EXFO INC.
Form 20-F/A
December 10, 2012

This amended annual report on Form 20-F includes: i) the English version of the Auditor's Report in replacement of its French version filed in the November 26, 2012 filing; ii) the certifications dated December 10, 2012 on Exhibits 12-1; 12-2; 13-1 and 13-2 and excludes all other exhibits filed on the November 26, 2012 filing.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g)
OF THE SECURITIES EXCHANGE ACT OF 1934; or

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended August 31, 2012; or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the transition period ________ to ________; or

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
Date of event requiring this shell company report

Commission File No. 0-30895

EXFO INC.
(Exact name of registrant as specified in its charter)

Not Applicable
(Translation of Registrant’s name into English)

Canada
(Jurisdiction of Incorporation or organization)

400 Godin Avenue, Quebec, Quebec, G1M 2K2, Canada
(Address of principal executive offices)

Benoit Ringuette, (418) 683-0211, benoit.ringuette@exfo.com, (418) 683-9839, 400 Godin Avenue,
Quebec, Quebec, G1M 2K2, Canada
(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

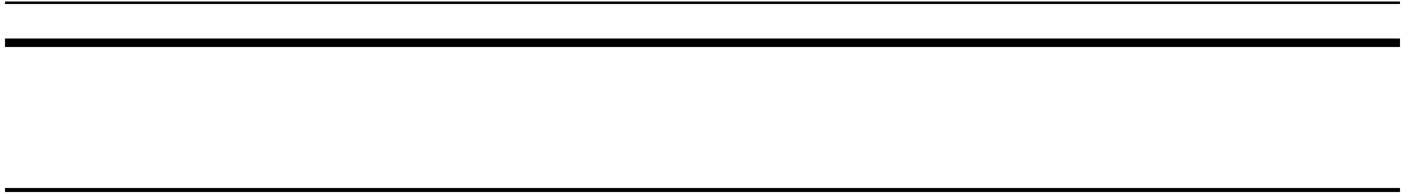
Title of each class	Name of each exchange on which registered
Subordinate Voting Shares without par value	NASDAQ
Subordinate Voting Shares without par value	TSX

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

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None



As of August 31, 2012, the registrant had 28,710,891 Subordinate Voting Shares outstanding and 31,643,000 Multiple Voting Shares outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes o No x

If this report is an annual report or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP	o	International Financial Reporting Standards as issued by the International Accounting Standards Board	x	Other	o

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 o

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

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DISCLOSURE REGARDING FORWARD-LOOKING INFORMATION

This Annual Report contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition. Words such as may, will, expect, believe, plan, anticipate, intend, could, estimate, continue, or similar expressions or the negative of such expressions are intended to identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events and circumstances are considered forward-looking statements. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including, but not limited to, macro-economic uncertainty and/or recession (including our ability to quickly adapt cost structures with anticipated levels of business and our ability to manage inventory levels with market demand); capital spending and network deployment levels in the telecommunications industry; future economic, competitive, financial and market conditions; limited visibility with regards to customer orders and the timing of such orders; fluctuating exchange rates; consolidation in the global telecommunications test and service assurance industry and increased competition among vendors; concentration of sales; timely release and market acceptance of our new products and other upcoming products; our ability to successfully integrate businesses that we acquire; our ability to successfully expand international operations; and our retention of key technical and management personnel. Assumptions relating to the foregoing involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. Other risk factors that may affect our future performance and operations are detailed in this Annual Report. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure you that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document.

All dollar amounts in this Annual Report are expressed in US dollars, except as otherwise noted.

PART I.

Item 1. Identity of Directors, Senior Management and Advisers

Not Applicable.

Item 2. Offer Statistics and Expected Timetable

Not Applicable.

Item 3. Key Information

A. Selected Financial Data

The consolidated statements of earnings data for the years ended August 31, 2011 and 2012 and the consolidated balance sheets data as at September 1, 2010 and August 31, 2011 and 2012 have been derived from our audited consolidated financial statements that are included elsewhere in this Annual Report, which have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB).

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The selected financial data should be read in conjunction with our audited consolidated financial statements and the related notes included elsewhere in this Annual Report, and "Item 5. Operating and Financial Review and Prospects" of this Annual Report.

	Years ended August 31, 2012	2011
	(in thousands of US dollars, except share and per share data)	
Consolidated Statements of Earnings Data:		
Sales	$ 249,966	$ 269,743
Cost of sales (1, 2)	91,792	100,296
Selling and administrative (2)	94,139	87,062
Net research and development (2)	49,854	47,927
Depreciation of property, plant and equipment	6,169	6,655
Amortization of intangible assets	7,819	9,183
Changes in fair value of cash contingent consideration	(311)	(2,685)
Earnings from operations	504	21,305
Interest and other income	131	511
Foreign exchange loss	(657)	(3,808)
Earnings (loss) before income taxes	(22)	18,008
Income taxes	3,571	8,814
Net earnings (loss) from continuing operations	(3,593)	9,194
Net earnings from discontinued operations		12,926
Net earnings (loss) for the year	$ (3,593)	$ 22,120
Basic and diluted net earnings (loss) from continuing operations per share	$ (0.06)	$ 0.15
Basic net earnings from discontinued operations per share	$	$ 0.22
Diluted net earnings from discontinued operations per share	$	$ 0.21
Basic net earnings (loss) per share	$ (0.06)	$ 0.37
Diluted net earnings (loss) per share	$ (0.06)	$ 0.36
Basic weighted average number of shares used in per share calculations (000's)	60,453	60,000
Diluted weighted average number of shares used in per share calculations (000's)	60,453	61,488
Other consolidated statements of earnings data:		
Gross research and development	$ 59,282	$ 57,226
Net research and development	$ 49,854	$ 47,927

	As at August 31, 2012	As at August 31, 2011	As at September 1, 2010
		(in thousands of US dollars)	
Consolidated Balance Sheets Data:			
Cash	$ 58,868	$ 22,771	$ 21,440
Short-term investments	8,236	47,091	10,379
Total assets	306,683	322,355	274,432
Long-term debt (excluding current portion)	282	968	1,419
Share capital	110,965	110,341	106,126
Shareholders' equity	$ 253,281	$ 264,511	$ 218,689

(1) The cost of sales is exclusive of depreciation and amortization, shown separately.

(2) Include restructuring charges of $264,000 (nil in 2011) in cost of sales, $1,181,000 (nil in 2011) in selling and administrative expenses and $884,000 (nil in 2011) in net research and development expenses.

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B. Capitalization and Indebtedness

Not Applicable.

C. Reasons for the Offer and Use of Proceeds

Not Applicable.

D. Risk Factors

Our business and operating results could continue to be adversely affected by unfavorable macro-economic and market conditions, resulting in reductions of capital and operating expenditures by our customers.

Broad macro-economic weakness previously resulted in sustained periods of decreased demand for our products and services that have adversely affected our operating results. In response to these conditions, many of our customers significantly reduced their capital and operating expenditures as they sought to conserve capital, reduce debt or address uncertainties or changes in their own business models.

Weak market conditions in the telecommunications industry continued in fiscal 2012 due a sluggish global economic environment, the European debt crisis and its effects on other regional economies, as well as decreased capital spending among network operators. We are uncertain as to how long these weak macro-economic and market conditions will persist, the pace of recovery, and the magnitude of the impact of these market conditions on our business and results of operations.

Continued or increasingly adverse economic and market conditions could result in, among other things:

- Difficulty forecasting, budgeting and planning due to the uncertain spending plans of current or prospective customers;
- Increased competition for fewer network projects and sales opportunities;
- Increased pricing pressure that may adversely affect revenue and gross margin;
- Higher cost structure compared to revenue level;
- Increased risk of charges related to excess and obsolete inventories and the write off of other intangible assets and goodwill;
- Customer financial difficulty and increased difficulty in collecting accounts receivable; and
- Additional restructuring costs.

Our business and operating results could continue to be materially affected by periods of unfavorable macro-economic and market conditions or the worsening of those conditions, globally or specific to a particular region where we operate, and any resulting reductions in the level of capital and operating expenditures by our customers.

Fluctuations in the exchange rates between the Canadian dollar, US dollar, euro and other currencies may adversely affect our operating results.

Most of our sales are denominated in US dollars and euros. However, a significant portion of our cost of goods sold, operating expenses and capital expenditures are denominated in Canadian dollars and foreign currencies such as euros, British Pounds, Rupees (India) and Renminbis (China). As a result, even though we manage to some extent our

exposure to currency risks with forward exchange contracts (by selling US dollars for Canadian dollars) and certain operating expenses denominated in currencies other than the Canadian dollar, we are exposed to fluctuations in the exchange rates between the US dollar on one hand and the Canadian dollar, euro and other currencies on the other. For example, the average exchange rate of the Canadian dollar versus the US dollar was 1.0094 in fiscal 2012 compared to 0.9894 in fiscal 2011, resulting in a decrease of 2.0% of our Canadian-based costs year-over-year when reported in US dollars. Any decrease in the value of the US dollar relative to the Canadian dollar and other currencies, or any unfavorable variance between the value of the Canadian dollar and the contractual rates of our forward exchange contracts, could have a material adverse effect on our operating results and provide competitive advantages to our competitors.

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We must continue to overcome significant competition in our targeted industries in order to gain market share and achieve our growth strategy.

The market for our business activity namely designing, manufacturing, marketing and selling telecommunications test and service assurance equipment for fixed and mobile networks is rapidly evolving and is marked by intense competition and technical innovation. We anticipate the pace of change to remain high or even accelerate for our targeted industries in the future. We might see the emergence of new competitors or the consolidation of current competitors, as the market for telecommunications test and service assurance equipment evolves in response to technical innovations and economic conditions.

Main competitors in the test environment include global suppliers like Anritsu Corporation, JDS Uniphase Corporation, and Yokogawa Electric Corporation, as well as other players like Fluke (an operating division within Danaher Corporation), IXIA and VeEX Inc. On the service assurance side, we mainly compete against Anritsu Corporation, Ineoquest Technologies, Inc., JDS Uniphase Corporation, NetScout Systems, Inc., Spirent Communications plc, and Tektronix, Inc. (an operating division within Danaher Corporation).

Some competitors may have greater financial, technical and/or marketing resources than us. Consequently, they may be able to devote greater resources to the development, marketing, manufacturing, selling and support of their products in order to capture market share.

Competitors also may be better positioned than us to capture market share or to acquire companies and new technologies that would potentially displace our products or render them obsolete. We cannot predict whether current or future competitors will develop or market products that offer higher performance, more features, or are more cost-effective than our current or future products. To remain competitive and achieve our growth strategy, we must increase our sales and develop cost-effective products and product enhancements that offer higher performance and more functionality, in current and new sectors, so that we can increase our market share. Our failure to do so may harm our business, results of operations and financial condition.

We have faced pricing pressure on our existing products and expect this pressure will continue. If we do not continue to lower our manufacturing costs or introduce new products with higher margins, our gross margin may decrease and our operating results may be adversely affected.

Increased competition in the telecommunications test and service assurance industry, along with consolidation among competitors and customers, will likely result in ongoing downward pressure on average selling prices. For example, some of our customers have been subject to consolidation and could obtain products from a vendor other than us, or demand more favorable terms and conditions from us, which would harm our sales and operating results. In addition, some customers may merge with or acquire our competitors and discontinue their relationships with us. This, in turn, may negatively affect our gross margin. Pricing pressure can result from a number of factors such as, among other things:

- increased competition for business;
- reduced demand;
- limited number of potential customers;
- competition from companies with lower production costs, including companies operating in lower-cost environments;
- introduction of new products by competitors;
- greater economies of scale for higher-volume competitors;
- large customers, who buy in high volumes, can exert substantial negotiating leverage over us; and

resale of used equipment.

In addition, our gross margin may be negatively affected by fluctuations between the US and Canadian currencies, increased costs of raw materials, obsolescence and excess costs, warranty costs, product and customer mix, and under-absorption of fixed manufacturing costs.

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As pricing pressure will likely continue to affect our existing products, we may have to increase the number of units sold to maintain our existing sales levels. If we are unable to increase our sales levels, lower our manufacturing costs, or introduce new products with higher margins, our gross margin may decline and our operating results may suffer.

We may not be able to make the acquisitions or strategic alliances needed for the development of our business and, if we do make such acquisitions or strategic alliances, we may not be able to successfully integrate the acquired businesses, products, technologies and personnel.

We intend to carefully seek businesses, whose products and technologies are complementary to ours, or which will enable us to expand our markets and/or our market share. However, we may not be able to make any such beneficial transactions or a sufficient number of such transactions to meet our strategic goals. Our competitors may be in a better position to acquire the same businesses, products and technologies that we wish to acquire. Our fluctuating stock price, cash position, or ability to raise capital or issue debt on favorable terms at the time of an acquisition may affect our ability to complete such an acquisition. In addition, such acquisitions or partnerships could distract management's attention from our day-to-day business and operations.

In the event of any future acquisition or strategic alliance, we could, among other things:

- issue shares that would dilute individual shareholder percentage ownership;
- incur debt;
- assume liabilities and commitments;
- incur significant expenses related to acquisition costs;
- incur significant expenses related to amortization of additional intangible assets;
- incur significant impairment losses of goodwill and intangible assets related to such acquisitions; and
- ncur losses from operations.

In the event that we complete an acquisition or sign a strategic partnership, we may be unable to successfully integrate them or realize the expected benefits of a partnership. These integration risks include, among other things:

- the risk of not realizing the expected benefits or synergies from such acquisitions or alliances;
- problems integrating the acquired operations, technologies, products and personnel;
- risks associated with the transfer of acquired know-how and technology;
- unanticipated costs or liabilities;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience; and
- potential loss of key employees, particularly those of acquired organizations.

Ultimately, the failure to make acquisitions or strategic alliances, or the inability to effectively integrate them could disrupt our overall business and harm our financial condition.

If we fail to adapt appropriately to the challenges associated with operating internationally, the expected growth of our business may be impeded and our operating results may be affected.

For the fiscal year ended August 31, 2012, customers outside of the United States and Canada accounted for 54.7% of our sales. Our international sales will be limited if we cannot establish and maintain relationships with international distributors, set up additional foreign operations, expand international sales channel management, hire additional personnel, develop relationships with international network operators and network equipment manufacturers, and

operate adequate after-sales support internationally.

Even if we are able to successfully operate and expand our international operations, we may not be able to maintain or increase international market demand for our products. Our international operations are subject to a number of risks, including, among other things:

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- challenges in staffing and managing foreign operations due to the limited number of qualified candidates, employment laws and business practices in foreign countries, any of which could increase the cost and reduce the efficiency of operating in foreign countries;
- fluctuations among currencies;
- our inability to comply with import/export, environmental and other trade compliance regulations of the countries in which we do business, together with unexpected changes in such regulations;
- measures to ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future;
- failure to adhere to laws, regulations and contractual obligations relating to customer contracts in various countries;
- difficulties in establishing and enforcing our intellectual property rights;
- inability to maintain a competitive list of distributors for indirect sales;
- tariffs and other trade barriers;
- economic instability in foreign markets;
- wars, acts of terrorism and political unrest;
- language and cultural barriers;
- lack of integration of foreign operations;
- potential foreign and domestic tax consequences;
- technology standards that differ from those on which our products are based, which could require expensive redesign and retention of personnel familiar with those standards;
- longer accounts receivable payment cycles and possible difficulties in collecting payments which may increase our operating costs and hurt our financial performance; and
- failure to meet certification requirements.

Any of these factors could harm our international operations and negatively affect our business, results of operations and financial condition. The recurrence of weakness in these economies or of weakness in other foreign economies could have a significant negative effect on our future operating results.

Our reliance on software development resources in India and manufacturing personnel in China may expose us to unanticipated costs or liabilities.

In addition to our research and development centers in Quebec City, Canada, Montreal, Canada, Concord, Canada, Boston, United States, and Oulu, Finland, we maintain software development centers in Pune, India and Bhubaneswar, India. We are in the process of consolidating our Bhubaneswar and Pune software development activities at the location in Pune. We also manufacture high-volume, low-complexity telecom products at our wholly-owned production facility in Shenzhen, China.

Over the years, we have significantly increased our software development and manufacturing activities in India and China, respectively. There is no assurance that our reliance on software development resources in India and manufacturing personnel in China will enable us to maintain our cost structure at current levels, achieve additional cost reductions, or generate greater resource efficiency. Furthermore, our software development and manufacturing efforts abroad involve significant risks in addition to the ones disclosed in previous risk factors:

- difficulty in hiring and retaining appropriate engineering and manufacturing resources due to intense competition for such resources and resulting wage inflation;
- exposure to misappropriation of intellectual property and proprietary information;
- heightened exposure to changes in the economic, regulatory, security, and political conditions of these countries;
- fluctuations in currency exchange rates and tax compliance in India and China;
- cash management and repatriation of profit; and

high inflation rates which could increase our operating costs.

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If we are unable to adapt to current and future changes in technology or if we are unable to introduce new and enhanced products on a timely basis, our products may become obsolete, which could prevent us from achieving our growth strategy and adversely affect our operating results.

The industries that we target are characterized by rapidly evolving technology and industry standards that result in frequent new product introductions. Any failure by us to anticipate or respond to new technological developments, customer requirements or evolving standards could have a material adverse effect on our business, results of operations and financial condition. The development of proprietary technology entails significant technical and business risks and requires substantial expenditures and lead times. The success of our new product introductions will depend on several factors, including, among other things, our ability to:

- properly identify and anticipate customer needs;
- innovate and develop new products;
- gain timely market acceptance for new products;
- manufacture and deliver our new products on time, in sufficient volume and with adequate quality;
- price our products competitively;
- continue investing in our research and development programs; and
- anticipate competitors’ announcements of new products.

Failure to do the above could be exploited by our competitors. If we lose market share as a result of lapses in our product development, our business would suffer.

Our products may have unforeseen defects that could harm our reputation, impede market acceptance of our products and negatively impact our business, results of operations and financial condition.

