



advanced technologies

cae annual report for the year ended march 31, 1999

cae annual report
for the year ended march 31, 1999

cae at a glance

cae electronics group 5,000 employees

The CAE Electronics Group is the world leader in the design and manufacture of highly sophisticated commercial and military simulation equipment. The Group also offers leading-edge solutions for visual simulation systems, land-based systems simulators, aircrew selection systems, sensor stimulation systems, power plant simulators and control systems for marine applications and electric power generation, transmission, and distribution.



cae fiber processing technologies 1,175 employees

CAE Fiber Processing Technologies supplies leading-edge advanced sawmill optimization and sawing systems, specialized equipment for the manufacture of oriented strand board and advanced screening for pulp and paper.



cae cleaning technologies 480 employees

CAE Cleaning Technologies is a leading supplier of advanced technology cleaning, waste management equipment and chemistries. This Group provides a full range of leading-edge technologies, including spray and immersion, ultrasonics, and CO₂, to customers in the automotive, electronics, medical and industrial sectors.



cae railway technologies and services 240 employees

CAE Railway Technologies & Services is a leader in advanced maintenance technologies for North American Freight and Transit Railways. The company provides complete maintenance, repair and overhaul services for locomotive and freight car axles, as well as locomotive traction motor combos.

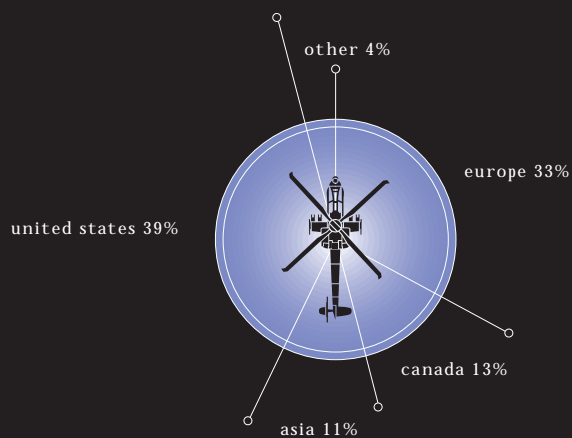


financial highlights

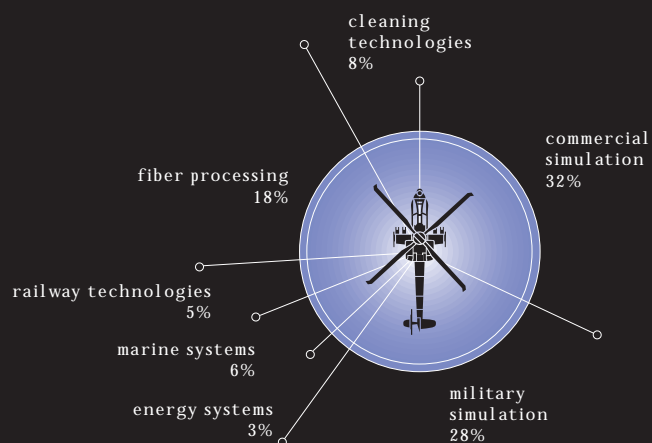
(amounts in thousands except per share amounts)

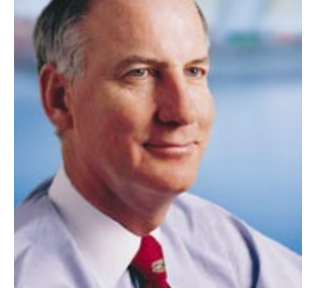
	1999	1998
operating results		
Revenue	\$ 1,070,061	\$ 922,369
Net earnings	\$ 77,342	\$ 70,236
financial position		
Total assets	\$ 1,101,157	\$ 928,179
Total debt, net of cash	\$ 273,541	\$ 68,116
per share		
Net earnings	\$ 0.70	\$ 0.64
Dividends	\$ 0.16	\$ 0.16
Shareholders' equity	\$ 3.03	\$ 2.50

geographic distribution of revenue



revenue by product line





letter from john e. caldwell

We believe there are three fundamental elements in building sustained value for shareholders – performance, strategy and resources.

At CAE, a number of years ago we set a simple performance goal – to double earnings and size every five years. I am proud to report since 1994, CAE's earnings have increased by 123% and revenue has grown by 81%. This represents compound growth rates of 17% and 13% respectively. In each of the five years we have earned a return of more than 25% on shareholders' equity.

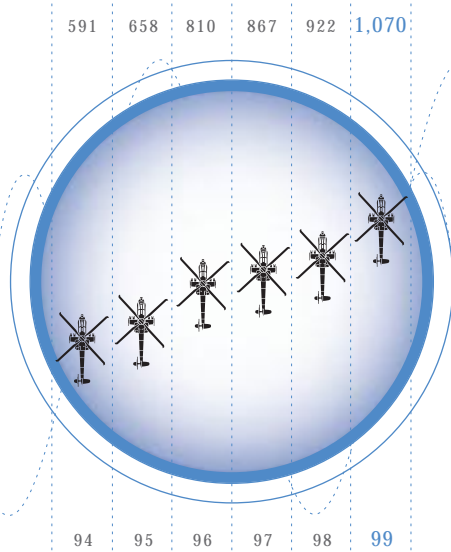
In fiscal 1999, revenue at \$1.070 billion was 16% above last year. Excluding non-recurring gains in fiscal 1998 results, net earnings advanced by 17%. These results were achieved in mixed markets. Civil simulation was particularly strong while the forest products and automotive sectors were depressed. Your company made four acquisitions in fiscal 1999 which generated accretive net earnings after financing costs.

Performance is more than financial results. Performance starts with customers. As you read through this report you will see numerous references to customers. Creating value for our customers ultimately creates value for shareholders.

The second component in value creation is strategy. Strategy must not only be focussed, comprehensive and dynamic, it also must be built around fundamental principles. We believe in designing, developing and building products which create high value for our customers and exceed their expectations. We are committed to innovation and technology leadership on a global scale. We are driven to retain world market leadership premised on high entry barriers and powerful competitive advantage. We are motivated and challenged by the opportunity for growth.

revenue

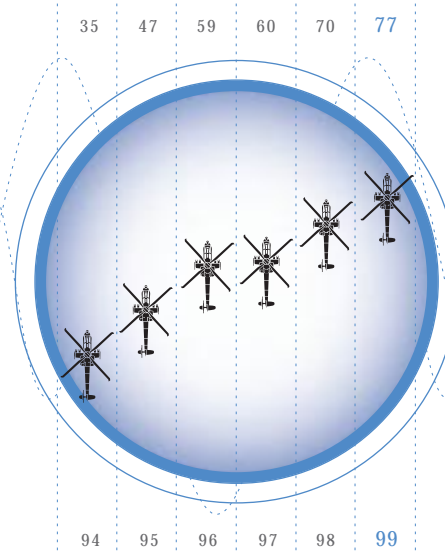
(from continuing operations,
in millions of dollars)



revenue rose 16 percent in fiscal 1999 due to higher commercial and military simulation sales and the contribution from acquisitions.

earnings

(from continuing operations,
in millions of dollars)



earnings in fiscal 1999 increased ten percent due to strong performance in simulation and the accretive impact, after financing costs, from acquisitions, excluding the positive effect of several non-recurring items in fiscal 1998, consolidated earnings increased by 17 percent.

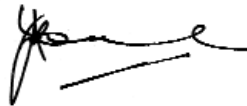
On pages six through nine of this report, we show a strategic framework for value creation. It is predicated on developing products incorporating technologies for data acquisition, data transformation and data application to add value to our customers' businesses. Few companies have the skills and proprietary technology to develop and integrate products with these three dimensions. The similarity of our simulation and sawmill optimization products and technologies, while on the surface not obvious, is well demonstrated in this model.

The best strategy cannot be executed without resources. With engineering skills in short supply throughout the world, understandably our people are in strong demand. We are determined to not only retain but to build upon our skills and diversity of capabilities. Our challenge is to continue to adapt our work environment to meet the needs of today's employees.

Capital is also an important resource. Your company has maintained a sound, conservative yet cost-effective capital structure designed to provide sufficient financing to support future growth.

Your company is well positioned to continue to grow. We are confident that fiscal 2000 will be an even better year.

Our Chairman, Mr. David Race, plans to step down following our Annual Meeting in June. He has devoted virtually his entire working life to CAE, starting as an engineer in 1951, rising through the ranks to President and Chief Executive Officer and, subsequently, to Chairman. We are indeed fortunate to have benefited from his vision, dedication, energy and support.

A handwritten signature in black ink, appearing to read "John E. Caldwell". The signature is fluid and cursive, with a prominent initial "J" and "C".

john e. caldwell (signed)

President and Chief Executive Officer

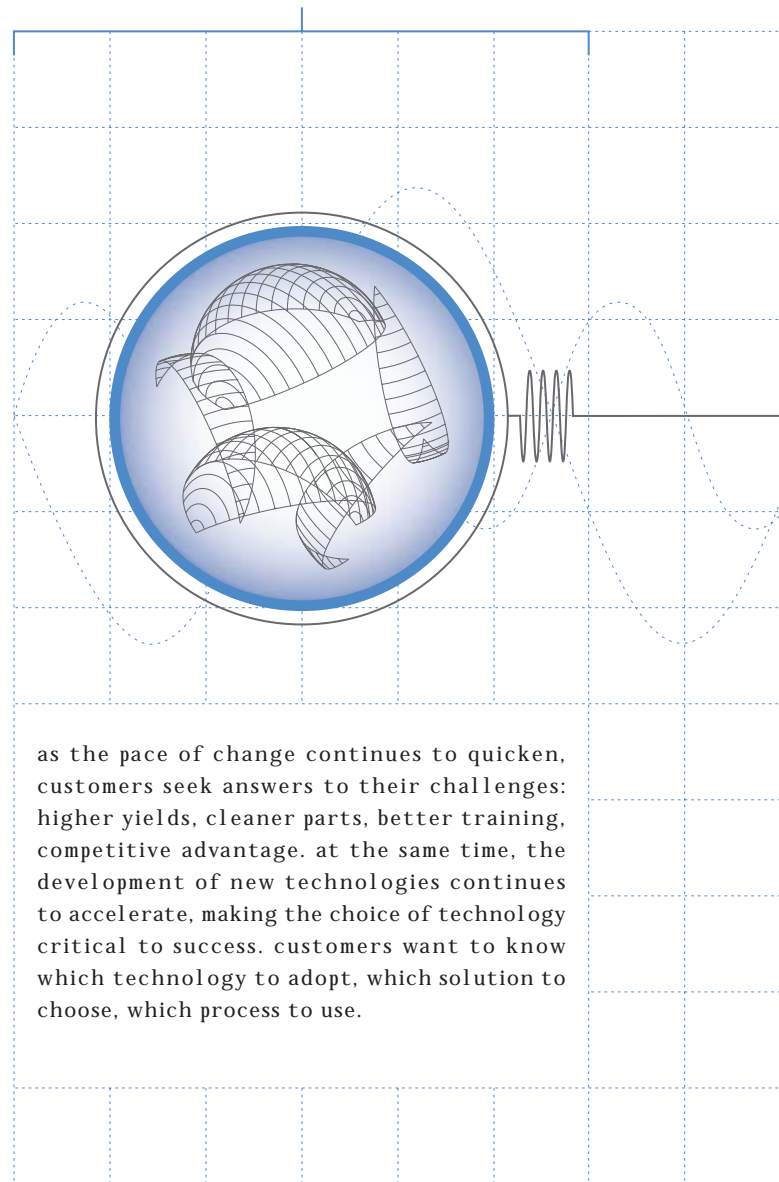
Advanced Technologies Our commitment to our customers is the common denominator. We create value by understanding their needs and then applying advanced thinking to their results. Our goal, whether in cleaning or railway technologies, is to provide services designed to improve performance.

ment to advanced technology for our
tor that unifies our companies.
the challenges of our customers,
and engineered solutions to improve
flight simulation, fiber processing,
to offer exceptional products and
formance and lower cost.

advanced technologies

Advanced technologies are at the heart of every CAE business. We start with an intimate understanding of a specific industry. We work closely with our customers to apply advanced thinking and the latest available technologies. We create solutions that provide long-term customer value. In whatever industry we participate, CAE consistently builds businesses that dominate their markets through the use of advanced technology.

