basis as an adjustment to interest income or interest expense. Under US GAAP, all derivatives (including embedded derivatives in purchase and sale contracts) are recorded on the balance sheet at fair value. Realized and unrealized gains and losses resulting from the valuation of derivatives at market value are recognized in net earnings as the gains and losses arise and not concurrently with the recognition of the transactions being hedged, as the Company does not apply the optional hedge accounting provisions of SFAS 133, 138 and 149.

D) ADJUSTMENTS FOR CHANGES IN ACCOUNTING POLICIES

Under US GAAP, the cumulative effect of certain accounting changes must be included in earnings in the year of the change. Under Canadian GAAP, the impact is reflected through retained earnings.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

E) FOREIGN EXCHANGE GAIN ON PURCHASE OF SUBSIDIARY

Under Canadian GAAP, upon the purchase of Schreiner, a foreign exchange gain was recorded in fiscal 2002 as a reduction of goodwill on the forward contract hedge of the foreign currency denominated purchase price. Under US GAAP, this gain was recorded in earnings. In fiscal 2005, Management performed a comprehensive review of current performance and strategic orientation of its business units, which led to the review of the carrying amount of certain assets such as the goodwill of Schreiner (Note 4). Accordingly, an additional impairment charge of $7.9 million (net of tax of $3.7 million) was recorded in earnings as per US GAAP.

F) REDUCTION IN STATED CAPITAL

On July 7, 1994, the Company applied a portion of its deficit as a reduction of its stated capital in the amount of $249.3 million. Under US GAAP, the reduction of stated capital would not be permitted.

G) VARIABLE INTEREST ENTITIES

The Company enters into sale and leaseback arrangements with special purposes entities (SPEs) relating to simulation equipment used in the Company's training center. Prior to the adoption of FASB Interpretation ("FIN") No. 46 "Consolidation of Variable Interest Entities", the Company was consolidating SPEs for which legal stated capital represented less than 3% of their assets. Under those rules, three SPEs were consolidated.

In January 2003, the Financial Accounting Standards Board (FASB) issued FIN 46, Consolidation of Variable Interest Entities. This interpretation clarifies how to apply Accounting Research Bulletin ("ARB No. 51") Consolidated Financial Statements to those entities defined as Variable interest entities, when equity investors are not considered to have a controlling financial interest or they have not invested enough equity to allow the entity to finance its activities without additional subordinated financial support from other parties. This interpretation requires that existing unconsolidated variable interest entities be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. An entity that holds a significant variable interest but is not the primary beneficiary is subject to specific disclosure requirements.

In December 2003, the FASB revised FIN No.46 to make certain technical corrections and address certain implementation issues that had arisen. FIN No.46R provides a new framework for identifying variable interest entities (VIEs) and determining when a company should include the assets, liabilities, non-controlling interests and results of activities of a VIE in its consolidated financial statements. The Company was required to replace FIN No. 46 provisions with FIN No. 46R provisions to all newly created post-January 31, 2003 entities as of the end of the first period ending after March 15, 2005. As a foreign private issuer, the company will apply the provisions of FIN 46R to entities created before February 1, 2003, starting April 1, 2004. The Company adopted FIN No. 46R on April 1, 2004.

Upon adoption by the Company of FIN No. 46R, the Company concluded that two out of the three SPEs that were consolidated under the old rules did not require to be consolidated anymore. The impact on CAE's net earnings of the deconsolidation is $0.6 million.

A similar accounting standard under Canadian GAAP, AcG 15–Consolidation of Variable Interest Entities, has been adopted by the Company on January 1, 2005 (Note 1). Due to a different application date between Canadian and US GAAP, the Company had to record in fiscal 2005 a decrease of $0.6 million (net of taxes of $0.5 million) in its net earnings as per US GAAP.

H) FOREIGN CURRENCY TRANSLATION ADJUSTMENT

Under US GAAP, foreign currency translation adjustment is included as a component of "Comprehensive income". Under Canadian GAAP, the concept of comprehensive income is not yet applicable for the Company, and the currency translation adjustment is included as a component of "Shareholders' equity". In fiscal 2005, the Company transferred to earnings an amount of $6.6 million, as a results of reductions in net investments in self-sustaining foreign operations. Under US GAAP the reduction in currency translation adjustment account would not be permitted.

I) COMPREHENSIVE INCOME

US GAAP requires disclosure of comprehensive income, which comprises income and other components of comprehensive income. Other comprehensive income includes items that cause changes in shareholders' equity but are not related to share capital or net earnings, which, for the Company, comprises currency translation adjustments and change in minimum pension liability. Under Canadian GAAP, the requirement to report comprehensive income will be applicable for the Company only in fiscal 2007 with the adoption of section 1530 *"Comprehensive Income".*

J) MINIMUM PENSION LIABILITY

Under US GAAP, if the accumulated benefit obligation exceeds the market value of plan assets, a minimum pension liability for the excess is recognized to the extent that the liability recorded in the balance sheet is less than the minimum liability. Any portion of the additional liability that relates to unrecognized past service costs is recognized as an intangible asset while the remainder is charged to comprehensive income. The concept of additional minimum liability does not currently exist under Canadian GAAP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 27. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (CONT'D)

K) SHARE ISSUE COSTS

Under Canadian GAAP, costs related to share issuance can be presented in retained earnings, net of taxes. Under US GAAP, these costs were recorded as a reduction of capital stock.

ACCOUNTING CHANGES

ACCOUNTING FOR STOCK-BASED COMPENSATION

Prior to April 1, 2003, CAE had elected to measure stock-based compensation using the intrinsic value base method of accounting. In that instance, however, under SFAS 123, the Company is required to make pro forma disclosures of net earnings, basic earnings per share and diluted earnings per share using the fair value method of accounting for stock-based compensation granted prior to April 1, 2003.

Pro forma net earnings and pro forma basic and diluted net earnings per share are presented below:

(amounts in millions of Canadian dollars, except per share amounts)	**2005**	2004	2003
Net (loss) earnings, as reported per US GAAP	**$ (200.1)**	$ 57.5	$ 95.9
Compensation expense recorded	**2.0**	1.3	—
Net (loss) earnings before the effect of Stock-based compensation	**(198.1)**	58.8	95.9
Pro forma impact	**(6.4)**	(6.0)	(5.6)
Pro forma net (loss) earnings	**(204.5)**	52.8	90.3
Pro forma basic and diluted net (loss) earnings per share	**(0.83)**	0.23	0.41

DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

In fiscal 2004, the Company adopted SFAS 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities.* SFAS 149 amends and clarifies the financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS 133. SFAS 149 had no impact on CAE's financial position.

PENSION AND OTHER RETIREMENT BENEFITS

During 2003, the Financial Accounting Standards Board revised SFAS 132, *Employers' Disclosures about Pensions and Other Postretirement Benefits.* The revised SFAS 132 retains and revises the disclosure requirements contained in the original SFAS 132. It also requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other postretirement benefit plans.

CAE adopted revised SFAS 132, in fiscal 2004.

RECENT ACCOUNTING DEVELOPMENTS

EXCHANGES FOR NON-MONETARY ASSETS

During 2004, the Financial Accounting Standards Board issued SFAS 153, *Exchanges for Non-Monetary Assets.* SFAS 153 amends APB Opinion No.29, *Accounting for Non-Monetary Transactions,* and requires that all non-monetary exchanges be accounted for at fair value except for the exchanges of non-monetary assets that do not have commercial substance. The Company still evaluating the impact of this new standard on its financial statements, and is required to apply it to all non-monetary asset exchanges occurring in periods beginning after July 1, 2005.

STOCK-BASED COMPENSATION

In December 2004, the FASB has issued SFAS 123 (revised). This standard amends SFAS 123 *Accounting for Stock-Based Compensation.* The principal amendments require companies to recognize the costs of providing stock options to employees based on the fair value of the options at the grant date. The obligations to pay cash to employees based on the company's share price must be recorded at fair value using an option pricing model. The Company still evaluating the impact of this new standard on its financial statements, and is required to apply this standard for periods beginning after June 15, 2005.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ADDITIONAL DISCLOSURES

Additional disclosures required under US GAAP are as follows:

I) STATEMENTS OF EARNINGS

For the years ended March 31 (amounts in millions)	**2005**		2004		2003	
	CANADIAN GAAP	**US GAAP**	CANADIAN GAAP	US GAAP	CANADIAN GAAP	US GAAP
Revenues from sales of simulators	**$ 456.4**	**$ 453.5**	$ 456.1	$ 434.3	$ 530.6	$ 516.0
Revenues from sales of services	**$ 529.8**	**$ 529.9**	$ 482.3	$ 482.3	$ 446.2	$ 446.2
Cost of sales from simulators	**$ 280.9**	**$ 281.7**	$ 282.6	$ 281.6	$ 231.4	$ 231.4
Cost of sales from services	**$ 317.8**	**$ 302.6**	$ 277.0	$ 274.0	$ 239.5	$ 246.5
Research and development expenses	**$ 93.5**	**$ 100.8**	$ 81.0	$ 84.6	$ 108.3	$ 116.8
Rental expenses	**$ 94.0**	**$ 94.0**	$ 91.9	$ 79.0	$ 87.5	$ 73.2
Selling, general and administrative expenses	**$ 105.2**	**$ 105.2**	$ 115.3	$ 115.3	$ 115.7	$ 115.7
Impairment charges	**$ 443.3**	**$ 440.4**	$ —	$ —	$ —	$ —
Interest expense	**$ 32.1**	**$ 33.9**	$ 22.4	$ 22.2	$ 28.1	$ 44.6

II) BALANCE SHEET

Accounts payable and accrued liabilities on a Canadian GAAP basis are presented below:

As at March 31 (amounts in millions)	**2005**	2004
Accounts payable trade	**$ 93.0**	$ 91.0
Contract liabilities	**90.1**	101.9
Income tax payable	**7.7**	23.8
Other accrued liabilities	**122.0**	105.3
Accounts payable and accrued liabilities	**$ 312.8**	$ 322.0

Accounts receivable from government amounted to $52.4 million as of March 31, 2005 (2004–$33.9 million).

III) INCOME TAXES

The components of earnings from continuing operations and income taxes on a Canadian GAAP basis are as follows:

For the years ended March 31 (amounts in millions)	**2005**	2004	2003
Earnings before income taxes and other items			
Canada	**$ (87.0)**	$ (13.8)	$ 96.4
Other countries	**(318.1)**	72.7	69.9
	$ (405.1)	$ 58.9	$ 166.3
Current income taxes			
Canada	**$ (1.8)**	$ 1.8	$ 37.8
Other countries	**15.3**	12.6	(1.6)
	$ 13.5	$ 14.4	$ 36.2
Future income taxes			
Canada	**$ (25.8)**	$ (6.9)	$ (1.4)
Other countries	**(88.1)**	4.0	17.6
	$ (113.9)	$ (2.9)	$ 16.2
Income tax provision	**$ (100.4)**	$ 11.5	$ 52.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 27. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (CONT'D)

VI) PRODUCT WARRANTY COSTS

The Company has warranty obligations in connection to the sale of its civil and military simulators. The original warranty period is usually for a two-year period. The cost incurred to provide for these warranty obligations are estimated and recorded as an accrued liability at the time revenue is recognized. The Company estimates its warranty cost for a given product based on past experience. The change in the Company's accrued warranty liability as at March 31, are as follows:

(amounts in millions)	**2005**	2004
Accrued warranty liability at beginning of year	**$ 6.6**	$ 10.7
Warranty settlements during the year	**(5.5)**	(7.5)
Warranty provisions	**3.9**	3.0
Adjustments for changes in estimates	**0.3**	0.4
Accrued warranty obligations at the end of the year	**$ 5.3**	$ 6.6

V) PENSION

Obligations and funded status:

The accumulated benefit obligation (ABO) for all defined benefit pension plans was $158.5 million for March 31, 2005 and $139.8 million for March 31, 2004. At these dates, all plans had accumulated benefit obligation in excess of plan assets.

As at March 31 Before taxes (amounts in millions)	**2005**	2004	2003
Minimum Liability	**$ 30.4**	$ 20.9	$ 30.1
Balance — fiscal year end:			
Additional liability	**$ 33.2**	$ 26.8	$ 39.5
Intangible Assets	**(6.1)**	(5.8)	(5.2)
Accumulated Net Additional Liability	**$ 27.1**	$ 21.0	$ 34.3
Change in Accumulated Net Additional Liability	**$ 6.1**	$ (13.3)	$ 34.3

VI) IMPAIRMENT OF GOODWILL, TANGIBLE AND INTANGIBLE ASSETS

During the third quarter of fiscal 2005, the Company recorded an impairment charge of $443.3 million. For US GAAP purposes the impairment will be different has the company expenses development and pre-operating costs when incurred and because the carrying amount of goodwill is different for Canadian and US GAAP (Refer to E).

Accordingly, the Company recorded a $440.4 million impairment charge for US GAAP purposes, virtually all related to its Civil business, detailed as follows:

(amounts in millions)	**2005**
Goodwill	**$ 216.8**
Customer relations	**86.7**
Trades names	**20.4**
Property, plant and equipment (simulators)	**78.4**
Inventories	**33.3**
Other assets	**4.8**
	$ 440.4

NOTE 28.

COMPARATIVE FINANCIAL STATEMENTS

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation adopted in the current year.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the year ended March 31, 2005 as of May 10, 2005

For purposes of this discussion, "CAE" or the "Company" refers to CAE Inc. and its subsidiaries. This Management's Discussion and Analysis ("MD&A") for the year ended March 31, 2005, current as of May 10, 2005, focuses on the core businesses of CAE: Military Simulation and Training ("Military") and Civil Simulation and Training ("Civil").

HIGHLIGHTS OF FISCAL 2005

ORGANIZATION

- Robert E. Brown became CAE's new CEO on August 12, 2004 and on February 11, 2005, outlined a comprehensive restructuring plan aimed at restoring the Company's profitability, cash flow and return on investment.
- The restructuring plan is progressing in accordance with the initial timetable and within the estimated costs.
- As of April 1, 2005, CAE is organized in three business groups; Civil Training & Services, Military Simulation & Training and Simulation Products, and will start reporting results under this format at the end of the first quarter of fiscal 2006.