Given their complexity, our products may contain undetected software or hardware defects, inaccurate calibration or compatibility problems, or regulatory compliance issues, particularly when they are first introduced or when new versions are released. There can be no assurance that, despite our testing and diligent efforts, defects will not be found in new products after they have been fully deployed and operated under peak stress conditions, or that customized products will meet customer sign-off acceptance requirements. If we are unable to fix defects or other problems or meet custom requirements, we could experience, among other things:

- costly repairs;
- product returns or recalls;
- damage to our brand reputation;
- loss of customers, failure to attract new customers or achieve market acceptance;
- diversion of development and engineering resources;
- legal actions by our customers, including claims for consequential damages and loss of profits; and
- legal actions by governmental entities, including actions to impose product recalls and/or forfeitures.

The occurrence of any one or more of the foregoing could seriously harm our business, results of operations and financial condition.

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Our intellectual property and proprietary technology are important to the continued success of our business. Our failure to protect this proprietary technology may significantly impair our competitive position.

Our success and ability to compete depend to a significant extent on our proprietary technology, with which we attempt to keep others from using the innovations that are central to our existing and future products. As of August 31, 2012, our records indicate that we held 38 actively-maintained granted U.S. patents, 49 granted or validated patents in countries of the European Community, 8 patents in Canada, 5 patents in China, and one patent in the Russian Federation. In addition, we have 23 patent applications pending in the U.S., 7 in Canada, 8 in China, 1 in Finland, 12 regional patent applications at the European Patent Office, and 7 applications in other countries, as well as 2 International Applications under the Patent Cooperation Treaty that have not yet entered the national/regional phase. We also rely on a combination of copyright and trademark laws, trade secrets, confidentiality procedures, contractual provisions and license agreements to protect our proprietary technology. We may have to engage in litigation or formal Opposition Proceedings in order to protect our patents and other intellectual property rights, or to determine the validity or scope of the proprietary rights of others. Such litigation and Opposition Proceedings can be time-consuming and expensive, regardless of whether we win or lose.

The process of seeking patent protection can be long and expensive and we cannot be certain that any currently pending or future applications will actually result in issued patents, or that, even if patents are issued, they will be of sufficient scope or strength to provide meaningful protection or any commercial advantage to us. We also rely on trade secret protection for our technology, in part through confidentiality agreements with our employees, consultants, distributors and third parties. However, these agreements may be breached or otherwise not effective and we may not have adequate remedies for any breach or shortfall of these agreements. In any case, others may come to know about our trade secrets through a variety of methods. In addition, the laws of some jurisdictions in which we sell our products may not protect our intellectual property rights to the same extent as do the laws of Canada and the United States.

Our intellectual property rights, particularly our existing or future patents, may be invalidated, circumvented, challenged or required to be licensed to others.

Our intellectual property rights are important assets for us. Various events outside of our control pose a threat to our intellectual property rights, as well as to our products, services and technologies. For example, effective intellectual property protection may not be available in every country in which our products and services are distributed. Also, the efforts we have taken to protect our proprietary rights may not be sufficient or effective.

Furthermore, others may develop technologies that are similar or superior to our technology, duplicate or reverse engineer our technology, or design around the patents owned or licensed by us. We cannot be sure that the steps that we take to protect our technology will prevent misappropriation or infringement. If we fail to protect our technology so that others may copy or use it, we will be less able to differentiate our products and our sales may decline.

Others may claim that our products infringe upon their intellectual property rights, or they may infringe our intellectual property, and we may expend significant resources enforcing or defending our rights or suffer competitive injury.

Litigation regarding intellectual property rights is common in the technology industry and third-party infringement claims involving technologies may increase. If an infringement claim is filed against us, we may be prevented from using some of our technologies and may incur significant costs to resolve the claim. Conversely, we may be required to spend significant resources to monitor and enforce our intellectual property rights.

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We could incur substantial costs in defending ourselves and our customers against infringement claims or in bringing infringement claims against others. Litigation could also adversely affect sales of the challenged product or technology and divert the efforts of our management and technical personnel. In the event of an infringement claim, we may be required to obtain one or more licenses from third parties. We cannot assure you that we, or our customers, could obtain necessary licenses from third parties at a reasonable cost or at all. If we fail to obtain a license where one is required, we could incur substantial liabilities and be forced to suspend the marketing of the challenged products.

We may make misjudgments in our strategic planning that could have material adverse effects on our business, results of operations and financial condition.

We devise a three-year strategic business plan, which is prepared by management and approved by our Board of Directors. This strategic plan, reviewed by management on a regular basis, is mainly based on market research and analysis related to future market trends and demands. In our strategic plan, we have made and will continue to make judgments based on our analysis of future market trends and customer requirements. These decisions may involve substantial investments in the development of new product lines, diversification of our business on a geographic basis, as well as expansion into new market segments — either organically or through acquisitions. We may make misjudgments in our strategic planning that could have material adverse effects on our business, results of operations and financial condition.

Our quarterly revenues and operating results are subject to significant fluctuations and you should not rely on them as an indication of our future performance.

Our sales and operating results have fluctuated from quarter to quarter in the past and significant fluctuations may occur in the future. Because our service assurance and wireless test systems vary in size and complexity and in certain instances require customer acceptance before revenue recognition occurs, our sales may fluctuate significantly on a quarterly basis. Many of our deals involve lengthy sales cycles, contract negotiations as well as extensive product testing, laboratory or network certification, including network-specific or region-specific processes.

In addition, our sales and operating results generally depend on the volume and timing of the orders we receive from customers as well as our ability to fulfill received orders. Our operating expenses, which include manufacturing overhead costs, selling and administrative, research and development, and depreciation and amortization expenses, are relatively fixed in the short term. If we sell fewer products than anticipated, if there is a delay in the launch of new products, or if prices for our products decline, we may not be able to quickly reduce our operating expenses in response to lower sales. Factors that could affect the amount and timing of our sales, and cause quarterly fluctuations in our revenue and operating results include, among other things:

- length of the sales cycle for certain products, especially those that are higher priced and more complex;
- sales cycle prolonged by lengthy customer acceptance;
- timing of product launches and market acceptance of new products for us as well as our competitors;
- our ability to sustain product volumes and high levels of quality across all product lines;
- timing of shipments for large orders;
- effect of seasonality on sales and bookings; and
- losing key accounts and not successfully developing new ones.

Our sales and operating results could also be volatile due to a number of factors, some of which we have little or no control over, including, without limitation:

- fluctuating demand for telecommunications test and service assurance equipment;

- changes in the capital spending and operating budgets of our customers, which may cause seasonal or other fluctuations in product mix, volume, timing and number of orders we receive from our customers;
- order cancellations or rescheduled delivery dates;
- pricing changes by our competitors or suppliers;
- variations in the mix between higher and lower-margin products and service;

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- customer bankruptcies and difficulties in collecting accounts receivable;
- restructuring and impairment charges;
- foreign exchange rate fluctuations;
- general economic conditions, including a slowdown or recession; and
- distorted effective tax rate due to non-taxable/deductible elements and unrecognized deferred tax assets.

We may in the future choose to reduce prices, increase spending, or modify our product portfolio in response to actions by competitors or as an effort to pursue new market opportunities. These actions may also adversely affect our business and operating results and may cause our quarterly results to be lower than the results of previous quarters. Due to these factors, you should not rely on quarter-to-quarter comparisons of our results of operations as an indication of our future performance.

If customers fail to meet their financial commitments to us, it could have a material adverse effect on our business, results of operations and financial condition.

Some of our customers experienced cash flow problems during the global economic recession of 2009 and may endure similar problems due to the current uncertain market environment. Consequently, our customers may delay payments or may not be able to meet their financial commitments to us. Furthermore, they may not order as many products from us as originally forecasted or they may cancel their orders outright. The failure of customers to meet their financial commitments to us or a material decrease in their orders could result in bad debt expenses or a decrease in revenues for us, which could have a material adverse effect on our business, results of operations and financial condition.

If we fail to predict our supply requirements accurately, we may have excess inventory or insufficient inventory, either of which could cause us to incur additional costs and/or experience manufacturing delays.

We provide non-binding forecasts of our requirements to some of our suppliers up to six months prior to scheduled delivery of products to our customers. If we overestimate our forecasted requirements, we may have excess inventory, which could harm our relationships with our suppliers due to reduced future orders, increase our costs and require inventory write-offs. If we underestimate our requirements, we may have an inadequate inventory of parts, which could interrupt manufacturing of our products and result in shipment delays. In addition, lead times for our raw materials and parts may be long and depend on factors such as the procedures of, or supply terms with, a specific supplier, worldwide demand for each part at a given time, or the onset of a natural disaster.

We depend on short-term arrangements with a single supplier or a limited number of suppliers for some key components and materials in our products, which makes us susceptible to supply shortages or price fluctuations that could adversely affect our operating results.

We depend on a single supplier or a limited number of suppliers for some of the parts used to manufacture our products for which alternative sources may not be readily available. In addition, all of our orders are placed through individual purchase orders and, therefore, our suppliers may stop supplying parts to us at any time. Our reliance on a single source or limited number of suppliers could result in increased costs, delivery problems, reduced control over product pricing and quality and could require us to stockpile critical parts. Following the natural disaster in Japan in March 2011, for example, we increased our inventory of critical parts from certain Japanese single-source suppliers to ensure that we were able to deliver our products to customers without interruption.

Financial difficulties of suppliers could also affect our ability to obtain necessary parts in a timely manner. Any interruption or delay in the supply of any of these parts could significantly harm our ability to meet scheduled product

deliveries to our customers and cause us to lose sales. Furthermore, the process of qualifying a new manufacturer for complex parts designed to our specifications, such as our optical and mechanical parts, is lengthy and would consume a substantial amount of time of our technical personnel and management. If we were required to change a supplier in a short period of time, our business would be disrupted. In addition, we may be unsuccessful in identifying a new supplier capable of meeting and willing to meet our needs on acceptable terms. Consolidation involving suppliers could further reduce the number of alternatives available to us and increase the cost of parts, which would make our products less competitive and result in lower margins.

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If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial information or prevent fraud, which could harm our operating results and cause investors to lose confidence in our reported financial information.

Effective internal controls are necessary for us to provide reliable and accurate financial information and effectively prevent fraud. We devote significant resources and time to comply with the internal control over financial reporting requirements of the Sarbanes-Oxley Act of 2002. In addition, Section 404 of the Sarbanes-Oxley Act of 2002 requires that we assess and that our auditors attest to the design and operating effectiveness of our controls over financial reporting. Our compliance with the annual internal control report requirement for each fiscal year will depend on the effectiveness of our financial reporting as well as data systems and controls throughout our company and operating subsidiaries. Furthermore, we cannot be certain that these measures will ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future, especially in the event of acquiring companies that are not in compliance with Section 404 of the Sarbanes-Oxley Act of 2002. As well, the complexity of our systems and controls may become more difficult to manage as we transform our operating structure and continue to reduce infrastructure costs. To effectively manage these changes, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. Any failure to implement required new or improved controls, difficulties encountered in their implementation or operation, or difficulties in the assimilation of acquired businesses into our control system, could harm our operating results or cause it to fail to meet our financial reporting obligations. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on our share price and our access to capital.

Regulatory changes may cause us to incur increased costs.

Changes in the laws and regulations affecting public companies may increase our expenses as we may have to devote resources to respond to these new requirements. In particular, we incurred and may incur additional general administrative expenses to comply with Section 404 of the Sarbanes-Oxley Act and IFRS (International Financial Reporting Standards). Compliance with new rules could require the further commitment of significant financial resources and result in the diversion of management’s time and attention from revenue-generating activities. Finally, the impact of these changes could make it more difficult for us to attract and retain qualified persons to serve on our Board of Directors or as executive officers, which could harm our business.

We require employees and managers who are knowledgeable about the specialized nature of our business. If we are unable to attract and retain sufficient numbers of highly skilled technical, sales, marketing, senior management and other personnel, our operations and financial results will suffer.

Due to the specialized nature of our business, we are highly dependent on the continued service of and on our ability to attract qualified engineering, sales, marketing, senior management and other personnel. If we are unable to attract and retain such qualified personnel, it could have a material adverse effect on our business, results of operations and financial condition.

We must also provide significant training for our employee base due to the highly specialized nature of the telecommunications test and service assurance industry. Our current personnel may be inadequate and we may fail to assimilate and train new employees. Highly skilled employees with the education and training that we require – especially employees with significant experience and expertise in international business development, product management, sales, engineering and operations – may be difficult to find. Once trained, our employees may also be hired by our competitors or leave the organization.

Our insurance may not be sufficient to cover all potential liability. A successful claim exceeding our policy limits will reduce our cash position, increase our expenses and have a negative effect on our business, operating results and financial condition.

Our products are designed to help network operators, network equipment manufacturers, cable operators and component manufacturers ensure network reliability. The failure of our products to perform to customer expectations could give rise to product liability and warranty claims. We carry insurance for product liability and take accounting reserves for warranty claims that we consider adequate in view of industry practice.

In addition, we may face other types of claims by third parties in relation to the conduct of our business; a successful claim against us for an amount exceeding our policy limits would force us to use our own resources to pay the claim, which could result in a reduction of our cash available for other uses, increase our expenses and have a negative effect on our business, results of operations and financial condition.

Our reported financial results could suffer if there are charges related to impairment of goodwill or of intangible assets.

We are required to test annually and review, when events or circumstances warrant, our goodwill related to business combinations, and determine if impairment has occurred. Intangible assets are also reviewed for impairment at each reporting date whether there is an indication that an asset may be impaired. As at August 31, 2012, we had $29.2 million of goodwill and $9.4 million of intangible assets on our balance sheet related to the acquisitions of Brix Networks in 2008 and NetHawk Oyj in 2010, respectively.

Our stock price is volatile and may remain volatile in the future. See " Our stock price is volatile." Our stock price may decrease, which may lead to goodwill impairment in the future. Furthermore, discounted cash flows may be lower than expected, which may cause the recoverable amount of certain intangible assets to be lower than their carrying value. Consequently, this could result in future intangible asset impairment. Any additional impairment of goodwill or of intangible assets would negatively impact our operating results. We last recorded a pre-tax impairment charge of $21.7 million in fiscal 2009. We performed our last goodwill impairment test in the fourth quarter of fiscal 2012 and we concluded that goodwill was not impaired.

We may become involved in costly and time-consuming litigation that may substantially increase our costs and harm our business.

We may from time to time become involved in various lawsuits and legal proceedings. For example, we were a defendant in a putative securities class action suit filed in the United States District Court for the Southern District of New York, involving approximately 300 other issuing companies, from 2001 to 2012. Appeals of the opinion granting final approval were filed, all of which have been dismissed or settled as of January 9, 2012. The settlement payment on behalf of EXFO has been made by the insurers, the settlement among the parties is final, and the case is concluded. Litigation is subject to inherent uncertainties and an adverse result may arise from time to time that could have a material adverse effect on our business, results of operations or financial condition. Any litigation to which we are subject could require significant involvement of our senior management and may divert management attention from our business and operations.

If we suffer loss to our factories or facilities, our operations could be seriously harmed.

Our factories and facilities may be subject to catastrophic losses due to fire, vandalism, terrorism or other natural or man-made disasters. We do not have redundant multiple-site capacity and if any of our facilities or factories were to experience a catastrophic loss, it would disrupt our operations, delay production, shipments and revenue and result in large expenses, thereby harming our results of operation.

Unexpected declines in our research and development and other tax credits and grants may have an adverse effect on our business.

Our historical operating results reflect substantial benefits from programs sponsored by federal and provincial governments for the support of research and development activities. In addition, NetHawk Oyj, which was acquired in 2010, is entitled to government grants from a Finnish technology organization for research and development activities

conducted in Finland. Altogether, research and development tax credits and grants represented 15.9% of our gross research and development expenses for the year ended August 31, 2012.

Our research and development projects entitling to government grants from the Finnish technology organization must be pre-approved and the grant is subject to certain conditions. In the event a condition is not met, we may be required to reimburse a portion or the entire amount of the grant received, which would have material adverse effect on our results of operations and financial condition.

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If changes in laws or government policies terminate or adversely modify the Canadian federal and Quebec provincial government programs or the Finnish government program, under which we receive the majority of our research and development and other tax credits and grants, or if we unexpectedly become unable to participate in or take advantage of these programs, then our net research and development and other expenses will materially increase or we may decrease our research and development activities. For example, in March 2012, the Canadian federal government announced a series of measures that will, among other things, decrease our Canadian federal tax credit rate on eligible expenses from 20% to 15% starting in calendar 2014.

In addition, to the extent that we may increase our research and development activities in India, or potentially acquire new companies, our increased R&D activities may not be eligible for these programs. If we were required to decrease our research and development activities, or were unable to benefit from other tax credits and grants, this could have a material adverse effect on our business, results of operations and financial condition.

Changes in our effective tax rate or adverse outcomes resulting from tax audits may have an adverse impact on our results.

As an international corporation, we are subject to taxation in the various jurisdictions in which we conduct business. Significant judgment is required in the determination of our worldwide provision for income taxes and this determination requires the interpretation and application of complex tax laws and regulations. Our effective tax rate may be adversely impacted by the level of earnings, by changes in the mix of earnings/losses among companies and countries which may have different statutory tax rates, by the write off of our deferred tax assets, and by changes in tax rules and regulations. We are also subject to income tax audits and transfer pricing audits in the respective jurisdictions in which we conduct business and we regularly assess the likelihood of adverse outcomes resulting from these audits to ascertain the adequacy of our provisions for income taxes and transfer pricing policies. There can be no assurance that the outcomes of these tax audits, if any, will not have an adverse impact on our result and financial condition.

Our current principal stockholder has effective control over our business.

As of November 1, 2012, Germain Lamonde, our Chairman of the Board, President and Chief Executive Officer, held 92.86% of the voting rights in our stock. By virtue of his stock ownership, Mr. Lamonde has effective control over all matters submitted to our stockholders, including the election of our Directors, and exercises significant control over our policies and affairs. Such concentration of voting power could have the effect of delaying, deterring or preventing a change in control or other business combinations that might otherwise be beneficial to our stockholders and may harm the market price of our shares.