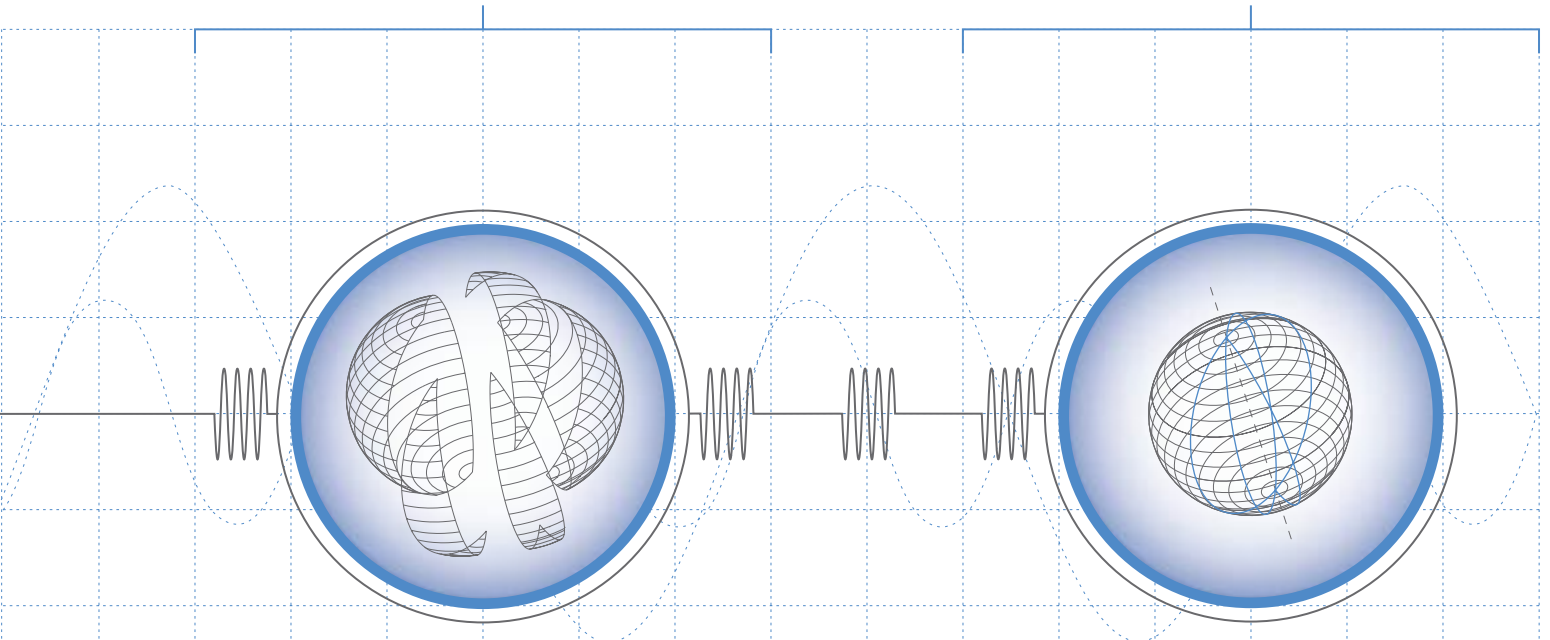
opportunities



as the pace of change continues to quicken, customers seek answers to their challenges: higher yields, cleaner parts, better training, competitive advantage. at the same time, the development of new technologies continues to accelerate, making the choice of technology critical to success. customers want to know which technology to adopt, which solution to choose, which process to use.

application technologies

value creation



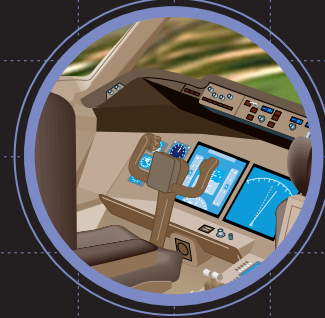
our skill is not just in visualizing the possibilities, but in turning that vision into reality. we challenge ourselves with new ideas. we apply our capabilities in software, electrical, electronic, mechanical, and systems engineering. we push the limits of software and hardware technology. the result: world-leading solutions that bridge the gap between the world of our customer and the world of technology.

because our solutions address the specific challenges of our customers, they must have a direct, measurable, and long-term value. creating value for our customers creates value for our shareholders. our growth is assured by the evolution of technology within dynamic markets we can dominate, and our ability to move to where advanced technology is needed to solve real problems.

advanced applications

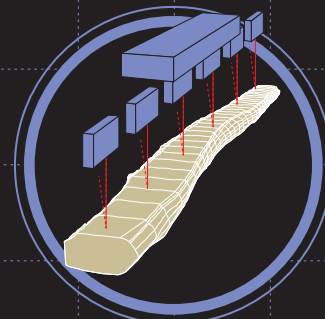
The future of CAE is in advanced technologies where information is transformed into productivity. Two of our major businesses – flight simulation and fiber processing – best illustrate this model. Data is collected through specialized sensors and other electronic interfaces. Software and hardware developed by CAE transform the raw data to drive highly engineered systems. With a simulator, it's the extraordinarily faithful simulation of a real-world environment where pilots can train without flying the actual aircraft. With a curve saw optimizer, it's the scanner-simulated profile of a log, calculated for its highest possible yield then cut in real-time by robotic saw systems. Data. Information. Productivity.

data acquisition



flight simulation the cockpit of a flight simulator imitates perfectly the conditions of the actual aircraft. the real-world actions and reactions of the pilot are converted to data through a wide variety of sensors and simulated cockpit instrumentation, then, through custom-designed interface systems, are transmitted to a real-time management and control center.

sawmill optimization a log enters the cae curve sawing optimizer and is instantly scanned using laser profiling, specialized cameras or x-ray sensors. the raw data is conveyed to a real-time management and control center.

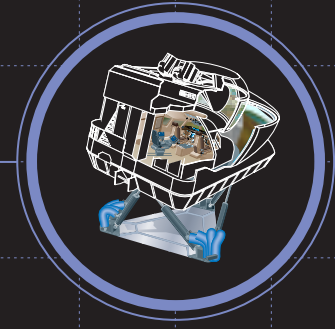


data transformation

with proprietary algorithms and software developed by cae engineers, the simulator's control center compares the data representing the pilot's actions to stored data representing the specific aircraft and variable flight conditions. numerous disciplines are applied, from embedded application software, and electronic hardware design, to robotics, and human factors engineering.

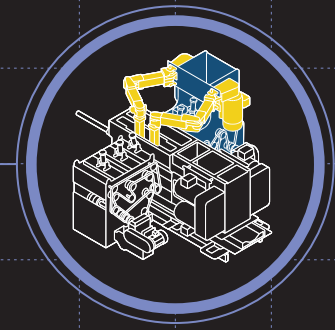
the data is translated by cae computers into a three-dimensional profile of the log - a virtual reality. it is analyzed and "optimized" using cae-developed proprietary software and algorithms. once again, embedded application software plays a key role, as does specialized software application design, electronic hardware design, and robotics. cae's motion control software signals the robotic saws which position themselves for the optimal cuts.

data application



in millions of calculations, the virtual world of the simulator "reacts" to the pilot's actions in real-time like an actual aircraft in flight. onboard computers inform a host of flight simulation technologies including motion controllers, force feedback controllers, and image generators. pilots are efficiently trained in a virtual reality.

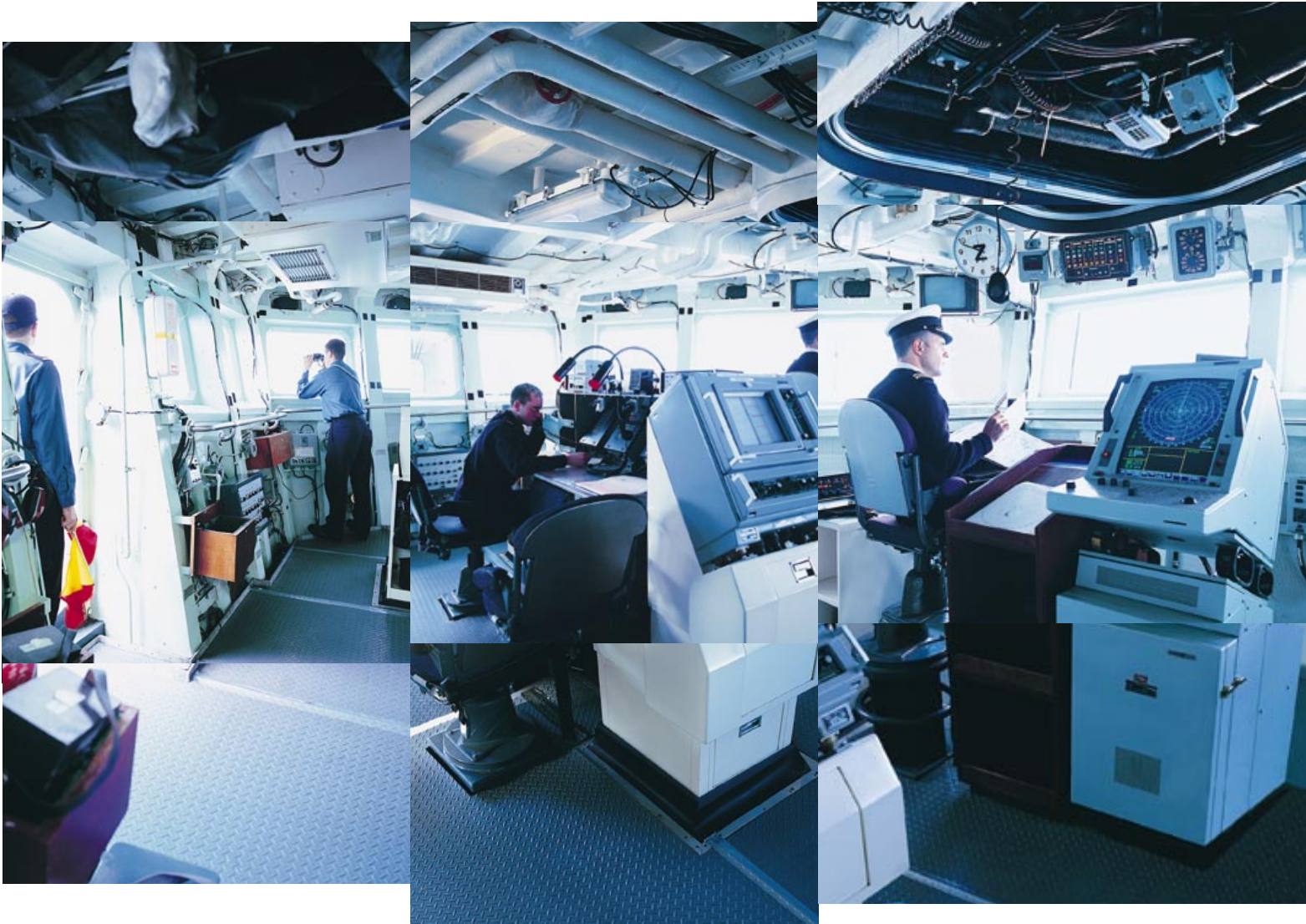
as the log continues its rapid movement through the optimizer, the saws cut along specified curves with the aid of motion controls, saw controls, and material-handling controls, programmed to improve yield, quality, and profits.



value creation

Leadership in World Markets CAE
tries. But our real business is infor
hardware, and engineering experi
tomer's data into a profitable appli
The applications may differ. But
We build smart technologies that
information into productivity.

is a global leader in selected industries. Using proprietary software, hence, our job is to transform each customer. The industries may differ. the underlying principle is the same. convert data into information, and



leadership in marine control systems



Naval vessels have traditionally been labor intensive. The crew manually operates most functions, from propulsion and climate control to electrical systems and damage assessment. Our marine control customers want to reduce crew size and increase automation, enabling their ships to operate more efficiently from a central control station. For over 15 years, we have worked with customers around the world to better control the major onboard systems of large ships. Today, we are a world leader.



leadership in flight simulation



Our flight simulator customers must efficiently train pilots to fly specific types of aircraft. Often, the customer's fleet is growing or changing so rapidly, there is a pressing need for personnel. Using the real aircraft is no longer economically viable and sometimes pilots even require training on aircraft still in the design stage. True-to-life simulation is the only answer. We have become the world leader in flight simulation by working closely with customers, cultivating strong technological capabilities, and providing creative people with an environment geared to innovation. In fiscal 1999, we supplied 70% of the world market in commercial simulators.



leadership in sawmill optimization



The business challenge for our sawmill automation customers is to increase the yield from each log that enters their sawmill. Traditional saws cut in straight lines. With CAE optimization and curve sawing technology, the value of a log can be maximized by cutting along its specified curves, maximizing yield, minimizing waste, and improving profits. By understanding our customers' challenges and knowing how to apply advanced technologies in a sawmill environment, we have become the world leader in sawmill optimization equipment.



leadership in cleaning technologies



Customers of CAE Cleaning Technologies are seeking better ways to clean complex parts. From printed circuit boards and disk drives to transmission components, cleaner parts mean superior assembly, improved performance, fewer failures, and lower warranty costs. By applying a variety of aqueous, ultrasonic, and CO₂ technologies, our engineers develop highly customized, waste-minimizing cleaning systems that are the best of their kind in the world.

Exceeding Expectations Our custo
people in their industries. Procure
tions. Our customers seek strategic
ness and offer tailored solutions
CAE is known throughout the world
est standards of customer service.
work with the best, you have to

mers are among the most discerning
ment is no longer about supplier auc-
partners who comprehend their busi-
that will improve their bottom line.
for quality technology and the high-
We understand that if you want to
offer something more.

american airlines

roland desjardins

Director of Commercial Flight Operations,

Dallas, U.S.A.

“As part of a long-term agreement with CAE, American Airlines owns or is in the process of acquiring nine simulators. We have been extremely satisfied. CAE is certainly on the leading edge of technology. And customer service is exceptional. They stay in close touch with us during the building of our machines, and when their people recognize there might be a better way to do something, they react immediately. Because we normally have to get to the marketplace quickly, we made a request for five simulators in a one-year time frame. It was a major demand and it was satisfied beyond our expectations. I think that says a lot about CAE’s dedication to making it happen for its customers.”





navistar international
transportation company

don conrad

Senior Manufacturing Engineer,

Indianapolis, U.S.A.

“We are the world’s largest truck manufacturer and the largest manufacturer of mid-range diesel engines. In late 1997, we evaluated a number of suppliers and decided to order a crank case final washer and a cylinder head final washer from CAE Ransohoff. Their technology was superior and they shortened their lead-time for delivery by almost half. We needed the washers in 26 weeks to take advantage of our annual two-week production downtime. Not only did CAE meet the deadline, they worked closely with our engineers to exceed it by two weeks and ensure installation was exceptionally smooth. Since then, customer service, in my opinion, has been outstanding. They are extremely responsive. Because we work 24 hours a day, seven days a week, we can’t afford to have any machine down for any length of time. With CAE Ransohoff that just hasn’t been a concern.”