OPERATIONS

- Revenue from continuing Military and Civil businesses increased by 5% over last year, notwithstanding an appreciation of the Canadian dollar versus its U.S. counterpart.
- Earnings from continued operations for fiscal 2005 reached $0.19 per share net of impairment, restructuring and other non-recurring items.
- Net cash flow provided by continuing operating activities reached $186 million for the year.
- During the third quarter, CAE recorded a non-cash charge of $443 million ($354 million after taxes) as a result of the impairment of goodwill, intangible and tangible assets for the Civil business.
- As of March 31, 2005, the Company incurred $25 million in restructuring charges, tracking in line with the global $55 to $65 million restructuring plan.
- CAE completed the divestiture of substantially the entire Marine Controls segment to L-3 Communications ("L-3") during the fourth quarter in a transaction valued at $239 million, resulting in an after-tax gain of approximately $104 million. In accordance with the purchase agreement, L-3 will also acquire two other components of the Marine Controls segment, including the assumption of the CAE's guarantee of £23 million of project-finance related debt for the U.K. Astute Class submarine training program.

FINANCING

- Net proceeds of the Marine Controls divestiture were used to reduce debt.
- Two sale and leaseback transactions for three full-flight simulators were completed, raising $44 million. The transactions also triggered the recognition of $4 million of tax benefits related to prior years' net operating losses for tax purposes in the United States.
- CAE's Board of Directors took the decision to reduce the quarterly dividend to $0.01 per share, conserving $20 million of cash annually.

ORDERS / INVESTMENT

- With an order intake of $681 million, Military reached a new record. More than 40% of fiscal 2005 equipment orders came from U.S.-based customers.
- Military secured approximately €152 million of backlog from a contract awarded by the German Armed Forces on the new NH90 platform.
    - The €488 million program, structured as a Private Financing Initiative, will be executed through Helicopter Flight Training Services GmbH ("HFTS"), an industrial consortium consisting of CAE, Eurocopter, Rheinmetall Defence Electronics and Thales, each owning a 25 percent share.
    - The Consortium concluded the non-recourse financing of this project on April 29, 2005.
- CAE-led Landmark Training Ltd. was selected as intended preferred bidder for the £1 billion British Army's Armoured Vehicle Training Services program.
- CAE and Dassault partnered for the Dassault Falcon 7X training program.

- CAE continued deployment of its training network:
  - in Latin America: CAE signed a $40 million 10-year deal with LAN Chile S.A. airlines and acquired its training centre;
  - in Europe: CAE became easyJet's training provider;
  - in North America: CAE expanded its footprint in the U.S. with the announcement of a new training centre in Morris County, NJ; and
  - in the Middle East: Emirates-CAE Flight Training continued its expansion.
- For fiscal 2005, CAE was awarded 17 of 22 competed civil full-flight simulator orders (77% market share).

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

Founded in 1947 and headquartered in Montreal, Canada, CAE is a leading provider of simulation and modelling technologies and integrated training services for civil aviation and defence customers worldwide. CAE employs more than 5,000 people in manufacturing operations and training facilities in 17 countries on five continents. More than 90% of CAE's annual revenues are derived from worldwide exports and international activities.

Prior to the sale of its Marine Controls division ("Marine") in the fourth quarter of fiscal 2005 the Company also provided simulators and training services for sea-based activities and supplied marine automation systems for military and civil applications.

For a further description of the Company's core businesses please refer to *Business Profile and Strategy* of this MD&A.

The MD&A, which includes a review of the operations of each business segment and the financial condition of CAE, is intended to assist in the understanding and assessment of significant trends, risks and uncertainties related to the results of operations for each business segment and should be read in conjunction with the audited consolidated financial statements and accompanying notes contained on pages 44 to 86.

This MD&A contains statements from CAE management ("Management") regarding CAE's strategy, operating results and financial condition. Management is responsible for its accuracy, integrity and objectivity, and has developed, maintains and supports the necessary systems and controls to provide reasonable assurance as to the validity and completeness of the disclosures contained herein.

CAE's common shares are listed on the Toronto and New York stock exchanges under the symbols CAE and CGT respectively.

CAE's fiscal year end is March 31, and unless otherwise indicated, all references to the current year or 2005 are for the year ended March 31, 2005, and all references to last year, prior year, or a year ago are for the year ended March 31, 2004.

Except as otherwise indicated, all financial information related herein is determined in accordance with Canadian generally accepted accounting principles ("GAAP") and all dollar amounts referred to herein are in Canadian dollars.

CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION

This MD&A contains forward-looking statements with respect to CAE and the operations of each business segment based on assumptions that CAE considered reasonable at the time they were prepared and may include information concerning the Company's future financial performance, business strategy, plans, goals and objectives. These forward-looking statements, by their nature, necessarily involve risks and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking statements. Statements preceded by the word "believe", "expect", "anticipate", "intend", "continue", "estimate", "may", "will", "should" and similar expressions are forward-looking statements. CAE cautions the reader that the assumptions regarding future events, many of which are beyond the control of CAE, may affect the extent to which a particular projection materializes and/or could ultimately prove to be incorrect. Factors that could cause actual results or events to differ materially from current expectations are discussed herein. (Refer to *Business Risks and Uncertainties* of this MD&A for additional information.) The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise. In particular, forward-looking statements do not reflect the potential impact of any merger, acquisition or other business combinations or divestitures that may be announced or completed after such statements are made.

NON-GAAP FINANCIAL MEASURES

This MD&A provides comments on non-GAAP financial measures. Readers should be cautioned that this information should not be confused with or used as an alternative for performance measures determined in accordance with GAAP. CAE believes that these measures provide useful supplemental information to GAAP financial measures. However, these non-GAAP financial measures have no standardized meaning prescribed by GAAP and therefore are unlikely to be comparable to similar measures presented by other companies.

EBIT

EBIT is a financial term used to report a company's earnings as they would be without specific deductions including non-operating expenses (such as interest, taxes and other non-core expenses).

CAE considers EBIT to be useful supplemental information since by eliminating the effects of some financing and accounting decisions, performance can be analyzed between different periods, different companies and different industries with dissimilar capital structure.

FOREIGN EXCHANGE

The Company's reporting currency is the Canadian dollar and assets, liabilities and transactions measured in foreign currencies need to be translated to Canadian dollars at various exchange rates as required by GAAP. For the purposes of this MD&A, foreign exchange (current financial information restated at the rates in use for the same period a year ago) is presented on a consistent basis from period to period. CAE considers foreign exchange exclusion to be useful supplemental information as it provides an indication of performance comparable to a year ago excluding the impact of currency fluctuation, which can significantly affect the Company's operations and financial results.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The year-end exchange rates used to translate assets and liabilities were as follows as at March 31:

	2005	2004	(DECREASE)
U.S. dollar (USD or US$)	**1.2096**	1.3105	(8%)
Euro (€)	**1.5689**	1.6109	(3%)
British pound (£ or GBP)	**2.2848**	2.4116	(5%)

The average exchange rates used to translate revenues and expenses were as follows for the fiscal years ended March 31:

	2005	2004	INCREASE/ (DECREASE)
U.S. dollar (USD or US$)	**1.2789**	1.3539	(6%)
Euro (€)	**1.6064**	1.5893	1%
British pound (£ or GBP)	**2.3573**	2.2903	3%

FREE CASH FLOW

Free cash flow is defined by Management as net cash flows provided by continuing operating activities less capital expenditures and dividends paid, plus proceeds from sales and leaseback of simulators. CAE considers free cash flow to be an indicator of the financial strength and liquidity of its business as it shows how much cash is available to repay debt and to meet its ongoing obligations.

NET DEBT

Net debt (total debt including amounts due within one year less cash and cash equivalents) is presented on a consistent basis from period to period. CAE considers net debt to be an indicator of the Company's overall financial position.

NON-RECURRING ITEMS

Non-recurring items are items identified by their nature as outside of the normal course of business because they are infrequent and/or unusual. Management considers that highlighting non-recurring items and providing operating results excluding these items is useful supplemental information that allows for analysis of CAE's underlying operating performance.

BUSINESS PROFILE AND STRATEGY

CAE provides a wide range of simulation and training products and services including full-flight simulators ("FFS"), full-mission simulators, visual systems, training devices and systems, flight training centres, and support services. The Company operates in two core markets: Civil and Military.

CAE's Civil business is the world leader in the design and manufacture of civil flight simulators and visual systems used to train airline and business jet pilots. In addition, CAE is the second largest independent civil aviation training provider, with a global network of 22 training centres equipped with 105 FFS.

CAE's Military business is also a global leader in the design of advanced military training systems for air, land and sea applications, having supplied the defence forces of more than 30 nations with military training systems and services. In addition to its comprehensive training services, the Company offers a range of simulation equipment and modelling and simulation software. CAE has designed one of the widest ranges of military helicopter simulators in the world and more training systems for the C-130 Hercules than any other company.

Over the past five years, the Company transformed itself, evolving from a supplier of equipment to a provider of integrated training solutions. CAE's strategy going forward revolves around taking the necessary steps to restore shareholder value.

Following Robert E. Brown's arrival as Chief Executive Officer in August 2004, an in-depth strategic review of CAE's markets, customers and other stakeholders as well as the Company's internal resources and capabilities was conducted. As a result of this review, the Company has reconfirmed its strategic direction. It adopted a plan intended to protect its technological leadership while at the same time fostering synergies between its various operating units, and implementing sound business practices. The plan maintains the existing Civil and Military Groups, and adds a third: Simulation Products. The reorganization, which became effective April 1, 2005, is expected to result in significant savings to the Company and to position it well to face new market realities.

The major priorities of the newly formed Civil Training & Services ("CT&S") Group are to increase revenue per simulator in the Company's global network of training centres, and to deliver the most cost-effective and competitive training service in the marketplace. To this end, the CT&S Group is expected to consolidate training centres where duplication exists, and to reallocate a number of simulators to maximize yield.

The Military Simulation & Training ("MS&T") Group's main goals are to service the defence market with technological excellence in modelling and simulation; to increase the Company's market share of the military training market, and to explore opportunities in non-traditional areas of the defence market, including such areas as analysis and planning.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The newly formed Simulation Products Group consolidates all manufacturing activities and includes engineering, program management, global procurement, and the marketing and sales of Civil equipment. Its immediate focus is to substantially reduce the costs associated with manufacturing simulation equipment intended both for sale to third parties as well as for installation in the Company's own global network of training centres.

Fiscal year 2006 will be a transitional year for CAE while the Company addresses its business processes and cost structure, with the goal of ending the year with a restructured and solid earnings base.

CAE's strategy is to leverage its extensive experience in modelling and simulation to expand both vertically into other products and services within the aerospace and defence industry, as well as horizontally to pursue opportunities presented by emerging markets such as homeland defence and urban simulation. In order to be able to respond to growth opportunities, CAE must continue to invest in new and innovative technologies.

CONSOLIDATED RESULTS

STATEMENT OF EARNINGS

SUMMARY OF CONSOLIDATED RESULTS

(amounts in millions, except per share amounts)	**2005**	2004	2003
Revenue	**$ 986.2**	$ 938.4	$ 976.8
EBIT	**(373.0)**	81.3	194.4
Interest	**32.1**	22.4	28.1
Income taxes	**(100.4)**	11.5	52.4
Earnings (loss)			
Continuing operations	**(304.7)**	47.4	113.9
Discontinuing operations	**104.8**	16.6	3.3
Net (loss) earnings	**(199.9)**	64.0	117.2
EPS from continued operations	**(1.23)**	0.20	0.52
Basic EPS	**(0.81)**	0.27	0.53

CONSOLIDATED REVENUE FROM CONTINUING OPERATIONS

For the twelve-month period ended March 31, 2005, consolidated revenue from continuing operations reached $986.2 million, representing an increase of $47.8 million, or 5% over the $938.4 million reported for the previous year. This net increase in consolidated revenue is due to a $58.4 million, or 13% increase in Civil revenues, partially offset by a $10.6 million, or 2% decreased contribution from Military.

Consolidated revenue from continuing operations, excluding the impact of foreign currency fluctuations (mainly the decrease of the USD), would have been slightly over $1 billion, an increase of 8% over last year.

Further analysis on each segment is provided in *Segmented Results.*

CONSOLIDATED EBIT FROM CONTINUING OPERATIONS

Consolidated EBIT amounted to a loss of $373.0 million, compared to earnings of $81.3 million last year. The loss is mainly due to non-recurring items, such as impairment and restructuring charges together with other unusual items that are further discussed in a separate section hereunder. Excluding the impact of these non-recurring items, consolidated EBIT would have amounted to $88.3 million, compared to $90.6 million a year ago on the same basis. On a segmented basis, Civil's EBIT would have been $41.2 million, a marginal increase of $2.2 million from the previous year, and Military's EBIT would have declined by 9% to $47.1 million, from $51.6 million a year ago.

Further analysis of non-recurring items is provided in *Reconciliation of Non-Recurring Items.*

Further analysis on each segment is provided in *Segmented Results.*

INTEREST

Interest expense amounted to $32.1 million compared to $22.4 million a year ago, an increase of $9.7 million. The increase results mainly from one-time costs arising from repayments of various debts with the proceeds generated from the sale of Marine. The main increase in interest expense is due to the early settlement of a long-term debt facility with a Brazilian financial institution, which resulted in the write-off of $4.7 million (non-cash) of financing costs that were deferred in the balance sheet and amortized over the term of the facility (53 months were remaining). In addition, CAE incurred a $2.5 million charge in the form of an early repayment premium which also contributed to the non-recurring increase. Both amounts are included in the interest expense line in the statement of earnings. In addition, there was a total of $2.0 million of costs associated with the unwind of one interest rate swap ($0.9 million) which converted the floating rate debt under the revolving credit facility to fixed rate debt, and the restructuring of another interest rate swap ($1.1 million) converting a floating rate debt to fixed rate debt, related to the non-recourse project financing for the MSH project. Excluding the impact of these early settlements and interest rate swaps, interest expense would have been $22.9 million for the current fiscal year, slightly above last year as a result of higher interest rates prevailing during fiscal 2005 and a lower level of interest capitalized. (Refer to *Non-recourse Project Financing).*

MANAGEMENT'S DISCUSSION AND ANALYSIS

INCOME TAXES

Income taxes amounted to a net recovery of $100.4 million for the year compared to $11.5 million tax expense last year. This year's tax recovery results from the various elements including non-recurring charges taken during fiscal 2005, together with the recognition of $23.5 million of tax assets. Of the $23.5 million, $12.2 million is related to the reduction in the valuation allowance on CAE's net operating losses in the United States. The remaining amount relates to the materialization of the net capital losses in the United States as a result of the sale of Marine. The later recognition of the net capital losses was not included in the gain on disposition of Marine.