If we complete major acquisitions of complementary businesses, products or technologies, we may need additional capital, and may not be able to raise additional capital on favorable terms or at all, which could limit our ability to grow and could increase our costs.

Our future liquidity and capital requirements are difficult to predict because they depend on numerous factors, including the success of our existing and new product offerings as well as competing technology and market developments. As a result, we may not be able to generate sufficient cash flows from our operations to meet additional working capital requirements, support additional capital expenditures or take advantage of acquisition opportunities. As at August 31, 2012, we held $67.1 million in cash and short-term investments.

We may need to raise additional capital in the future. Our ability to obtain additional financing will be subject to a number of factors, including market conditions, effects of the financial crisis, reduced access to credit facilities and

our operating performance. These factors may render the timing, amount, terms and conditions of additional financing unattractive for us. If we raise additional funds by selling equity securities, the relative ownership of our existing investors could be diluted or new investors could obtain terms more favorable than previous investors. If we raise funds through debt financing, we could incur significant borrowing costs and be required to meet restrictive debt covenants. If we are unable to raise additional funds when needed or at terms satisfactory to us, our ability to operate and grow our business could be impeded.

Our business and operations would suffer in the event of a failure of our information technology infrastructure.

We rely upon the capacity, efficiency and security of our information technology hardware and software infrastructures and those from third parties, as well as our ability to expand and update these infrastructures in response to our evolving needs. Any failure to manage, expand, update or secure our information technology infrastructures or any failure in the operation of these infrastructures could harm our business.

Our information systems and third-party systems are vulnerable to damages from computer viruses, natural disasters, unauthorized access, theft of information and other similar disruptions. Any system failure, accident or security breach could result in disruptions to our operations. To the extent that any disruption or security breach results in a loss or damage to our data, or inappropriate disclosure of confidential information, it could harm our business. In addition, these events may force us to devote more money and resources in order to protect ourselves against damages caused by these disruptions or security breaches in the future.

A security breach or cyber-attack of our networks could interrupt our operations or harm our reputation.

Our systems may be vulnerable to attacks such as data theft, computer viruses, programming errors, attacks by third parties or similar problems. If we were to experience a security breach, or cyber -attack, we could be required to incur substantial costs and liabilities, including but not limited to, expenses attributable to rectifying the security breach or cyber-attack including the cost of repairing any damage to our systems, liability for stolen assets or information, lost revenue and income resulting from any system downtime, increased costs for cyber security protection, and damage to our reputation causing customers and possibly investors to lose confidence in us.

Our stock price is volatile.

Our stock price has experienced substantial volatility in the past and may remain volatile in the future. Volatility in our stock price can arise from a number of factors discussed in this “Risk Factors” section. The turmoil in credit markets and in the broader economy has contributed to share price and volume fluctuations in global stock markets that have reduced the market price of many technology stocks, including ours in fiscal 2009. In addition, in fiscal 2011 and 2012, our stock price was volatile as the stock market experienced extreme price and volume fluctuations. During fiscal 2012, our closing stock price on NASDAQ ranged from a high of US$8.23 per share to a low of US$4.56 per share. The stock market has experienced extreme price and volume fluctuations that have affected the share price of many technology companies, with such volatility often unrelated to the operating performance of these companies. Divergence between our actual or anticipated financial results and published expectations of analysts can cause significant swings in our stock price. Our stock price can also be affected by announcements that we, our competitors, or our customers may make, particularly announcements related to acquisitions, significant transactions or financial guidance. These factors, as well as conditions affecting the general economy or financial markets, may materially affect our stock price in the future.

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Item 4. Information on the Company

A. History and Development of the Company

Our legal name and commercial name is EXFO Inc. / EXFO inc. Our head office is located at 400 Godin Avenue, Quebec, Quebec, Canada, G1M 2K2 and our main telephone number is (418) 683-0211. Our e-mail address is info@EXFO.com and our website is www.EXFO.com. Information on our website is not incorporated by reference in this Annual Report. Our agent for service in the United States is CT Corporation System, 111 Eighth Avenue, New York, New York 10011. Our Transfer Agent and Registrar is Canadian Stock Transfer Inc. (CST) as administrative agent for CIBC Mellon Trust Company, 2001 University Street, Suite 1600, Montreal, Quebec, Canada, H3A 2A6. This Annual Report contains trademarks and registered trademarks of us and other companies.

We were incorporated in Canada on September 18, 1985 pursuant to the Canada Business Corporations Act. Since that date, we have amended our articles on various occasions mainly to modify our legal and corporate names and our share capital.

Since we are using this Form 20-F as an annual report, we have provided herein the information required pursuant to Item 4A(4) for the period beginning as at September 1, 2011 until the date of this Annual Report. For information responsive to this Item 4A(4) for prior periods, please refer to our previously filed Annual Reports on Form 20-F. Information in our previously filed Annual Reports on Form 20-F is not incorporated by reference in this Annual Report.

On November 7, 2011 we announced that our Board of Directors approved the renewal of our share repurchase program, by way of a normal course issuer bid on the open market of up to 2% of our public float (as defined by the Toronto Stock Exchange), or 575,690 of subordinate voting shares at the prevailing market price. From November 10, 2011 through November 9, 2012, we repurchased for cancellation 565,748 shares under that program for an aggregate net purchase price of US$2.8 million.

In June 2012, we committed to implement a restructuring plan to align our cost structure with the challenging market environment. This plan will result in one-time expenses of approximately US$3.3 million, mainly for severance expenses. Most of the plan was executed in the fourth quarter of fiscal 2012 and it resulted in charges of $2.3 million in severance expenses during that period; the remaining of the plan will be executed in the first half of fiscal 2013.

On November 7, 2012 we announced that our Board of Directors approved the renewal of our share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of our issued and outstanding subordinate voting shares, representing 2,072,721 subordinate voting shares at the prevailing market price. We expect to use cash, short-term investments or future cash flow from operations to fund the repurchase of shares. The normal course issuer bid started on November 12, 2012, and will end on November 11, 2013, or on an earlier date if we repurchase the maximum number of shares permitted under the bid. The program does not require that we repurchase any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled. We shall provide to any person or company, upon request to our Secretary, at 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2, phone number (418) 683-0913 ext. 23704 or fax number (418) 683-9839, a copy of the notice sent to the Toronto Stock Exchange (TSX) according to our normal course issuer bid.

B. Business Overview

EXFO is a leading provider of next-generation test and service assurance solutions for wireline and wireless network operators and equipment manufacturers in the global telecommunications industry. We offer core-to-edge solutions that assess the performance and reliability of converged IP networks. Our test and service assurance solutions specifically target high-growth market opportunities related to optimizing next-generation networks: wireless backhaul, 4G/LTE (Long-Term Evolution), fiber-to-the-home (FTTH)/fiber-to-the-curb (FTTC)/fiber-to-the-node (FTTN) and 40G/100G network upgrades. The Life Sciences and Industrial Division, which provided solutions in medical device and opto-electronics assembly, fluorescence microscopy and other life science sectors, was sold to The Riverside Company, a private equity firm, in October 2010.

We were founded in 1985 in Quebec City, Canada. Our original products were focused on the needs of installers and operators of fiber-optic networks. Customers use these field-portable test solutions for the installation, maintenance and troubleshooting of optical networks. Over the past several years, we have enhanced our competitive position in the global telecommunications test and service assurance industry through acquisitions of transport and datacom, copper/xDSL and wireless test companies as well as an IP service assurance business.

We launched 21 new products in fiscal 2012 compared to 19 in 2011 and 20 in 2010. Key product introductions in fiscal 2012 included among others the FTB-85100G Packet Blazer, a multi-rate, multi-service test solution for characterizing high-speed networks reaching 100G; Ethernet One, a centralized Ethernet service activation and monitoring solution that we believe enables operators to improve the operational efficiency of their networks from the core to the last mile; EXFO Apps, a portal offering software applications that we believe boosts the capabilities and productivity of the FTB Ecosystem of smart platforms and test modules; the QA-805/QA-813 QualityAssurer, a highly scalable platform (simulates more than 12 million active subscribers) for load simulation of converged 3G, 4G/LTE and IMS (IP Multimedia Subsystem) networks; the portable iPro, a capture and analysis probe for wireless networks up to 10 Gbit/s; and the MaxTester 600 series for VDSL2 installation and repair work on copper links.

Industry Background

Market conditions in the telecommunications industry remain difficult due a sluggish macro-economic environment, the European debt crisis and its effects on other regional economies, as well as the decrease in capital spending among network operators. In addition, network operators are attempting to monetize their investments in next-generation fixed and mobile networks as data revenue growth is not keeping pace with the required level of expenditures. Consequently, network operators are reassessing their business models and spending levels in efforts to improve profitability.

Despite these constraints, we believe the fundamental drivers toward broadband deployments and fixed-mobile Internet protocol (IP) network convergence are firmly entrenched in the telecommunications industry. Although we do not expect that network operators will increase capital expenditures in fiscal 2013, we believe they will spend more in select, high-growth areas to accommodate bandwidth-intensive broadband applications and to facilitate the migration to more flexible and cost-effective fixed and mobile IP networks.

According to Cisco's Visual Networking Index, global IP traffic will nearly quadruple from 2011 to 2016, reaching 1.3 zettabytes per year in 2016. (A zettabyte is equal to 1,000 exabytes or 250 billion DVDs). According to Cisco, global mobile traffic, a subset of this larger group, is expected to increase 18-fold during the same period. We believe this explosive growth is being driven by a proliferation of media-rich mobile communication devices (smart phones and tablets), a growing number of Internet users, faster broadband speeds and increased video usage.

To support such bandwidth growth, wireline networks are being transformed into next-generation IP-based infrastructures. Legacy SONET/SDH networks, which were established in the mid-1980s, do not have the flexibility to seamlessly mix and transport voice, data and video services. These networks are not capable of efficiently carrying triple-play services because they were designed for point-to-point voice communication. As a result, new optical transport network (OTN) standards, which are at the very heart of what the industry is labeling next-generation IP networks, have been defined to carry IP applications over Ethernet. Network operators are increasingly turning to such next-generation, IP-based networks in order to offer customers higher-margin triple-play services while lowering their operating costs.

Fiber-to-the-home (FTTH) has also become the access network architecture of choice for wireline operators wishing to provide a superior user experience for a combined voice, data and video offering. This architecture allows operators

to meet heightened bandwidth requirements and future-proof their access networks as residential bandwidth demands grow from 1 to 5 Mbit/s (megabits per second) to 30 to 100 Mbit/s required for the long term. We expect architectures, combining copper and fiber (fiber-to-the-curb, or FTTC, and fiber-to-the-node, or FTTN), will also increase in the short term, since they are less expensive methods to increase bandwidth and can be mass-deployed quickly.

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As bandwidth growth in access networks continues to increase, it has begun placing a strain on metro rings and core networks. It is also driving the need for higher-speed technologies. For example, 43 Gbit/s (gigabits per second) SONET/SDH is becoming mainstream, while commercial deployments of 100 Gbit/s Ethernet networks are under way. In the long run, we expect these solutions will offer a more economical way to add capacity to congested network links, especially if trenches need to be dug in order to deploy new fiber in metro and long-distance routes.

On the wireless side, operators are also faced with major investments to meet soaring bandwidth demand. Wireless operators are accelerating deployments of 3G networks, fast-tracking 4G/LTE adoption, and investing in mobile backhaul networks in order to increase transmission rates for bandwidth-hungry consumers to approach wireline speeds. Furthermore, as these consumers expect wireline and wireless networks to transport any content to any device at any time, both fixed and mobile networks are converging to a common IP-based infrastructure supported by IMS (IP multimedia subsystem) for seamless network interoperability.

Growth Strategy

Our long-term goal is to become the market leader in the global telecom test and service assurance industry. Given soaring bandwidth demand and IP convergence, wireless and wireline network operators and equipment manufacturers are faced with a major investment cycle.

To achieve our goal, we plan to:

- Increase our presence with wireless operators;
- Enable network operators to reduce their operating expenses;
- Expand our sales to existing Tier-1 network operators; and
- Accelerate profitability through execution.

Customers

Telecom customers on a global basis use our test and service assurance solutions to enable their wireline and wireless networks to perform optimally during their complete life cycles: research, development, manufacturing, installation, maintenance and monitoring. From December 2000 to October 2010, we also had select customers in the high-precision assembly and life science sectors that required our solutions to render them more efficient in their respective fields.

We initially developed telecom test equipment for wireline network operators and, to a lesser extent, component vendors and equipment manufacturers, but over the years we have expanded our offering to wireless network operators, cable television companies, public utilities, private network operators, third-party installers, equipment rental companies, large enterprises and laboratory researchers.

Our life science and industrial customers consisted of major manufacturers of medical devices, microelectronics, optical displays, electronic storage systems, photonic components and microscopes, as well as universities, medical schools, governments, and private and industrial research laboratories. Our UV digital print customers consisted of printing equipment manufacturers who develop products for wide format graphics printing, label production and product marking.

In fiscal 2012, our top customer accounted for 4.4% of our sales and our top three customers represented 12.0%. In comparison, our top customer accounted for 7.2% of sales and our top three customers represented 16.3% in 2011, while our top customer accounted for 4.9% of sales and our top three customers represented 12.2% in 2010.

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Products

We offer an extensive range of wireline and wireless test and service assurance solutions to the global telecommunications industry. We believe our success has been largely predicated on our core expertise in developing test equipment for wireline networks. Following the acquisition of Brix Networks in April 2008, we expanded our product portfolio into the service assurance market for next-generation IP networks. Through the acquisition of NetHawk Oyj in March 2010, we offer test and service assurance solutions for 2G, 3G and 4G/LTE wireless networks.

We believe the competitive advantages of our products include a high degree of innovation, modularity (especially wireline products) and ease of use. Ultimately, we believe our products enable network equipment manufacturers and operators to design, deploy, troubleshoot and monitor wireline and wireless networks, and also help customers reduce their operating expenses.

Products for Network Operators

Wireline Test Equipment

We provide an extensive range of portable test solutions that are mainly used by network operators to install, turn up and maintain their optical and copper-based telecommunications networks. These products are available as handheld test instruments, portable platforms with related modules, and as rack-mounted chassis with related modules. Our handheld instruments are durable, compact and easy to use. Our field-test platforms, namely the FTB-1 Platform, FTB-200 Compact Platform and FTB-500 Platform, are at the core of our wireline product portfolio.

Our FTB-1 Platform, which is designed for frontline technicians in the field, is a single-slot, modular platform dedicated to fiber-optic, copper, Ethernet, fiber-to-the-home and multiservice testing applications. Our FTB-200 Compact Platform, for the “super field technician”, holds up to two interchangeable modules that are fully compatible with our more advanced FTB-500 platform. Test technologies well suited for the FTB-200 Compact Platform include a wide range of singlemode and multimode optical time-domain reflectometers (OTDRs), automated optical loss test sets (OLTSs), SONET/SDH analyzers up to 10 Gbit/s, as well as Gigabit Ethernet (GigE) and 10 Gigabit Ethernet testers. Our third-generation field-testing platform, the FTB-500, is available in two configurations for various high-end tasks with transmission rates up to 100 Gbit/s. The four-slot model is designed for datacom testing, OTDR analysis, optical loss, and Ethernet testing. The eight-slot model is a high-performance, multiple-protocol unit that allows users to combine next-generation SONET/SDH functions with Ethernet, Fibre Channel and optical-layer testing capabilities. It can handle dispersion characterization (PMD and CD), as well as DWDM/ROADM testing with optical spectrum analysis. All three portable platforms support USB, mobile, Wi-Fi, and Bluetooth connectivity capabilities to efficiently manage testing and reporting operations in the field.

These PC-centric, open-ended platforms, combined with cloud-based software applications, can be transformed into a fully connected test environment called the FTB Ecosystem. Leveraging platform connectivity, customers can keep track of their entire test fleet, manage software updates and schedule calibration procedures. All test data can be stored in a central database and used as a point of reference against future measurements. In addition, field technicians can view instructional videos during periods of downtime. Consequently, this enhanced test environment enables customers to increase productivity and reduce operating expenses.

Wireless Test Equipment

We offer 2G, 3G and 4G/LTE protocol analyzers for network operators. These instruments analyze mobile network elements in order to validate functionality according to wireless technology specifications, whether these elements interoperate with each other effectively when combined to form a network, and how well the live network performs. These test tools allow engineers to troubleshoot networks in order to find the source of errors and fix them as fast as possible. Our protocol analyzers support multi-interface testing and all major mobile technologies: GSM/GPRS/EDGE/UMTS/LTE. They enable fully automated testing and run powerful applications for protocol monitoring, call and session tracing, quality of service and radio optimization measurement.

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EXFO's network simulators are also used by network service providers in their pre-deployment labs to simulate real-world, large-scale network traffic and end-user behavior in order to predict network behavior, uncover faults and optimize networks before new wireless network components and/or services are deployed.

Wireline/Wireless Service Assurance Systems

We provide a converged service assurance solution, called the Brix System, for wireline and wireless network operators, as well as for the managed services arms of network equipment manufacturers in support of service-level agreements (SLAs) required by their customers.

The Brix System is an integrated hardware and software solution that delivers end-to-end quality of service (QoS) and quality of experience (QoE) visibility as well as real-time IP service monitoring and verification for next-generation networks. Built around a distributed architecture, we believe the Brix System enables the successful launch and ongoing profitable operation of IP-based voice, video and data applications and services across wireline and wireless networks.

We believe a competitive advantage of EXFO's service assurance solution is the ability to implement SLA monitoring and assure any IP service, over any network, to any endpoint—all from the same open and extensible platform. Key capabilities include:

- Performance monitoring and analysis;
- Advanced data correlation and analysis engine;
- VoIP service assurance;
- IP/MPLS service assurance;
- Mobile backhaul and metro Ethernet service assurance;
- IP video service assurance;
- Advanced analytics and reports; and
- Custom solutions services.