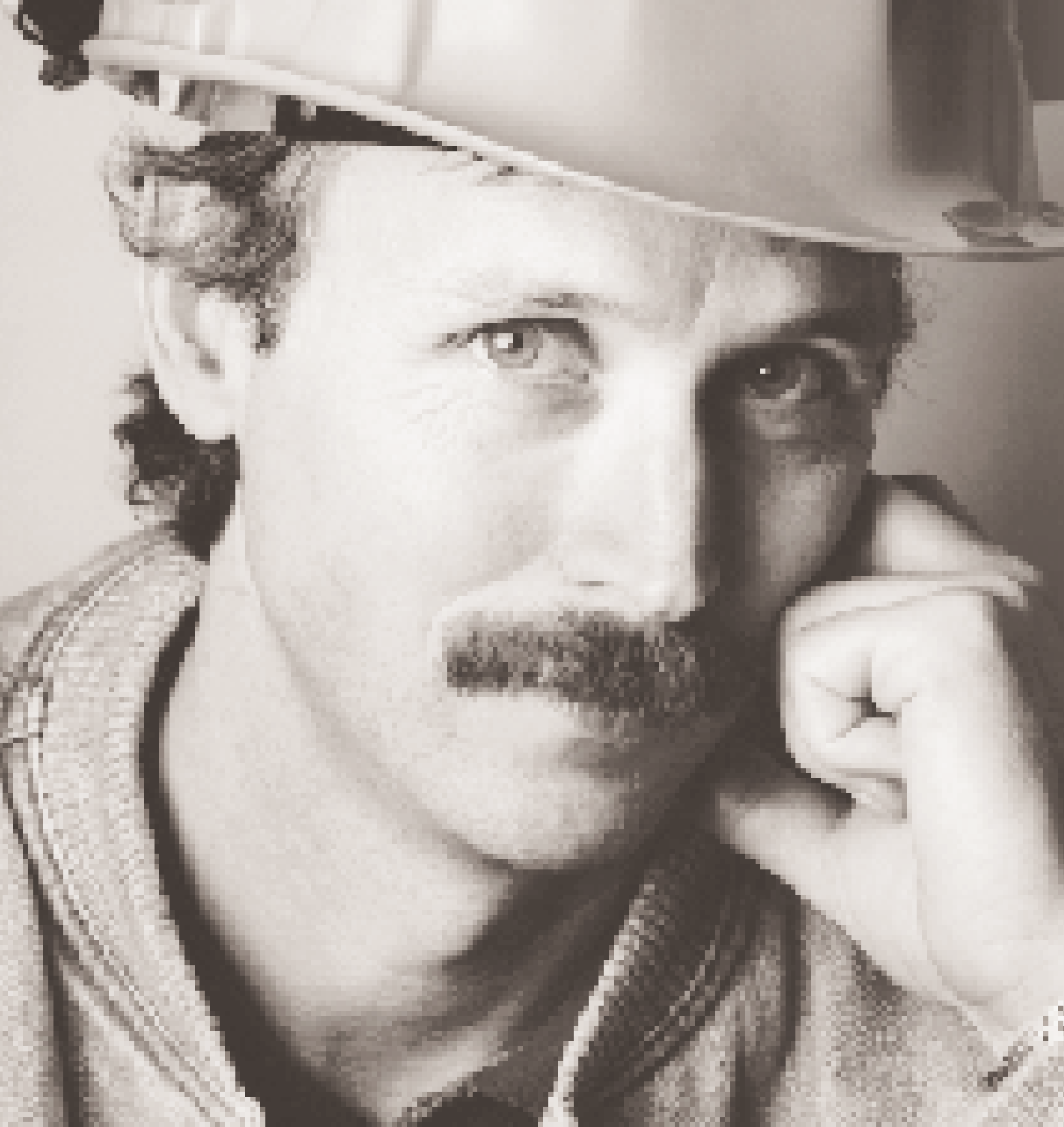
u.k. ministry of defence

colonel peter williams

*Commandant, Royal School of Artillery,
Salisbury, England*

“We have enjoyed an especially productive relationship with CAE Invertron in connection with the technological development of our new Warrior OPV trainer. We seconded one of our Sergeant Majors to work on the project, which meant that the software designers were able to integrate our requirements precisely. The fidelity of the trainer is impressive – it replicates the real life system extraordinarily well. Procurement action was outstanding; development of the complete OPV trainer took just 23 months – very fast given the system’s complexity. In view of this short developmental timescale, one might imagine that the system would have loads of bugs in it; however, ours was ready to go on Day One and the system’s subsequent stability has been remarkable. Overall, this has been a really successful developmental project. All of us at the Royal School of Artillery – both instructors and students alike – consider ourselves fortunate to have taken delivery of such a potent training system.”





tolko industries

mike harkies

*Area Manager, Nicola Valley Division,
Merritt, Canada*

“Over the years our company has acquired quite a number of different CAE products: multi-saw trimmers, material handling equipment and, most recently, curve sawing gangs and optimizers that yield more product from each tree. CAE is very good at putting technologies into place that address business issues. They show foresight as to what will be beneficial for the next steps in making the forest products business more profitable. So when we look to partner with companies for future development, CAE is definitely a company we consider.”

A Culture of Commitment Nothing
our customers and, ultimately, our
people. As technology changes rapid
new opportunities emerge, innova
that reason, CAE hires only except
culture of innovation and excellence.
our people transform bright ideas

is more important to the success of
shareholders than the caliber of our
ly, as business requirements shift, as
tion is the only path to growth. For
ional people. We are motivated by a
Using various tools and technologies,
into brilliant applications.



richard knox

project engineer,

Medium Support Helicopter Program, CAE Electronics plc,

Burgess Hill, England

“We build and maintain advanced military training equipment and simulators. Innovation is critical to continued development of the process. We are always seeking new ways to improve the thinking that goes into our products. Sometimes this comes from the customers themselves. One quality expressed and appreciated by the British Ministry of Defence is the close liaison and their involvement from design concept to beyond system delivery. This relationship allows us to optimize and agree on the solution to meet their requirement. This proven approach provides our customer with the most advanced simulators within their budget.”

patrick wouters

co-program manager,
*Program Management Department, CAE Elektronik GmbH,
Stolberg, Germany*

“I saw my first flight simulator at the age of 13 or 14 and it was, in fact, a CAE simulator. Somehow it stuck and when I was a student I was committed to entering the flight simulation industry. Working for CAE challenges innovative thinking. If you really want to be innovative you have to dream of things that never were and ask yourself “Why not?” And if you consistently ask that question, you can really make the dreams become reality. Here, that happens. We make things happen.”





brian stroud

project manager,

Sawmill Primary Business, CAE Newnes Ltd.,

Salmon Arm, Canada

“CAE Newnes is very customer focussed. We simply won’t let a customer down. We go to extraordinary lengths to solve problems for our customers. Our prime job is to meet the needs of an industry that is always looking for faster, more efficient ways of applying advanced technology to process wood fiber and get the most value from it. Our curve sawing systems lead the world. Our new log breakdown and log bucking optimizer equipment that we are currently developing will allow the mill to integrate all the optimizer systems to allow for total mill control of value and production.”

fragitsa halkias

software engineer,

Virtual Environment, CAE Electronics Ltd.,

Montreal, Canada

“In many places, software engineers like me just sit and write code all day. Here at CAE, I have been able to work on an entire product line, doing marketing support, project coordination, and interacting with the customer. There is amazing value in that. We actually feel like artists here. Ideas are always around us. We have an extremely talented team. We are all excited about using the newest technologies and pushing them constantly beyond their boundaries.”



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review of operations and management discussion and analysis

summary of consolidated results

Revenue

Consolidated revenue for fiscal 1999 reached \$1.1 billion, an increase of 16% over the fiscal 1998 level of \$922 million. The increase in consolidated revenue is due to significantly higher activity in commercial and military simulation and the contribution from the acquisition of four companies – Newnes, McGehee, Alpheus and Beyss – completed during this fiscal year. The higher simulation activity combined with these acquisitions more than offset the revenue included in fiscal 1998 for CAE Aviation, which was sold in the fourth quarter of that year.

Net Earnings

Consolidated net earnings increased 10% to \$77.3 million or \$0.70 per share compared with fiscal 1998 consolidated earnings of \$70.2 million or \$0.64 per share. Excluding the \$6.0 million pretax non-recurring gains recorded in fiscal 1998, consolidated net earnings increased 17% year over year due to the higher activity in the CAE Electronics Group noted above along with higher operating earnings for CAE Fiber Processing Technologies. The improvement at CAE Fiber Processing Technologies stems from operational efficiencies obtained from the consolidation of the North American screen plate manufacturing operations, which occurred in the latter part of fiscal 1998, and the contributions from the Newnes and McGehee acquisitions. These improvements were partially offset by lower results from CAE Cleaning Technologies and higher interest expense, as bank indebtedness increased to fund the acquisitions and facilities expansion.

Cash Flow

The cash consideration for the four previously noted acquisitions combined with higher capital expenditures contributed to a reduction of \$177.2 million in cash balances. The increase in capital expenditures was attributable to the construction of new facilities at CAE's U.K. operation, the building of the training facility for the Medium Support Helicopter Program, the expansion at both CAE Electronics in Montreal to manage growth and CAE ScreenPlates in Lennoxville resulting from the consolidation of the North American manufacturing operations, and the cost to build simulators under long-term lease arrangements. In addition, non-cash working capital increased due to the growth and timing of milestone payments on various commercial and military simulation programs.

Backlog

Order backlog reached another record at \$1.9 billion compared with \$1.7 billion at March 31, 1998. The significant increase in backlog reflects higher commercial simulation orders, as well as recent order bookings by CAE Cleaning Technologies and CAE Fiber Processing Technologies.

cae electronics group

The CAE Electronics Group consists of five strategically located operations – CAE Electronics Ltd. (Canada), CAE Elektronik GmbH (Germany), CAE Electronics plc (United Kingdom), CAE Electronics Inc. (United States) and CAE Electronics (Australia) Pty Ltd. The Group is the world-leading supplier of commercial and military flight simulators and visual systems and also supplies a variety of other military simulation and training systems, real-time energy control systems and marine control systems. In addition, CAE has established a new subsidiary, CAE Aircrew Training Services plc, in the UK in connection with the Medium Support Helicopter Program. CAE owns 74% with the balance held by the other consortium partners. This subsidiary is building and will own and operate a training centre on land it leases from the U.K. Ministry of Defence (MoD).

financial results

(figures in thousands of dollars)	1999	1998	1997	1996	1995
Revenue	\$ 736,782	715,272	656,310	620,972	523,257
Operating Earnings	\$ 82,289	74,384	57,790	53,115	42,124
Backlog	\$ 1,767,449	1,624,411	787,407	831,022	657,665
Capital Expenditures, net	\$ 69,023	57,431	29,856	24,401	15,027

Revenue and operating earnings of the CAE Electronics Group improved for the sixth consecutive year. Excluding the 1998 revenue for CAE Aviation, the 12% growth in revenue was due to higher commercial simulation activity and the timing of work on certain military simulation and marine control system programs.

Operating earnings rose 11%, consistent with the revenue increase.

The increase in backlog reflects CAE's continued high rate of awards in the buoyant commercial simulation marketplace.

Capital expenditures increased due to several major projects including the completion of a new, 60,000 square foot facility at CAE Electronics plc in Burgess Hill, UK; facility expansion at CAE Electronics Ltd. to manage growth; construction of the training facility for the Medium Support Helicopter Program; and the cost to build four commercial full flight simulators and visual systems, which have been leased to certain customers.

operational highlights by product line

commercial flight simulation and visual systems

CAE Electronics Ltd. enjoyed continued success in a buoyant commercial simulation market. CAE won 30 out of 42 Full Flight Simulator (FFS) orders and five out of eight Flight Training Device (FTD) orders, representing a worldwide market share of 70%. Over the past two years, a record total of 117 devices were ordered worldwide. This strong demand reflects an ongoing fleet renewal, particularly in North America, the effect of increased air passenger miles, the introduction of new aircraft types and increased use of simulators for training for regional and business aircraft.

Part of CAE's success is attributable to the company's decision to pre-build certain simulators to shorten delivery time in anticipation of the increase in demand. Lead time continues to be an important factor in determining market success. CAE plans to achieve a long-term market advantage through a cycle time reduction program. In addition, CAE maintains long-term supply agreements with both American Airlines and Delta Airlines for their future simulation needs.

over the past two years, a record total of 117 flight simulators were ordered worldwide. this strong demand reflects an ongoing fleet renewal, particularly in north america, the effect of increased air passenger miles, the introduction of new aircraft types and increased use of simulators for training for regional and business aircraft.

A growing area of opportunity for CAE is the regional jet and business aircraft markets. During fiscal 1999, CAE was awarded a significant number of contracts for these aircraft types including:

- CAE's largest single order for business jet training equipment from GE Capital SimuFlite Training International for two Gulfstream FFS and two Citation FFS with MAXVUE Plus™ visual systems;
- a Bombardier CRJ-700 FFS with MAXVUE™, an FTD and a computer aided training software package for Bombardier Aerospace;
- a Bombardier CRJ-200 FFS and a Dornier 328 FFS with MAXVUE Plus™ visual systems for Friendship Simulation Company of the Netherlands;
- an Embraer ERJ-145 FFS with MAXVUE Plus™ visual system for Continental Express; and
- a Bombardier CRJ-200 FFS and a British Aerospace RJ-85 FFS with MAXVUE Plus™ visual systems for Pan Am Flight Academy.