Excluding the non-recurring items, the income tax expense would have been $18.5 million, representing a tax rate of 28% for the year, which is in line with the prior year.

As at March 31, 2005, the Company had approximately US$101.3 million of accumulated non-capital tax losses carried forward that can be used to offset tax payable on future earnings from U.S. operations. CAE also had accumulated non-capital tax losses carried forward relating to its operations in other countries of approximately $66.8 million.

RESULTS FROM DISCONTINUED OPERATIONS

On February 3, 2005, CAE completed the divestiture of substantially all of its Marine business to L-3 Communications Corporation ("L-3"). The results of Marine have been reported as discontinued operations since the second quarter, in line with applicable GAAP requirements, and previously reported statements have been reclassified accordingly. The net earnings of these discontinued operations for the year amounted to $104.8 million and includes the recognition of a gain of $103.9 million (net of taxes of $25.1 million) on the sale of Marine. This gain includes $7.0 million of release of cumulative translation adjustments associated with the Company's foreign investments in Marine. Excluding this gain, earnings from discontinued operations would have amounted to $0.9 million compared to $16.6 million last year. In addition, a $4.4 million charge was recorded during the current year in relation to CAE's former Cleaning Technologies.

For a complete discussion on the sale of the Marine segment refer to *Acquisitions, Business Combinations and Divestitures.*

NET (LOSS) EARNINGS

CAE reported a consolidated net loss for the year of $199.9 million compared to earnings of $64.0 million a year ago. The loss resulted mainly from an impairment, the restructuring measures announced in February 2005, and other non-recurring charges incurred during the third and the fourth quarter. These elements are partially offset by the one-time investment tax credits ("ITC") recognition in the first quarter, the gain on the sale of Marine, and the various tax recoveries in the fourth quarter previously discussed. Excluding the impact of these non-recurring items, net earnings would have amounted to $46.9 million for the year.

EPS

Basic EPS amounted to a loss of $1.23, compared to earnings of $0.20 last year. Net of non-recurring items, basic EPS would have amounted to $0.19 and $0.21, respectively.

RECONCILIATION OF NON-RECURRING ITEMS

The table below shows how certain non-recurring items have affected the Company's results in the respective reporting periods. The Company believes that this supplemental information is useful as it provides an indication of the Company's underlying performance excluding these non-recurring items. Readers should be cautioned, however, that this information should not be confused with or used as an alternative for net earnings (loss) determined in accordance with GAAP as an indicator of performance.

RECONCILIATION OF NON-RECURRING ITEMS

	2005			2004		
(amounts in millions, except per share amounts)	**AMOUNT PRE-TAX**	**AMOUNT AFTER TAX**	**PER SHARE**	AMOUNT PRE-TAX	AMOUNT AFTER TAX	PER SHARE
Earnings (loss) from continuing operations	**$ (405.1)**	**$ (304.7)**	**$ (1.23)**	$ 58.9	$ 47.4	$ 0.20
Impairment of goodwill, intangible and tangible assets	**443.3**	**354.2**	**1.43**	—	—	—
Restructuring charges	**24.5**	**16.7**	**0.07**	9.3	6.4	0.03
Additional ITC recognition (FY00–FY04)	**(14.2)**	**(10.1)**	**(0.04)**	—	—	—
Costs associated with the early settlement of long-term debts	**9.2**	**8.6**	**0.03**	—	—	—
Tax recoveries	**—**	**(23.5)**	**(0.09)**	—	(4.4)	(0.02)
Other non-recurring items	**7.7**	**5.7**	**0.02**	—	—	—
Earnings (loss) from continued operations, excluding non-recurring items (not in accordance with GAAP)	**$ 65.4**	**$ 46.9**	**$ 0.19**	$ 68.2	$ 49.4	$ 0.21

Each specific item highlighted in the above table is further discussed below.

MANAGEMENT'S DISCUSSION AND ANALYSIS

IMPAIRMENT OF GOODWILL, INTANGIBLE AND TANGIBLE ASSETS

The Company performs the annual testing for impairment of its long-lived assets as at December 31 of each year using the two-step method prescribed under GAAP. Based on the test performed as at December 31, 2004, CAE concluded that an impairment charge was required.

As part of the first step, the total fair value of each reporting unit (Military and Civil) was compared with its respective carrying amount (net book value), including goodwill, in order to identify a potential impairment. The fair values of the reporting units were estimated using generally accepted valuation techniques including discounted cash flow and comparable analysis. The process of determining fair values requires Management to exercise judgment in making assumptions about future results, including revenue and cash flow projections and discount rates.

If the fair value of a reporting unit is lower than its carrying amount, the goodwill of this reporting unit may be impaired and the reporting unit must proceed with a second step in order to quantify the amount of impairment, if any. Under a second step, the fair value of goodwill is determined in the same manner as the value of goodwill would be determined in a business combination context. If, after performing the second step, it is determined that the goodwill recorded is higher than the implied fair value of goodwill, an impairment charge is recorded in the period.

During the third quarter of fiscal 2005, CAE's Management initiated a comprehensive review of current performance and the strategic orientation of its Civil and Military business units. This strategic review revealed that several factors have emerged and/or worsened over the course of the past year that severely affect the Civil business, including:

- the enduring adverse economic and financial environment of the airline industry creating a new market reality, including a decreased level of interest in pilot training outsourcing;
- the appreciation of the Canadian dollar;
- the erosion of the less than 50-seat regional jet market; and
- the escalating cost of acquiring data, parts and avionics for the manufacturing of full-flight simulators.

Most of these elements are outside the direct control of the Company and currently show only modest signs of abatement. These elements caused Management to recalibrate some key assumptions in Civil's strategic planning.

New Market Reality

The enduring adverse economic environment of the airline industry, first initiated in 2001 with the 9/11 terrorist attacks, and was further impacted by the SARS outbreak in Asia and by the Iraq war, was, in 2004, exacerbated by soaring fuel costs and declining yields. These factors continue to offset the extensive cost-cutting initiatives the airlines have undertaken to such a point that U.S. airlines lost an estimated US$5 billion in 2004 when less than a year ago, analysts were forecasting a break-even year. This fourth consecutive year of important losses for U.S. airlines shows that there are no immediate solutions underway. In addition, the four years of lost growth will not easily be made up as only in mid-2004 did traffic volume return to pre-9/11 levels. CAE is now in a new market reality where cost management is at the centre of all decisions. In addition, interest in training outsourcing, which could contribute to improving cost-effectiveness, is low on the airline industry's priority list, where the focus is mainly on reducing labour and fleet costs. This new reality has translated into continued price pressures on Civil's equipment and training businesses.

Appreciation of the Canadian Dollar

The vast majority of Civil equipment revenues are based in U.S. dollars while Civil's manufacturing costs are primarily in Canadian dollars. Therefore, the appreciation of the Canadian dollar to over US$0.83 (or C$1.20) in calendar 2004 had a material adverse impact on the profitability of Civil's business.

Erosion of the Less Than 50-Seat Regional Jet Market

The latter part of calendar year 2004 saw a major shift in demand for regional jets from the sub 50-seat segment to newer, larger platforms (70-to-100+ seat range). The value proposition for smaller regional jets has been severely impacted by the new low-yield market environment. In addition, legacy airlines are relaxing scope clauses, which previously restricted their use of 70-seat jets. Bombardier and Embraer have both reduced their 20-year market forecast in the less than 50-seat range and Bombardier has severely reduced its planned production for CRJ200s as evidenced by significant workforce reductions in 2004. These factors also make it less likely that production of the Dornier 328JET, for which CAE was the exclusive entitlement training provider, will be restored.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Escalating Cost of Acquiring Data, Parts and Avionics for the Manufacturing of Full-Flight Simulators

In 2002, CAE launched its next generation FFS design, which was intended to reduce manufacturing and life cycle costs. However, as the Company experienced reduced throughput in its manufacturing facilities, the anticipated savings have not materialized, which has prompted Management to make this issue a key priority to address.

Furthermore, CAE has also incurred increased costs for acquiring data, parts and avionics in the past few years, with these costs representing a major component in its manufacturing of FFS.

Therefore, based on the preceding factors and the results of the strategic review previously mentioned, CAE concluded its annual testing for impairment of its long-lived assets, including goodwill, intangibles and property, plant and equipment as well as certain other assets and deferred costs. The Company concluded that the carrying value of some of Civil's tangible and intangible assets (including goodwill) were impaired and, on this basis, recorded in the third quarter of fiscal 2005 a $443.3 million impairment charge detailed as follows:

DETAILED IMPAIRMENT CHARGE

(amounts in millions)	IMPAIRMENT AMOUNT
Goodwill	$ 205.2
Customer relations	86.7
Trade names and other intangible assets	20.4
Other assets	19.3
Property, plant and equipment (simulators)	78.4
Inventories	33.3
Total before taxes	$ 443.3
Tax recovery	89.1
Total impairment charge, net of tax	**$ 354.2**

The 20% tax recovery rate associated with the impairment charge was a result of the non-deductibility, for tax purposes, of some of the goodwill and intangibles assets impairment charge.

As indicated in the table above, the after-tax effect of this non-cash charge on CAE's consolidated net earnings in the third quarter of 2005 was $354.2 million or $1.43 per share.

RESTRUCTURING CHARGES

On February 10, 2005, CAE announced a comprehensive restructuring plan (the "Plan"), that will materially change the manner in which CAE conducts its business, and is aimed at restoring the Company's profitability, cash flow and return on investment. This Plan, to be executed over the next 18 months, results from the extensive strategic review of CAE's markets, customers and other external stakeholders as well as its internal resources and capabilities undertaken by the Management under the leadership of the new CEO.

The Plan, geared towards the elimination of duplication and the achievement of a more competitive cost structure, includes actions such as:

- the rationalization of its Civil training centres footprint including the consolidation of training centres where duplication exists and relocation of a number of FFS to maximize yield and streamlining of the management structure; and
- the consolidation, into the new Simulation Products division as of April 1, 2005, of all manufacturing activities including engineering, program management and global procurement. These functions had previously existed in various business units and regionally, resulting in duplication.

The Company is reducing headcount; as of May 10, 2005, 400 of the 450 employees have already left the Company since the announcement of the Plan.

In addition, as part of the Plan, the Company will be implementing an enterprise resource planning system ("ERP"), a business management system that integrates all aspects of the business, including planning, manufacturing, and sales and marketing, in order to improve transparency, accountability and information flow. Finally, CAE's compensation structure has been reoriented, with a specific emphasis on building shareholder value through focus on delivery of free cash flows and adequate return on capital invested.

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The Company accounts for the restructuring charges in accordance with GIGA EIC-134 *Accounting for Severance and Termination Benefits and EIC-135 Accounting for Costs Associated with Exit and Disposal Activities (Including Costs Incurred in a Restructuring)* as described in Note 24 of the consolidated financial statements. These CICA abstracts provide guidance on the timing of recognition and measurement of liabilities as well as disclosures for the various types of costs associated with an exit or disposal activity, including restructuring. Under EIC-135, a liability for a cost associated with a restructuring can only be recorded when that liability is incurred and can be measured at fair value. A liability is incurred when an event obligates the Company to transfer or use assets, or more explicitly, when an event leaves the Company little or no discretion to avoid transferring or using the assets in the future. Under these rules, commitment to an exit plan or a plan of disposal expresses only Management's intended future actions and, therefore, does not meet the requirement for recognizing a liability and the related expense.

The Company intends to report as restructuring costs, all costs associated with the closure of business activities, the relocation of business activities from one location to another, the changes in management structure, and all other costs related to the restructuring as it affects the nature and focus of the operations.

In order to comply with accounting requirements, all restructuring costs incurred by the Company prior to establishment of its "formal restructuring plan" were not included in the restructuring charge line of the financial statements and were expensed as part of the normal operations. Please refer to *Other non-recurring items* for further information.

During fiscal 2005, the Company has recorded a $24.5 million restructuring charge for workforce reduction and related expenses. In line with the Plan previously announced, an additional restructuring cost in the range of $30 to $40 million should be incurred by the Company in fiscal 2006.

RECOGNITION OF ADDITIONAL ITC FOR FY00 TO FY04

While investment tax credits ("ITC") are a normal, recurring part of CAE's business, fiscal 2005 results from continuing operations were positively affected by the recognition, in the first quarter, of additional ITC totalling $14.2 million ($10.1 million, net of tax) for continuing operations. During the year tax authorities completed their audit of R&D expenses thereby enabling CAE to release provisions for tax expenses. Hence CAE reviewed its methodology to provide for tax expenses for fiscal 2004 and 2005.

The additional ITC included in the fiscal 2005 EBIT of Civil and Military were, respectively, $9.8 million and $4.4 million.

EARLY SETTLEMENT OF LONG-TERM DEBT

At the end of the fourth quarter, as part of the restructuring of its balance sheet and the reduction of its debt level, CAE fully repaid the term loan related to the project financing for its training centre in São Paulo, Brazil. The one-time cost associated with these elements is further described in *Interest.* In addition the Company settled two swaps.