The Brix System offers a multi-play capability such that customers can leverage one, several or all of the above on a single platform, which we believe delivers significant savings in capital and operating expenditures.

We believe the highly scalable BrixWorx correlation and analysis engine architecture is well suited for the needs of operators' networks and IP services. It works together with network-wide monitoring sources — including Brix verifiers, third-party devices and standards-based interfaces — and Brix software applications. BrixWorx conducts network and IP service testing and monitoring, while collecting, storing, correlating and analyzing essential data to produce detailed graphical reports and analytics on end-to-end service performance.

Brix software applications include:

- BrixCall: Voice quality and performance management;
- BrixNGN: IP/MPLS and carrier Ethernet (mobile backhaul and metro Ethernet) service quality monitoring;
- BrixVision: Comprehensive IP video quality and performance management; and
- BrixView: Advanced analytics and business intelligence software.

Products for Network Equipment Manufacturers

Wireline Test Equipment

Our network equipment manufacturer solutions, mainly built around our IQS-600 platform, are available as test modules or stand-alone benchtop instruments. The next-generation IQS-600 platform can efficiently run as many as 100 optical test modules using a single controller unit. Its system-based approach – one box, several test modules – combined with an open architecture (PXI, Windows, LabVIEW™, etc.) and ease of programming, produces a highly flexible test environment.

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The IQS-600 also provides backward compatibility with recent IQ-generation test modules, while delivering all the power and advantages of a next-generation platform. EXFO's wide selection of high-performance test modules includes high-speed power meters, light sources, WDM laser sources, tunable laser sources, variable attenuators, polarization controllers, optical spectrum analyzers and optical switches.

Outside our IQS family of products, we offer advanced, stand-alone test solutions for network equipment manufacturers in the process of developing ultra-high-speed optical networks.

The PSO-200 is the first turn-key optical modulation analyzer for complete characterization of signals up to 100 GBaud. Very high-speed network transmission is enabled through the efficient modulation of signals, whether it is phase, amplitude or both. To design 100G systems based on such advanced modulation schemes and to make sure they are ready for deployment, network equipment manufacturers have used in-house test solutions, which are often complex or limited. The introduction of the PSO-200 Optical Modulation Analyzer changes the picture as engineers working in R&D labs and manufacturing environments now have access to a turnkey and comprehensive test instrument that makes bandwidth limitation irrelevant.

The PSO-100 Series are among the industry's fastest sampling oscilloscopes, allowing characterization of optical signals at data rates up to 640 Gbits/s. The PSO-100 all-optical sampling oscilloscopes enable distortion-free, eye-diagram analysis and pattern visualization within existing high-speed optical networks.

Wireless Test Equipment

We offer 2G, 3G and 4G/LTE test solutions mainly for network equipment manufacturers. We provide two main product lines for the wireless test and measurement market: simulators and analyzers.

EXFO's network simulators simulate real-world, large-scale network traffic and end-user behavior in a laboratory environment in order to predict network behavior, uncover faults and optimize networks before wireless networks and services are deployed. Typical tests include regression and load testing.

EXFO's protocol analyzers analyze mobile network elements in order to validate functionality according to wireless technology specifications, whether these elements interoperate with each other effectively when combined to form a network, and how well the live network performs. These test tools allow engineers to troubleshoot networks in order to find the source of errors and quickly fix them. Our protocol analyzers support multi-interface testing and all major mobile technologies: GSM/GPRS/EDGE/UMTS/LTE. They enable fully automated testing and run powerful applications for protocol monitoring, call and session tracing, quality of service and radio optimization measurement.

We believe our wireless test tools optimize network performance and ensure a high-quality user experience. The following table summarizes our wireless test solutions and their typical applications for the telecommunications industry.

Wireless Test and Solutions

Product Type	Product Line	Typical Application
Protocol Analyzer	Hawk portfolio, including M5 analysis tool	Protocol analysis to verify correct network behavior.
Network Simulator	EAST portfolio, Navtel portfolio	Regression and load testing.
Mobile Communications Intelligence Tools	NetHawk F10, NetHawk X6 and NetHawk C2	Intelligence tools for police, armed forces and other governmental

organizations to fight organized
crime and terrorists.

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Products for Life Sciences and Industrial Customers

From December 2000 until the divestiture of our Life Sciences and Industrial Division in October 2010, we developed and acquired a number of core technologies that we leveraged in selected high-precision assembly and life sciences markets. For example, we offered several light-based curing solutions for optical component manufacturing applications and adapted our approach for other industries, such as semiconductor, microelectronic, and medical device manufacturing, in order to maximize revenues. Omnicure® systems delivered precise doses of the appropriate spectral light onto photosensitive adhesives to significantly reduce bonding time and increase repeatability. These light-based curing systems, supported by patented optical feedback, thermal control and radiometry technology, produced a high-quality bonding solution. Our technology and application knowledge placed us at the forefront of this market.

Another key product line was the X-Cite fluorescence illumination systems for microscope manufacturers. X-Cite systems deliver excellent image quality and at least 2000 hours of lamp life, which is over 60% longer than previous models and up to 10 times longer than conventional illumination systems. X-Cite systems are self-contained illumination units separate from a microscope. A simple light guide attachment through custom-coupling optics ensures a uniformly illuminated field of view with no heat from the lamp being transferred to the microscope. Models range from the basic X-Cite 120XL for routine imaging applications to the full-featured X-Cite Exacte, designed to provide maximum illumination stability and control for the most advanced live cell research. In addition, this division was developing UV curing solutions for the graphics digital printing market.

Research and Development

Our global R&D operations fall under the management of a vice-president. We maintain R&D centers in Quebec City, Canada, Montreal, Canada, Toronto, Canada, Chelmsford, USA, Oulu, Finland, Gothenburg, Sweden and Pune, India. Gross research and development expenditures in fiscal 2012 totaled $59.3 million, compared to $57.2 million in 2011 and $44.6 million in 2010.

We believe that our future success largely depends on our ability to introduce new solutions and product enhancements to our core technologies. Through market-oriented product portfolio review processes, we ensure that our investments in research and development are aligned with market opportunities and customers' needs. This process enables us to maximize our returns on R&D investments by focusing our resources on prioritized projects. Product portfolio review meetings, which occur three times per year, enable us to select the right mix of new products and allocate the necessary resources for their development. All our projects, including those already underway, are reviewed, given a priority rating and allocated budgets and resources. Existing projects can be stopped or substantially redefined if there have been significant changes in market conditions, or if the project development schedule or budget has significantly changed.

Product development projects, once they are underway, are managed through a structured process known as the stage-gate approach. The stage-gate approach is based on a systematic review of a project's progress at various stages of its lifecycle. The following are the key review stages of the stage-gate approach:

- Market study and research feasibility;
- Product definition;
- Development feasibility;
- Development;
- Qualification; and
- Transfer to production.

At each stage, we review our project risks, costs and estimated completion time. We compare our design to anticipated market needs and ensure that our new product development is synchronized with other internal departments and external industry events.

We also carried out research and development at our Life Sciences and Industrial Division in Toronto, Canada, until its divestiture in October 2010. The product development process was managed using a similar stage-gate process, while projects were reviewed and approved through a portfolio review.

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Sales

We sell our telecom wireline and wireless test and service assurance solutions through direct and indirect sales channels in the Americas (US, Canada, Central and South America), Europe, Middle East and Africa (EMEA) and Asia-Pacific regions.

In the Americas, we use a hybrid model, combining key account management with direct and indirect sales coverage. We typically use key account managers to serve large customers that generate high sales volumes or might potentially represent high sales volumes in the future. These key account managers are supplemented by regional sales managers, sales engineers, sales representatives and distributors in the US as well as Central and South American metropolitan areas, and regional sales managers and sales engineers in Canada.

We opt for a direct sales approach when selling higher-end, highly technical products to sophisticated buyers. Sales of low- to medium-level complexity products to less stringent technical buyers are usually done through a manufacturer representative organization or distributors supported by regional sales managers. Our main sales offices in the Americas are located in Plano, Texas, Quebec City, Canada, Toronto, Canada and Mexico. They are supplemented by a regional presence in cities across the US, Central and South America, as well as Canada.

On the international front, we have sales personnel covering strategic areas in EMEA and Asia-Pacific.

Our sales network in EMEA is supported by a main office and service center in Southampton, UK, which serves as headquarters of our European sales operations and also provides repair, calibration and technical support services for our EMEA customers. We also have additional sales offices in multiple countries across EMEA to serve and support our various customers and distribution partners.

As for Asia-Pacific, our main sales offices for South East Asia are located in Singapore and Hong Kong, while our main sales representative offices for mainland China are located in Beijing and Shenzhen. In addition, we have other sales offices in strategic locations around the world to support our network of distributors and various customers.

We also rely on a network of distributors worldwide to work with us in supporting mostly our international sales and to participate in a large number of international events. We believe that the local presence and cultural attributes of our distributors allow us to better serve our global markets.

Our direct telecom sales team consists of a vice-president responsible for each major geographic region: Americas, EMEA and Asia-Pacific. These three sales executives are supported by regional sales directors that lead a widely distributed team acting as key account managers, regional sales managers, sales engineers and application engineers. Our sales people are located throughout major metropolitan areas around the world. This group of sales professionals has on average more than 15 years of experience in the fields of telecommunications, fiber optics, or test and service assurance. Within each major geographic region, we have sales staff dedicated to wireline, wireless and service assurance customers.

We also have an in-house Customer Service Group to meet the needs of existing and new customers. This group is responsible for providing quotations to customers, supporting our sales force, managing demonstration units, order management, technical support and training as well as calibration and repair services.

Sales to customers in the Americas (US, Canada, Central and Latin America) represented 52% of our sales in fiscal 2012, while sales to customers in EMEA (Europe, Middle East and Africa) and Asia-Pacific accounted for 29% and 19% of our sales, respectively. In comparison, the Americas, EMEA and Asia-Pacific accounted for 51%, 32% and

17% of our sales, respectively, in 2011, and 52%, 30% and 18%, respectively, in 2010.

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The main office for our Life Sciences and Industrial Division was located in Toronto, Canada. We used mixed sales channels to serve various markets supported by this division, depending on product line and geography. Optical light sources and related accessories used for industrial applications were sold in North America through a network of manufacturer representatives and, internationally, through a network of distributors. UV light sources for digital print applications were sold directly to customers globally. The X-Cite 120 and Exacte Fluorescence Illumination Systems were sold through value-added reseller agreements with major microscope companies and system integrators in North America and Europe. Positioning products were sold directly to customers in North America, which includes the United States and Canada, and internationally through a network of technical distributors.

Product Management, Marketing/Communications and Global Services

Product Management

Our telecom product management duties fall under the responsibility of one of two vice-presidents, Test and Measurement or Systems and Service Assurance. Each product management executive is supported by directors and product managers who have various degrees in engineering, science and business administration. Directors and product managers are responsible for all aspects of our telecom marketing program including product strategy, new product introductions, definition of new features and functions, pricing, product launches and advertising campaigns. We follow up our marketing initiatives by attending industry trade shows. Furthermore, we have a customer relationship management (CRM) system to compile market and customer information including forecasts, opportunities, leads and competitive data. We use this information to make strategic business decisions. Finally, strategic marketing specialists analyze our markets of interests, compile competitive information and identify macro-trends in our sector.

Our Life Sciences and Industrial Group consisted of a director – responsible for both life sciences and precision assembly sectors – as well as product managers who had various degrees in engineering, science and business administration. Product managers, under the direction of the director, were responsible for all aspects of their business line marketing programs including product strategy, new product introductions, definition of new features and functions, pricing, product launches and advertising campaigns.

Marketing/Communications

Our Marketing-Communications team, which mainly consists of a director, project managers, marketing writers, translators and graphic artists, supports our product management team by producing marketing and corporate documentation. Literature includes specification sheets, application notes, product catalogues, advertising copy and an electronic corporate newsletter. This Marketing-Communications team is also responsible for all sales tools required by our worldwide sales force and for updating the marketing contents of our website.

The Life Sciences and Industrial Division's Marketing-Communications team shared a variety of marketing initiatives within EXFO. This group was assisted by product managers, who provided the technical data and collaborative support required to produce product specification sheets, catalogues, application notes and multimedia marketing tools. This Marketing-Communications team was responsible for all advertising material, Website updates, events planning (including trade shows) and direct promotional marketing such as mass mailings and telemarketing. This team also provided the sales tools required by the Life Sciences and Industrial Division's worldwide sales channels, including maintaining our channel partner programs and support.

Global Services

EXFO's Global Services operation, which falls under the responsibility of a vice-president, provides customers with a broad array of support and services worldwide. This team has in-house staff in North America, Europe, and Asia. It also provides local support in specific countries through select partners. Such a strategy enables EXFO to have a global reach while maintaining strong local ties.

This team's objective is to directly contribute to the customer's success and to achieve EXFO's long-term mission by providing internal and customer-facing services. Specifically, it fulfills its mission by offering:

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Customer Relationship Management (CRM) Administration – Business Ownership of EXFO's CRM toolset and evolution.

Sales Support – Leverage the effectiveness of its sales force by providing pre-sales and demo support, as well as guiding customers in purchasing the correct equipment for their respective applications, issuing quotations, and promoting our extended warranty service and support program.

Order Management – Accurately process customer orders from entry through fulfillment and delivery, and manage order changes.

Customer Service – Serve as a primary interface for inbound and outbound customer communication. Provide customers with one central point of contact and work with the customer from purchasing equipment to helping them arrange for service, if necessary.

Product Support – Provide expert technical support and deliver product service worldwide. Directly manage EXFO's Worldwide Service Centers, and the Service Partner Program. Where applicable, furnish installation and on-site servicing for more complex equipment and applications.

Systems Services – Provide pre-sale, delivery, post-sale technical support, and systems actualization of EXFO's network monitoring and converged service assurance systems.

Education Services – Aggregate expertise, develop material, and deliver free and fee-based training.

Professional Services – Provide value-added solution services for EXFO's test and system customers.

Manufacturing

Our telecom manufacturing operations consist mainly of material planning, procurement, sub-assembly, final assembly and test, software loading, calibration, quality control, shipping, billing and customs management. Most of our telecom manufacturing activities, which occupy a total of approximately 122,000 square feet, take place at our plants in Quebec City, Canada (2) and Shenzhen, China (1), but we also have facilities in Chelmsford, USA, and Oulu, Finland, for final assembly of service assurance and wireless test equipment. All our manufacturing operations fall under the supervision of a vice-president.

Our Quebec City, Canada, operations mainly produce low-volume, high-complexity telecom products. It has maintained ISO 9001 certification since 1994 and first obtained TL 9000 certification in July 2012. Our manufacturing plant in Shenzhen, China, which started operations in September 2007, is responsible for the production of high-volume, low-complexity telecom products. Our Shenzhen plant, which follows the same corporate quality standards, was first certified ISO 9001 in January 2009 and also obtained TL 9000 certification in July 2012.

All of our products meet required industry standards, and some of our products meet additional voluntary standards, such as those set by Telcordia, formerly Bellcore, IEC, IETF, ETSI and other bodies that issue industry standards. During manufacturing, each product has a related quality-assurance plan, with rigorous checkpoints, to ensure product conformity. Various tasks in the quality assurance process include quality control, conformity testing, product documentation, product improvement, regulatory compliance, metrology and calibration.

Our telecom manufacturing operations include the following responsibilities:

Production. From production planning to product shipment, our production department is responsible for manufacturing high-quality products on time. Factories are organized in work cells; each cell consists of specialized technicians and equipment and has full responsibility over a product family. Technicians are cross-trained and versatile enough, so that they can carry out specific functions in more than one cell. This allows shorter lead times by alleviating bottlenecks.

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Product Engineering and Quality. This department, which supports our production cells, acts like a gatekeeper to ensure the quality of our products and the effectiveness of our manufacturing processes. It is responsible for the transfer of products from research and development to manufacturing, product improvement, documentation, metrology, and the quality control and regulatory compliance process. Quality control represents a key element in our manufacturing operations. Quality is assured through product testing at numerous stages in the manufacturing process to ensure that our products meet stringent industry requirements and our customers' performance requirements.

Supply-Chain Management. This department is responsible for sales forecasting, raw material procurement, material-cost reduction and vendor performance management. Our products consist of optical, electronic and mechanical parts, which are purchased from suppliers around the world. Approximately one-third of our parts are manufactured to our specifications. Materials represent the largest portion of our cost of goods. Our performance is tightly linked to vendor performance, requiring greater emphasis on this critical aspect of our business.

Our manufacturing operations are subject to environmental laws in various jurisdictions around the world. Our product designs comply with Directive 2002/96/EC and Directive 2002/96/EC (RoHS), legislation enacted by the European Union regarding, respectively, the disposal of waste electrical and electronic equipment (WEEE) and the restriction of the use of certain hazardous substances in electrical and electronic equipment, for all products exported to Europe. As climate change, environmental and biodiversity issues have become critical to our global society, EXFO has established a plan to be certified ISO 14001 in 2013 and, therefore, reduce its environmental footprint.

Our Life Sciences and Industrial Division's manufacturing operations occupied 8,000 square feet in Toronto, Canada. This group manufactured light sources and related accessories, fluorescence illumination systems and precise positioning equipment for the life sciences and high-precision assembly markets. Operations consisted of manufacturing, procurement, warehousing, quality control and document control managed by various elements of the ISO 9001 certified quality system. Recognizing the importance of reduced time-to-market for our solutions, we focused efforts on designing products with an emphasis on standardization, modularity, as well as ease of fabrication and assembly.

Sources and Availability of Raw Materials

We use various suppliers to provide parts for the manufacture and support of multiple product lines. Although our intention is to establish at least two sources of supply for materials whenever possible for certain parts, we obtain certain materials from single or limited source supply arrangements. We may not be able to procure these parts from alternative sources at acceptable prices within a reasonable time; therefore, the loss or interruption of such arrangements could have an impact on our ability to deliver certain products on a timely basis. See Item 3D of this Annual Report under "Risk Factors" We depend on short-term arrangements with a single supplier or a limited number of suppliers for some key components and materials in our products, which makes us susceptible to supply shortages or price fluctuations that could adversely affect our operating results".