CAE enjoys continued success with its MAXVUE™ visual system. In 1997, the company introduced MAXVUE Plus™, which was developed using input from the commercial flight training community as well as technology advancements to provide enhanced realism. MAXVUE Plus™ reinforces CAE's commitment to offer state-of-the-art performance to customers, while providing a modular upgrade path for earlier systems. In fiscal 1999, CAE captured 46 of 62 visual system orders, representing a 74% market share, its strongest year since the introduction of the original MAXVUE™ system in 1992. This included CAE's largest commercial visual system order from GE Capital SimuFlite Training International for 15 new MAXVUE™ visual systems to upgrade its existing simulator fleet.

maxvue™ medallion complements and extends the maxvue™ family of visual system products and delivers the level of performance needed to support very high visual scene complexity for defense training.

During the third quarter of fiscal 1999, CAE announced a visual simulation system alliance with SOGITEC Industries SA of France to co-develop, market and sell image generators and database tools for the military and civil simulation markets. CAE and SOGITEC will create a broad range of visual simulation system products spanning performance requirements that address the full scope of training and research application needs, from the low cost requirements of the civil flight training device to the very high scene complexity and resolution demands of the military full mission simulator.

The first product arising out of the alliance, MAXVUE™ Medallion, was introduced during the year. MAXVUE™ Medallion complements and extends the MAXVUE™ family of visual system products and delivers the level of performance needed to support very high visual scene complexity for defense training.

CAE can now offer its customers the full range of visual simulation system products including the most competitive, high-end visual system in the market today. The alliance also strengthens CAE's position in Europe and provides the company with a new, enhanced architecture for the next generation image generator at a lower cost and in a shorter timeframe than would be otherwise feasible.

Outlook

Commercial simulator orders are driven by a number of factors including growth in aircraft fleets, changes in aircraft mix, regulatory changes in training requirements and pilot attrition. In addition, the use of simulators for training has continued to increase due to improving technology and the significant cost savings as compared with real flight time training.

These factors, combined with the anticipated continued growth in air travel, growth in the regional and business aircraft training segments, the generally strong financial position of the airline industry, and the order backlog for delivery of new aircraft, should lead to a consistent order level of approximately 25 to 30 devices over the next few years. CAE expects to maintain its commanding leadership position due to its focus on customer relationships, its commitment to innovation and technology, product quality, reliability and efficiency, and its continuing effort to shorten delivery cycles through process improvements.

Visual system orders are driven in part by the new FFS simulator market. However, incremental growth in this market is anticipated as the installed base of aging visual systems reach their economic life limits. This trend is occurring in the military market as well.

military systems & training

CAE continued its success in the military simulation market during fiscal 1999. In the first quarter of this year the company was selected by MILIT-AIR Inc. with Bombardier acting as their agent, for the design and manufacture of four Level Seven Flight Training Devices for the NATO Flying Training in Canada (“NFTC”) program. NFTC is a pilot training program offered to NATO and other nations seeking a complete training solution. The concept of this program is to ensure a long-term cost-efficient training solution. The value of the contract to CAE is \$68 million to provide two Raytheon T-6A-1 and two Hawk Mk 115 flight training devices including MAXVUE™ visual systems. In addition, CAE will be responsible for the maintenance and support of these devices.

Other noteworthy contracts received by CAE this year include:

- a \$12 million contract from the Government of Canada to update the CAE built CC-130 Operational Flight Trainer for the Canadian Forces located at CFB – Trenton, Ontario;
- a \$26.5 million contract from Flight Safety Services Corporation (FSSC) for the development of a C-5 Weapon System Trainer. This simulator, the eighth for CAE, is to be located at Kelly AFB in Texas; and
- a contract from Lockheed Martin to develop and supply the Radio Communications Network Systems and Mock Battlefield Headquarters vehicles for the U.K. Combined Arms Tactical Training simulator for the U.K. Ministry of Defence (MoD).

Operationally, significant progress was achieved this year on the Medium Support Helicopter program for the U.K. MoD. This contract, CAE’s largest ever, requires CAE and its consortium partners to build, own and operate a training facility at RAF Benson in Oxfordshire. Training will be provided over an initial twenty-year period on six full flight helicopter simulators – three Chinooks, two Merlins and one Puma – and also includes a Tactical Control Centre. The six simulators are in the build phases of assembly, integration, test and pre-factory system demonstrations, respectively. The facility construction at RAF Benson is nearing completion and currently is being readied for installation of the training equipment.

In connection with the contract, CAE established a subsidiary, CAE Aircrew Training Services plc, of which it owns 74% with the balance held by the other consortium partners. This subsidiary leased the land from the MoD, and is building the training centre, which it will own and operate.

At the beginning of April 1999, CAE Elektronik GmbH started the in-plant installation and integration of the first UH-1D and CH-53 simulators for the Night Time low level Flight (NTF) program in Germany. These systems will grow from purely mechanical assemblies into full flight simulators. A total of 12 full flight simulators will be delivered to the German Army Aviation School in Bückeburg by the end of 2002, where they will be used for primary flight training and advanced low-level night flying training.

The CF-18 System Engineering Support contract continues to be a showpiece of synergistic partnership. With Bombardier as prime contractor, CAE “sets the standard” of what can be achieved doing in-service support for complex, highly integrated, distributed weapons systems.

The first of the five Warrior Observation Post Vehicle (WOPV) simulators sold to the British Army successfully entered service in October 1998; the remaining systems will be delivered in accordance with the demanding delivery schedule during 1999 both in the UK and Germany. The £16 million contract is a complex, software-intensive project, which will eventually see five training systems in service, each composed of three WOPV simulators and an instructor command module. The WOPV trainers will enable training all year round, in a cost effective and highly realistic environment.

Outlook

The military simulation and training market is driven 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. In addition to technology and price, the customers’ – in most cases governments – key purchase criteria include the contractor’s local presence and capability to finance, maintain and operate a turnkey training center. CAE is well positioned to capitalize on opportunities in the international market, with operations in Canada, the United States, Germany, the United Kingdom and Australia, as well as teaming and/or collaboration arrangements in other countries, similar to the visual systems alliance with SOGITEC described earlier.

The procurement of helicopter and transport aircraft is expected to increase over the next few years and this growth will translate into several simulation opportunities for CAE to pursue worldwide. Upcoming programs include the Eurofighter 2000, the next generation tactical fighter for the United Kingdom, Germany, Italy and Spain; helicopter programs for the Eurocopter 135/155 and NH-90 for Germany, France, Italy, and The Netherlands; and the Tiger program, a joint French/German initiative.

marine systems

CAE remained the Integrated Platform Management System (IPMS) automation supplier of choice for the world's navies, building on the successes of the initial technology launch from the Canadian Patrol Frigate Program. CAE has supplied or has been selected to supply advanced IPMS technology for approximately 90 warships for 11 of the world's premier navies.

During fiscal year 1999, CAE was awarded a contract by GEC Marine Yarrow Shipbuilders Ltd. (YSL) of Glasgow, Scotland, to supply IPMS's for three Offshore Patrol Vessels being built by YSL for the Royal Brunei Navy. The contract is valued at approximately \$10 million.

In 1997, CAE was on the team selected to build the U.S. Navy's next generation amphibious assault ship, the LPD-17. CAE is providing the engineering control system used to control the ship's propulsion, auxiliary, electrical and damage control systems. The initial contract for one ship, valued at US\$15.5 million, is on schedule. In February, 1999, the second option of a total number of 12 planned LPDs, was exercised.

CAE was awarded a Phase 1 conceptual design contract from Raytheon Marine for the United States Navy DD-21 future generation Destroyer. CAE is the integrated platform management team leader for this phase of the program.

Another activity within this product segment is the design and manufacture of power plant simulators and the provision of power plant simulator software upgrades. In July 1998, CAE was selected by Atomic Energy of Canada Ltd. (AECL) to supply a full-scope, real-time nuclear power plant simulator for the Qinshan project in China. The value of the contract is approximately \$20 million. The plant-specific Qinshan simulator is expected to be ready for early training in the beginning of 2002, prior to the reactors entering into service.

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Outlook

With its leading technology solution, CAE is well positioned to capitalize on upcoming international Marine Programs including: the Royal Malaysian Navy's Patrol Vessel Program to build up to a total of 27 ships; the ASTUTE Nuclear Submarine Program for the U.K. Royal Navy; and a 20 ship Frigate Program, entitled HORIZON, for the French, Italian and U.K. Navies. In the U.S. marketplace, future opportunities include the U.S. Coast Guard Deep Water Program for up to 25 ships; and the DD-21 (Destroyer) Program for up to a total of 32 ships, as well as CAE's entrée into the U.S. Navy's aircraft carrier programs.

energy control systems

Competition and retail energy trading is revolutionizing the world of electric power production, transmission and distribution in many parts of the world. This has in recent years forced a change in focus for the world's major power utilities. CAE has been updating and modifying its software applications to allow its clients to operate efficiently and react immediately to ensure power is supplied to the end users. The systems CAE supplies allow utilities to maintain and grow their market share by providing the correct real-time information and tools required to manage their complex networks. The new tools provide the energy supplier with different ways to directly target their customers to offer improved customer service. The tools developed can still be utilized in traditional environments where deregulation has not occurred as correct operating information and good consumer relations ultimately lead to efficient operation of the electrical grid.

In the past year, CAE was selected to provide new, real-time information systems to utilities that span the globe. Significant contracts include: EDELCA of Venezuela where the system will control the power production and distribution from the Guri dam, the second largest operating dam in the world; Taiwan Power Corporation of Taiwan as the prime foreign supplier for four Area Dispatch & Control Systems and 12 Distribution Dispatch & Control Systems; and Henan Electrical Power Corporation of Henan province in China for an energy management system.

Outlook

Two independent market drivers affect CAE's Energy Control Systems business. The first driver is the increasing demand for electrical power, which is occurring in Asia and other developing regions of the world. The significant opportunities in the Asia-Pacific region continue despite the region's recent economic crisis and are driving infrastructure needs.

The second driver is deregulation. As the energy markets are re-structured, there will be an increasing demand for Energy Control Systems and services for generation, transmission, distribution, and market related applications. Deregulation on a large scale was first initiated in the U.K., followed by Australia, the northern European countries and North America.

CAE's successes position the company very well in infrastructure and deregulated markets. The worldwide Energy Control Systems market is expected to be buoyant over the next few years. CAE's open architecture, leading-edge technology and advanced applications have placed the company at the forefront of its competitors in the control systems market.

cae fiber processing technologies

CAE Fiber Processing Technologies supplies leading-edge advanced sawmill optimization and sawing systems, specialized equipment for the manufacture of oriented strand board, and advanced screening for pulp and paper. The Group comprises CAE ScreenPlates, the world's leading supplier of precision stainless steel screen cylinders and plates, nearly half of which incorporate patented technology; CAE Trislot, a leading supplier of wedge wire products; CAE Machinery, the leading manufacturer of proprietary machinery for oriented strand board producers and of debarkers; and two companies acquired during fiscal 1999, CAE Newnes, a technological leader in solid wood optimization through proprietary defect recognition systems, optimization software and specialized machinery; and CAE McGehee, supplier of world leading proprietary sawing systems allowing further solid wood optimization through unique curve sawing technology.

financial results

(figures in thousands of dollars)	1999	1998	1997	1996	1995
Revenue	\$ 197,373	109,444	138,723	149,102	101,247
Operating Earnings	\$ 33,339	16,299	19,920	28,114	19,307
Backlog	\$ 63,968	23,931	28,337	51,018	56,954
Capital Expenditures, net	\$ 7,462	6,336	13,318	4,745	5,070

Revenue of CAE Fiber Processing Technologies increased 80% in fiscal 1999 due primarily to the contributions from the two new acquisitions. Operating earnings rose 105% with the contributions from these acquisitions and strong results in the North American screen plate operation.

cae newnes and cae mcgehee

With high quality wood fiber in ever shorter supply and recognizing a significant opportunity for revenue and earnings growth, in June 1998, CAE acquired two companies: Newnes Machine Ltd. of Salmon Arm, British Columbia, renamed CAE Newnes, and McGehee Equipment Company of Ukiah, California, renamed CAE McGehee. These companies are world leaders in supplying advanced technology sawmill machinery, including automatic natural defect recognition and associated optimization software systems developed to improve lumber yield in the forest products industry.

The companies today primarily serve the North American sawn wood manufacturing industry consisting of about 800 softwood sawmills and many smaller hardwood mills. The sawn wood is used primarily for residential construction and renovation.

The key issues facing the sawn wood industry are the diminishing supply of logs, due to environmental pressures; a reduction in log diameters; and an increasing supply from poor quality second growth logs. These issues have dramatically increased the demand for advanced technology to increase the recovery rate from logs, both in terms of volume and quality. This has led to the development of several innovative new products by CAE Newnes and CAE McGehee.

The companies recently jointly developed a patented solution to improve the volumetric recovery of logs with a bow of as little as one inch with a cant curve sawing and optimizer edger system, which resulted in an 80% market share in the current reporting period.

Even more important than improving recovery rates is improving the recovery of higher grade material. Detecting knots and other natural defects significantly increases the value of sawn lumber. CAE Newnes has developed optimization equipment to maximize the yield of wood by scanning planed dried wood to effectively remove biological defects to create the highest value material. The “AddVantage™” optimizer uses a suite of technologies, including x-ray, moisture scanning, wane (a rounded edge) measurement, and visioning, to allow its customers to produce the desired grade of wood in various sizes.

In addition, CAE McGehee has developed a unique optimized small log system to recover sawn wood from logs as small as four inches in diameter and ordinarily used to make wood chips. This new product offers new growth opportunities and increases the recovery of wood compared with any other competitive products.

Despite the weaker commodity prices for lumber, which impacted the demand for capital equipment, CAE Newnes and CAE McGehee met expectations over the balance of the fiscal year while the companies were under CAE ownership, aided by the products noted above, which provide significant returns to their customers.