TAX RECOVERIES

Non-recurring items include the recognition of a $23.5 million tax asset from a reduction in the valuation allowance for net operating losses and for capital losses for income tax purposes in the United States. During fiscal 2004 the Company had recognized a $4.4 million tax benefit related to prior years' tax losses in Australia.

Refer to *Income Taxes* for further details.

OTHER NON-RECURRING ITEMS

The amount includes a variety of items that were not classified under restructuring charges in the statement of earnings or that are not part of the day-to-day operations of the Company, including:

- the costs related to employees and executives who were terminated prior to the adoption of a formal restructuring plan (as defined by GAAP);
- the costs related to the closing of the Toronto head office; and
- the incremental costs associated with the recent strategic review.

BALANCE SHEET

The Company's shareholders' equity excluding currency translation adjustment ("CTA") at the end of fiscal 2005 amounted to $717.9 million, a decrease of $213.0 million compared to $930.9 million at the end of fiscal 2004. The decrease reflects the net loss of $304.7 million from continued operations, distribution of $24.7 million in dividends offset by the $104.8 million contribution from discontinued operations (including a gain of $103.9 million net of tax), a $3.3 million adjustment resulting in the adoption of a new accounting standard and an increase of $6.3 million and $2.0 million in capital stock and contributed surplus, respectively. The following table describes the significant variances in the consolidated balance sheet from March 31, 2004 to March 31, 2005.

MANAGEMENT'S DISCUSSION AND ANALYSIS

SIGNIFICANT BALANCE SHEET VARIANCES

(amounts in millions, unless otherwise noted)	INCREASE /(DECREASE)	EXPLANATION
Accounts receivable	$ (60.8)	During the course of the fiscal year the Company received funds on a number of large outstanding Military receivables. In addition CAE entered into a program under which it sells accounts receivable to a third party without recourse. The total amount sold as at March 31, 2005 was $16.5 million.
Inventories	(46.7)	The decrease is mainly due to a write-down of $33.3 million mainly of obsolete FFS parts for less than 50-seat aircraft.
Intangible assets	(109.0)	The decrease is mainly due to an impairment charge of $107.1 million of customer relationship and trade names-type intangible assets.
Goodwill	(208.6)	The decrease is due to an impairment charge of $205.2 million for Civil. The remaining amount of $3.4 million is due to the net effect of foreign exchange fluctuations and business acquisitions and combinations.
Assets held for sale (current and long-term)	(166.4)	The decrease is as a result of the sale of Marine in the fourth quarter of the fiscal year. The remaining assets held for sale includes mainly assets of two Marine businesses to be sold to L-3 in fiscal 2006.
Liabilities held for sale (current and long-term)	(53.5)	The decrease is as a result of the sale of Marine in the fourth quarter of the year.
Long-term debt (including current portion)	(241.4)	Proceeds received from the sale of Marine ($238.6 million) in the fourth quarter were used to reduce long-term debt levels. The reduction was slightly offset by the inclusion in the financial statements of a variable interest entity which increased long-term debt by $38.8 million.
Currency translation adjustment	(54.2)	The decrease is due mainly to the effect of changes in exchange rates during the year on net investment in self-sustaining subsidiaries, and the release of $7.0 million as a result of the sale of Marine.

VARIABLE INTEREST ENTITIES

On January 1, 2005, the Company adopted Accounting Guideline "Consolidation of Variable Interest Entities" ("AcG-15") on a retroactive basis without restatement of prior periods. AcG-15 provides a framework for identifying variable interest entities ("VIEs") and determining when an entity should include the assets, liabilities and results of operations of a VIE in its consolidated financial statements.

In general, a VIE is a corporation, partnership, limited-liability corporation, trust, or any other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has a group of equity owners that are unable to make significant decisions about its activities, or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

AcG-15 requires a VIE to be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a variable interest holder) is exposed to a majority of the risk of loss from the VIEs activities, is entitled to receive a majority of the VIEs residual returns (if no party is exposed to a majority of the VIEs losses), or both (the primary beneficiary). Upon consolidation, the primary beneficiary generally must initially record all of the VIEs assets, liabilities and non-controlling interests at fair value at the date the enterprise became the primary beneficiary. However, for variable interest entities created prior to the initial adoption of AcG-15, the assets, liabilities and non-controlling interest of these entities must be initially consolidated as if the entities were always consolidated. AcG-15 also requires disclosures about VIEs in which the variable interest holder is not required to consolidate, but it has a significant variable interest.

A key element of CAE's finance strategy to support the investment in its Civil training business is the sale and leaseback of certain FFS installed in the Company's global network of training centres. This provides CAE with a cost-effective long-term source of fixed-cost financing. A sale and leaseback transaction can only be executed after the FFS has achieved certification by regulatory authorities (i.e. the simulator is installed and is available to customers for training). The sale and leaseback structures are typically structured as leveraged leases with an owner participant.

Typically, the Company has the option to purchase the equipment at a specific period during the lease terms at a specific purchase price. Some leases include renewal options at the end of the term. In some cases, the Company has provided guarantees for the residual value of the equipment at the expiry date of the leases or at the date the Company exercises its purchase option. These Special Purpose Entities ("SPEs") are financed by secured long-term debt and third-party equity investors who, in certain cases, benefit from tax incentives. The equipment serves as collateral for the SPEs' long-term debt. The Company's variable interests in these SPEs are solely through residual value guarantees and fixed purchase price purchase options. These leases expire in different periods up to 2023.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following table summarizes total assets and total liabilities of the SPEs that the Company has identified as VIEs as at March 31, 2005:

CIVIL SIMULATION AND TRAINING

SALE AND LEASEBACK STRUCTURES *(amounts in millions)*	ASSETS	LIABILITIES
Air Canada Training Centre -Fiscal 2000	$ 15.4	$ 15.4
Toronto Training Centre -Fiscal 2002	26.6	26.6
Denver / Dallas Training Centre -Fiscal 2003	58.7	58.7
SimuFlite- Fiscal 2004	83.1	83.1
Amsterdam Training Centre -Fiscal 2002	44.1	40.8
	227.9	224.6
Less assets and liabilities:		
Newly consolidated under AcG-15	44.1	40.8
Assets and liabilities of non-consolidated VIEs subject to disclosure	$ 183.8	$ 183.8

The Company is the primary beneficiary for only one of the above VIEs. The Company's participation in this VIE results from the acquisition of Schreiner Aviation Training B.V. in August 2001. As part of this acquisition, CAE assumed a sale leaseback transaction, for simulators in the Company's Amsterdam Training Centre, arranged by Fortis Bank. The deal was structured through a SPE with MeesPierson XXX as owner trustee and owner participant.

Pursuant to the adoption of AcG-15 on January 1, 2005, the consolidation of the SPE, resulted in an increase in total assets, total liability, and shareholders' equity of $46.4 million, $43.2 million, and $3.2 million.

Detailed impact by balance sheet element is as follows as of January 1, 2005:

(amounts in millions)	NEWLY CONSOLIDATED
Assets	
Prepaid expenses	$ (0.5)
Property, plant and equipment	46.9
	$ 46.4
Liabilities	
Accounts Payable and Accrued Liabilities	$ 0.1
Long-term debt (including portion due within one year)	41.3
Future Tax Liabilities	1.8
	$ 43.2
Shareholders Equity	
Retained Earnings	$ 3.3
Currency Translation Adjustment	(0.1)
	$ 3.2
	$ 46.4

The liabilities recognized as a result of consolidating this VIE do not represent additional claims on the Company's general assets; rather, they represent claims against the specific assets of the consolidated VIE. Conversely, assets recognized as a result of consolidating this VIE do not represent additional assets that could be used to satisfy claims against the Company's general assets. Additionally, the consolidation of this VIE did not result in any change in the underlying tax, legal or credit exposure of the Company.

For all of the other SPEs that are VIEs, the Company is not the primary beneficiary and consolidation is not appropriate under AcG-15. For additional information on the Company's VIEs, see Note 25 of the consolidated financial statements.

STATEMENT OF CASH FLOW

The Company's cash and cash equivalents at the end of fiscal 2005 amounted to $57.1 million, an increase of $2.4 million compared to $54.7 million at the end of fiscal 2004. In 2005, CAE generated $186.0 million of cash from continuing operating activities and $137.4 million of cash from investing activities of continuing operations, while it used $340.5 million of cash for financing activities of continuing operations. The major cash contribution during 2005 came from the divestiture of Marine.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following table summarizes the major elements of the statements of cash flow for the fiscal year ending March 31, 2005, with prior year comparatives:

STATEMENTS OF CASH FLOW

(amounts in millions unless otherwise noted)	**2005**	2004	EXPLANATION
Cash and cash equivalents, beginning of the year	**$ 61.9**	$17.1	
Provided by (used in):			
Operating activities	**207.6**	5.7	The majority of cash generated from operating activities is from positive non-cash working capital and cash generated from operating results. The impairment charge is non-cash and therefore has no impact on cash flow from operating activities.
Investing activities	**131.6**	24.5	Cash generated from investing activities is mainly a result of proceeds from disposal of discontinued operations for $239.4 million ($238.6 million relates to the sale of Marine) and proceeds from sale and leaseback of assets for $43.8 million offset by capital expenditures of $ 118.0 million and deferred costs.
Financing activities	**(337.3)**	17.8	Cash used by repayments of long-term debt of $588.5 million (financed in part by proceeds from disposal of discontinued operations) and dividends paid of $24.0 million offset mainly by proceeds from long-term debt.
Total cash provided in the year	**$ 1.9**	**$**48.0	
Effect of foreign exchange rate changes on cash and cash equivalents	**(2.3)**	(3.2)	
Cash and cash equivalents, end of year	**$ 61.5**	$61.9	

CONTINUING OPERATING ACTIVITIES

Cash generated from continuing operating activities totalled $186.0 million in 2005, compared to $1.5 million in 2004. The increase in cash generated by operating activities was mainly due to an increase in operating results from continuing activities, excluding the non-cash items, together with cash generated of $85.6 million in non-cash operating working capital in 2005.

The positive non-cash operating working capital in fiscal 2005 is mainly due to a $60.8 million decrease in accounts receivable, following large collections on several Military projects and a receivables factoring program together with a $46.7 million reduction of inventories mainly as a result of impairment write-off. The current level of working capital is low and some reversal should be expected for the first quarter of fiscal 2006.

Accounts receivable in the previous year were enhanced by progress towards the achievement of milestones on two major programs: the German Night-Time Low-Level Flight ("NTF") helicopter program and the Chinook helicopter simulator program for the Government of Singapore.

FINANCING ACTIVITIES OF CONTINUING OPERATIONS

Cash used in financing activities of continuing operations totalled $340.5 million in fiscal 2005, compared to a cash generation of $7.4 million in 2004. The decrease of cash generated was mainly due to lower proceeds of long-term debt in the current year and the fact that there was a common stock issuance in the prior year for $176.4 million.

Long-term debt, including the current portion, amounted to $342.9 million as at March 31, 2005 compared to $584.3 million last year. The decrease in long-term debt was mainly due to the repayment of long-term debt with cash generated by the sale of Marine as well as the impact of the strengthening of the Canadian dollar on U.S. dollar denominated debt.

INVESTING ACTIVITIES OF CONTINUING OPERATIONS

The Company generated $137.4 million of cash for investing activities of continuing operations in fiscal 2005, compared to $36.5 million in 2004. In fiscal 2005, the Company generated $238.6 million from the sale of Marine but used $118.0 million for capital expenditures (compared to $86.8 million in fiscal 2004). Major elements included in growth are related to the expansion of the Civil training network, including deployment of FFS to CAE's centres in China, Chile, Middle East and in the U.K. together with the progression of our investment in the Dassault Falcon 7X and Airbus A380 programs.

FREE CASH FLOW

Free cash flow from continuing operations for the year improved by $78.0 million, to reach $87.8 million. The improvement results from positive variances in non-cash working capital offset marginally by an increase in capital expenditures.

MANAGEMENT'S DISCUSSION AND ANALYSIS

BACKLOG

CAE's consolidated continuing operations backlog as at March 31, 2005 stood at $2.5 billion, $212.3 million higher than a year ago. These figures exclude any amounts for CAE's contract with Dassault Aviation to provide entitlement training on its new Falcon 7X business jet.

SEGMENTED RESULTS

CIVIL

REVIEW OF OPERATIONS

Equipment Orders

CAE won a total of 17 FFS orders out of a possible total of 22 competed orders, maintaining a 77% market share.

For the first order of fiscal 2005, CAE and Qantas signed a contract with a value of approximately $25 million for a suite of Airbus A380 integrated training solutions, including a FFS and a CAE Simfinity™ training device. This was CAE's third A380 FFS order, further evidence of CAE's success in developing A380 integrated training solutions.

During the Farnborough air show in early July 2004, CAE secured a competed order from Dubai's Emirates airline for three FFS–two Airbus A380-800s and one Airbus A340-600– for a value of approximately $65 million. These were the fourth and fifth A380 FFS orders for CAE. Under the terms of the agreement, CAE became Emirates' exclusive provider of FFS for 10 years.

Emirates-CAE Flight Training ("ECFT") expanded its aviation training facility with the addition of three CAE FFS. As part of this expansion, Emirates bought two new FFS from CAE: a Boeing 777 and an Airbus A320, worth approximately $31 million. The third FFS, an Airbus A330/A340, is an existing device to be relocated from within CAE's global network.

In a number of contracts from airlines in the Asia-Pacific region with a total list-price value of $88 million, longstanding CAE customer Japan Airlines International purchased a CAE Boeing 777-200ER FFS; China Airlines International ordered an A330-200 FFS equipped with a new-generation CAE Tropos™ visual system; and China Eastern Airlines ordered an Airbus A330-200/A340-600 convertible FFS, also featuring the CAE Tropos visual system. As part of the latter contract, CAE undertook to provide a range of CAE Simfinity classroom training products and a second CAE Tropos visual system to upgrade an existing simulator owned by China Eastern. CAE agreed to provide an Airbus A320 FFS and an A320 CAE Simfinity Integrated Procedure Trainer ("IPT") as well as a Boeing 737NG IPT to Zhuhai Flight Training Centre, a joint venture between CAE and China Southern Airlines. CAE was selected by Singapore Flying College, a subsidiary of Singapore Airlines, to deliver a Learjet 45 FFS and an IPT to its branch in Maroochydore, Australia.