We will continue to reduce the risk of production interruptions and shortages of parts by: (1) selecting and qualifying alternative sources of supplies for key parts whenever possible, and (2) maintaining an appropriate supply of key parts.

Seasonality

Historically, we have been subject to seasonality mainly in our second quarter (December, January and February) due to the Christmas holidays and delays in approval of network operators' spending budgets for the new calendar year.

These two factors can have negative effects on our bookings in our second quarter, but they are mitigated by the renewal of annual maintenance contracts and sometimes calendar year-end spending on the part of network operators. Following the acquisition of NetHawk Oyj in 2010, we are also subject to seasonality in the fourth quarter (June, July and August), since bookings activity tends to slow down during the summer months, especially in Europe. These seasonal effects to do not apply consistently and do not always correlate to our financial results. Accordingly, they should not be considered as a reliable indicator of our future revenue or results of operations.

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Competition

The telecommunications wireline and wireless test and service assurance industry is highly competitive and subject to rapid change as a result of technological developments and market conditions. We compete with many different companies, depending on product family and geographical market. We believe that the main competitive factors in the industry include the following:

- product performance and reliability;
- solution's contribution to productivity;
- price and quality of products;
- level of technological innovation;
- product lead times;
- breadth of product offerings;
- ease of use;
- brand-name recognition;
- customer service and technical support;
- strength of sales and distribution relationships; and
- financial stability.

Main competitors in the test and measurement equipment environment include global suppliers like Anritsu Corporation, JDS Uniphase Corporation, and Danaher Corporation (Tektronix Communications and Fluke Networks), as well as other players like Yokogawa Electric Corporation, IXIA, Spirent Communications plc, AFL, Kingfisher International, ShinewayTech and VeEX Inc. On the service assurance side, we mainly compete against Tektronix Communications, Anritsu Corporation, JDS Uniphase Corporation, NetScout Systems, Inc., IXIA and Spirent Communications plc. See Item 3D of this Annual Report under "Risk Factors" We must continue to overcome significant competition in our targeted industries in order to gain market share and achieve our growth strategy."

Competition for our life sciences and industrial solutions was quite varied, depending upon product line. OmniCure's competitors, which sell light-based curing products, included Dymax Corporation, Henkel Corporation in North America and Europe, as well as Hamamatsu Photonics K.K., Ushio Inc., Omron Corporation, Hoya Corporation and Panasonic Corporation in Asia. Excelerate competed globally with products from well-established companies such as Dr. Honle, Nordson and Integration Technologies. With regard to the X-Cite® Fluorescence Illumination Systems, main competitors consisted of microscope manufacturers who had developed lamp housings for low-wattage mercury burners in-house. Additional competitors included CoolLED and Prior Scientific. Finally, our motion-control instruments, which were designed for various life science applications, competed against products from companies like Sutter Instruments and Narishige.

Employees

As at November 1, 2012, we had 1,732 full-time employees compared to 1,752 and 1,656 for the same periods in 2011 and 2010, respectively. Our workforce as of November 1, 2012 included 356 employees in manufacturing, 816 employees in research and development, and 560 employees in sales and marketing as well as general and administrative functions.

Our future performance depends, to a significant degree, on our continued ability to attract and retain highly skilled and qualified technical, sales and marketing, and senior management personnel. Our employees are not represented by a labor union with the exception of our manufacturing personnel in Quebec City, Canada. We consider relations with our employees to be good. See Item 3D of this Annual Report under "Risk Factors We require employees and

managers who are knowledgeable about the specialized nature of our business. If we are unable to attract and retain sufficient numbers of highly skilled technical, sales, marketing, senior management and other personnel, our operations and financial results will suffer".

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Regulatory Environment

In most countries where our products are sold, our products must comply with the regulations of one or more governmental entities. These regulations often are complex and vary from country to country. Depending upon the country and the relevant product, the applicable regulations may require product testing, approval, registration, marking and unique design restrictions. Accordingly, we have appointed a team of engineers who are responsible for ensuring that our products comply with all applicable regulations.

In the United States, our products must comply with the regulations of some agencies of the U.S. federal government, including the Federal Communications Commission (FCC), the Food and Drug Administration (FDA) and the Occupational Safety and Health Administration (OSHA). Under the FCC's regulations, our products must comply with certain electromagnetic compatibility (EMC) requirements to insure they do not generate electromagnetic noise which could possibly cause undesirable operation, as well as affect other surrounding devices. Additionally, some of our products must comply with the FDA's non-medical performance standards and related rules concerning light-emitting products, such as lasers. The FDA's regulations applicable to our products are intended to promote safety by limiting human exposure to harmful non-iodizing radiation. Similarly, our products must comply with safety standards adopted by OSHA. Furthermore, for our Life Science and Industrial Division, certain U.S. states require mandatory product registration and reporting of Mercury-added products being imported. This registration is controlled by the Interstate Mercury Education and Reduction Clearinghouse (IMERC).

Similar regulations apply in other countries. For example, in Canada our products must comply with the applicable standards adopted by the Standards Council of Canada (SCC). These include product safety standards developed in collaboration with the Canadian Standards association as well as EMC requirements adopted by Industry Canada. Countries in the European Union require product compliance as dictated by the applicable directives, which are required to be authorized to apply the CE marking on the product. This includes testing to ensure compliance with harmonized European Norm (EN) standards for product safety, EMC requirements and now RoHS.

In Europe, with the implementation of the WEEE directives for recycling of electronic products in selected European Countries (2002/96/EC revisited later and named 2012/19/EU), EXFO has established a process to ensure full compliance with regulations and oversee the management, logistics, recycling rate, disposal services and activities related to recycling of electronic equipment and products within the member states.

Additionally, to address the issue of environmental compliance, the European Union has mandated the Restriction of the Use of Certain Hazardous Substances or "RoHS" Directive (2002/95/EC revisited later and named 2011/65/EU), which applies to all products included within the scope of WEEE directive with the exception of Categories 8 (Medical devices) and 9 (Monitoring and control instruments). Mandatory product compliance includes the ban of certain substances within specified concentrations, unless formally exempted by the directive. To ensure compliance to this directive, a formal restricted substances control (RSC) program was implemented for our products included within the scope of WEEE. This program ensures the design, procurement and manufacturing of affected products prevents the inclusion of the banned substances as specified by the RoHS directive.

Other significant types of regulations not described in this Annual Report also may apply, depending upon the relevant product and country of destination.

Intellectual Property

Our success and ability to compete are dependent in part on our ability to develop and protect our proprietary technology. We file U.S. and international applications to protect technology, inventions and improvements important

to the development of our business. We also rely on a combination of copyright, trademark, trade secret rights, licensing and confidentiality agreements. See Item 3D of this Annual Report under "Risk Factors Our intellectual property and proprietary technology are important to the continued success of our business. Our failure to protect this proprietary technology may significantly impair our competitive position"; Risk Factors Our intellectual property rights, particularly our existing or future patents may be invalidated, circumvented, challenged or required to be licensed to others" and "Risk Factors Others may claim that our products infringe upon their intellectual property rights, or they may infringe our intellectual property, and we may expend significant resources enforcing or defending our rights or suffer competitive injury."

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As of August 31, 2012, our records indicate that we held 38 actively-maintained granted U.S. patents, 49 granted or validated patents in countries of the European Community, 8 patents in Canada, 5 patents in China, and one patent in the Russian Federation. In addition, we have 23 patent applications pending in the U.S., 7 in Canada, 8 in China, 1 in Finland, 12 regional patent applications at the European Patent Office, and 7 applications in other countries, as well as 2 International Applications under the Patent Cooperation Treaty that have not yet entered the national/regional phase. The expiration dates of our active issued patents range from 2012 to 2030.

We consider seven of our inventions for which patents have either been granted or are pending to be material. These inventions are:

a method and apparatus for characterizing optical power levels in three-wavelength, bidirectional fiber-to-the-home systems. This invention describes how the optical power can be measured at the two-downstream and one upstream wavelengths used to connect a residence or business customer, while maintaining the signal continuity necessary to keep the home-based Optical Network Terminal operating. This invention underlies the two-port version of our PPM-350 series of PON power meters;

a method for determining the optical signal-to-noise ratio employing an optical spectrum analyzer, which is particularly advantageous for use with tightly-filtered DWDM signals used in high-bandwidth optical networks. This invention is a key value-added option to our FTB-5240-S series of portable optical spectrum analyzers;

a method and apparatus to determine the theoretical and practical data rates for a cable under test. This invention forms the basis of the EXFO CableSHARK product, describing how two test devices, communicating with each other via the cable under test, can predict the performance of a pair of ADSL (Asymmetric Digital Subscriber Line) modems, and in case of problems, analyze the cause of the modems' failure to synchronize;.

a method and system for hardware time stamping packetized data to provide sub-microsecond accuracy in test measurements, which is embedded in the Brix100M, Brix1000, and Brix2500 Series Verifiers;

a method for actively analyzing a data packet delivery path to provide diagnostics and root cause analysis of network delivery path issues, which is embedded in BrixCall, BrixNGN, and BrixVision applications of EXFO Service Assurance;

a distributed protocol analyzer for quality-of-service measurement. This invention underlies the combined QoS measurements offered in the NetHawk iPro and NetHawk M5 products; and

a communication methodology used to perform independent bi-directional protocol testing over a connection or connectionless network between two test instruments, wherein the transfer mechanism of status and intermediate test results during an active test and the transmission of the final results to one of the instruments enables the user to perform a bidirectional single-ended test. This invention is at the heart of the EXFO Datacom product families, including applications in conformity with our EtherSAM standard test suite.

Confidentiality and proprietary information agreements with our senior management, employees and others generally stipulate that all confidential information developed or made known to these individuals by us during the course of their relationship is to be kept confidential and not disclosed to third parties, except in specific circumstances. The agreements also generally provide that all intellectual property developed by the individual in the course of rendering services to us belongs exclusively to us. These efforts afford only limited protection.

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C. Organizational Structure

As of November 1, 2012, the following chart presents our corporate structure, the jurisdiction of incorporation of our subsidiaries and the percentage of shares (which is also the percentage of voting power) that we hold in those subsidiaries.

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D. Property, Plants and Equipment

Our head offices are located in Quebec City, Province of Quebec, Canada where we occupy two buildings. These buildings house our executive and administrative offices, research and development facilities and production facilities. We also have offices in Montreal, Province of Quebec, Canada (formerly Avantas Networks Inc), in Concord, Ontario, Canada (formerly Consultronics Limited), in Chelmsford, Massachusetts, United States (formerly Brix Networks Inc., now EXFO Service Assurance Inc.), in Eastleigh, Hampshire, United Kingdom (EXFO Europe Limited), in Shenzhen, China (EXFO Telecom Equipment (Shenzhen) Co. Ltd.), in Pune, India (EXFO Electro-Optical Engineering India Private Ltd.), in Gothenburg, Sweden (EXFO Sweden Aktiebolag), in Oulu, Finland (NetHawk Oyj), in Lappeenranta, Finland (NetHawk Oyj), in Bhubaneswar, India (NetHawk Networks India Pvt. Ltd.), in Richardson, Texas, United States (EXFO America Inc.).

In addition, we maintain sales offices and/or have regional sales managers located in China, Czech Republic, France, Germany, Great Britain, India, Mexico, Singapore, Spain, Sweden, United Arab Emirates and the United States.

In September 2010, in April 2011 and in August 2012, we purchased premises in Magarpatta, Pune, India.

In May 2012, we completed the construction and relocated our R&D activities (located in St-Laurent) into a new building of 125,000 sq. ft. We occupy approximately 50% of the premises and intent to lease the remaining for an undetermined period. This project costs incurred total $21.5 million and was paid cash.

The following table sets forth information with respect to the main facilities that we occupy as of November 1, 2012.

Location	Use of Space		Square Footage	% of Utilization	Type of Interest
436 Nolin Street Quebec (Quebec) G1M 1E7	Occupied for manufacturing of products		44,000	50%	Owned
400 Godin Avenue Quebec (Quebec) G1M 2K2	Occupied for research and development, customer services, manufacturing, management and administration	(1)	129,000	80%	Owned
2500 Alfred-Nobel St-Laurent (Quebec) H4S 2C3	Occupied for research and development, management and administration		75,000	50%	Owned
2500 Alfred-Nobel St-Laurent (Quebec) H4S 2C3	Available for rent		50,000	0%	Owned
160 Drumlin Circle Concord (Ontario) L4K 3E5	Occupied for research and development, product management and administration		23,500	40%	Owned
270 Billerica Road Chelmsford, MA 01824	Occupied for research and development,		29,000	65%	Leased

United States	manufacturing, management and administration

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Location	Use of Space	Square Footage	% of Utilization	Type of Interest
Winchester House School Lane Chandlers Ford, Eastleigh, Hampshire SO53 4DG United Kingdom	Occupied for European customer service, sales management and administration	13,000	60%	Leased
3rd Floor, Building 10, Yu Sheng Industrial Park (Gu Shu Crossing) No. 467, National Highway 107 Xixiang, Bao An District Shenzhen 518126, China	Occupied for manufacturing of telecom products	56,000	80%	Leased
Offices No 102, 602, 603, 604 and 702 Tower S-4 Cybercity Magarpatta , Hadapsar Pune 411 013 India	Occupied for research and development	31,947	80%	Owned
Elektroniikkatie 2 FI-90590 Oulu, Finland	Occupied for research and development, manufacturing, management and administration	47,097	60%	Leased
NetHawk Networks India Private Ltd. 5th floor, IDCO Tower 2000 Mancheswar Industrial Area Bhubaneswar 751010, India	Occupied for research and development	25,239	70%	Leased

(1) Including the warehouse space. Premises without the warehouse are approximately 115,000 square feet.

Item 4A. Unresolved Staff Comments

Not applicable.

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Item 5. Operating and Financial Review and Prospects

This discussion and analysis contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition. Words such as may, will, expect, believe, plan, anticipate, intend, could, estimate, continue, or similar expressions or the negative of such expressions are intended to identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events and circumstances are considered forward-looking statements. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including, but not limited to, macro-economic uncertainty and/or recession (including our ability to quickly adapt cost structures with anticipated levels of business and our ability to manage inventory levels with market demand); capital spending and network deployment levels in the telecommunications industry; future economic, competitive, financial and market conditions; limited visibility with regards to customer orders and the timing of such orders; fluctuating exchange rates; consolidation in the global telecommunications test and service assurance industry and increased competition among vendors; concentration of sales; timely release and market acceptance of our new products and other upcoming products; our ability to successfully integrate businesses that we acquire; our ability to successfully expand international operations; and our retention of key technical and management personnel. Assumptions relating to the foregoing involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. Other risk factors that may affect our future performance and operations are detailed in this Annual Report. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure you that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document.

The following discussion and analysis of financial condition and results of operations is dated November 7, 2012.

All dollar amounts are expressed in US dollars, except as otherwise noted.

TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

On September 1, 2011, we adopted International Financial Reporting Standards (IFRS) as issued by the “International Accounting Standards Board (IASB)”. Our consolidated financial statements for the year ended August 31, 2012 have been prepared in accordance with IFRS 1, “First-Time Adoption of International Financial Reporting Standards”, as issued by the IASB. Previously, we prepared our consolidated financial statements in accordance with Canadian generally accepted accounting principles, in effect prior to September 1, 2011 (previous GAAP). Comparative information as at August 31, 2011 and for the year ended August 31, 2011 has been restated to comply with IFRS. Note 3 to our consolidated financial statements details the most significant adjustments to our reported statement of change in shareholders’ equity, statements of earnings, comprehensive income and cash flows for the comparative year.

INDUSTRY OVERVIEW

Market conditions in the telecommunications industry remain difficult due to a sluggish macro-economic environment, the European debt crisis and its ripple effects on other economies, as well as the tightening of capital

spending among network operators. In addition, network operators are attempting to monetize their investments in next-generation fixed and mobile networks as data revenue growth is not keeping pace with the required level of expenditures. Consequently, network operators are reassessing their business models and spending levels in efforts to improve profitability.

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Despite these constraints, the fundamental drivers toward broadband deployments and fixed-mobile Internet protocol (IP) network convergence are firmly entrenched in the telecommunications industry. Although we do not expect that network operators will significantly increase capital expenditures in fiscal 2013, we believe they will spend more in select, high-growth areas to accommodate bandwidth-intensive broadband applications and to facilitate the migration to more flexible and cost-effective fixed and mobile IP networks.

Growing Bandwidth Demand

According to Cisco's Visual Networking Index, global IP traffic will nearly quadruple from 2011 to 2016, reaching 1.3 zettabytes per year in 2016. (A zettabyte is equal to 1,000 exabytes or 250 billion DVDs). According to Cisco, global mobile traffic, a subset of this larger group, is expected to increase 18-fold during the same period. We believe this explosive growth is being driven by a proliferation of media-rich mobile communication devices (smart phones and tablets), a growing number of Internet users, faster broadband speeds and increased video usage.

IP-Based Services

To support such bandwidth growth, wireline networks are being transformed into next-generation IP-based infrastructures. Legacy SONET/SDH networks, which were established in the mid-1980s, do not have the flexibility to seamlessly mix and transport voice, data and video services. These networks are not capable of efficiently carrying triple-play services because they were designed for point-to-point voice communication. As a result, new optical transport network (OTN) standards, which are at the very heart of what the industry is labeling next-generation IP networks, have been defined to carry IP applications over Ethernet. Network operators are increasingly turning to such next-generation, IP-based networks in order to offer customers higher-margin triple-play services while lowering their operating costs.