Outlook

While the North American sawmilling industry is mature in terms of growth in output due to log supply constraints and the deterioration in raw material supply, CAE Newnes and CAE McGehee, through the development of leading-edge technologies, create a ready market for their products at over 800 sawmills. The companies have already positioned themselves in the largest North American region: The U.S. Southeast. With the recent stability and improvement in lumber prices, the further market penetration of new products and opportunities to expand into the international market bode well for next year’s results. In March of 1999, the companies booked orders totaling \$30 million contributing to their highest backlog ever as they enter fiscal 2000.

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cae screenplates and cae trislot

Operational Highlights

Throughout fiscal 1999, pulp prices remained at historically low levels. This, combined with the financial crisis in the Asia-Pacific region and further consolidation within the pulp and paper industry, contributed to a decline in deliveries of screen plate cylinders and plates, as no new capacity was added. As a result, it was timely for CAE to complete the consolidation of its North American manufacturing operations into a

single site in Lennoxville, Quebec, which recently completed an expansion of its facilities to accommodate future growth. The food and beverage processing and industrial water treatment filter markets, served by CAE Trislot, were also impacted by the economic climate in Asia and South America.

Several new products were under development during the year, including a new, high capacity screen known as MacroFlow™. The new screen cylinder will improve screening capacity, performance and reliability for customers. CAE ScreenPlates successfully introduced the first MacroFlow™ screens during the year. CAE Trislot also brought on stream new equipment designed to make wedge wire mats used to make screens for the pulp and paper industry. The wedge wire screen is used to coat paper.

Outlook

CAE ScreenPlates continues to be the world's leading supplier of stainless steel plates and cylinders to the pulp and paper industry. Further advances in new products and equipment, including MacroFlow™ and a wedge wire product developed in collaboration with CAE Trislot, together with the cost benefits of consolidating the manufacturing operations in North America, position the company well for the future. Any recovery in the pulp and paper industry as well as an improvement in the economic climate in Asia would also provide an added benefit.

cae machinery

Operational Highlights

In the second half of the fiscal year, an improvement in the demand for Oriented Strand Board ("OSB") resulted in a significant number of new orders for capital equipment. The volume of OSB produced continued to grow due to its success in replacing plywood as the builder's material of choice. As a result, CAE Machinery reported higher than expected sales of stranders and flakers and maintained its dominant position as the market leader for proprietary flaking machinery used to make OSB products. During the year the company was awarded its first installation of disposable knives for the Louisiana Pacific OSB mill in Tomahawk, Wisconsin, U.S.A. The key factor in the success of disposable knives is the lowering of cost for CAE's customers.

The King Debarker, launched four years ago, continued to gain market acceptance. The product's key feature of removing bark from small diameter and crooked logs displaces the traditional drum debarker sold by competitors. Pulp prices, however, remained low, resulting in the delay of several capital projects.

CAE Machinery, with assistance from the Alberta Research Council and OSB customers, is in the final stages of the design and development of a Panel MSR® (Machine Stress Rated) machine designed to measure the stiffness of wood based panels. This process optimization and quality assurance technology could completely revolutionize the structural panel industry. Partial funding for this project was received from customers, National Research Council and B.C. Science Council. Trials for the prototype machine will occur this summer.

Outlook

In the latter part of fiscal 1999, CAE Machinery booked a record number of capital equipment orders for the OSB market. As a result, the company heads into fiscal 2000 with a backlog of over \$20 million, the second highest level in the company's history. In addition, the recent demonstrated success of disposable knives should result in new orders. King Debarker and pulp mill repair activities, which are dependent on the price of pulp, should be consistent with fiscal 1999 unless a recovery in pulp price occurs.

cae cleaning technologies

CAE Cleaning Technologies is North America's leading designer and supplier of advanced technology cleaning systems and associated waste minimization equipment and services for industrial cleaning. As the demand for sophisticated environmentally friendly cleaning systems for precision parts and components continues to increase, CAE Cleaning Technologies continues to invest in the development of unique and innovative solutions for its customers. During the year, the company continued its overall strategy of expanding its global market presence and adding complementary technologies, evidenced by the acquisition of Alpheus Cleaning Technologies of Rancho Cucamonga, California, renamed CAE Alpheus Inc., and the Beyss GmbH Co. KG of Aachen, Germany, renamed CAE Beyss GmbH.

CAE Alpheus is an industry leader in the design and manufacture of a patented technology using CO₂ dry ice cleaning, which is used in a variety of industries including automotive, rubber and plastic molding, printing and pulp and paper. CAE Cleaning Technologies has introduced this new technology to its existing customers through its domestic and international sales and distribution network with great success.

CAE Cleaning Technologies also enhanced its position in the European automotive market with the acquisition of CAE Beyss in October, 1998. CAE Beyss, located in Aachen, Germany, is a recognized technology leader in the supply of precision automated cleaning and deburring systems for automotive drive train components and centralized coolant filtration systems. Shortly following the acquisition, CAE Cleaning Technologies, through a joint effort of CAE Ransohoff and CAE Beyss, was awarded its two largest contracts ever, valued at a combined total of \$39 million, from General Motors Corporation for cleaning systems and coolant pump over stations for their new global engine program.

CAE Cleaning Technologies now comprises six operating units – CAE Ransohoff and CAE Environmental Systems, both in Ohio, U.S.A., CAE Ultrasonics, New York, U.S.A., CAE Cleaning Technologies plc, Bradford, U.K., CAE Alpheus, California, U.S.A. and CAE Beyss, Aachen, Germany.

financial results

(figures in thousands of dollars)	1999	1998	1997	1996	1995
Revenue	\$ 83,990	59,577	41,071	12,473	—
Operating Earnings	\$ 3,400	5,252	3,577	71	—
Backlog	\$ 54,705	22,650	30,813	23,754	—
Capital Expenditures, net	\$ 2,611	1,526	2,348	429	—

Operational Highlights

Despite the growth in revenue this year, due entirely to acquisitions and more than offsetting a slow down at CAE Ransohoff, operating earnings were considerably lower. The lower operating earnings were attributable to lower volumes at CAE Ransohoff as several orders were delayed in the first half of the year, and the integration cost of establishing a global marketing, sales and distribution network for the group of companies. In addition to integrating the two previously noted acquisitions this year, CAE Cleaning Technologies also completed two acquisitions in the last month of fiscal 1998 and consolidated the operations of CAE Blackstone with CAE Ney, renaming the joint operations CAE Ultrasonics. Although the operating earnings were lower than anticipated, the company has a record backlog and has successfully positioned itself as a global leader in providing advanced technology cleaning solutions and services.

Outlook

With the integration activities and global distribution network completed, and a record backlog stemming from the recent General Motors contracts, CAE Cleaning Technologies is positioned to achieve a significant improvement in operating earnings in fiscal 2000. The fully integrated group of companies today offers the industry's broadest range of cleaning equipment in both standard and customized designs.

cae railway technologies & services

CAE Railway Technologies & Services is a leader in advanced maintenance technologies for North American Freight and Transit Railways. The company provides complete maintenance, repair and overhaul services for locomotive and freight car axles, as well as locomotive traction motor combos. Strategically located close to its customers, with eight facilities equipped with modern CNC equipment and American Association of Railroads certification to perform axle and wheel set repairs, the company provides comprehensive solutions to meet its customers' maintenance needs.

financial results

(figures in thousands of dollars)	1999	1998	1997	1996	1995
Revenue	\$ 51,916	38,076	31,240	27,256	33,088
Operating Earnings	\$ 4,471	3,783	4,824	3,155	4,847
Backlog	\$ 37,445	30,664	43,366	25,364	25,877
Capital expenditures, net	\$ 3,362	1,180	1,033	2,227	1,951

Operational Highlights

The primary contributor to the 36% revenue growth was the doubling of revenue for locomotive services, including the start-up of a new locomotive combo shop in Rocklin, California. Also contributing to growth were initial sales of CAE's patented procedure to retrofit General Motors EMD division locomotive

traction motor support bearings with a roller bearing assembly (TM Conversion). The Rocklin facility was the third plant opened in the last three years to perform traction motor maintenance and repair operations for major North American freight railroads. In the Locomotive Services segment, CAE is a partner with GE Transportation Systems providing full service maintenance packages for GE-built locomotives, a rapidly growing segment of GE's transportation business. In addition, successful introduction of the Dustguard Process in rebuilding railway axles combined with increased demand for 70-ton intermodal flat cars contributed to the increase in activity for maintenance axles. The Dustguard Process is a CAE patented repair procedure for freight car axles that substantially extends the life of each axle.

The company is also positioned to grow its transit wheel set services business with the recent award from VIA Rail of a multi-year contract for maintenance of wheel sets for their locomotive and commuter rail fleet. The contract, valued in excess of \$10 million, represents the largest single award in the history of the Transit Services Division.

Outlook

Significant growth should be achieved next year with the recent opening of the Rocklin locomotive combo facility and full commercialization of the TM Conversion product. The western facility acquisition is strategic for the company as it provides access to EMD traction motor combo maintenance, the largest installed fleet. The Rocklin facility will also provide opportunities to market its services to other customers located in the region. Operational improvements will be achieved as well for Locomotive Services following last fall's relocation of its Kansas City shop to a larger and more efficient facility in Lawrence, Kansas.

The axle maintenance market should expand with the success of the Dustguard Process, increased emphasis on Research & Development in new technologies to extend life cycles of customer's wheels and axles, the strong demand for 70-ton axles for new car construction, and the company's continued focus as a comprehensive product and service provider (a rebuilt, downsized or new axle).

With the recent multi-year contracts from VIA, GO Transit and TTC, CAE is now the dominant provider of wheel set maintenance services in the Canadian transit corridor. The company plans to expand its Montreal shop to meet the increased demand.

With North American Railroads spending over US\$2 billion annually on freight car and locomotive maintenance, there are additional significant opportunities to bring advanced maintenance technologies to the rail industry. As a result, CAE Railway Technologies & Services is exploring potential acquisitions to better position the company as a leading provider of maintenance technologies and optimized maintenance solutions.

liquidity and capital resources

CAE utilized its financial flexibility to realize its growth initiatives through the acquisition of four companies and investment in new facilities and equipment. In addition, as the company expanded its military and commercial simulation business, so has its need to support higher non-cash working capital levels. In summary, CAE's cash position decreased by \$177.2 million from the March 31, 1998 level of \$202.8 million.

The fair value of the net assets for the acquisition of Alpheus Cleaning Technologies, Newnes Machine Ltd., McGehee Equipment Company and Beyss GmbH, was \$193 million. Consideration given included \$99.9 million in cash, the assumption of \$11.6 million of bank debt, the issue of 600,000 common shares of the company for \$7 million, and contingent consideration of \$74.5 million which is payable based primarily on the future earnings of the acquired companies.

Capital expenditures, net of proceeds from fixed asset disposals, totaled \$82.5 million compared with \$66.5 million in fiscal 1998. This is the highest level ever recorded for CAE. Capital projects included the completion of facilities expansion initiated last year at CAE Electronics plc, CAE Electronics, Montreal, and CAE ScreenPlates, Lennoxville, Quebec to facilitate growth; the construction of the training facility for the MSH Program; the manufacture of four full flight simulators for long-term leases to specific customers; and strategic investments in new production equipment and information systems.

CAE employs foreign exchange forward contracts to manage the exposure created when sales are made in foreign currencies. The amount and timing of forward contracts varies on a number of factors, including milestone billings and the use of foreign materials and/or subcontractors on the program. As at March 31, 1999 CAE had \$288 million in Canadian equivalent foreign exchange contracts which, if marked to market at that date, would result in a foreign exchange loss of \$5.5 million. These would be equally offset by future gains of foreign denominated cash flows over the balance of the contracts.

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. In order to benefit from the low short term interest rates prevailing in the Canadian market, CAE concluded interest rate swap agreements with three Canadian financial institutions for periods between eight and fifteen years. At March 31, 1999, CAE had interest rate swaps covering long-term debt amounting to \$95 million which, if marked to market at that date, would result in a loss of \$1.7 million. CAE deals only with sound counterparties in executing any of its financial instruments.

As at March 31, 1999, CAE also has US\$177 million of accumulated non-capital loss carry forwards that can be used to offset income taxes payable on future earnings from U.S. operations.

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.

Market Cycles

CAE's companies participate in competitive global markets that are subject to worldwide economic trends and political influences. Many of the Company's products are affected by industry market cycles. The commercial simulation market generally follows the trend established in the commercial airline industry, particularly the delivery of new aircraft. Military simulation programs, awarded mainly by governments, are dependent on price, technology, life cycle costs, delivery and quality, government spending on defense programs, and may also be influenced by in-country presence. Forest product commodity prices such as the price of pulp, sawn lumber and OSB panel board, which, in turn, are governed by the demand for paper and the health of the construction industry,

impact demand for various equipment and services offered by CAE Fiber Processing Technologies. Similarly, capital investment in new equipment, affected by the introduction of new engines and/or transmissions for the automotive industry cycle will impact the demand for CAE Cleaning Technologies' products.

CAE has positioned itself in a variety of industries, geographically and by business sector, to help moderate these risks.

Product Innovation

The continued success of the company is also dependent upon the advancement of technology on existing products and the introduction of new products. In response, CAE expends a significant amount on research and development which in many cases is sponsored by the customer. Certain initiatives also receive the support of the Canadian Government through the Technology Partnership Program.

Changes in Contract Cost

CAE's operating results may fluctuate from a change in the cost to complete long-term fixed-price contracts. Typically these contracts incorporate new technological solutions, the cost of which is difficult to estimate.