CAE won a contract to supply two Airbus A330/A340 FFS with the CAE Tropos visual systems to Etihad Airways, a new airline based in the United Arab Emirates, and a first-time customer to CAE. In addition, WestJet purchased a Boeing 737-700 FFS, also equipped with CAE Tropos. These contracts were valued at approximately $48.0 million.

CAE was awarded a contract with a value of approximately $31.0 million, at list price, to provide Airbus with two new Airbus A330/A340 FFS scheduled for installation at Airbus' training centre in Toulouse, France.

As part of its last civil equipment simulator contract of fiscal 2005, CAE sold an Embraer 170 FFS featuring the CAE Tropos visual system to a third-party customer.

Training Contracts

CAE signed a 10-year services agreement with LAN Chile S.A. ("LAN") to provide training on Boeing 737-200 and Airbus A320 FFS beginning in 2004 and on the Boeing 767-300ER FFS commencing in the last quarter of 2005. The total value of the contract, together with third-party revenues, is expected to be $40 million. Training takes place in Santiago, Chile, at LAN's training centre, which CAE acquired for $0.9 million on April 22, 2004.

CAE ratified a contract to train pilots of European low-fare carrier easyJet on the Airbus A320 family of aircraft for a minimum of seven years. The value of the agreement is expected to be in the range of $40 to $60 million.

At the Farnborough air show CAE and Dassault Aviation signed a contract making CAE the exclusive provider of entitlement training–the initial training provided by the aircraft manufacturer with the purchase of an aircraft–for the all-new Falcon 7X, the first fly-by-wire business jet. Also included in this agreement was entitlement training for pilots, maintenance personnel and cabin crew. This was the first contract of this kind to be awarded to CAE by a business jet manufacturer.

CAE signed a number of multi-year aviation training agreements for centres in North America and Europe. Sun Country Airlines and Skyway, a wholly owned subsidiary of Midwest Airlines, signed agreements for training at CAE's North American centres. Baron Air, Italy First and TUI Airlines Belgium are among 13 airlines, many of them new customers, who signed agreements to train at CAE's European centres. These agreements are cumulatively valued at about $15 million, based on expected training volume.

ECFT is slated to become a Bell Associated Training Facility for Middle East-based operators of the Bell 412 helicopter, with Doha-based Gulf Helicopters, who signed a five-year exclusive agreement, as its first customer.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CAE Training Centres

Following a number of new training contracts, CAE plans to open a civil aviation training centre in the area of London, U.K. Intended to be operational by fall 2006, the proposed centre will serve both airlines and business aircraft operators, beginning with anchor customers easyJet and Dassault.

CAE is also in the process of building a new business aviation training centre in Morris County, New Jersey. The new centre is expected to be operational by summer 2006, when entitlement training will begin for the Falcon 7X business aircraft. Once the centre is operational, CAE's global network will include four major business aviation training centres strategically located around the world: Morris County and Dallas, U.S., Dubai, U.A.E., and London, U.K.

FINANCIAL RESULTS

(amounts in millions, except operating margins in %)	**2005**	2004	2003	2002	2001
Revenue	**$ 520.2**	461.8	517.2	545.2	481.5
EBIT	**$ 47.6**	39.0	115.6	157.3	114.4
Operating margins	**% 9.2**	8.4	22.4	28.9	23.8
Backlog	**$ 1,103.1**	1,021.3	877.1	805.6	656.9
Capital expenditures	**$ 111.5**	81.7	212.1	216.7	72.9

Civil's revenue amounted to $520.2 million for the year, up 13% over the prior year. Training revenue increased as result of the addition of the new CAE–Iberia training centre in Madrid, Spain (which contributed an additional 6.6% to Civil's training revenue) and additional simulators in the Dubai training facility. Equipment and services revenue benefited from the higher order intake in the current year. Offsetting these gains is a $19.8 million negative foreign exchange impact. Excluding foreign exchange, revenue would have amounted to $540.0 million, $78.2 million above last year.

Civil achieved EBIT growth of 22% compared to last year, to reach $47.6 million. This includes $9.8 million from additional ITC recognized in the first quarter, related to expenditures of prior years. Civil also absorbed approximately $3.4 million of non-recurring costs in the third and fourth quarter of fiscal 2005. Excluding the additional ITC benefit and other non-recurring items, Civil's EBIT would have been $41.2 million, 6% higher than last year. Fiscal 2005 was marked with continued competitive pressure in the equipment market, further compounded by the stronger Canadian dollar which directly impacts on pricing. In training, EBIT growth significantly outpaced revenues despite the higher operating lease expenses associated with the Company's ongoing FFS sale and leaseback program, offset by growth in training revenue. Excluding the impacts of foreign exchange Civil's EBIT would have amounted to $55.9 million, $16.9 million above last year.

BACKLOG

Backlog for Civil consists of both equipment sales and training services. The training services portion includes revenue from customers under both long- and short-term contractual arrangements where training revenues are guaranteed or expected based on current customer requirements. CAE's ability to complete contracted sales included in its order backlog is dependent in part on the long-term financial condition of the contracting customers.

As at March 31, 2005, Civil's backlog stood at $1.1 billion, $81.8 million higher than a year ago. Order intake amounted to $668.0 million for the year compared to $662.8 million last year.

OUTLOOK

Notwithstanding the issues discussed earlier in this MD&A under *Reconciliation of non-recurring items,* Management saw some signs that the civil aviation market was beginning to recover commencing late in calendar 2004, as traffic levels surpassed pre-9/11 levels for the first time and pilot hiring and aircraft deliveries were up over calendar 2003. However, the U.S. airline industry still lost an estimated US$5 billion in calendar 2004 and is forecast to lose money again in 2005.

In the near term, the Asian and Middle Eastern markets are expected to drive the majority of equipment demand as these regions continue to expand faster than the more mature North American and European markets. Airlines in the latter markets, particularly the legacy carriers, are being affected by high fuel costs and weakening domestic yields, which Management expects will continue to limit their capital spending. The equipment demand in these markets will mainly be driven by the introduction of new platform types (e.g., Airbus A380, Embraer 170/190, Boeing 787) into airline fleets.

Civil's near-term priorities are to optimize returns on existing training investments while pacing its entry into developing growth markets. CAE's immediate financial goals are to drive positive free cash flow and improve return on invested capital.

MANAGEMENT'S DISCUSSION AND ANALYSIS

MILITARY

REVIEW OF OPERATIONS

Equipment Orders

CAE was awarded a number of contracts that further solidify its presence in its various markets around the world.

In the U.S., CAE USA was awarded a contract valued at approximately US$26 million by the US Army Program Executive Office–Simulation, Training & Instrumentation ("PEO STRI") to manufacture an MH-60 Black Hawk Block 1 combat mission simulator ("CMS") for the U.S. Army's 160th Special Operations Aviation Regiment-(Airborne) ("SOAR(A)"). In addition, PEO STRI awarded CAE contracts valued at approximately US$9.5 million to provide its CAE Medallion–S™ visual system for two upgrades to combat mission simulators for the SOAR(A).

When Lockheed Martin signed a contract to provide three KC-130J Weapon Systems Trainers ("WST") to the US Marine Corps, the design, manufacture, and integration of these KC-130J WSTs was subcontracted to CAE USA in a contract valued at approximately US$34 million.

The United States Navy awarded CAE USA a contract valued at US$60 million to develop three MH-60S tactical operational flight trainers and four MH-60S weapons tactics trainers. The contract includes options for more simulators of these types as well as support services that could bring the total value to more than US$75 million.

CAE USA also won a contract, valued at US$12.5 million, to upgrade two P-3C flight simulators for the United States Navy. This contract includes options to upgrade four more simulators, which are expected to be exercised in 2006 and 2007 and could bring the total contract value to approximately US$23 million.

CAE USA was also awarded contract options for the C-130J Maintenance and Aircrew Training System program as well as the C-130 Aircrew Training System program.

In Europe, the Royal Netherlands Navy selected CAE to perform a $9 million upgrade of the Lynx helicopter full-mission flight trainer at Naval Air Station de Kooy in Den Helder, The Netherlands. CAE will add new radar and communications systems to the simulator, as well as enhance a range of other helicopter systems. Furthermore, the German Armed Forces awarded CAE a contract of approximately $33 million for on-site maintenance and support services, as well as various upgrades and modifications to flight simulation equipment. CAE also signed a subcontract with Lockheed Martin valued at $13.4 million to perform upgrades on the U.K. Royal Navy Merlin Training System.

In line with its strategy to expand its products offering, CAE introduced a suite of CAE Simfinity integrated training solutions for the C-130 aircraft at the 2004 Airlift/Tanker Association Convention. Designed for both aircrew and maintenance training programs, CAE Simfinity integrated training solutions are based on the same high fidelity simulation software found on CAE's full-mission simulators.

Training & Services

Eurofighter Simulation Systems GmbH awarded a contract to CAE to provide a range of engineering and on-site support services for the visual systems on the Eurofighter Aircrew Synthetic Training Aids program. The contract is valued at approximately $30 million over five years.

CAE-led Landmark Training Ltd. was selected as the intended preferred bidder for the British Army's Armoured Vehicles Training Services ("AVTS") program. The program, valued at approximately £1.0 billion over 30 years, is a private finance initiative ("PFI") designed to provide turnkey driver, gunnery and command information systems training to crews of armoured fighting vehicles. Landmark Training Ltd. is owned 65% by CAE, 25% by AgustaWestland, the Anglo-Italian helicopter company owned by Italy's Finmeccanica, and 10% by Interserve Plc.

In another PFI, the German government awarded a contract to Helicopter Flight Training Services GmbH ("HFTS") to provide NH90 helicopter training to the German Armed Forces. HFTS was founded by an industrial consortium consisting of CAE, Eurocopter, Rheinmetall Defence Electronics and Thales, each owning a 25% share. HFTS will design, build, and operate three NH90 training centres in Germany. The total contract signed by HFTS is valued at €488.0 million, of which CAE's share is €122.0 million.

FINANCIAL RESULTS

(amounts in millions, except operating margins in %)	**2005**	2004	2003	2002	2001
Revenue	**$ 466.0**	476.6	459.6	465.5	338.8
EBIT	**$ 47.2**	51.6	78.8	66.6	26.4
Operating margins	**% 10.1**	10.8	17.1	14.3	7.8
Backlog	**$ 1,401.6**	1,271.1	1,258.6	1,393.7	988.9
Capital expenditures	**$ 6.5**	5.1	12.1	14.1	1.8

Military's revenue amounted to $466.0 million, a decrease of $10.6 million from last year. The majority of the decrease ($8.3 million) is due to a negative foreign exchange impact together with delays in contractual awards. Excluding this impact revenue would have amounted to $474.3 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

EBIT amounted to $47.2 million, a decrease of $4.4 million compared to the same period last year. The shortfall compared to the previous year was mainly attributable to higher costs to complete certain programs, particularly in the first quarter, together with the absorption of approximately $4.3 million of non-recurring costs in the third and fourth quarter and the negative foreign exchange impacts of approximately $1.2 million. This was partially offset by lower selling and marketing expenses, as well as $4.4 million of additional ITC recognition in the first quarter of fiscal 2005. Military's cumulative EBIT, excluding the impact of additional ITC and other one-time items, would have amounted to $47.1 million, $4.5 million lower than a year ago.

BACKLOG

As at March 31, 2005, Military's backlog stood at $1.4 billion, $130.5 million higher than a year ago. Military's total order book for the year stands at a record $681.4 million compared to $506.7 million last year, an increase of 34%. Successes in Europe with the award of the German NH90 PFI program and in the U.S. market where Military has more than doubled its order intake over the last two years have contributed strongly to CAE's success and underlined the criticality of local presence. Military's backlog is strong and contains a well-balanced mix of near-term equipment delivery contracts and long-term training service contracts which provide predictable and growing cash flow.

OUTLOOK

Military experienced solid order intake ($127 million) in the last quarter of fiscal 2005 with more than 75% of orders coming from its CAE USA operation, including additional orders from the U.S. Special Operations Forces. As well, CAE USA achieved significant new business in the past year with a new customer- the U.S. Navy. CAE is well-positioned as the Navy's provider of training solutions for the MH-60S helicopter, which should also lend credibility to CAE's pursuit of future U.S. Navy helicopter training opportunities.

Looking forward to next fiscal year, Military is expecting continued solid and well-balanced order intake. The first quarter is expected to bring training support services orders in Canada and a range of equipment orders in the U.S. Military will also continue to strengthen its position as a training system integrator to governments and a key lead systems integrator. In this vein, CAE-led Landmark Training Ltd. is actively engaged in the negotiations to achieve preferred bidder status for the British Army's AVTS program.

Military's focus is continued growth in its core market and pursuit of growth opportunities where it can leverage its technology leadership. The recent creation of CAE Professional Services, a line of business integrated with Military, focused on modelling and simulation and homeland defence is a concrete example of CAE's adaptation to the changing nature of warfare. These fast-growing domains, fuelled with new sources of funding, rely heavily on the application of the same simulation and modelling technology which has been a hallmark for CAE. Military has experienced successes in these areas this year, with nearly $30 million in orders and intends to grow its Professional Services capabilities at a rapid pace and in a well-focused manner throughout the next year.

With a keen attention to customers' satisfaction, CAE remains focused on program execution and best-in-class technology which indeed have been the driving force behind Military's growing backlog and winning new business. Through well-targeted R&D plans, Military is committed to technology leadership and helping CAE's customers address their security needs in dealing with terrorism and conflict situations requiring a new breed of mission rehearsal and training solutions.

BUSINESS SEGMENTS: GOING FORWARD

As described in *Business Profile and Strategies,* starting in fiscal 2006 CAE will provide results on a newly segmented basis. This will enable stakeholders to properly assess the operational performance, financial condition and prospects of each of the Company's three business groups: Civil Training & Services, Military Simulation & Training, and Simulation Products.