FTTH and Hybrid Networks

Fiber-to-the-home (FTTH) has also become the access network architecture of choice for wireline operators wishing to provide a superior user experience for a combined voice, data and video offering. This architecture allows operators to meet heightened bandwidth requirements and future-proof their access networks as residential bandwidth demands grow from 1 to 5 Mbit/s (megabits per second) to 30 to 100 Mbit/s required for the long term. Hybrid architectures, combining copper and fiber (fiber-to-the-curb, or FTTC, and fiber-to-the-node, or FTTN), will also increase in the short term, since they are less expensive methods to increase bandwidth and can be mass-deployed quickly.

Core Network Expansion Initiatives

As bandwidth growth in access networks continues to increase, it has begun placing a strain on metro rings and core networks. It is also driving the need for higher-speed technologies. For example, 43 Gbit/s (gigabits per second) SONET/SDH is becoming mainstream, while commercial deployments of 100 Gbit/s Ethernet networks are under way. In the long run, we expect these solutions will offer a more economical way to add capacity to congested network links, especially if trenches need to be dug in order to deploy new fiber in metro and long-distance routes.

Wireless Network Investments

On the wireless side, operators are also faced with major investments to meet soaring bandwidth demand. Wireless operators are accelerating deployments of 3G networks, fast-tracking 4G/LTE adoption, and investing in mobile backhaul networks in order to increase transmission rates for bandwidth-hungry consumers to approach wireline speeds. Furthermore, as these consumers expect wireline and wireless networks to transport any content to any device

at any time, both fixed and mobile networks are converging to a common IP-based infrastructure supported by IMS (IP multimedia subsystem) for seamless network interoperability.

These market dynamics affected telecom test and service assurance vendors in fiscal 2012.

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COMPANY OVERVIEW

We are a leading provider of next-generation test and service assurance solutions for wireline and wireless network operators and equipment manufacturers in the global telecommunications industry. We offer core-to-edge solutions that assess the performance and reliability of converged, IP (Internet Protocol) fixed and mobile networks. Our test and service assurance solutions specifically target high-growth market opportunities related to optimizing next-generation networks: wireless backhaul, 4G/LTE (long-term evolution), fiber-to-the-home (FTTH)/fiber-to-the-curb (FTTC)/fiber-to-the-node (FTTN), carrier Ethernet, and 40G/100G network upgrades. Customers on a global basis rely on our test and service assurance solutions to enable their wireline and wireless networks to perform optimally during their complete lifecycles: research, development, manufacturing, installation, maintenance and monitoring. Our success has been largely predicated on our core expertise in developing telecom test equipment for wireline network operators and to a lesser extent equipment manufacturers, but over the years we have expanded our offering to wireless network operators, cable television companies, public utilities, private network operators, third-party installers, equipment rental companies, large enterprises, component vendors and laboratory researchers.

We have a staff of approximately 1700 people in 25 countries, supporting more than 2000 telecom customers in approximately 100 countries around the world. We operate three main manufacturing sites, which are located in Quebec City, Canada, in Shenzhen, China and in Oulu, Finland. We also have five main research and development expertise centers in Boston, Toronto, Montreal, Quebec City and Oulu, supplemented by a software development center in India.

In fiscal 2012, we completed the construction of our new building in Montreal, Canada, which we occupy since June 2012.

In fiscal 2012, we committed to implement a restructuring plan to align our cost structure with the challenging market environment. This plan will result in one-time expenses of approximately US$3.3 million, mainly for severance expenses. Most of the plan was executed in the fourth quarter of fiscal 2012 and it resulted in charges of $2.3 million in severance expenses during that period; the remaining of the plan will be executed in the first half of fiscal 2013.

We launched 21 new products in fiscal 2012. Key product introductions in 2012 included amongst others the FTB-85100G Packet Blazer, a multi-rate, multi-service test solution for characterizing high-speed networks reaching 100G; Ethernet One, a centralized Ethernet service activation and monitoring solution that enables operators to improve the operational efficiency of their networks from the core to the last mile; EXFO Apps, a portal offering software applications that boost the capabilities and productivity of FTB platforms and test modules; the QA-805/QA-813 QualityAssurer, the industry's most scalable platform (simulates more than 12 million active subscribers) for load simulation of converged 3G, 4G/LTE and IMS networks; the portable iPro, an intelligent high-performance capture and analysis probe for wireless networks up to 10 Gbit/s; and the MaxTester 600 series for cost-effective VDSL2 (very-high-speed-digital subscriber line 2) installation and repair work on copper links.

We reported sales of $250.0 million in fiscal 2012, which represents a decrease of 7.3% year-over-year from $269.7 million in 2011, mainly due to global economic conditions and reduced spending by network operators.

We reported a net loss from continuing operations of $3.6 million, or $0.06 per share, in fiscal 2012, compared to net earnings from continuing operations of $9.2 million, or $0.15 per diluted share, in 2011. The net loss from continuing operations in fiscal 2012 included $7.8 million in after-tax amortization of intangible assets, $1.9 million in stock-based compensation costs, $1.9 million in after-tax restructuring charges and a gain of $0.3 million for the changes in the fair value of the cash contingent consideration. Net earnings from continuing operations

for fiscal 2011 included $8.7 million in after-tax amortization of intangible assets, $2.0 million in stock-based compensation costs and a gain of $2.7 million for the changes in the fair value of the cash contingent consideration. Earnings from operations (from continuing operations) amounted to $504,000, or 0.2% of sales in fiscal 2012 compared to $21.3 million, or 7.9% of sales in 2011.

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Adjusted EBITDA (net earnings (loss) before interest, income taxes, depreciation of property, plant and equipment, amortization of intangible assets, changes in the fair value of the cash contingent consideration and gain from disposal of discontinued operations) amounted to $13.5 million, or 5.4% of sales, in fiscal 2012, compared to $30.6 million, or 11.3% of sales in 2011. Adjusted EBIDTA in fiscal 2012 included a foreign exchange loss of $657,000, compared to $3.8 million in 2011. See further in this document for a complete reconciliation of adjusted EBITDA and IFRS net earnings (loss).

On November 7, 2011, we announced that our Board of Directors had approved the renewal of our share repurchase program, by way of a normal course issuer bid on the open market of up to 2% of the issued and outstanding subordinate voting shares, representing 575,690 subordinate voting shares at the prevailing market price. The normal course issuer bid started on November 10, 2011, and will end on November 9, 2012.

On November 7, 2012, we announced that our Board of Directors approved the renewal of our share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of the issued and outstanding subordinate voting shares, representing 2,072,721 subordinate voting shares at the prevailing market price. We expect to use cash, short-term investments or future cash flow from operations to fund the repurchase of shares. The normal course issuer bid will start on November 12, 2012, and will end on November 11, 2013, or on an earlier date if we repurchase the maximum number of shares permitted under the bid. The program does not require that we repurchase any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled. We shall provide to any person or company, upon request to our Secretary, at 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2, phone number (418) 683-0913 ext. 23704 or fax number (418) 683-9839, a copy of the notice sent to the Toronto Stock Exchange (TSX) according to our normal course issuer bid.

Sales

We sell our products to a diversified customer base in approximately 100 countries through our direct sales force and channel partners, such as sales representatives and distributors. Most of our sales are denominated in US dollars and euros.

In fiscal 2011 and 2012, no customer accounted for more than 10% of our sales, with our top customer representing 7.2% and 4.4% of our sales respectively.

We believe that we have a vast array of products, a diversified customer base, and a good spread across geographical areas, which provides us with reasonable protection against the concentration of sales and credit risk.

Cost of Sales

The cost of sales includes raw materials, salaries and related expenses for direct and indirect manufacturing personnel, as well as overhead costs. Excess, obsolete and scrapped materials are also included in the cost of sales. However, the cost of sales is exclusive of depreciation and amortization, which are shown separately in the statements of earnings.

Operating Expenses

We classify our operating expenses into three main categories: selling and administrative expenses, research and development expenses, as well as depreciation and amortization expenses.

Selling and administrative expenses consist primarily of salaries and related expenses for personnel, sales commissions, travel expenses, marketing programs, professional services, information systems, human resources and other corporate expenses.

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Gross research and development expenses consist primarily of salaries and related expenses for engineers and other technical personnel, material component costs as well as fees paid to third-party consultants. We are eligible to receive research and development tax credits and grants on research and development activities carried out in Canada and Finland. All related research and development tax credits and grants are recorded as a reduction of gross research and development expenses.

OUR STRATEGY AND KEY PERFORMANCE INDICATORS

Three-Year Strategic Objectives

Our long-term goal is to become the market leader in the global telecom test and service assurance industry. To help us reach our eventual goal, we had established a growth strategy that took advantage of soaring bandwidth demand and IP network convergence on fixed and mobile networks. This strategy, which was fine-tuned over the years, consisted of:

- Increasing our wireless presence;
- Enable network operators to reduce their operating expenses;
- Expanding our share of wallet with Tier-1 network operators; and
- Accelerating profitability through execution.

To gauge the success of our strategy, we had established three corporate performance objectives for the three-year period ended in fiscal 2012:

- o Increase sales by a CAGR* of at least 25%
- o Raise gross margin to 65%
- o Increase adjusted EBITDA** in dollars by a CAGR of at least 30%

* Compound annual growth rate

** EBITDA is defined as net earnings (loss) before interest, income taxes, depreciation of property, plant and equipment, amortization of intangible assets and impairment of goodwill. Adjusted EBITDA represents EBITDA excluding changes in the fair value of the cash contingent consideration and the gain from the disposal of discontinued operations.

Results Achieved in Fiscal 2012

Our corporate performance objectives take into account the sales and operating results of our Life Sciences and Industrial Division, which are presented as discontinued operations in our figures for fiscal 2009, 2010 and 2011.

Following are our results of our three-year plan:

Corporate Performance Objectives (Fiscal 2010-2012)

		Results After		
Objectives	Metrics	1 Year	2 Years	3 Years
Increase sales by a CAGR of at least:	25%	32.0%	25.4%	13.1%
Raise gross margin from 61.3% to:	65%	62.4%	62.7%	63.3%
	30%	88.8%	45.4%	-2.2%

Increase adjusted EBITDA** in dollars by a
CAGR of at least:

In fiscal 2012, our sales amounted to $250.0 million, which represents a CAGR of 13.1% for the three-year period. Our gross margin, reached 63.3% in fiscal 2012. Finally, adjusted EBITDA amounted to $13.5 million, or 5.4 % of sales, in fiscal 2012, representing a negative CAGR of 2.2% for the three-year period. See further in this document for a reconciliation of IFRS net earnings (loss) to adjusted EBITDA.

We were on track to achieve our corporate performance objective two years into our three-year plan. In fiscal 2012, however, a sluggish macro-economic environment, combined with the debt crisis in Europe, caused several network operators to hold off on their capital-intensive spending projects; consequently, we fell short of our three-year goals. However, during this three-year period, we remained committed to our growth strategy, which led our actions.

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RESULTS OF OPERATIONS
(in thousands of US dollars, except per share data, and as a percentage of sales for the periods indicated)

Consolidated statements of earnings data:	2012	2011	2012	2011
Sales	$249,966	$269,743	100.0 %	100.0 %
Cost of sales (1)	91,792	100,296	36.7	37.2
Selling and administrative	94,139	87,062	37.7	32.3
Net research and development	49,854	47,927	19.9	17.7
Depreciation of property, plant and equipment	6,169	6,655	2.5	2.5
Amortization of intangible assets	7,819	9,183	3.1	3.4
Changes in the fair value of cash contingent consideration	(311)	(2,685)	(0.1)	(1.0)
Earnings from operations	504	21,305	0.2	7.9
Interest and other income	131	511	0.1	0.2
Foreign exchange loss	(657)	(3,808)	(0.3)	(1.4)
Earnings (loss) before income taxes	(22)	18,008	–	6.7
Income taxes	3,571	8,814	1.4	3.3
Net earnings (loss) from continuing operations	(3,593)	9,194	(1.4)%	3.4 %
Net earnings from discontinued operations	–	12,926		
Net earnings (loss) for the year	$(3,593)	$22,120		
Basic and diluted net earnings (loss) from continuing operations per share	$(0.06)	$0.15		
Basic net earnings (loss) per share	$(0.06)	$0.37		
Diluted net earnings (loss) per share	$(0.06)	$0.36		
Other selected information:				
Gross margin (2)	$158,174	$169,447	63.3 %	62.8 %
Research and development data:				
Gross research and development	$59,282	$57,226	23.7 %	21.2 %
Net research and development	$49,854	$47,927	19.9 %	17.7 %
Restructuring changes included in:				
Cost of sales	$264	$–	0.1 %	– %
Selling and administrative expenses	$1,181	$–	0.5 %	– %
Net research and development expenses	$884	$–	0.4 %	– %

Adjusted EBITDA (2)	$13,524	$30,583	5.4 %	11.3 %
Consolidated balance sheets data:				
Total assets	$306,683	$322,355		

(1) The cost of sales is exclusive of depreciation and amortization, shown separately.
(2) Refer to page 50 for non-IFRS measures.

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RESULTS FROM CONTINUING OPERATIONS (formerly the Telecom Division)

SALES

In fiscal 2012, our sales decreased 7.3% to a $250.0 million, compared to $269.7 million in 2011.

In fiscal 2012, market conditions in the telecommunications industry remained tenuous due to macro-economic uncertainty, the European debt crisis and its ripple effects on other economies, the tightening of capital spending among network operators as well as delays in customers' orders. In addition, Europe turned out to be more impacted than we expected, the anticipated pick-up of spending in the Americas did not materialize, especially with Tier-1 operators, while China has been sluggish. This has rendered our end-markets very difficult in the short term and has resulted in lower sales in fiscal 2012, compared to 2011.

In addition, network operators are grappling with issues of monetizing their investments in next-generation fixed and mobile networks as data revenue growth is not keeping pace with the required level of expenditures. Consequently, network operators are reassessing their business models and spending levels in efforts to improve profitability, as they are increasingly scrutinizing their capital expenditures and even delaying some purchasing decisions. Reduced capital spending and less capital-intensive network deployments mostly affected our physical-layer solutions sales in fiscal 2012, compared to 2011.

Also, in fiscal 2012, as a result of the above-mentioned factors, we did not benefit from the same level of calendar year-end budget spending from some of our customers compared to 2011. The magnitude of customers' calendar year-end budget spending may fluctuate year-over-year.

Furthermore, in fiscal 2011, we received a follow-on order worth over $6 million from a Tier-1 European operator for our AXS-200/635 triple-play tester. We did not recognize such large single order in fiscal 2012, which reduced our sales of physical-layer solutions year-over-year.

Also, in fiscal 2012, the increase in the average value of the US dollar compared to the euro had a negative impact of approximately $2 million on our sales compared to 2011 as we report our results in US dollars; this represents a decrease of 0.7% of sales year-over-year.

Finally, in fiscal 2012, we recorded in our sales foreign exchange gains of $1.1 million on our forward exchange contracts, compared to $2.8 million in 2011, which contributed to decrease our sales 0.6% year-over-year.

Despite current challenging market conditions on a global basis and the general decrease in our sales year-over-year in fiscal 2012, we delivered a 4.4% sales growth for our protocol products year-over-year. Protocol sales are less dependent on large network rollouts and benefited from system upgrades from 10 Gbit/s to 40 Gbit/s and 100 Gbit/s as well as investments in wireless backhaul networks.

The following table summarizes changes in sales by product lines:

	Years ended		
	August 31, 2012	August 31, 2011	Change in %
Physical-layer solutions	$135,141	$ 158,002	(14.5) %
Protocol-layer solutions	113,700	108,946	4.4

Foreign exchange gains on forward exchange contracts	1,125	2,795	(59.7)
Total sales	$249,966	$ 269,743	(7.3) %

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Bookings

Bookings decreased 10.1% year-over-year to $244.8 million in fiscal 2012 from $272.3 million in 2011, for a book-to-bill ratio of 0.98 in fiscal 2012.

As mentioned earlier, we believe that difficult market conditions in the telecommunications industry, which led to reduced capital spending and less capital intensive deployments, had a negative impact on our bookings in fiscal 2012 compared to 2011, especially for our physical-layer solutions. Our protocol products bookings, benefited from system upgrades from 10 Gbit/s to 40 Gbit/s and 100 Gbit/s as well as investments in wireless backhaul networks, which limited the year-over-year decrease in bookings for this product line.

Geographic distribution

In fiscal 2012, sales to the Americas, Europe, Middle-East and Africa (EMEA) and Asia-Pacific (APAC) accounted for 52%, 29% and 19% of sales respectively, compared to 51%, 32% and 17% respectively in 2011.

GROSS MARGIN (non-IFRS measure – refer to page 50 of this document)

Gross margin amounted to 63.3% and 62.8% of sales in fiscal 2012 and 2011 respectively.

The increase in our gross margin in fiscal 2012, compared to 2011, can be explained by the following factors.

First, in fiscal 2012, the product mix was more favorable as we sold more protocol testing products compared to 2011, which resulted in a higher gross margin year-over-year. Protocol testing products deliver higher gross margin than our other product lines. In addition, in fiscal 2011, we reported larger orders for copper-access solutions, which typically deliver lower margins than our other test solutions, and we granted larger volume discounts on a significant part of these sales.

Furthermore, in fiscal 2012, our warranty provision decreased compared to 2011; this resulted in a positive impact on our gross margin year-over-year.

In addition, in fiscal 2012, a larger portion of our sales came from products manufactured in our facilities in China compared to 2011; those products have a lower cost of goods than those manufactured in our facilities in Canada, thus resulting in an improvement in our gross margin year-over-year.

On the other hand, a lower sales volume in fiscal 2012 compared to 2011 (7.3%) resulted in a lower absorption of our fixed manufacturing costs, which prevented us from further improving our gross margin year-over-year.

In addition, in fiscal 2012, we faced increased pricing pressure, which negatively affected our gross margin year-over-year.

Also, in fiscal 2012, we recorded $264,000 in restructuring charges in the cost of sales, which negatively impacted our gross margin year-over-year.

Furthermore, in fiscal 2012, due to the decrease in the value of the Canadian dollar versus the US dollar, we reported a lower gain on our forward exchange contracts in our sales compared to the same period last year, which negatively affected our gross margin year-over-year.