Key Personnel

CAE is dependent on the continued service of, and its ability to attract and retain, qualified technical personnel. CAE applies a compensation philosophy designed to mitigate this risk.

Year 2000

CAE, like most other companies, is vulnerable to the failure of computerized systems or business disruption caused by the Year 2000 issue. CAE depends on technology for business applications (e.g., accounting and management systems), engineering design and support systems (e.g. CAD and communication systems) that could be date-sensitive. System dependency and the potential scope of the Year 2000 problem vary from operating company to operating company.

Each operating company of CAE has established a Year 2000 Compliance Team reporting to a senior executive charged with overseeing the Company's preparation for the Year 2000. The Compliance Teams provide regular status reports to the Vice President Finance and Chief Financial Officer of CAE Inc. These are reviewed with the Audit Committee of the Board of Directors.

Each CAE operating company completed a comprehensive review and assessment of its computer-based systems, including hardware, and proprietary and third party software affecting all financial and operational systems. The review also encompassed electronic interfaces with customers and suppliers, telephone and other communication systems, automated security and access systems and any other devices dependent upon computer or embedded chip technology.

CAE Electronics, Montreal, which represents approximately 60% of the Company's activities encompassing 4,000 employees, is replacing its financial systems. The new general ledger and accounts receivable system was implemented on

April 1, 1999 and the project costing system is scheduled for implementation on May 30, 1999. The new system is Year 2000 compliant. All other related financial systems are Year 2000 compliant. All operating systems have been upgraded to versions that are Year 2000 ready and a test partition was created to allow for testing. External consultants have been engaged and are currently testing the modified software. This activity should be completed with all systems validated for Year 2000 readiness by June 1999.

The company has also substantially completed a personal computer upgrade program to ensure all machines are compliant. All telephone and communication systems as well as automated security and access systems at CAE Electronics, Montreal have been reviewed and modified and are Year 2000 compliant. In addition, letters of Year 2000 compliance have been received from all critical suppliers, and alternative suppliers have been identified. All customers have been contacted, informed and are satisfied with the operating company's Year 2000 program. CAE Electronics' products have been Year 2000 compliant since January 1, 1998, and the company has offered an update program to all customers for products delivered before that date.

As at March 31, 1999, CAE's other operating companies have completed the replacement or rewrite of software code of their existing operating and financial systems and have updated other date sensitive systems including communication and security systems. These companies have also contacted their suppliers to ensure the products and services they receive are Year 2000 compliant. Based on these communications, all significant products and services are already compliant and/or an alternative source of supply has been identified. In addition, the companies have initiated communications and/or responded to their customers on this matter. These companies have modified or replaced most of their systems affected by this issue. All remaining modifications have been identified and are expected to be completed over the next few months.

No assurance can be given that CAE will not be impacted by third party suppliers. Contingency plans, including alternate supply sources, have been identified wherever possible.

Excluding personal computer purchases, over the last two years CAE has spent over \$4 million on hardware and software to upgrade systems to be Year 2000 compliant. These expenditures go beyond just the Year 2000 issue as changes were needed to support the growth of the businesses. The cost of the computer hardware and software is depreciated over a three-year period. External consulting fees have been expensed as incurred. The cost of internal manpower assigned to the Year 2000 project team has also been expensed as incurred.

The effort for CAE's Year 2000 compliance has been substantially completed. However, further costs will be incurred in fiscal 2000, but are not expected to have a material impact on results.

Each operating company will continue to provide timely updates and progress reports as CAE enters the next millennium.

management and auditors' reports

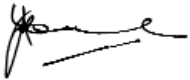
management report

Management is responsible for the integrity and objectivity of the information contained in this annual report and for the consistency between the financial statements and other financial and operating data contained elsewhere in the report. The accompanying financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada, using policies and procedures established by management, and reflect the Corporation's financial position, results of operations, and changes in financial position.

Management has established and maintains a system of internal control which is designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and that financial information is reliable and accurate. The Corporation also maintains an internal audit function that evaluates and formally reports to management and the Audit Committee on the adequacy and effectiveness of internal controls.

The financial statements have been examined by external auditors appointed by the shareholders. Their examination provides an independent view as to management's discharge of its responsibilities insofar as they relate to the fairness of reported operating results and financial condition. They obtain an understanding of the Corporation's accounting systems and procedures and conduct such tests and related procedures as they deem necessary to arrive at an opinion on the fairness of the financial statements.

Ultimate responsibility to the shareholders for the financial statements rests with the Board of Directors. An Audit Committee is appointed by the Board to review the financial statements in detail and to report to the Directors prior to such statements being approved for publication. The Audit Committee meets regularly with management, the internal auditors and the external auditors to discuss their evaluation of internal accounting controls, audit results and the quality of financial reporting. The external auditors have free access to the Audit Committee, without management's presence, to discuss the results of their audit.



john e. caldwell (signed)

President and

Chief Executive Officer



paul g. renaud (signed)

Vice President, Finance,

Chief Financial Officer, and Secretary

auditors' report to the
shareholders of cae inc.

We have audited the consolidated balance sheets of CAE Inc. as at March 31, 1999 and 1998 and the consolidated statements of earnings, retained earnings and changes in financial position for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance as to 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 Corporation as at March 31, 1999 and 1998 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.



PricewaterhouseCoopers LLP (signed)

Chartered Accountants

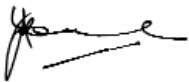
toronto, canada

april 28, 1999

consolidated balance sheets

as at march 31 (amounts in thousands of dollars)	1999	1998
assets		
current assets		
Cash	\$ 25,575	\$ 202,811
Accounts receivable	324,615	283,432
Inventories (note 4)	143,521	84,419
Prepaid expenses	16,493	7,656
Income taxes recoverable	25,698	3,399
	535,902	581,717
property, plant and equipment, net (note 5)	274,421	197,680
goodwill	233,560	76,691
other assets (note 6)	57,274	72,091
	\$ 1,101,157	\$ 928,179
liabilities and shareholders' equity		
current liabilities		
Accounts payable and accrued liabilities	\$ 231,490	\$ 246,655
Deposits on contracts	147,862	93,100
Long-term debt due within one year	936	1,072
	380,288	340,827
long-term debt (note 7)	298,180	269,855
other long-term liabilities (note 2)	75,194	17,233
deferred income taxes	9,220	23,811
	762,882	651,726
shareholders' equity		
Capital stock (note 9)	154,191	145,070
Retained earnings	194,233	134,668
Currency translation adjustment	(10,149)	(3,285)
	338,275	276,453
	\$ 1,101,157	\$ 928,179

Approved by the Board:



john e. caldwell (signed)
Director



david h. race (signed)
Director

consolidated statements of earnings

years ended march 31 (amounts in thousands of dollars, except per share amounts)	1999	1998
revenue	\$ 1,070,061	\$ 922,369
costs and expenses		
Manufacturing	797,204	687,365
Selling and administrative	116,977	105,847
Amortization	34,985	29,857
Interest expense, net	13,475	8,745
Other items (note 3)	—	(5,997)
	962,641	825,817
Earnings before income taxes	107,420	96,552
Income taxes (note 10)	30,078	26,316
net earnings	\$ 77,342	\$ 70,236
earnings per share	\$ 0.70	\$ 0.64
average number of shares outstanding	111,059	110,244

consolidated statements of retained earnings

years ended march 31 (amounts in thousands of dollars)	1999	1998
retained earnings at beginning of year	\$ 134,668	\$ 82,081
Net earnings	77,342	70,236
Dividends	(17,777)	(17,649)
retained earnings at end of year	\$ 194,233	\$ 134,668

consolidated statements of changes in financial position

years ended march 31 (amounts in thousands of dollars)	1999	1998
operating activities		
Net earnings	\$ 77,342	\$ 70,236
Add items not affecting cash		
Amortization	34,985	29,857
Deferred income taxes	(1,085)	8,508
Gain on disposition of business unit (note 3)	—	(19,000)
Other	(1,376)	(2,060)
	109,866	87,541
(Used for) Provided from non-cash working capital (note 11)	(93,462)	23,693
cash provided by operating activities	16,404	111,234
investing activities		
Proceeds on disposition of business unit (note 3)	—	67,192
Acquisitions (note 2)	(111,468)	(12,073)
Purchase of property, plant and equipment, net of proceeds from disposal	(82,458)	(66,473)
Decrease (increase) in other assets	15,621	(14,103)
cash used in investing activities	(178,305)	(25,457)
financing activities		
Net advance of long-term debt	10,253	118,214
Dividends, net of stock dividends	(17,557)	(17,256)
Foreign currency translation and other	(8,031)	(7,776)
cash (used in) provided by financing activities	(15,335)	93,182
cash (decrease) increase during the year	(177,236)	178,959
cash at beginning of year	202,811	23,852
cash at end of year	\$ 25,575	\$ 202,811

notes to consolidated financial statements

years ended march 31, 1999 and 1998 (amounts in thousands of dollars)

1. summary of significant accounting policies

Accounting policies of the Corporation and its subsidiaries conform with generally accepted accounting principles in Canada and reflect practices appropriate to the industries in which they operate.

Consolidation

The consolidated financial statements include the accounts of the Corporation and all subsidiaries. All inter-corporate accounts and transactions have been eliminated.

Acquisitions are accounted for by the purchase method and accordingly the results of operations of subsidiaries are included from the dates of acquisition.

Portfolio investments are accounted for using the cost method.

Revenue Recognition

Revenue from long-term contracts is recognized using the percentage of completion method, where revenue, earnings and unbilled accounts receivable are recorded as related costs are incurred. Revisions in cost and earnings estimates during the term of the contract are reflected in the period in which the need for revision becomes known. Losses, if any, are recognized fully when first anticipated.

All other revenue is recorded and related costs transferred to cost of sales at the time the product is shipped or the service is provided.

Cash

Cash consists of cash and cash equivalents which are short-term, highly liquid investments with maturity of 90 days or less.

Inventories

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

Property, Plant and Equipment

Property, plant and equipment is stated at cost. The declining balance and straight-line methods are used in computing amortization of property, plant and equipment based on the following useful lives: buildings and improvements, 20 to 40 years; machinery and equipment, 3 to 10 years; and property under capital lease, over the term of the lease.

Foreign Currency Translation and Financial Instruments

Assets and liabilities denominated in currencies other than Canadian dollars are translated at exchange rates in effect at the balance sheet date. Revenue and expense items are translated at average rates of exchange for the year. Translation gains or losses are included in the determination of earnings, except for gains or losses arising on translation of accounts of foreign subsidiaries considered self-sustaining and gains or losses arising from the translation of foreign currency debt that has been designated as a hedge of the net investment in subsidiaries, which are deferred as a separate component of shareholders' equity. Gains or losses arising from the translation of foreign currency debt not designated as a hedge of the net investment in subsidiaries are deferred, included in other assets and amortized on a straight-line basis over the term of the debt.

The Corporation enters into forward contracts to manage exposures resulting from foreign exchange fluctuations in the ordinary course of business. The contracts are normally for terms up to 12 months and are used as hedges of foreign denominated cash flows. Gains and losses on outstanding contracts are offset against the gains and losses of the hedged item at the maturity of the underlying transactions. The company negotiates forward contracts only with financially sound counterparties.

The carrying value of financial instruments approximate fair value except where indicated.

Goodwill

The excess purchase price paid on the acquisition of businesses over the value assigned to identifiable net assets acquired is allocated to goodwill. Goodwill is stated at cost less accumulated amortization and is being amortized on a straight-line basis over 40 years. The value of goodwill is evaluated by reviewing the financial returns of the related business, taking into account the risk associated with the business, and is written down when there has been an impairment of its value.

Income Taxes

The Corporation follows the tax allocation method of accounting for income taxes whereby earnings are charged with income taxes relating to reported earnings. Differences between such taxes and taxes currently payable or recoverable are reflected in deferred income taxes and arise because of differences between the time certain items of revenue and expense are reported in the accounts and the time they are reported for income tax purposes. Investment tax credits arising from research and development are deducted from the related costs and are accordingly included in the determination of earnings in the same year as the related costs. Investment tax credits arising from the acquisition of property, plant and equipment are deducted from the cost of those assets with amortization calculated on the net amount.

Post-Retirement Benefits

Pensions

Pension expense includes the cost of pension benefits, related to defined benefit plans, accrued for employees' services for the year and the past service costs, adjustments for plan amendments, and experience gains and losses amortized on a straight-line basis over the expected average remaining service life of the plan participants.

Benefits Other than Pensions

The Corporation accrues estimates of future costs of retiree post-employment benefits over the employees' average remaining service life. The long-term portion of all post-employment benefits is included in Other Long-Term Liabilities on the consolidated balance sheet.

Earnings per Share

The calculation of earnings per share is based on the weighted average number of shares outstanding. Conversion of the outstanding stock options would not materially dilute earnings per share.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of the contingent assets and liabilities at the date of the financial statements and revenue and expenses for the period reported. Actual results could differ from those estimates.

2. acquisitions

During fiscal 1999, the Corporation acquired the outstanding common shares of the following four companies:

- Alpheus Cleaning Technologies of Rancho Cucamonga, California, a designer and manufacturer of CO₂ dry ice blast cleaning equipment, effective June 3, 1998;
- Newnes Machine Ltd. of Salmon Arm, British Columbia, and McGehee Equipment Company of Ukiah, California, manufacturers of optimization equipment for the forest products industry, effective June 29, 1998;
- Beyss GmbH Co. KG of Aachen, Germany, a leading supplier of cleaning equipment in Europe, effective October 5, 1998.