ACQUISITIONS, BUSINESS COMBINATIONS AND DIVESTITURES

The Company's strategy with respect to acquisitions and dispositions is to re-align itself by divesting its non-core businesses and to focus on its two key market segments: Civil and Military. Civil training centre acquisitions enable the Company to expand its training facility network. Military acquisitions have allowed the Company to continue to expand its product offerings in the area of modelling and simulation.

MARINE CONTROLS

In the second quarter of fiscal 2005, the Board of Directors approved a plan to divest its Marine business. The plan was consistent with the Company's strategic process of focusing on its core competency-the development and use of simulation and modelling technology to provide training solutions. On February 3, 2005, CAE completed with L-3 the sale of the substantial components of its Marine Controls segment for cash consideration of $238.6 million. This amount is subject to completion of a net working capital audit of the Marine Controls segment. CAE does not believe this provision will result in a material adjustment to the cash consideration received. In accordance with the purchase agreement, L-3 will also acquire two other components of the Marine Controls segment, including the assumption of the CAE's guarantee of $53.0 million (£23.0 million) of project finance related debt for the U.K. Astute Class submarine training program. The sale of these components is subject to regulatory approvals and expected to be completed during fiscal 2006. The expected proceeds on the sale of these components are nominal.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The results of Marine have been reported as discontinued operations and previously reported statements have been reclassified. Interest expense relating to debt not directly attributable to the continuing operations and expected to be paid with the proceeds of the sale of the Marine business has been allocated to the discontinued operations based on their share of net assets. This transaction resulted in a gain of $103.9 million, net of taxes of $25.1 million.

For the 10-month period starting on April 1, 2004 and ending at the closing of the transaction, Marine's revenues amounted to $109.6 million compared to $154.8 million for the 12-month period ended March 31, 2004. Apart from the difference in the number of days between this year and last year the decline is primarily due to continuing customer delays, which consequently led to delays in recognition of revenues as well as lower volume from some of Marine's larger programs.

Net earnings for the divested Marine business, excluding the gain on sale, amounted to $5.5 million, $14.5 million lower than the same period last year due to the same reasons as mentioned above.

SERVICIOS DE INSTRUCTION DE VUELO, S.L.

In February 2004, CAE and Iberia Lineas Aereas de Espana, SA ("Iberia") agreed to combine their aviation training operations in Spain after receiving regulatory clearance from the Spanish authorities to commence operations, under an agreement entered in October 2003.

On May 27, 2004, in connection with the financing of the combined operation, CAE Servicios Globales de Instruccion de Vuelo (Espana), S.L. ("SGIV"), a wholly owned subsidiary of CAE, and Iberia contributed the net assets of their respective training centre facilities to Servicios de Instruccion de Vuelo, S.L. ("SIV"), with SGIV obtaining ownership of 80% of SIV. SIV financed the acquisition of the assets from SGIV and Iberia through an asset-backed financing transaction (refer to Note 11 of the consolidated financial statements). As part of this transaction, should the October 2003 agreement be terminated, SGIV and Iberia will be obliged to repurchase the assets they contributed, in proportion to the fair market value of the assets, for a total amount equal to the outstanding balance under the financing transaction.

GREENLEY & ASSOCIATES INC.

On November 30, 2004, the Company acquired all the issued and outstanding shares of Greenley & Associates Inc. ("G&A"), now known as CAE Professional Services, which provides services in the areas of project management, human factors, modelling and simulation. Total consideration for this acquisition was $4.4 million payable in equivalent common shares issued by CAE in four instalments as follows: 424,628 shares (representing $2.0 million) at the closing date, $0.8 million on November 30, 2005, $0.8 million on November 30, 2006 and 169,851 shares (representing $0.8 million) to be issued on November 30, 2007. The number of shares issued (to be issued) to satisfy the first and the fourth payments was calculated based on the average closing share price of CAE common shares on the Toronto Stock Exchange ("TSX") for the 20-day period ending two days prior to November 30, 2004. The number of shares to be issued to satisfy the second and third payments will be based on the average closing share price of CAE common shares on the TSX for the 20-day period ending two days before their respective date of issuance. The purchase price is subject to an adjustment based on performance of the business for the 12-month period following the acquisition. Any changes in the total consideration will be accounted for as a change in goodwill.

FLIGHT TRAINING CENTRE CHILE S.A.

On April 22, 2004, the Company acquired from LAN Chile S.A. all the issued and outstanding shares of Flight Training Centre Chile S.A. ("FTC Chile") located in Santiago, Chile, for a total cash consideration of $0.9 million (US$0.7 million). This acquisition expands the Company's pilot-training operations into the growing South American market.

These acquisitions and business combinations were accounted for using the purchase method and operating results have been included from their respective acquisition date (Refer to Note 2 of the consolidated financial statements).

LIQUIDITY

The Company's financing needs are met through internally generated cash flow, available funds under credit facilities, and direct access to capital markets for additional long-term capital resources. CAE considers that its present and expected capital resources and current credit facilities will enable it to meet all its current and expected financial requirements for the foreseeable future.

The Company plans to generate sufficient cash from operating activities in fiscal 2006 to pay for capital expenditures and dividends. CAE also expects to be able to repay contractual obligations maturing in 2006 and future years through cash on hand, cash generated from operations or by issuing new debt.

During the final quarter of fiscal 2005, the Company disposed of it's Marine segment for US$196.8 million. The proceeds of disposal were used to substantially reduce the borrowings under the revolving credit facilities as well as project financing related to its Brazil Training Centre.

MANAGEMENT'S DISCUSSION AND ANALYSIS

SOURCES OF LIQUIDITY

CAE maintains committed bank lines at floating rates, each provided by a syndicate of lenders. These credit facilities permit the Company and certain designated subsidiaries to borrow funds directly for operating and general corporate purposes. The total available amount of committed bank lines at March 31, 2005, was $580.3 million, of which 5% ($30.4 million) was utilized. As at March 31, 2004, the total available was $619.8 million, of which 49% ($305.3 million) was utilized. The decrease of total availability results from the fact that the committed lines are denominated in U.S. dollars and Euros and thus the appreciation of the Canadian dollar against these currencies has created a reduction in availability in Canadian dollar equivalent. The decrease in total utilization was mainly due to the repayment of debt subsequent to the disposal of the Marine business.

In connection with the impairment charge taken during the third quarter of fiscal 2005, CAE obtained amendments to certain definitions related to financial covenants from both its banking syndicate, with respect to the unsecured revolving credit facilities, and its senior note holders. These amendments resulted in the Company being compliant with the financial covenants associated with each agreement. As at March 31, 2005 CAE is in full compliance with its financial covenants.

CAE also has the ability to borrow under non-committed operating lines in various currencies for up to $31.0 million, of which $11.2 million was drawn as at March 31, 2005.

As at March 31, 2005, CAE had long-term debt totalling $342.9 million. This compared to long-term debt of $584.3 million as at March 31, 2004. As at March 31, 2005, the short-term portion of the long-term debt was $35.3 million compared to $8.8 million as at March 31, 2004. The increase in the short-term portion results mainly from the classification of a June 2005 maturity of a $20 million senior notes. The decrease of total debt results from repayments of borrowings under the revolving credit facilities and the Brazil Training Centre debt offset by an increase in debt assumed for the CAE-Iberia training centre and additional debt due to the consolidation of previously treated off-balance sheet debt, subsequent to the implementation of AcG-15. Refer to *Variable Interest Entities for further information.*

Under an agreement dated March 24, 2005, the Company has the possibility to sell third party receivables on a non-recourse basis to a financial institution for an amount of up to $25.0 million. Under the terms of the agreement, the Company will continue to act as collection agent. A: at March 31, 2005, $16.5 million of specific accounts receivable were sold to the financial institution pursuant to this agreement. Net proceeds of the sale were used to repay borrowings under the Company's committed credit facilities.

DIVIDENDS

During fiscal 2005, the Board of Directors took the decision to reduce the quarterly dividend to $0.01, conserving $20 million of cash annually. With the current dividend policy and with the 248.1 million common shares outstanding as at March 31, 2005, CAE expects to pay annual dividends of approximately $10 million.

CONTRACTUAL OBLIGATIONS

In the normal course of business, CAE enters into certain contractual obligations and commercial commitments, such as debentures and notes, letters of credit and others. The table below provides a summary of the Company's contractual obligations of the various components and maturities of the Company's long-term debt for the year ended March 31, 2005.

CONTRACTUAL OBLIGATIONS

(amounts in millions)	2006	2007	2008	2009	2010	THEREAFTER	TOTAL
Long-term debt	32.8	43.8	46.5	21.7	84.2	94.6	323.6
Capital lease	2.5	1.9	1.3	0.2	0.1	13.3	19.3
Operating leases	80.8	84.8	72.7	59.4	55.4	361.5	714.6
Purchase obligations	12.8	10.0	11.4	11.9	11.3	67.0	124.4
Other long-term obligations	4.3	3.4	2.2	2.2	2.1	2.5	16.7
Total	**133.2**	**143.9**	**134.1**	**95.4**	**153.1**	**538.9**	**1,198.6**

The long-term debt includes $30.4 million drawn under CAE's committed credit facilities maturing in fiscal 2007. The Company has begun work on the renegotiations of the facilities on a similar basis, and intends to complete this in the course of fiscal 2006. The total availability of the committed credit facilities is equal to $580.3 million.

Rental expense related to operating leases was $94.0 million in fiscal 2005 compared to $92.5 million in fiscal 2004. The sale and leaseback of certain FFS installed in the Company's global network of training centres accounted for $42.7 million of the total rental expense.

Other purchase obligations are related to agreements to purchase goods or services that are enforceable and legally binding on CAE and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Principally, the purchase obligations are related to agreements with subcontractors to provide services in the context of long-term contracts with the Company's clients.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Other long-term obligations include a total of $10.3 million of repayments under various government assistance programs.

As at March 31, 2005 CAE had other long-term liabilities that were not included in the table above. They consisted of some accrued pension liabilities, deferred revenue and gains on assets and various other long-term liabilities. Cash obligations of accrued employee pension liability depend on various elements such as market returns, actuarial losses and gains and interest rate.

CAE did not include future income tax liabilities since future payments of income taxes depend on the amount of taxable earnings and on whether there are tax loss carry-forwards available to reduce income tax liabilities.

COMMITMENTS

CAE's commitments for capital expenditures include investments to add new facilities to its training centre network in order to meet customer demand. R&D expenditures are incurred to provide new products to the marketplace, as alternative ways of training are developed and different types of training equipment are needed for our clients training needs.

OFF-BALANCE SHEET ARRANGEMENTS

GUARANTEES

In the normal course of business, CAE issued letters of credit and performance guarantees for a total amount of $73.3 million at March 31, 2005, compared to $168.6 million at March 31, 2004. The reduction results mainly from the expiry of advance payment guarantees related to the completion of one major project ($36.9 million) and many smaller projects, as well as the reduction of guarantees issued in support of the project financing for the Brazil training centre ($37.0 million).

SALE AND LEASEBACK TRANSACTIONS

A key element of CAE's finance strategy to support the investment in its Civil training business is the sale and leaseback of certain FFS installed in the Company's global network of training centres. This provides CAE with a cost-effective long-term source of fixed-cost financing. A sale and leaseback transaction can only be executed after the FFS has achieved certification by regulatory authorities (i.e., the FFS is installed and is available to customers for training). Prior to completing a sale and leaseback transaction, CAE records the cost to manufacture the simulator as a capital expenditure, which is included as a fixed asset on the Company's balance sheet. On the execution of a sale and leaseback transaction, CAE records the transaction as a disposal of a fixed asset. The cash proceeds received on the disposal approximate the fair market value of the FFS. The difference between the proceeds received and CAE's cost to manufacture (approximately the margin that CAE would record if it had a completed FFS sale to a third party) is recorded under deferred gains and other long-term liabilities and is then amortized over the term of the sale and leaseback transaction as a reduction of rental expense, net of the guaranteed residual value where appropriate. At the end of the term of the sale and leaseback transaction, the guaranteed residual value is taken into income should no reduction occur in the value of the underlying FFS.

During fiscal 2005 CAE sold and leased back three FFS for net proceeds of $43.8 million. The following is a summary as at March 31, 2005 of the existing sale and leaseback transactions for FFS' currently in service in Civil's training locations, accounted for as operating leases on CAE's financial statements.

EXISTING FULL-FLIGHT SIMULATORS UNDER SALE AND LEASEBACK

(amounts in millions, unless otherwise noted)	FISCAL YEAR	NUMBER OF SIMULATORS (UNITS)	LEASE OBLIGATION	INITIAL TERM (YEARS)	IMPUTED INTEREST RATE	UNAMORTIZED DEFERRED GAIN	RESIDUAL VALUE GUARANTEE
SimuFlite	2002 to 2005	14	$ 211.4	10 to 20	5.5% to 6.7%	$ 13.1	$ —
Toronto training centre	2002	2	42.7	21	6.4%	16.2	9.2
Air Canada training centre	2000	2	33.1	20	7.6%	14.9	8.3
Denver/Dallas training centres	2003	5	86.9	20	5.0%	30.9	—
China Southern joint venture[1]	2003	5	22.7	15	3.0%	—	—
Others	—	7	26.3	3 to 10	2.9% to 10.1%	15.6	15.6
		35	$ 423.1			$ 90.7	$ 33.1
Annual Lease Payments (upcoming 12 months)			$ 38.7				

1 Joint venture in which CAE has a 49% interest.

Future minimum lease payments for such arrangements, amounting to $423.1 million as at March 31, 2005, are included in Note 20 "Operating Lease Commitments" to the consolidated financial statements.