Finally, the decrease in the value of the Canadian dollar, compared to the US dollar over the last few months had a negative impact on our gross margin in fiscal 2012 compared to 2011; in fact, our procurement costs increased as the Canadian dollar decreased compared to the US dollar, as a significant portion of our raw material purchases are denominated in US dollars and our raw material costs of parts purchased in US dollars are measured in Canadian dollars in our financial statements.

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Outlook for fiscal 2013

Considering the expected sales growth, the expected increase in sales of protocol products as well as software-intensive products and services, the cost-effective design of our products, our increased manufacturing activities in China and our tight control on operating costs, we expect our gross margin to improve in the future. However, our gross margin may fluctuate quarter-over-quarter due to the mix of our products and as our sales may fluctuate. Furthermore, our gross margin can be negatively affected by increased competitive pricing pressure, customer concentration and/or consolidation, increased obsolescence and warranty costs, shifts in customer and product mix, under-absorption of fixed manufacturing costs and increases in product offerings by other suppliers in our industry.

SELLING AND ADMINISTRATIVE EXPENSES

Selling and administrative expenses were $94.1 million and $87.1 million for fiscal 2012 and 2011 respectively. As a percentage of sales, selling and administrative expenses amounted to 37.7% and 32.3% for fiscal 2012 and 2011 respectively.

In fiscal 2012, we continued intensifying our sales and marketing efforts, including additional employees, both domestically and internationally, and we incurred bad debt expenses compared to bad debt recovery in 2011; in addition, despite a lower sales volume year-over-year (7.3%), our commission expenses to our sales channels were almost flat compared to 2011 due to the shift in product and territory mix; this caused our expenses to increase as a percentage of sales year-over-year.

In addition, in fiscal 2012, we recorded $1.2 million, or 0.5% of sales, in restructuring charges in our selling and administrative expenses for the employees laid off as part of our restructuring plan in the fourth quarter of the year.

However, the increase in the average value of the US dollar in fiscal 2012 compared to the Canadian dollar and the euro year-over-year had a positive impact on our selling and administrative expenses, as a portion of these expenses are incurred in Canadian dollars and euros and we report our results in US dollars.

Outlook for fiscal 2013

For fiscal 2013, we expect our selling and administrative expenses to decrease as percentage of sales and range between 33% and 35% of sales. However, any increase in the strength of the Canadian dollar and the euro versus the US dollar would cause our selling and administrative expenses to increase, as a significant portion of these expenses are incurred in Canadian dollars and euros.

RESEARCH AND DEVELOPMENT EXPENSES

Gross research and development expenses

Gross research and development expenses totaled $59.3 million and $57.2 million for fiscal 2012 and 2011 respectively. As a percentage of sales, gross research and development expenses amounted to 23.7% and 21.2% for fiscal 2012 and 2011 respectively, while net research and development expenses accounted for 19.9% and 17.7% of sales for these respective years.

In fiscal 2012, we intensified our research and development activities, including additional headcounts, which resulted in increased gross research and development expenses compared to 2011. In addition, in fiscal 2012, the mix and calendar of research and development projects resulted in increased gross research and development expenses compared to 2011.

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In addition, in fiscal 2012, we recorded $884,000, or 0.4% of sales, in restructuring charges in our gross research and development expenses for the employees laid off as part of our restructuring plan implemented in the fourth quarter of the year.

However, the increase in the average value of the US dollar in fiscal 2012 compared to the Canadian dollar, the euro and the Indian rupee year-over-year had a positive impact on our gross research and development expenses, as most of these expenses are incurred in these currencies and we report our results in US dollars.

Tax credits and grants

We are entitled to tax credits from the Canadian federal and provincial governments for eligible research and development activities conducted in Canada. We are also eligible for grants by a Finnish technology organization on certain research and development projects conducted in Finland.

Tax credits and grants for research and development activities were $9.4 million and $9.3 million for fiscal 2012 and 2011 respectively. As a percentage of gross research and development expenses, tax credits reached 15.9% and 16.2% for fiscal 2012 and 2011 respectively.

Outlook for fiscal 2013

For fiscal 2013, we expect our net research and development expenses to decrease as percentage of sales and range between 16% and 18% of sales. However, any increase in the strength of the Canadian dollar, the euro and the Indian rupee versus the US dollar in the upcoming quarters would cause our net research and development expenses to increase, as most of these expenses are incurred in these currencies.

DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

In fiscal 2012, depreciation of property, plant and equipment amounted to $6.2 million, compared to $6.7 million in 2011.

The decrease in depreciation expense in fiscal 2012, compared to 2011, is due to the fact that some assets became fully depreciated as well as the increase in the average value of the US dollar versus the Canadian dollar, the euro and the Indian rupee year-over-year, as most of the depreciation expense is incurred in these currencies and we report our results in US dollars.

Outlook for fiscal 2013

For fiscal 2013, we expect our depreciation expense to slightly decrease compared to 2012.

AMORTIZATION OF INTANGIBLE ASSETS

In conjunction with the business combinations we completed over the past several years, we recorded intangible assets, primarily consisting of core technology and customer relationships. In addition, intangible assets include software. These intangible assets resulted in amortization expenses of $7.8 million and $9.2 million for fiscal 2012 and 2011 respectively.

The decrease in amortization expenses in fiscal 2012, compared to 2011, comes from the fact that core technologies related to the acquisition of Consultronics Limited became fully amortized in the second quarter of 2011. In addition, the increase in the average value of the US dollar compared to the Canadian dollar and the euro had to some extent, a positive impact on our amortization expense, as most of this expense is incurred in these currencies.

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CHANGES IN THE FAIR VALUE OF THE CASH CONTINGENT CONSIDERATION

In fiscal 2012, changes in the fair value of the cash contingent consideration amounted to $311,000, compared to $2.7 million in 2011.

Under the acquisition agreement of NetHawk Oyj, we have a cash contingent consideration of up to €8.7 million ($11.0 million) based on a sales volume of certain NetHawk products over a three-year period ending on December 2012. We record the cash contingent consideration payable at fair value in each balance sheet date based on actual and forecasted sales over the period of the contingent consideration. Changes in the fair value of the cash contingent consideration payable are recorded in the consolidated statements of earnings.

As at August 31, 2012, the fair value of the cash contingent consideration payable was estimated to nil based on actual and forecasted sales of certain NetHawk products over the period of the contingent consideration; the resulting change in the fair value during the year ended August 31, 2012, in the amount of $311,000 (€235,000), has been recorded in the consolidated statements of earnings for that year.

As at August 31, 2011, the fair value of the cash contingent consideration payable was estimated to $338,000 (€235,000), which resulted in a change in the fair value of $2.7 million, recorded in the statement of earnings in fiscal 2011.

INTEREST AND OTHER INCOME

Our interest income mainly resulted from our short-term investments, less interests and bank charges.

Interest and other income amounted to $131,000 in fiscal 2012 compared to $511,000 in 2011.

In fiscal 2011, we sold non-core capital assets for proceeds of $568,000, which resulted in a gain for the same amount recorded in the interest and other income line item in the statements of earnings for that year. Otherwise, interest and other income would have slightly increased in fiscal 2012 compared to 2011.

FOREIGN EXCHANGE GAIN (LOSS)

Foreign exchange gains and losses are mainly the result of the translation of operating activities denominated in currencies other than our functional currency, which is the Canadian dollar. A large portion of our foreign exchange gains or losses results from the translation of cash balances and deferred income taxes denominated in US dollars. We manage our exposure to currency risks in part with forward exchange contracts. In addition, some of our entities' operating activities are denominated in US dollars, euros or other currencies, which further hedges these risks. However, we remain exposed to currency risks and any increase in the value of the Canadian dollar, compared to the US dollar and the euro, would have a negative impact on our operating results.

We reported a foreign exchange loss of $657,000 in fiscal 2012, compared to $3.8 million in 2011.

In fiscal 2012, we witnessed some volatility in the value of the Canadian dollar as it fluctuated compared to the US dollar, which overall resulted in a foreign exchange loss of $657,000. In fact, the period-end value of the Canadian dollar slightly decreased 0.9% to CA$0.9863 = US$1.00 in fiscal 2012, compared to CA$0.9784 = US$1.00 in 2011, and the average value of the Canadian dollar compared to the US dollar

was CA$1.0094 = US$1.00.

In comparison, in fiscal 2011, the value of the Canadian dollar significantly increased versus the US dollar, compared to August 31, 2010, which resulted in a large foreign exchange loss of $3.8 million during the year. The period-end value of the Canadian dollar increased 9.0% versus the US dollar to CA$0.9784 = US$1.00 in fiscal 2011, compared to CA$1.0665 = US$1.00 in 2010.

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Foreign exchange rate fluctuations also flow through the P&L line items as a significant portion of cost of sales and our operating items are denominated in Canadian dollars, euros and Indian rupees, and we report our results in US dollars. Consequently, the increase in the average value of the US dollar in fiscal 2012, compared to these currencies year-over-year, resulted in a positive impact on our financial results. In fact, the average value of the US dollar in fiscal 2012 increased 2.0%, 6.2% and 12.3% respectively, compared to the Canadian dollar, the euro and the Indian rupee.

INCOME TAXES

We recorded income tax expenses of $3.6 million and $8.8 million in fiscal 2012 and 2011 respectively.

In fiscal 2012, we reported income tax expenses of $3.6 million on a loss before income taxes of $22,000. This situation mainly resulted from the fact that we did not recognize deferred income tax assets for some of our subsidiaries at loss and we had some non-deductible loss and expenses, such as stock-based compensation costs. However, in fiscal 2012, we recognized previously unrecognized deferred income tax assets of one of our subsidiaries, which resulted in a one-time income tax recovery of $557,000. In fact, in fiscal 2012, based on available positive and negative evidence, as well as on the level and the nature of cumulative and expected profits of one of our subsidiaries located in Asia, we concluded that it was probable that deferred income tax assets of that subsidiary (mainly operating losses carried forward) would be realizable. Otherwise, the actual tax rate would have been closer to the combined Canadian and provincial statutory tax rate of 27% in fiscal 2012.

In fiscal 2011, we reported an income tax expense of $8.8 million on earnings before income taxes of $18.0 million, for an effective income tax rate of 48.9%. Our combined Canadian and provincial statutory tax rate was 29%. This situation mainly resulted from the fact that a significant portion of our foreign exchange loss was created by the translation of financial statements of our foreign operations, and was therefore non-deductible. In addition, we did not recognize deferred income tax assets for some of our subsidiaries at loss and we had some non-deductible expenses, such as stock-based compensation costs. However, the changes in the fair value of the cash consideration, which resulted in a gain of $2.7 million, were non-taxable. Otherwise, the actual tax rate would have been closer to the statutory tax rate.

Please refer to note 22 to our consolidated financial statements for a full reconciliation of our income tax provision.

RESULTS OF DISCONTINUED OPERATIONS (formerly the Life Sciences and Industrial Division)

On October 1, 2010, we completed the sale of our Life Sciences and Industrial Division and that Division contributed one month to our results of the first quarter of fiscal 2011. Results from operations for that Division for the first quarter of fiscal 2011 were included in net earnings from discontinued operations along with the gain on the sale of the Division.

SALES

In fiscal 2011, sales of the discontinued operations (one-month contribution) amounted to $2.0 million.

NET EARNINGS

In fiscal 2011, we reported net earnings from discontinued operations of $12.9 million, which included a gain on disposal of discontinued operations of $13.2 million and $264,000 in stock-based compensation costs.

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LIQUIDITY AND CAPITAL RESOURCES

Cash requirements and capital resources (from continuing operations)

As at August 31, 2012, cash and short-term investments totaled $67.1 million, while our working capital was at $117.7 million. Our cash and short-term investments decreased $2.8 million in fiscal 2012, compared to 2011. In fiscal 2012, we made cash payments of $23.8 million for the purchase of capital assets, mainly for our new building in Montreal, Canada, $2.2 million for the redemption of share capital under our share repurchase program and $1.4 million for the repayment of our bank loan and long-term debt. In addition, we recorded an unrealized foreign exchange loss on our cash and short-term investments of $836,000. This unrealized foreign exchange loss resulted from the translation, in US dollars, of our Canadian-dollar-denominated cash and short-term investments and was included in the accumulated other comprehensive income in the balance sheet. However, operating activities generated $25.3 million in cash.

Our short-term investments consist of banker acceptances issued by high-credit quality corporations; therefore, we consider the risk of non-performance of these financial instruments to be limited. These debt instruments are not expected to be affected by a significant liquidity risk. For the purpose of managing our cash position, we have established a cash management policy, which we follow and monitor on a regular basis. Our cash and short-term investments will be used for working capital and other general corporate purposes, potential acquisitions as well as our share repurchase program. As at August 31, 2012, cash balances included an amount of $36.2 million that bears interest at a rate of 1.3%.

We believe that our cash balances and short-term investments will be sufficient to meet our liquidity and capital requirements for the foreseeable future, including the effect of our normal course issuer bid. In addition to these assets, we have unused available lines of credit totaling $15.8 million for working capital and other general corporate purposes and unused lines of credit of $26.3 million for foreign currency exposure related to forward exchange contracts. However, possible operating losses, additional restructuring costs and/or possible investments in or acquisitions of complementary businesses, products or technologies may require additional financing. There can be no assurance that additional debt or equity financing will be available when required or, if available, that it can be secured on satisfactory terms.

As at August 31, 2012, our commitments under operating leases amount to $3.6 million in 2013, $1.9 million in 2014, $1.3 million in 2015, $0.9 million in 2016 and $1.3 million in 2017 and after, for total commitments of $9.0 million.

Sources and uses of cash

We finance our operations and meet our capital expenditure requirements mainly through cash flows from operating activities, the use of our cash and short-term investments as well as the issuance of subordinate voting shares.

Operating activities (including discontinued operations)

Cash flows provided by operating activities were $25.3 million in fiscal 2012, compared to $23.3 million in 2011.

Cash flows provided by operating activities in fiscal 2012 were mainly attributable to the net earnings after items not affecting cash of $12.0 million and the positive net change in non-cash operating items of $13.3 million; this was mainly due to the positive effect on cash of the decrease of $8.0 million in our accounts receivable, due to the decrease in sales year-over-year and the timing of sales within the year, the decrease of $10.9 million in our inventories due the decrease in sales year-over-year and an improved inventory turn, as well as the increase

of $538,000 in our accounts payable, accrued liabilities, provisions and other liabilities due to timing of purchases and payments during the year. These positive effects on cash were offset in part by the negative effect of the increase of $5.6 million in our income taxes and tax credits recoverable due to tax credits earned during the period not yet recovered and the increase of $589,000 in our prepaid expenses due to the timing of payments during the year.

Investing activities (including discontinued operations)

Cash flows provided by investing activities amounted to $13.1 million in fiscal 2012, compared to cash flows used of $25.3 million in 2011.

In fiscal 2012, we disposed (net of acquisitions) of $36.9 million worth of short-term investments, but we paid $23.8 million for the purchase of capital assets, mainly for our new building in Montreal, Canada.

Financing activities (including discontinued operations)

Cash flows used by financing activities amounted to $3.3 million in fiscal 2012, compared to cash flows provided of $1.6 million in 2011.

In fiscal 2012, we reimbursed our bank loan of $782,000, we made a repayment of $577,000 of our long-term debt, and we redeemed share capital for a cash consideration of $2.2 million. However, we received $310,000 from the exercise of stock options.

FORWARD EXCHANGE CONTRACTS

We utilize forward exchange contracts to manage our foreign currency exposure. Our policy is not to utilize those derivative financial instruments for trading or speculative purposes.

Our forward exchange contracts, which are used to hedge anticipated US-dollar-denominated sales, qualify for hedge accounting; therefore, realized foreign exchange translation gains and losses on these contracts are recognized as an adjustment of the revenues when the corresponding sales are recorded.

As at August 31, 2012, we held forward exchange contracts to sell US dollars at various forward rates, which are summarized as follows:

Expiry dates		Contractual amounts	Weighted average contractual forward rates
September 2012 to August 2013	$	23,000,000	1.0228
September 2013 to August 2014		3,600,000	1.0439
Total	$	26,600,000	1.0256

The carrying amount of forward exchange contracts is equal to fair value, which is based on the amount at which they could be settled based on estimated current market rates. The fair value of forward exchange contracts amounted to net gains of $2.3 million as at August 31, 2011, and $932,000 as at August 31, 2012. The year-end exchange rate was CA$0.9863 = US$1.00 as at August 31, 2012.

CONTINGENCY

On November 27, 2001, a class action suit was filed in the United States District Court for the Southern District of New York against the company, four of the underwriters of its Initial Public Offering and some of its executive officers pursuant to the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder and Sections 11, 12

and 16 of the Securities Act of 1933. This class action alleges that the company's registration statement and prospectus filed with the Securities and Exchange Commission on June 29, 2000, contained material misrepresentations and/or omissions resulting from (i) the underwriters allegedly soliciting and receiving additional, excessive and undisclosed commissions from certain investors in exchange for which they allocated material portions of the shares issued in connection with the company's Initial Public Offering; and (ii) the underwriters allegedly entering into agreements with customers whereby shares issued in connection with the company's Initial Public Offering would be allocated to those customers in exchange for which customers agreed to purchase additional amounts of shares in the after-market at predetermined prices.

On April 2, 2009, a stipulation and agreement of settlement between the plaintiffs, issuer defendants and underwriter defendants was submitted to the Court for preliminary approval. The Court granted the plaintiffs' motion for preliminary approval and preliminarily certified the settlement classes on June 10, 2009. The settlement fairness hearing was held on September 10, 2009. On October 6, 2009, the Court entered an opinion granting final approval to the settlement and directing that the Clerk of the Court close these actions. Appeals of the opinion granting final approval were filed, all of which have been dismissed or settled as of January 9, 2012. The settlement payment on behalf of EXFO has been made by the insurers, the settlement among the parties is final, and the case is concluded.