The consideration was \$193 million and included cash of \$99.9 million, the assumption of \$11.6 million of debt, 600,000 common shares issued for \$7 million, and the balance, \$74.5 million of estimated contingent consideration, which has been accrued and is payable over a period not to exceed five years, based primarily on the future earnings of the acquired companies. If a change in the estimated contingent consideration is determinable an adjustment will be recorded to goodwill. The long-term portion of the accrual is included in Other Long-term Liabilities on the consolidated balance sheet.

During fiscal 1998, the Corporation made the following acquisitions:

- acquired the outstanding common shares of Tempest & Dibb Ltd., a manufacturer of industrial part washers located in Bradford, England, for cash, effective February 27, 1998;
- acquired the assets of Ney Ultrasonics, Inc. of Bloomfield, Connecticut, a manufacturer of ultrasonic cleaning equipment for cash and future consideration based on future earnings of the acquired company, effective February 28, 1998.

The net assets acquired from these acquisitions, at fair values, are summarized as follows:

	1999	1998
Net working capital	\$ 13,691	\$ 4,180
Property, plant and equipment	22,747	1,349
Goodwill	156,549	6,544
	\$ 192,987	\$ 12,073

3. other items

In 1998, the consolidated net earnings included a pre-tax gain for the following non-recurring items:

	1998
Gain on disposition of CAE Aviation (i)	\$ (19,000)
Foreign currency translation gain (ii)	(7,495)
Reorganization and rationalization of certain product lines (iii)	13,344
Consolidation of screen plate manufacturing operations (iv)	4,500
Writedown of investment in subsidiary (v)	2,654
	\$ (5,997)

(i) *Disposition of CAE Aviation*

On January 28, 1998, the Corporation completed the sale of substantially all the assets of CAE Aviation Ltd., a wholly owned subsidiary that provides aircraft maintenance system upgrades and publication services for commercial and military aircraft, resulting in a gain on disposition of \$19 million. The Corporation received proceeds of \$63.9 million, of which \$57.5 million was received in 1998. The purchase price is subject to further increases contingent upon the future award of a specific contract, the outcome of which is not currently determinable.

(ii) *Foreign Currency Translation Gain*

During fiscal 1998, the Corporation reorganized the ownership structure of its European wholly-owned subsidiary companies. As a result of the reorganization, a \$7.5 million gain from currency translation adjustments, previously deferred as part of Shareholders' Equity, was realized.

(iii) *Reorganization and Rationalization
of Certain Product Lines*

During fiscal 1998, CAE Electronics Ltd. was reorganized along four product lines – Commercial Simulation and Visual Systems, Military Systems and Training, Energy Systems and Marine Systems. As part of the reorganization and after careful review of future opportunities and the likelihood of achieving acceptable financial returns, the Corporation decided to discontinue its activities in Air Traffic Control, Advanced Aircraft Maintenance Systems and Process Control Training Systems.

(iv) *Consolidation of North American
Screen Plate Manufacturing*

In September 1997, the Corporation announced and subsequently completed the consolidation of its North American screen plate manufacturing operations with its Lennoxville, Quebec, facility resulting in the closure of the Glens Falls, New York, manufacturing operation. The cost for employee terminations and the writedown of assets to their net realizable value was \$4.5 million.

(v) *Writedown of Investment in
Swedish Screen Plate Operation*

As at March 31, 1998, it was determined that there had been an impairment in the carrying value of the Swedish screen plate operation and, accordingly, the Corporation wrote down the carrying value of related assets by \$2.7 million.

4. inventories

	1999	1998
Work in progress	\$ 88,021	\$ 52,862
Raw materials, supplies and manufactured products	55,500	31,557
	\$ 143,521	\$ 84,419

5. property, plant and equipment

1999	cost	accumulated amortization	net book value
Land	\$ 12,412	\$ —	\$ 12,412
Buildings and improvements	188,546	36,949	151,597
Machinery and equipment	250,618	147,576	103,042
Property under capital leases	12,543	5,173	7,370
	\$ 464,119	\$ 189,698	\$ 274,421

1998	cost	accumulated amortization	net book value
Land	\$ 9,529	\$ —	\$ 9,529
Buildings and improvements	113,185	32,031	81,154
Machinery and equipment	227,457	127,489	99,968
Property under capital leases	11,447	4,418	7,029
	\$ 361,618	\$ 163,938	\$ 197,680

6. other assets

	1999	1998
Investment tax credits (i)	\$ 29,355	\$ 56,694
Investment in and advances to CVS Leasing Ltd. (ii)	9,082	5,235
Deferred charges (ii)	8,993	8,596
Other	9,844	1,566
	\$ 57,274	\$ 72,091

- (i) Investment tax credits are available to reduce future federal income taxes payable in Canada.
- (ii) During fiscal 1998, the Corporation 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 fleet of the Royal Air Force. The contract covers a 40-year period, which can be terminated by the MoD after 20 years.

In connection with the contract, the Corporation has established a subsidiary, CAE Aircrew Training Plc (“Aircrew”) (formerly CVS Aircrew Training Plc), which it owns 74% thereof with the balance held by the other consortium partners. This subsidiary has leased the land from the MoD, has built the facility and will operate the training centre, and has been consolidated with the accounts of the Corporation.

The pre-operating expenditures in connection with this contract are being deferred until the aircrew training facility is ready for training and will be amortized over the remaining life of the initial 20-year period of the contract.

In addition, the Corporation has a minority shareholding of 11% in, and has advanced funds to, CVS Leasing Ltd., a company established to acquire the simulators and other equipment which will be leased to Aircrew.

7. debt facilities

A. Long-term Debt

	1999	1998
Senior notes (i), (v)	\$ 182,994	\$ 172,993
Five-year revolving term loan, to a maximum of US\$220,000, unsecured, due May 31, 2002 (v)	—	—
Five-year revolving term loan, to a maximum of Deutschmark 100,000, unsecured, due May 31, 2002 (ii), (v)	83,410	76,590
Eighteen-year term loan, to a maximum of £12,700, secured, maturing April 1, 2001 to October 1, 2015 (1999 – £9,900, 1998 – £6,218) (iii), 6 (ii), (v)	24,122	14,745
Obligations under capital lease commitments (iv), (v)	8,590	6,599
	299,116	270,927
Less: Long-term debt due within one year	936	1,072
	\$ 298,180	\$ 269,855

- (i) In June, 1997, pursuant to a private placement with certain investors, the Corporation borrowed US\$108 million and \$20 million. These unsecured senior notes, which rank equally with the term bank financing, are repayable after 8, 10, 12 and 15 years. Fixed interest of approximately 7.5% is payable semi-annually in June and December.
- (ii) Interest on bank term loans is charged at rates approximating LIBOR.
- (iii) In October, 1997, the Corporation arranged project financing for its subsidiary to finance the Corporation's Medium Support Helicopter Program for the Ministry of Defence in the United Kingdom. This term loan is secured by the project assets of the subsidiary and is repayable over 18 years to October 1, 2015. Interest on the loan is charged at a rate approximating LIBOR.
- (iv) The effective interest rate on obligations under capital leases was approximately 7.3% (1998 – 7.3%).

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

Year ending March 31,	2000	\$	936
	2001		3,963
	2002		90,013
	2003		4,329
	2004		3,244
	Thereafter		196,116
		\$	299,116

Interest expense on long-term debt was \$ 15.6 million (1998 – \$10.0 million).

The fair value of the long-term debt at March 31, 1999, including the effect of related interest rate swap agreements, is approximately \$318 million.

B. Short-term Debt

The Corporation has unsecured bank lines of credit available in various currencies totalling \$84.0 million (1998 – \$91.8 million). The effective interest rate on short-term borrowings was 7.6% (1998 – 5.9%).

8. financial instruments

The Corporation has estimated the fair values of its financial instruments as at March 31, 1999 using quoted market values where available and other information.

At March 31, 1999, the Corporation had outstanding forward contracts to hedge its foreign currency cash flows into Canadian dollars. These forward exchange contracts have maturity dates up to October, 2000. The fair value of these contracts if marked to market at March 31, 1999 would result in a loss of \$5.5 million. This would be equally offset by future gains of foreign denominated cash flows over the remaining terms of the contracts.

Effective June 9, 1997, the Corporation entered into interest rate swap agreements with two different financial institutions for a total nominal value of \$70 million whereby in the first instance the Corporation will receive a fixed interest rate of 7.2% semi-annually for 8 years and in the second instance the Corporation will receive a fixed interest rate of 7.7% semi-annually for 15 years. In both cases, the Corporation will pay quarterly variable interest established at bankers acceptance rates.

Pursuant to the requirements of its long-term project financing, on October 16, 1997, the Corporation's subsidiary entered into an interest rate swap agreement with two financial institutions for a maximum total nominal value of £12.7 million whereby the subsidiary will receive payments of floating rate interest and will pay a fixed interest rate of 6.8% semi-annually for 13 years.

Receipts and payments under interest rate swap agreements have been accounted for as adjustments to interest expense on long-term debt.

The fair value of the interest rate swap agreements if marked to market at March 31, 1999, would result in a loss of \$1.7 million.

9. capital stock

- (i) The Corporation's articles of incorporation authorize the issue of an unlimited number of preferred shares, issuable in series, and an unlimited number of common shares. To date the Corporation has not issued any preferred shares.
- (ii) A reconciliation of the issued common shares of the Corporation follows:

	1999		1998	
	number of shares	stated value	number of shares	stated value
Balance at beginning of year	110,490,405	\$ 145,070	110,040,146	\$ 142,046
Stock options exercised (a)	352,275	1,890	415,101	2,631
Stock dividends (b)	23,352	220	35,158	393
Treasury issue (note 2)	600,000	7,011	—	—
Balance at end of year	111,466,032	\$ 154,191	110,490,405	\$ 145,070

- (a) During the year, the Corporation granted 706,000 options, exercisable at \$12.85 per share, to purchase common shares to certain officers and key employees of the Corporation and its subsidiaries. The option price was equal to the closing price of the common shares on the Toronto Stock Exchange on the trading day immediately prior to the day the stock options were issued.

Stock options were outstanding at March 31, 1999 for the purchase of 2,500,800 common shares at prices ranging from \$7.25 to \$12.85 and expiring during the period from 1999 to 2004. 352,275 options were exercised, and 256,874 options expired in the year.

- (b) The Corporation provides that its shareholders may elect to receive common stock dividends in lieu of cash dividends.
- (c) The Corporation has a Plan for the Equal Treatment of Shareholders whereby one right has been issued for each outstanding common share of the Corporation. The rights remain attached to the shares and are not exercisable until the occurrence of certain designated events. The rights expire on March 7, 2000, unless terminated at an earlier date by the Board of Directors.

10. income taxes

The provision for income taxes comprises:

	1999		1998	
Current	\$	31,163	\$	17,808
Deferred		(1,085)		8,508
	\$	30,078	\$	26,316

The Corporation's effective income tax provision has been determined as follows:

	1999	1998
Combined federal and provincial statutory rate (1999 and 1998 – 44.6%)	\$ 47,930	\$ 43,081
Income taxed at different rates in other jurisdictions	(11,678)	(9,415)
Manufacturing and processing allowance	(6,290)	(6,285)
Tax benefit of losses not previously recognized	(4,494)	2,745
Research and development investment tax credits	(610)	(890)
Other	5,220	(2,920)
Income taxes	\$ 30,078	\$ 26,316

At March 31, 1999, the Corporation had accumulated non-capital losses for income tax purposes relating to operations in the United States, the potential benefit of which has not been recognized in the financial statements, as follows:

(stated in u.s. dollars)

Losses for income tax purposes	\$ 163,000
Amounts provided for in the financial statements which have not yet been claimed for income tax purposes	14,000
	\$ 177,000

The losses for income tax purposes expire in the years 2005 through 2013.

11. supplementary cash flow information

Cash provided from (used for) non-cash working capital:

	1999	1998
Accounts receivable	\$ (7,246)	\$ (56,480)
Inventories	(39,333)	(14,322)
Prepaid expenses	(8,225)	(1,233)
Income taxes recoverable	(24,648)	9,004
Accounts payable and accrued liabilities	(53,267)	41,384
Deposits on contracts	39,257	45,340
	\$ (93,462)	\$ 23,693

12. contingencies

(a) Through the normal course of operations, the Corporation 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 Corporation has no reason to believe that the ultimate outcome of these matters will have a material impact on its financial position.

(b) The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the Year 2000 as 1900 or some other date, resulting in errors when information using Year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers or other third parties, will be fully resolved.

13. government cost sharing

During fiscal 1997, the Corporation signed an agreement with the Government of Canada under which the Government will share in the costs of certain research and development programs over the period of 1997 to 2001. Funding under this program will not exceed \$31.2 million and is repayable in the form of royalties based on future sales levels related to the projects funded. Funding received or receivable under this program of \$19.3 million (1998 – \$11.6 million) reduced research and development expenses.

14. operating lease commitments

Future minimum lease payments under operating leases, the most significant of which relate to the Medium Support Helicopter contract with the U.K. MoD as described in Note 6 (ii), are as follows:

Year ending March 31,	2000	\$	15,323
	2001		36,979
	2002		33,027
	2003		35,295
	2004		34,114
	Thereafter		243,257
		\$	397,995

15. pensions

The Corporation has defined benefit plans that provide benefits based on length of service and final average earnings. The Corporation has an obligation to ensure there are sufficient funds in the plans to pay the benefits earned.