MANAGEMENT'S DISCUSSION AND ANALYSIS

NON-RECOURSE PROJECT FINANCING

During 1997, the Company arranged project financing for the Medium Support Helicopter ("MSH") program it entered into with to the U.K. Ministry of Defence. The contract was awarded to a consortium, CAE Aircrew Training Services Plc ("Aircrew"). The capital value of the assets supplied by Aircrew, is in excess of $200 million. The entity that owns the assets operated by the training centre is CVS Leasing Ltd. (in which CAE has a 14% interest). CAE manufactured and sold the simulators to CVS Leasing Ltd., and CVS Leasing Ltd. then leased this equipment to Aircrew for the full term of the MSH contract. As Aircrew is majority-controlled by CAE, its financial statements are consolidated in the Company's results. Future minimum lease payments associated with the simulators leased to Aircrew amount to approximately $187 million as at March 31, 2005, and are included in the amount disclosed in Note 20 "Operating Lease Commitments" of the consolidated financial statements as well as in the operating leases presented as contractual obligations in the liquidity section herein.

FINANCIAL INSTRUMENTS

The Company enters into forward, swap and option contracts to manage its exposures to fluctuations in foreign exchange rates, interest rates, and changes in share price. CAE assesses on an ongoing basis whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items. CAE deals only with sound counter parties in executing any of its derivative financial instruments.

CAE employs foreign exchange forward contracts to manage exposures created when sales are made in foreign currencies. The amount and timing of the maturity of these forward contracts varies according to a number of project-related factors, including milestone billings and the use of foreign materials and/or subcontractors. As at March 31, 2005, CAE had $305.0 million Canadian equivalent in forward contracts compared to $181.4 million Canadian dollar equivalent in forward contracts as at March 31, 2004. The increase is mainly due to additional hedging due to hedging of most of the new contracts signed during the last fiscal year.

CAE also uses financial instruments to manage its exposure to changing interest rates and to adjust its mix of fixed and floating interest rate debt at a desirable level. The mix of fixed rate versus floating rate debt on its long-term debt was 70% versus 30%, respectively, as at March 31, 2005. The variation in the mix since March 31, 2004, when it stood at 40% versus 60%, respectively, is due mainly to the decrease in borrowing under the revolving credit facility, which was mostly all, except for $35.0 million, on a floating rate basis. CAE had interest rate swaps converting mostly floating rate long-term debt into fixed rate long-term debt totalling $65.8 million, as at March 31, 2005, compared to $114.6 million as at March 31, 2004. The difference resulted from the termination of a floating to fixed swap as a result of the reduction in floating rate borrowings and partly from the lower amount of Canadian equivalent of the foreign denominated swaps due to the appreciation of the Canadian dollar.

As well, CAE reduced its exposure to the fluctuation in its share price, which impacts the cost of the management compensation deferred share unit ("DSU") programs. As at March 31, 2005, the hedging contract covered 600,000 shares of the Company, compared to 700,000 shares as at March 31, 2004. During fiscal 2005, the amount had been increased to 800,000 and subsequently reduced to the year-end position of 600,000 in order to reflect the variation in the amount of DSUs outstanding.

BUSINESS RISKS AND UNCERTAINTIES

CAE operates in different industry segments that involve various risk factors and uncertainties, which are carefully considered in the Company's Management policies. The risk factors and uncertainties stated below may impact the implementation of CAE's strategy.

EXECUTION OF THE RESTRUCTURING

CAE's future success depends in part on the ability of its current management team to timely deploy the restructuring plan described in *Restructuring Charges.*

PRODUCT RELIABILITY

CAE's success in civil aviation and military markets depends fundamentally on the reliability of its products, the quality of its services and its ability to adapt, in a timely manner, to changing customer needs and industry standards. The Company operates in different industry segments and global markets that involve various risk factors and uncertainties, including worldwide economic and political trends and developments.

CIVIL AVIATION INDUSTRY

CAE operates in the civil simulation equipment and training services markets, both of which are heavily dependent on demand for air transportation and the financial condition of commercial airlines. The major airline bankruptcies in Europe, the U.S., Canada and other CAE markets pose risks to CAE as an unsecured vendor and/or service provider to these and other potentially insolvent customers. Demand for simulation equipment tends to follow the trend established in the commercial airline industry, particularly the delivery of new aircraft. Any reduced demand may in turn lead to reduced production levels, which impacts margins negatively. The utilization of CAE's installed base of simulators in its training network depends on the extent to which simulated aircraft types match the configuration of in-use aircraft, as well as on the overall level of commercial air traffic.

CAE must comply with rules imposed by regulatory authorities that may change without notice, resulting in potential disruptions to sales and operations. The sale or licensing of virtually all of CAE's products is subject to various regulatory controls that change with some frequency.

LEVEL OF GOVERNMENT EXPENDITURES

CAE's Military business depends heavily on government programs and contracts that ultimately reflect the level of government expenditures directed towards national defence budgets (particularly capital equipment programs), the priority of various programs within defence budgets and in certain instances, the maintenance of government programs supporting R&D. Programs may be only partially funded pending future appropriations and may contain provisions permitting termination at the government's convenience, in whole or in part, without prior notice, upon payment of limited compensation. Government-funded military programs are also heavily regulated, and the regulation of certain government purchasing agencies limit the range of reimbursable costs in fixed-price contracts, including most financing costs and the amortization of various intangible assets.

CANADIAN DOLLAR

Fluctuations in the value of the Canadian dollar relative to foreign currencies could result in currency exchange gains and losses. Current hedging activities may not be successful.

COMPETITION

CAE operates in intensely competitive markets. Some of its competitors, particularly in military markets, possess substantially greater resources, well-established relationships with various procuring organizations and a greater in-country presence that may give them an advantage in winning contracts. Some competitors may benefit more, or suffer less, than CAE from currency fluctuations.

LENGTH OF SALES CYCLE

CAE's often lengthy and unpredictable sales cycle could result in volatility in its operating results. The Company must invest significant amounts of time and resources educating and informing potential customers about the benefits of products and services (particularly government agencies with lengthy internal budgeting approval and competitive evaluation processes), with no guarantee of compensatory revenue.

TECHNOLOGY

CAE's business could be harmed if its products do not successfully integrate or operate with other sophisticated and continually evolving software, computing and communications systems. If CAE experiences difficulties or does not meet project milestones in a timely manner, the Company could be obligated to devote more engineering and other resources to a particular project than originally anticipated. While CAE believes it has recorded adequate provisions for losses on fixed-price contracts, obligations under fixed-price and long-term supply contracts could subject the Company to contract losses in excess of provisions.

FINANCIAL CONDITION OF CUSTOMERS

CAE's ability to complete contracted sales included in its order backlog is dependent on the long-term financial condition of the contracting customers. In addition, approximately 60% of the backlog is comprised of long-term contracts where revenues are guaranteed or expected, based on current customer requirements. The contracting customer may terminate these contracts, unilaterally, if it desires.

PROTECTION OF INTELLECTUAL PROPERTY

CAE's ability to protect its intellectual property is limited and unauthorized parties may be able to use CAE's technology or products in ways that weaken CAE's competitive position. Reliance on the intellectual property of others, including data concerning the functions, design and performance characteristics of a product or system in the process of being simulated, could prevent or delay performance. Future litigation related to the defence of CAE's intellectual property rights or involving infringement claims brought against CAE or a customer could be lengthy and costly, with no assurance of success.

DOING BUSINESS IN FOREIGN COUNTRIES

CAE is subject to the risks of doing business in foreign countries, including: changes to laws and regulations in host countries; the cost and complexity of using foreign representatives and consultants; the imposition of tariffs, embargoes, controls and other restrictions impeding the free flow of goods, information and capital; the difficulties of managing and operating an enterprise and complying with laws in multiple jurisdictions; and general changes in economic and geopolitical conditions.

ENVIRONMENTAL LAWS AND REGULATIONS

CAE may be subject to liabilities imposed by new environmental laws and regulations or contractual indemnities; product liability and warranty claims or liabilities arising out of accidents or disasters involving aircraft or power plants for which CAE has provided training products or services. CAE cannot be certain that existing insurance coverage, if applicable to any such claims, will be sufficient to cover one or more substantial claims.

KEY PERSONNEL

CAE's continued success will depend in part on the ability to retain and attract key personnel with the relevant skills, expertise and experience. The Company applies a compensation policy designed to mitigate this risk.

MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL STATEMENTS DISCLOSURE

SIGNIFICANT CHANGES IN ACCOUNTING STANDARDS-FISCAL 2003 TO FISCAL 2005

Canadian Institute of Chartered Accountants ("CICA") Handbook Sections, Accounting Guidelines ("AcG") and Emerging Issues Committee Abstracts ("EIC")

CONSOLIDATION OF VARIABLE INTEREST ENTITIES

On January 1, 2005, the Company adopted AcG-15 *Consolidation of Variable Interest Entities* on a retroactive basis without restatement of prior periods. AcG-15 provides a framework for identifying variable interest entities ("VIEs") and determining when an entity should include the assets, liabilities and results of operations of a VIE in its consolidated financial statements.

In general, a VIE is a corporation, partnership, limited-liability corporation, trust, or any other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has a group of equity owners that are unable to make significant decisions about its activities, or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

AcG-15 requires a VIE to be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a variable interest holder) is exposed to a majority of the risk of loss from the VIE's activities, is entitled to receive a majority of the VIE's residual returns (if no party is exposed to a majority of the VIE's losses), or both (the primary beneficiary). Upon consolidation, the primary beneficiary generally must initially record all of the VIE's assets, liabilities and non-controlling interests at fair value at the date the enterprise became the primary beneficiary. However, for variable interest entities created prior to the initial adoption of AcG-15, the assets, liabilities and non-controlling interest of these entities must be initially consolidated as if the entities were always consolidated based on majority voting interest. AcG-15 also requires disclosures about VIEs that the variable interest holder is not required to consolidate, but in which it has a significant variable interest.

The adoption of AcG-15 on January 1, 2005 resulted in an increase in total assets, total liability, and retained earnings of $46.4 million, $43.2 million, and $3.3 million, respectively and a decrease in the currency translation adjustment of $0.1 million.

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES AND FINANCIAL STATEMENT PRESENTATION

On April 1, 2004, the Company adopted CICA Handbook Section 1100 *Generally Accepted Accounting Principles* and Section 1400 *General Standards of Financial Statement Presentation*. Section 1100 describes what constitutes Canadian GAAP and its sources, and provides guidance on sources to consult when selecting accounting policies and appropriate disclosure when a matter is not dealt with explicitly in the primary sources of GAAP, thereby recodifying GAAP hierarchy. Section 1400 clarifies what is fair presentation in accordance with GAAP and provides general guidance on financial presentation. The adoption of these standards did not have any material effect on the Company's consolidated financial statements.

HEDGING RELATIONSHIPS

Effective April 1, 2004, the Company adopted prospectively AcG-13 *Hedging Relationships* and EIC-128 *Accounting for Trading, Speculative or Non-Hedging Derivative Financial Instruments.* This guideline addresses identification, designation, documentation and effectiveness of hedging relationship for the purpose of applying hedge accounting, and the discontinuance of hedge accounting. Under this guideline, complete documentation of the information related to hedging relationships is required and the effectiveness of the hedges must be demonstrated and documented. The adoption of this guideline did not have a material impact on the Company's financial statements.

EMPLOYEE FUTURE BENEFITS

Effective April 1, 2004, CAE adopted the CICA Handbook Section 3461 *Disclosure Requirements Employee-Future Benefits.* The new required disclosures include items such as a narrative description of each type of plan, the measurement date of the plan asset and liability, the effective date of the last actuarial evaluation and the detail of the plan asset by major category.

STOCK-BASED COMPENSATION

Effective April 1, 2003, CAE commenced prospectively expensing its stock-based compensation using the fair value method, as prescribed by CICA Handbook Section 3870 *Stock-based Compensation and Other Stock-based Payments.* Since that date, the compensation cost for the Company's stock options has been recognized in net earnings, with a corresponding credit to contributed surplus (refer to Note 13 of the consolidated financial statements).

IMPAIRMENT OF LONG-LIVED ASSETS

Effective April 1, 2003, the Company adopted CICA Handbook Section 3063 *Impairment of Long-Lived Assets* which requires the recognition of an impairment loss for a long-lived asset to be held and used when events or changes in circumstances cause its carrying value to exceed the total undiscounted cash flows expected from its use and eventual disposition. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its fair value. It replaces the impairment provision in Section 3061 *Property, Plant and Equipment.* In the third quarter of 2005, the Company proceeded with a write-down of $78.4 million on its Long-Lived Assets (refer to *Impairment of goodwill, intangible and tangible assets* and to Note 4 of the consolidated financial statements).

MANAGEMENT'S DISCUSSION AND ANALYSIS

DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS

Effective April 1, 2003, the Company adopted CICA Handbook Section 3475 *Disposal of Long-Lived Assets and Discontinued Operations,* which provides guidance on recognizing, measuring, presenting and disclosing long-lived assets to be disposed of. It replaces the disposal provisions in Section 3061 *Property, Plant and Equipment,* and supersedes the former Section 3475 *Discontinued operations.* Under this section, an asset classified as held for sale is measured at the lower of its carrying amount or fair value less disposal costs, and is not depreciated while classified as held for sale.

DISCLOSURE OF GUARANTEES

Effective March 31, 2003, the Company adopted AcG-14 *Disclosure of Guarantees,* which requires disclosure of information concerning certain types of guarantees that may require payments, contingent on specified types of future events (refer to Note 14 of the consolidated financial statements).

SEVERANCE, TERMINATION BENEFITS AND COSTS ASSOCIATED WITH EXIT AND DISPOSAL ACTIVITIES

Effective April 1, 2003, the Company prospectively adopted the new EIC-134 *Accounting for Severance and Termination Benefits* and EIC-135 *Accounting for Costs Associated with Exit and Disposal Activities (Including Costs Incurred in a Restructuring)* relating to exit or disposal activities after March 31, 2003. These abstracts provide guidance on the timing of recognition and measurement of liabilities as well as disclosures for the various types of severance and termination benefits related to the termination of employees' services prior to normal retirement and costs associated with an exit or disposal activity. Under this new guidance, liabilities for these costs are to be recognized in the period when they are incurred and measured at their fair value. CAE applied these guidelines in EIC-134 for severance and other costs (as described in Note 24 of the consolidated financial statements).

REVENUE RECOGNITION

In December 2003, the Emerging Issues Committee issued EIC-141 *Revenue Recognition,* summarizing the principles set forth in Staff Accounting Bulletin 101 ("SAB 101") of the United States Securities and Exchange Commission and providing general interpretive guidance on the application of revenue recognition accounting principles. These recommendations were effective for CAE's fiscal year beginning April 1, 2004. The adoption of this abstract did not have any material effect on CAE's consolidated financial statements.

REVENUE ARRANGEMENTS WITH MULTIPLE DELIVERABLES

Also in December 2003, EIC-142 *Revenue Arrangements with Multiple Deliverables* was issued. EIC-142 addresses certain aspects of the accounting by a vendor for arrangements under which multiple revenue-generating activities will be performed. These recommendations were effective for CAE's fiscal year beginning April 1,2004. The adoption of this abstract did not have any material effect on CAE's consolidated financial statements.

FUTURE CHANGES IN ACCOUNTING STANDARDS

FINANCIAL INSTRUMENTS-RECOGNITION AND MEASUREMENT, HEDGES AND COMPREHENSIVE INCOME

In January 2005 the ASB issued three new standards dealing with financial instruments; (i) Financial Instruments-Recognition and Measurement; (ii) Hedges; and (iii) Comprehensive Income. The new standards are based on the US FASB Statement 133, Accounting for Derivative Instruments and Hedging Activities, and on the International Accounting Standards ("IAS") Board's new standard, IAS 39, Financial Instruments-Recognition and Measurement. These requirements will be applicable for CAE in the first quarter of fiscal 2007. The Company is currently evaluating the impact of these new Handbook Sections on its financial statements.

The Handbook Section 3855 *Financial Instruments, Recognition and Measurement prescribes* when a financial instrument is to be recognized on the balance sheet and the measurement method used, fair value or cost-based. It also specifies how financial instrument gains and losses are to be presented.

The new Handbook Section 3865 *Hedges* allows optional treatment providing that hedges be designated as either fair value hedges, cash flow hedges or hedges of a net investment in a self-sustaining foreign operation. For a fair value hedge, the gain or loss attributable to the hedged risk is recognized in net income in the period of change together with the offsetting loss or gain on the hedged item attributable to the hedged risk. The carrying amount of the hedged item is adjusted for the hedged risk. For a cash flow hedge or for a hedge of a net investment in a self-sustaining foreign operation, the effective portion of the hedging item's gain or loss is initially reported in other comprehensive income and subsequently reclassified to net income when the hedged item affects net income.

The ASB has issued new Handbook Section 1530 *Comprehensive Income,* and amended, Section 3250 *Surplus* to be renamed Section 3251 *Equity.* These standards require that an enterprise present comprehensive income and its components, as well as net income in its financial statements; and that an enterprise present separately changes in equity during the period, as well as components of equity at the end of the period, including comprehensive income.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with GAAP requires CAE's Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the period reported. On an ongoing basis, Management reviews its estimates, particularly as they relate to accounting for long-term contracts, useful lives, employee future benefits, income taxes, impairment of long-lived assets and goodwill, based on Management's best knowledge of current events and actions that the Company may undertake in the future. Significant changes in estimates and/or assumptions could result in impairment of certain assets. Actual results could differ from those estimates.

CAE's critical accounting policies are those that it believes are the most important in determining its financial condition and results, and require significant subjective judgment by Management. See Note 1 of the consolidated financial statements for a description of the Company's accounting policies. The Company considers an accounting estimate to be critical if the estimate requires Management to make assumptions about matters that were highly uncertain at the time the estimate was made, if different estimates could have been reasonably used or if changes in the estimate that would have a material impact on CAE's financial condition or results of operations are likely to occur from period to period.

A summary of the Company's significant accounting policies, including the critical accounting policies discussed below, is set out in the notes to the consolidated financial statements.

REVENUE RECOGNITION

Revenue from long-term contracts for the design, engineering and manufacturing of FFS is recognized, when recovery is reasonably certain, using the percentage-of-completion method. Revenue and earnings are recorded as related costs are incurred, on the basis of the percentage of actual costs incurred to date, relative to the estimated total costs to complete the contract. Accounts receivable, unbilled receivables and deposit on contract are recorded based on the payment schedule for such contracts, the terms of long-term contracts provide for progress billings based on completion of certain phases of work. Warranty provisions are recorded at the time revenue is recognized, based on past experience. Post-delivery customer support is billed separately and revenue is generally recognized over the support period.

The Company conducts quarterly reviews of its total estimated costs on long-term contracts. The effect of any revision is accounted for by way of a cumulative catch-up in the period in which the revision takes place. Losses on contracts, if any, are recognized fully when first anticipated.

For Military, full-flight mission simulators are more complex and the time to design and manufacture is at least two years. There are fewer repeat orders and the level of non-recurring cost in each simulator could be significant, making the predictability of total costs more difficult when compared to a Civil FFS.

With the focus of the Civil business on training, the number and amount of long-term contracts is down considerably from prior years. The cost of a FFS is very predictable particularly for repeat or common simulator types such as an A320 or B737. No revenue is recorded for FFS built for CAE's own training centres. The cost is reflected as a capital expenditure. Revenue derived from training is recorded when the training event occurs.

INCOME TAXES

The Company uses the tax liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined according to differences between the carrying value and the tax bases of assets and liabilities. This method also requires the recognition of future tax benefits such as net operating loss carry-forwards to the extent that realization of such benefits is more likely than not. Future tax assets and liabilities are measured by applying enacted or substantively enacted rates and laws at the date of the financial statements for the year for which the temporary differences are expected to reverse. CAE does not provide for income taxes on undistributed earnings of foreign subsidiaries that are not expected to be repatriated in the foreseeable future.

A valuation allowance is recognized to the extent that, in the opinion of Management, it is more likely than not that the future income tax assets will not be realized (Refer to Note 15 of the consolidated financial statements).

CAE is subject to examination by the taxation authorities in various jurisdictions. The Company provides for potential tax liabilities based on Management's best estimates. Differences between these estimates and the ultimate amounts of tax liabilities are recorded in earnings at the time they can be determined.

VALUATION OF GOODWILL AND INTANGIBLE ASSETS

Goodwill is no longer amortized, but instead tested for impairment, at least annually or more frequently if events or changes in circumstances indicate that it might be impaired.

The impairment test consists of a comparison of the fair value of the Company's reporting units with their carrying amount. When the carrying amount of the reporting unit exceeds the fair value, the Company compares, in a second step, the fair value of goodwill related to the reporting unit to its carrying value and recognizes an impairment loss equal to the excess. The fair value of a reporting unit is calculated based on one or more generally accepted valuation techniques.

The Company performs the annual review of goodwill as at December 31 of each year, and based on the impairment test performed as at December 31, 2004, CAE concluded that a goodwill impairment charge was required (refer to Note 4 of the consolidated financial statements).

CAE accounts for its business combinations under the purchase method of accounting, which requires that the total cost of an acquisition be allocated to the underlying net assets based on their respective estimated fair values. Part of this allocation process requires that the Company identify and attribute values and estimated lives to the intangible assets acquired. These determinations involve considerable judgment, and often involve the use of significant estimates and assumptions, including those with respect to future cash flows, discount rates and asset lives. These determinations subsequently affect the amount of amortization expense to be recognized in future periods, over the intangible assets' estimated useful lives.

DEFERRED DEVELOPMENT COSTS

Where CAE intends to produce or market a product under development that is clearly defined, has identifiable costs, is technically feasible, and has a clearly defined market or use, and the Company expects to have the financial resources to complete the project, the costs associated with the project are deferred (as per CICA Handbook Section 3450 *Research and Development Costs)* to the extent their recovery through future sales or use of the product is reasonably assured. This requires CAE to make judgments about the likelihood of recovery of the costs or assets if deferred. If the Company determines that recovery of the costs through future sales or use is no longer likely, deferred costs are charged against earnings in the period in which it becomes likely that the costs will not be recovered. Once the project is complete, CAE amortizes the deferred costs by reference to sales or use of the product over a period not to exceed five years (refer to Note 10 of the consolidated financial statements).

PRE-OPERATING COSTS

The Company defers costs incurred during the pre-operating period for all new training centres. Pre-operating costs are incremental in nature and are considered by Management to be recoverable from the future operations of the new training centre. Capitalization ceases at the opening of the training centre. Amortization of the deferred pre-operating costs is taken over five years in respect to civil training operations.

DEFERRED FINANCING COSTS

Costs incurred relating to the issuance of long-term debt are deferred and amortized on a straight-line basis over the term of the related debt. Costs related to sale and leaseback agreements are amortized on a straight-line basis over the term of the lease (refer to Note 10 of the consolidated financial statements).

EMPLOYEE FUTURE BENEFITS

The Company maintains defined benefit pension plans that provide benefits based on length of service and final average earnings. The service costs and the pension obligations are actuarially determined using the projected benefit method prorated on employee service and Management's best estimate of expected plan investment performance, salary escalation and retirement ages of employees. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the remaining service period of active employees. Past service costs, arising from plan amendments, are deferred and amortized on a straight-line basis over the average remaining service period of active employees at the date of amendment.

When a curtailment arises, any unamortized past service cost associated with the reduction of future services is recognized immediately. Also, the increase or decrease in benefit obligation is recognized as a loss or a gain net of unrecognized actuarial gains or losses. Finally, when the restructuring of a benefit plan gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to settlement (refer to Note 21 of the consolidated financial statements).

DISCLOSURE OF OUTSTANDING SHARE DATA

CAE's articles of incorporation authorize the issuance of an unlimited number of common shares, and an unlimited number of preferred shares, issuable in series. To date, the Company has not issued any preferred shares. As at March 31, 2005, CAE had 248,070,329 common shares issued and outstanding. As at the same date, the Company had 8,208,675 options outstanding, of which 3,731,085 were exercisable.

SYSTEMS, PROCEDURES AND CONTROLS

Management is responsible for establishing appropriate information systems, procedures and controls to ensure that all financial information disclosed externally, including this MD&A, and used internally by Management, is complete and reliable. These procedures include a review of the financial statements and associated information, including this MD&A, by the Audit Committee of the Board of Directors. The Company's Chief Executive Officer and Chief Financial Officer have a process to evaluate the applicable systems, procedures and controls and are satisfied they are adequate for ensuring that complete and reliable financial information is produced.

ADDITIONAL INFORMATION

Additional information relating to the Company, including its Annual Information Form ("AIF"), is available on-line at *www.sedar.com* as well as on the Company's website at *www.cae.com*.

EXHIBIT 4



PricewaterhouseCoopers LLP
Chartered Accountants
1250 René-Lévesque Boulevard West
Suite 2800
Montreal, Quebec
Canada H3B 2G4
Telephone +1 (514) 205 5000
Facsimile +1 (514) 205-5675

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the use in this Annual Report on Form 40-F of CAE Inc. for the year ended March 31, 2005, of our auditors' report dated May 10, 2005 on the consolidated balance sheets of CAE Inc. as at March 31, 2005 and 2004 and the consolidated statements of earnings, retained earnings and cash flows for each of the years in the three-year period ended March 31, 2005, and our related Comments by Auditor for U.S. Readers on Canada-U.S. Reporting Difference dated May 10, 2005.

We also consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-97185) of CAE Inc., relating to common shares to be offered to employees under employee benefit plans, of our auditors' report dated May 10, 2005 relating to the above-mentioned financial statements and of our related Comments by Auditors for U.S. Readers on Canada-U.S. Reporting Differences dated May 10, 2005.

/s/ PricewaterhouseCoopers LLP
Chartered Accountants

Montréal, Québec
June 28, 2005

PricewaterhouseCoopers refers to the Canadian firm of PricewaterhouseCoopers LLP and other members of the worldwide PricewaterhouseCoopers organization.

EXHIBIT 5

CERTIFICATION REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(a), PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Robert E. Brown, President and Chief Executive Officer of CAE Inc., certify that:

1. I have reviewed this annual report on Form 40-F of CAE Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the issuer and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Date: June 28, 2005

/s/ Robert E. Brown

Name: Robert E. Brown
Title: President and Chief Executive Officer

EXHIBIT 6

CERTIFICATION REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(a), PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Alain Raquepas, Vice-President Finance and Chief Financial Officer of CAE Inc., certify that:

1. I have reviewed this annual report on Form 40-F of CAE Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the issuer and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Date: June 28, 2005

/s/ Alain Raquepas

Name: Alain Raquepas
Title: Vice-President Finance and
Chief Financial Officer

EXHIBIT 7

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ENACTED PURSUANT TO
SECTION 906 OF THE U.S. SARBANES-OXLEY ACT OF 2002

CAE Inc. (the "Company") is filing with the U.S. Securities and Exchange Commission on the date hereof, its annual report on Form 40-F for the fiscal year ended March 31, 2005 (the "Report").

I, Robert E. Brown, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as enacted pursuant to section 906 of the U.S. Sarbanes-Oxley Act of 2002, that:

(i) the Report fully complies with the requirements of section 13(a) or 15(d) of the U.S. Securities Exchange Act of 1934; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Robert E. Brown
Robert E. Brown
President and Chief Executive Officer

Date: June 28, 2005

EXHIBIT 8

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ENACTED PURSUANT TO
SECTION 906 OF THE U.S. SARBANES-OXLEY ACT OF 2002

CAE Inc. (the "Company") is filing with the U.S. Securities and Exchange Commission on the date hereof, its annual report on Form 40-F for the fiscal year ended March 31, 2005 (the "Report").

I, Alain Raquepas, Vice-President Finance and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as enacted pursuant to section 906 of the U.S. Sarbanes-Oxley Act of 2002, that:

(i) the Report fully complies with the requirements of section 13(a) or 15(d) of the U.S. Securities Exchange Act of 1934; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Alain Raquepas
Alain Raquepas
Vice-President Finance and
Chief Financial Officer

Date: June 28, 2005