The actuarial present value of accrued pension benefits has been estimated taking into consideration economic and demographic factors over an extended future period. Significant assumptions used in the calculation are as follows:

	1999	1998
Return on plan assets	9.0%	9.0%
Discount rate for pension benefit obligations	8.0%	8.0%
Compensation rate increases	3.5% to 6.0%	3.5% to 6.0%

The funded status of the defined benefit pension plans at March 31 was as follows:

	1999	1998
Market value of assets	\$ 114,773	\$ 117,587
Present value of accrued pension benefits	\$ 97,349	\$ 95,409

16. business segments

In 1999, the Corporation adopted Canadian Institute of Chartered Accountants Section 1701, Segment Disclosures, which establish standards for reporting information about operating segments in financial statements issued to shareholders. Operating segments are defined as components of an enterprise about which separate financial information is available and which is evaluated regularly by senior management of the Corporation, in deciding how to allocate resources and in assessing performance.

The Corporation's significant operating segments include:

- (i) CAE Electronics Group – the world-leading supplier of commercial and military flight simulators and visual systems and also supplies a variety of other military simulation and training systems, real-time energy control systems and marine control systems. The CAE Electronics Group consists of six strategically located operations – CAE Electronics Ltd. (Canada), CAE Elektronik GmbH (Germany), CAE Electronics plc. (United Kingdom), CAE Electronics Inc. (United States), CAE Electronics (Australia) Pty Ltd. and CAE Aircrew Training Services plc (United Kingdom).
- (ii) CAE Fiber Processing Technologies supplies precision-engineered sawmill and composite wood products equipment, as well as advanced filtering equipment for the forest products, petrochemical and waste water industries. CAE Fiber Processing Technologies consists of CAE ScreenPlates, CAE Trislot, CAE Machinery, CAE Newnes and CAE McGehee.
- (iii) CAE Cleaning Technologies – North America's leading designer and supplier of advanced technology cleaning systems and associated waste minimization equipment and services for industrial cleaning. CAE Cleaning Technologies comprises six operating units – CAE Ransohoff, CAE Environmental Systems, CAE Ultrasonics, CAE Cleaning Technologies plc, CAE Alpheus, and CAE Beyss.
- (iv) CAE Railway Technologies & Services – this subsidiary is a leader in advanced maintenance technologies for North American Freight and Transit Railways. The subsidiary provides complete maintenance, repair and overhaul services for locomotive and freight car axles as well as locomotive traction motor combos.

Each operating segment is led by a president and offers different products and uses different technology and marketing strategies. The Corporation evaluates performance based on operating earnings before interest and income taxes and uses capital employed to assess resources allocated to each segment. Capital employed includes accounts receivable, inventories, prepaid expenses, property, plant and equipment, goodwill and other assets less accounts payable and accrued liabilities, deposits on contracts and contingent consideration due on acquisitions included in other long-term liabilities.

Financial information on the Corporation's operating and geographic segments is shown in the following table.

segmented information:

	1999	1998
revenue		
CAE Electronics Group	\$ 736,782	\$ 715,272
CAE Fiber Processing Technologies	197,373	109,444
CAE Cleaning Technologies	83,990	59,577
CAE Railway Technologies and Services	51,916	38,076
	\$ 1,070,061	\$ 922,369
operating earnings		
CAE Electronics Group	\$ 82,289	\$ 74,384
CAE Fiber Processing Technologies	33,339	16,299
CAE Cleaning Technologies	3,400	5,252
CAE Railway Technologies and Services	4,471	3,783
other items, (note 3)	-	5,997
corporate costs	(2,604)	(418)
earnings before interest and taxes	\$ 120,895	\$ 105,297
capital employed		
CAE Electronics Group	\$ 296,920	\$ 200,748
CAE Fiber Processing Technologies	168,343	71,600
CAE Cleaning Technologies	91,754	47,222
CAE Railway Technologies and Services	34,719	33,330
Other	3,602	12,081
total capital employed	\$ 595,338	\$ 364,981
Cash	25,575	202,811
Income taxes recoverable	25,698	3,399
Accounts payable and accrued liabilities	231,490	246,655
Deposits on contracts	147,862	93,100
Other long-term liabilities	75,194	17,233
total assets	\$ 1,101,157	\$ 928,179

segmented information (continued):

	1999	1998
capital expenditures, net of proceeds on disposal		
CAE Electronics Group	\$ 69,023	\$ 57,431
CAE Fiber Processing Technologies	7,462	6,336
CAE Cleaning Technologies	2,611	1,526
CAE Railway Technologies and Services	3,362	1,180
	\$ 82,458	\$ 66,473
amortization		
CAE Electronics Group	\$ 19,428	\$ 19,474
CAE Fiber Processing Technologies	10,146	6,441
CAE Cleaning Technologies	4,041	1,736
CAE Railway Technologies and Services	1,370	2,206
	\$ 34,985	\$ 29,857
total additions to goodwill		
CAE Fiber Processing Technologies	\$ 130,065	\$ —
CAE Cleaning Technologies	26,484	6,544
	\$ 156,549	\$ 6,544

geographic segments:

	1999	1998
revenue from external customers		
Canada	\$ 142,149	\$ 159,531
USA	417,136	319,644
Europe	358,111	298,396
Other Countries	152,665	144,798
	\$ 1,070,061	\$ 922,369
capital assets and goodwill		
Canada	\$ 221,500	\$ 109,432
USA	144,746	60,277
Europe	123,637	85,389
Other Countries	18,098	19,273
	\$ 507,981	\$ 274,371

Revenues are attributed to countries based on location of customer.

research and development:

Research and Development expenditures aggregated \$118.3 million during the year (1998 – \$96.6 million).

five-year review

(amounts in thousands of dollars
except when indicated by *)

	1999	1998	1997	1996	1995
continuing operations					
Revenue	\$ 1,070,061	922,369	867,344	809,803	657,592
Amortization	\$ 34,985	29,857	28,317	22,719	16,613
Earnings	\$ 77,342	70,236	60,276	58,591	47,327
Earnings per share*	\$ 0.70	0.64	0.55	0.54	0.44
Net earnings	\$ 77,342	70,236	60,276	58,591	15,631
Net earnings per share*	\$ 0.70	0.64	0.55	0.54	0.14
Ratio of current assets to current liabilities*	1.4	1.7	1.4	0.9	1.0
Number of registered shareholders*	2,600	2,800	3,100	3,400	3,800
Cash dividends paid per common share*	\$ 0.16	0.16	0.16	0.16	0.16

quarterly financial information

(amounts in thousands of dollars
except per share amounts)

	first quarter	second quarter	third quarter	fourth quarter
1999				
Revenue	\$ 205,836	276,912	279,062	308,251
Net earnings	\$ 12,969	17,517	23,032	23,824
Net earnings per share	\$ 0.12	0.16	0.21	0.21
Common share trading range:				
High	\$ 13.65	12.75	10.05	9.00
Low	\$ 11.25	8.30	8.00	7.85

(amounts in thousands of dollars
except per share amounts)

	first quarter	second quarter	third quarter	fourth quarter
1998				
Revenue	\$ 186,933	212,316	243,664	279,456
Net earnings	\$ 7,926	9,152	21,007	32,151
Net earnings per share	\$ 0.07	0.08	0.19	0.30
Common share trading range:				
High	\$ 11.75	11.80	13.00	11.60
Low	\$ 10.20	10.40	10.90	10.95



letter from david h. race

A year ago, your Board of Directors set as a goal to go beyond its traditional role of management oversight, the review and approval of plans, and monitoring progress against specific objectives. While management remains accountable for strategy, we believe your Board should further contribute to the success of the company by drawing upon its skills and experience to specifically assist and counsel management in this area. Accordingly, we set our agenda to focus Board attention and effort on strategy at both a consolidated and divisional level.

Your Board was active in fiscal 1999, meeting seven times including two full day visits to major company facilities and a three day strategy session. In addition, Board committees met 14 times.

Your Board believes that to create sustained increases in shareholder value requires a clear, focussed strategy effectively executed, and a superior performance as measured by annual financial results and by the criteria of our customers. Your Board is pleased with the performance of the company in fiscal 1999 as it met its goals for the year. Equally as important, we are confident in the future of CAE.

Mr. Michael Koerner will retire from the Board of Directors in June 1999. Mr. Koerner has been a member of CAE's Board since 1981 and has served in numerous committees over the years including the Audit, Compensation, Governance and Succession committees. Your Board benefited in no small measure from Mr. Koerner's experience and advice. On the occasion of his retirement from the Board and on behalf of the shareholders, I wish to extend our thanks to Mr. Koerner for his unfailing support, valuable counsel and dedication to CAE during his tenure.

On a personal note, June 16, 1999 will be a special occasion for me as I step down as Chairman of the Board. I have been associated with CAE since 1951. In the intervening 48 years, it has been my privilege to work at virtually every level of the differing CAE structures from that of engineer, through the management ranks to President and Chief Executive Officer and then, during the past six years as Chairman. I have many wonderful memories of those years but uppermost are my memories of the CAE people with whom I have been associated – fellow employees, customers, shareholders, suppliers, directors. These people, with the leadership of my predecessors in the CEO and Chairman's office, are the ones who have shaped the culture which is the CAE of today. It is this culture which will ensure the continuing future growth and success of your Company.

I would at this time wish to record my appreciation and my thanks to all the directors, past and present, who through the years have so willingly given me their support, their wise counsel and their "friendly" advice.

At the Annual General Meeting in June, a new Chairman is to be appointed. I wish our new Chairman, the shareholders and employees of CAE continued success in furthering CAE as a truly world leading, Canadian technology enterprise.

A handwritten signature in dark ink that reads "David Race". The signature is written in a cursive, slightly stylized font.

david h. race (signed)

Chairman of the Board

board of directors

david h. race^{1,3,4,5}

Chairman of the
Board of Directors
CAE Inc.
Toronto, Ontario

john e. caldwell¹

President and
Chief Executive Officer
CAE Inc.
Toronto, Ontario

r. fraser elliot,

c.m., q.c.¹

Senior Partner
Stikeman, Elliott
Toronto, Ontario

h. garfield emerson,

q.c.²

President and
Chief Executive Officer
NM Rothschild & Sons Canada
Limited
Toronto, Ontario

the honourable

james a. grant,

p.c., q.c.^{1,3}

Partner
Stikeman, Elliott
Montreal, Quebec

james f. hankinson²

President and
Chief Executive Officer
New Brunswick Power
Corporation
Fredericton, New Brunswick

roderick l. henry^{4,5}

President
Henrod Investments Inc.
Montreal, Quebec

michael m. koerner, c.m.⁵

President
Canada Overseas Investments
Limited
Toronto, Ontario

james w. mccutcheon,

q.c.³

Counsel
McCarthy Tétrault
Toronto, Ontario

george k. petty^{3,4}

President and
Chief Executive Officer
BCT. Telus
Edmonton, Alberta

lawrence n. stevenson⁴

President and
Chief Executive Officer
Chapters, Inc.
Toronto, Ontario

dr.-ing. hasso von

falkenhausen^{2,5}

Chairman of the
Board of Directors
DataCard Corp.
Minneapolis, Minnesota, U.S.A.

lynton r. wilson, o.c.^{1,2,3,4}

Chairman of the Board
BCE Inc.
Toronto, Ontario

1 Member of the Executive Committee

2 Member of the Audit Committee

3 Member of the Compensation Committee

4 Member of the Governance Committee

*5 Member of the Board Succession
Committee*

officers

david h. race

Chairman of the
Board of Directors

john e. caldwell

President and
Chief Executive Officer

fred veuger

Group President

paul g. renaud

Vice President, Finance,
Chief Financial Officer, and
Secretary

robert e. waite

Vice President
Corporate Relations and
Marketing

allan m. bignell

Vice President
Business Development

ruth h. brothers

Vice President
Human Resources

michael a. cossar

Treasurer

robert c. hedges

Controller and
Assistant Secretary

information for shareholders

cae common shares

CAE's shares are traded both on the Toronto Stock Exchange and the Montreal Stock Exchange under the symbol "CAE".

dividend reinvestment plan

Registered shareholders of CAE Inc. wishing to receive dividends in the form of CAE Inc. Common Shares rather than a cash payment may participate in CAE's dividend reinvestment plan.

Through this plan, quarterly dividends can be reinvested in CAE Common Shares at the Average Market Price. This price will be the weighted average trading prices of the Common Shares on each of the Toronto Stock Exchange and the Montreal Stock Exchange for the five (5) trading days immediately preceding the dividend payment date.

In order to obtain the dividend reinvestment plan form or for additional information regarding CAE's Common Shares, please contact:

Montreal Trust Company

Tel: (416) 981-9500
1-800-663-9633

direct deposit dividend

Registered shareholders who receive cash dividends may elect to have the dividend payment deposited directly to their bank account instead of receiving a cheque. In order to obtain the direct deposit dividend form please contact:

Montreal Trust Company

Tel: (416) 981-9500
1-800-663-9633

tentative quarterly results release dates for fiscal 2000

August 5, 1999
November 4, 1999
February 3, 2000
May 4, 2000

additional information

If you wish to receive additional copies of CAE's annual report or copies of the annual information form, please contact:

CAE Inc.

Corporate Relations
Royal Bank Plaza, Suite 3060,
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Tel: (416) 865-0070

1-800-760-0667

Fax: (416) 865-0337

Internet address: <http://www.cae.com>

version française

La version française du rapport annuel est disponible sur demande au département des relations d'entreprise, Royal Bank Plaza, Bureau 3060, C.P. 30, Toronto, Ontario m5j 2j1

annual meeting

The Annual Meeting of shareholders will be held at the Glenn Gould Studio, CBC Building, 250 Front Street West, Toronto, ON Wednesday, June 16, 1999, at 11:30 a.m.

auditors

PricewaterhouseCoopers, Chartered Accountants
Toronto, Ontario

transfer agent and registrar

Montreal Trust Company
Toronto, Ontario
Montreal, Quebec
Vancouver, British Columbia

trademarks

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Jamestown, U.S.
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