SHARE CAPITAL

Share capital

As at November 7, 2012, EXFO had 31,643,000 multiple voting shares outstanding, entitling to 10 votes each and 28,772,915 subordinate voting shares outstanding. The multiple voting shares and the subordinate voting shares are unlimited as to number and without par value.

OFF-BALANCE SHEET ARRANGEMENTS

As at August 31, 2012, our off-balance sheet arrangements consisted of letters of guarantee amounting to $5.4 million; these letters of guarantee expire at various dates through fiscal 2017. From this amount, we had $1.0 million worth of letters of guarantee for our own selling and purchasing requirements, which were for the most part reserved from one of our lines of credit. The remainder, in the amount of $4.4 million, was used to secure our line of credit in CNY (Chinese currency) of $4.0 million plus any accrued interests. This line of credit was unused as at August 31, 2012.

SPECIAL PURPOSE ENTITIES

As at August 31, 2012, we did not have interests in any special purpose entities.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our consolidated financial statements have been prepared in accordance with IFRS 1, "First-Time Adoption of International Financial Reporting Standards (IFRS)". Note 2 to our consolidated financial statements for the year ended August 31, 2012 details accounting policies that we adopted under IFRS. In addition, note 3 to our consolidated financial statements for fiscal 2012 discloses the impact of the transition to IFRS on our reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in our consolidated financial statements for the year ended August 31, 2011, under Canadian GAAP (previous GAAP).

Upon the transition to IFRS on September 1, 2010, we initially elected to discount the carrying value of our long-term tax credits; this initial election resulted in a decrease of our long-term tax credits of $2.5 million and an increase in deferred tax assets of $678,000 as at September 1, 2010, with a corresponding net decrease of $1.8 million in the opening balance of retained earnings. It also resulted in a decrease of $2.5 million in our long-term tax credits, an increase in deferred tax assets of $401,000, a decrease in deferred tax liabilities of 276,000 as at August 31, 2011, as

well as interest income of $227,000 and a related deferred income tax expense of $61,000 for fiscal 2011.

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In the fourth quarter of fiscal 2012, prior to issuing our first annual consolidated financial statements under IFRS, we changed our initial choice of accounting policy for measuring our long-term, non-refundable research and development tax credits and finally opted not to discount these tax credits; we retroactively applied this change in accounting policy at the transition date. Consequently, the carrying value of the previously disclosed long-term tax credits, deferred income tax assets and liabilities, and retained earnings as at September 1, 2010 and August 31, 2011, have been adjusted to reflect this change in accounting policy and the reconciliations from Canadian GAAP to IFRS in the following sections have been adjusted accordingly.

The preparation of financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses and the disclosures of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, we evaluate these estimates and assumptions, including those related to the fair value of financial instruments, the allowance for doubtful accounts receivable, the amount of tax credits recoverable, the provision for excess and obsolete inventories, the estimated useful lives of capital assets, the valuation of long-lived assets, the impairment of goodwill, the recoverable amount of deferred income tax assets, the amount of certain accrued liabilities, provisions and deferred revenue as well as stock-based compensation costs. We base our estimates and assumptions on historical experience and on other factors that we believe to be reasonable under the circumstances, the result of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates and assumptions.

The following summarizes our critical accounting policies as well as other policies that require the most significant judgment and estimates in the preparation of our consolidated financial statements.

(a) Inventories

We state our inventories at the lower of cost, determined on an average cost basis and net realizable value, and we provide reserves for excess and obsolete inventories. We determine our reserves for excess and obsolete inventories based on the quantities on hand at the reporting dates compared to foreseeable needs over the next twelve months, taking into account changes in demand, technology or market. It is possible that additional inventory reserves may occur if future sales are less than our forecasts or if there is a significant shift in product mix compared to our forecasts, which could adversely affect our future results.

(b) Income taxes

We are subject to income tax laws and regulations in several jurisdictions. Under these laws and regulations, uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. We maintain provisions for uncertain tax positions that we believe appropriately reflect our risk based on our interpretation of laws and regulations. In addition, we make reasonable estimates and assumptions to determine the amount of deferred tax assets that can be recognized in our consolidated financial statements, based upon the likely timing and level of anticipated future taxable income together with tax planning strategies. The ultimate realization of our deferred income tax assets is dependent upon the generation of sufficient future taxable income during the periods in which those assets are expected to be realized.

As at August 31, 2012, non-refundable research and development tax credits recognized in the balance sheet amounted to $41.5 million. In order to realize these non-refundable research and development tax credits, we need to generate approximately $270 million (CA$267 million) in pre-tax earnings at the Canadian federal level and approximately $11 million at the Canadian provincial level. In addition, as at August 31, 2012, we had deferred income tax assets in the balance sheet in amount of $12.1 million mainly in United States. In order to realize these

deferred income tax assets, we need to generate $30 million at the United States level.

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(c) Impairment of non-financial assets

Impairment exists when the carrying value of an asset or group of assets (cash generating unit (CGU)) exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction, available data from observable active market prices less incremental costs for disposing of the asset, or data from recent transactions of similar assets, within the same industry, when available. When such information is not available, or to supplement this information, we use discounted cash flows. The establishment of discounted cash flows requires the use of estimates, including management's expectations of future revenue growth, operating costs and profit margins as well as discount rates for each CGU.

i) Growth rates

The assumptions used are based on historical growth, our internal budget, expectations of future revenue growth as well as industry and market trends. We projected revenues, operating margins and cash flows for periods of five years, and we applied a perpetual growth rate thereafter.

ii) Discount rate

We used a discount rate to calculate the present value of estimated future cash flows, which represents our weighted average cost of capital (WACC).

Prior to fiscal 2012, we performed our annual goodwill impairment test in the third quarter of each fiscal year. In fiscal 2012, we changed the timing of our annual goodwill impairment for the fourth quarter to align the test with the year end and budget process. Consequently, in fiscal 2012, we performed our impairment test in the third quarter and the fourth quarter.

In the fourth quarter of fiscal 2012, we performed our annual goodwill impairment test for our two CGUs, using a combination of a market-based approach (sales multiples), based on recent relevant transactions in our industry, and discounted cash flows.

The sales multiple of recent relevant transactions ranged between 1.2 and 4 times sales.

For the discounted cash-flow calculations, we used a five-year sales compound annual growth rate (CAGR) of 20% for the NetHawk CGU, a five-year sales CAGR of 25% for the Brix CGU and a perpetual growth rate of 2%. For both CGUs, we used a discount rate of 18%.

Based on the market approach and the discounted cash-flow calculations, the recoverable amount for both CGUs exceeded their carrying value.

As at August 31, 2012, the carrying value of goodwill totaled $29.2 million and was allocated as follows to two CGUs:

NetHawk CGU	$11,520,000
Brix CGU	17,640,000
Total	$29,160,000

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NEW IFRS PRONOUNCEMENTS AND AMENDMENTS ISSUED BUT NOT YET ADOPTED

Financial Instruments

IFRS 7, “Financial Instruments: Disclosures”, has been amended to enhance disclosure requirements related to offsetting of financial assets and liabilities. The amendments are applicable retrospectively for annual periods beginning on or after January 1, 2013. We will adopt these amendments on September 1, 2013 and expect their adoption to have no significant impact on our consolidated financial statements.

IFRS 9, “Financial Instruments”, was issued in November 2009 and addresses classification and measurement of financial assets. It replaces the multiple category and measurement models in IAS 39, “Financial Instruments – Recognition and Measurement”, for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments. Such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where equity instruments are measured at fair value through other comprehensive income, dividends are recognized in profit or loss to the extent that they do not clearly represent a return on investment; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income indefinitely. Requirements for financial liabilities were added to IFRS 9 in October 2010, and they largely carried forward existing requirements in IAS 39, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss are generally recorded in other comprehensive income. This standard is effective for annual periods beginning on or after January 1, 2015. We have not yet assessed the impact that this new standard is likely to have on our consolidated financial statements.

Financial Statement Presentation

In June 2011, the IASB amended IAS 1, “Financial Statement Presentation”. The amendments to IAS 1 require entities to separate items presented in other comprehensive income into two groups, based on whether or not they may be recycled to the statement of earnings in the future. Items that will not be recycled will be presented separately from items that may be recycled in the future, such as unrealized gains and losses on cash-flow hedges. The amendment is effective for annual periods beginning on or after July 1, 2012. Early adoption is permitted and full retrospective application is required. We do not expect the standard to have a significant impact on our consolidated financial statements.

The IASB issued the following standards: IFRS 10, “Consolidated Financial Statements”, IFRS 11, “Joint Arrangements”, IFRS 12, “Disclosure of Interests in Other Entities”, and IFRS 13, “Fair Value Measurement”. Each of the new standards is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. We have not yet assessed the impact that the new and amended standards may have on our consolidated financial statements or whether or not to early adopt any of these new requirements.

The following is a brief summary of these new standards:

Consolidation

IFRS 10, “Consolidated Financial Statements”, requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when a company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces Standing Interpretations Committee (“SIC”) 12, “Consolidation – Special Purpose Entities” and parts of IAS 27, “Consolidated and

Separate Financial Statements".

Joint Arrangements

IFRS 11, "Joint Arrangements", requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operations. Joint ventures will be accounted for using the equity method of accounting, whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenues and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity-account for interests in joint ventures. IFRS 11 replaces IAS 31, "Interests in Joint Ventures", and SIC 13, "Jointly Controlled Entities – Non-Monetary Contributions by Venturers".

Disclosure of Interests in Other Entities

IFRS 12, "Disclosure of Interests in Other Entities", establishes disclosure requirements for interests in other entities, such as subsidiaries, joint arrangements, associates and structured entities. This standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

Fair Value Measurement

IFRS 13, "Fair Value Measurement", is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and, in many cases, does not reflect a clear measurement basis or consistent disclosures.

NON-IFRS FINANCIAL MEASURES

We provide non-IFRS financial measures (gross margin*, EBITDA** and adjusted EBITDA**) as supplemental information regarding our operational performance. We use these measures for the purposes of evaluating our historical and prospective financial performance, as well as our performance relative to our competitors. These measures also help us to plan and forecast future periods as well as to make operational and strategic decisions. We believe that providing this information to our investors, in addition to the IFRS measures, allows them to see the company's results through the eyes of management, and to better understand our historical and future financial performance.

The presentation of this additional information is not prepared in accordance with IFRS. Therefore, the information may not necessarily be comparable to that of other companies and should be considered as a supplement to, not a substitute for, the corresponding measures calculated in accordance with IFRS.

* Gross margin represents sales less cost of sales, excluding depreciation and amortization.

** EBITDA is defined as net earnings (loss) before interest, income taxes, depreciation of property, plant and equipment and amortization of intangible assets. Adjusted EBITDA represents EBITDA excluding changes in the fair value of the cash contingent consideration and the gain from the disposal of discontinued operations.

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The following tables summarize the reconciliation of EBITDA and adjusted EBITDA to IFRS net earnings (loss) and additional information, in thousands of US dollars:

EBITDA and adjusted EBITDA (including discontinued operations)

	Year ended August 31, 2012	Year ended August 31, 2011
IFRS net earnings (loss) for the year	$ (3,593)	$ 22,120
Add (deduct):		
Depreciation of property, plant and equipment		
Continuing operations	6,169	6,655
Discontinued operations	–	14
Amortization of intangible assets		
Continuing operations	7,819	9,183
Discontinued operations	–	4
Interest and other income (continuing operations)	(131)	(511)
Income taxes		
Continuing operations	3,571	8,814
Discontinued operations	–	201
EBITDA for the year	13,835	46,480
Changes in fair value of cash contingent consideration	(311)	(2,685)
Gain on disposal of discontinued operations	–	(13,212)
Adjusted EBITDA for the year	$ 13,524	$ 30,583
EBITDA in percentage of total sales	5.5 %	17.1 %
Adjusted EBITDA in percentage of total sales	5.4 %	11.3 %

Additional information

	Year ended August 31, 2012	Year ended August 31, 2011
Sales from continued operations	$ 249,966	$ 269,743
Sales from discontinued operations	–	1,991
Total sales	$ 249,966	$ 271,734

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Item 6. Directors, Senior Management and Employees

A. Directors and Senior Management

The following table sets forth information about our executive officers, senior managers and Directors as of November 1, 2012.

Name and Municipality of Residence	Positions with EXFO
PIERRE-PAUL ALLARD Pleasanton, California	Independent Director
JON BRADLEY Worminghall, United Kingdom	Vice-President, Sales — EMEA
STEPHEN BULL Quebec City, Quebec	Vice-President, Research and Development
DARRYL EDWARDS Weston Under Wetherley, United Kingdom	Independent Director
ÉTIENNE GAGNON Quebec City, Quebec	Vice-President, Test and Measurement Division
LUC GAGNON St-Augustin-de-Desmaures, Quebec	Vice-President, Manufacturing Operations and Customer Service
GERMAIN LAMONDE St-Augustin-de-Desmaures, Quebec	Chairman of the Board, President and Chief Executive Officer
PIERRE MARCOUILLER Magog, Quebec	Independent Lead Director
GUY MARIER Lakefield Gore, Quebec	Independent Director
CLAUDIO MAZZUCA LaSalle, Quebec	Vice-President, Systems and Service Assurance Division
PIERRE PLAMONDON Quebec City, Quebec	Vice-President, Finance and Chief Financial Officer
BENOIT RINGUETTE Boischatel, Quebec	General Counsel and Corporate Secretary
SYLVAIN ROULEAU Kirkland, Quebec	Vice-President, Human Capital

JOSEPH SOO Singapore	Vice-President, Sales — Asia-Pacific
SUSAN SPRADLEY Dallas, Texas	Independent Director
DANA YEARIAN Lake Forest, Illinois	Vice-President, Sales — Americas

The address of each of our executive officers, senior managers and Directors is c/o EXFO Inc., 400 Godin Avenue, Quebec, Quebec, Canada, G1M 2K2. The following is a brief biography of each of our executive officers, senior managers and Directors.

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Pierre-Paul Allard was appointed a member of our Board of Directors in September 2008 and has been a board member of many other technology companies in Canada and in the US. Mr. Allard is Senior Vice-President, Corporate Strategy and Development at Avaya Inc., a global provider of business collaboration and communications solutions. As Chief Strategy Officer, Mr. Allard is responsible for all go-to-market strategy at Avaya, as well as leading Avaya's mergers and acquisitions (M&A), marketing, analyst relations and strategic alliance initiatives on a global basis. Prior to joining Avaya in May 2012, Mr. Allard worked for 19 years at Cisco Systems, Inc., where he most recently held the position of Vice-President, Sales and Operations, Global Enterprise. Previously, Mr. Allard was President of Cisco Systems Canada, and before that he held various management roles at IBM Canada for 12 years. In 2002, Mr. Allard co-chaired the Canadian e-Business Initiative, a private-public partnership aiming to measure the role e-business plays in increasing productivity levels, job creation and competitive position. In 1998, he was the laureate of the Arista-Sunlife Award, for Top Young Entrepreneur in Large Enterprise, by the Montreal Chamber of Commerce. In 2003, he received the Queen's Golden Jubilee Medal, which highlights significant contributions to Canada. In the same year, he was also awarded the prestigious Trudeau Medal from the University of Ottawa's Telfer School of Management. Pierre-Paul Allard holds a bachelor's and master's degree in Business Administration from the University of Ottawa, in Canada.

Jon Bradley was appointed Vice-President, Sales, EMEA for EXFO in June 2010. He is responsible for managing telecom sales, both direct and indirect, and for the execution of sales strategies in the international arena. He manages an accomplished and diverse sales and distribution team. As a member of the Strategy and Management Committees, he also develops corporate strategy for EXFO. Prior to his appointment as Vice-President, Sales, EMEA, Dr. Bradley held the positions of Vice-President, International Sales, from 2007-2010, Sales Director for the Europe, Middle East and Africa (EMEA) territory from 2003 to 2007, and Regional Sales Manager from 1999 to 2003. Before joining EXFO in 1999, Dr. Bradley was employed as Sales and Marketing Director by Queensgate Instruments (UK) from 1997 to 1999 and as Sales Engineer by Lambda Photometrics (UK) from September 1993 to September 1997. Jon Bradley holds an honors degree in chemistry, as well as a Ph.D. in Raman spectroscopy from the University of Durham in the United Kingdom.

Stephen Bull joined EXFO in 1995 as an Engineering Manager (project management) for the Advanced Optics group. From September 1997 to December 1999, he held the position of Assistant Director of Engineering responsible for all the software development. Mr. Bull was then appointed EXFO's Vice-President of Research and Development in December 1999. Today, he manages a department that includes more than 760 engineers and technicians spread out over three continents and nine locations. He is responsible for EXFO's product development initiatives and manages the Project Management Office and related processes. Prior to joining EXFO, Mr. Bull was General Manager and Managing Director of Space Research Corporation, a military engineering company in Belgium, from June 1986 to March 1990, as well as of Taurus, an IT consulting firm, from 1990 to 1995. He is currently the President of the Institut de développement de produits (an institute dedicated to the advancement of product development practices) and a member of the Product Development Management Association (PDMA). He speaks regularly at conferences on product development. Stephen Bull holds a bachelor's degree in electrical engineering from Université Laval in Quebec City, and is a certified New Product Development Professional from the PDMA.

Darryl Edwards was appointed a member of EXFO’s Board of Directors in September 2011. Mr. Edwards is the President and CEO of ECI Telecom, a leading provider of access and transport network solutions. Prior to this, Mr. Edwards was the Chairman of the Board for MACH, a leading provider of hub-based mobile communication solutions. He was also an advisor to private equity firm Warburg Pincus, the majority shareholder in MACH, on telecommunications-related topics. He brings to EXFO more than 30 years of telecommunications experience gained from a number of senior executive leadership positions; most recently he was the Chief Executive Officer of AIRCOM International, successfully leading the company through to business sale. Mr. Edwards was previously at Nortel Networks for 17 years, where he held various executive officer positions, including President of EMEA and

President of Global Sales (Carrier Networks). He also was the Chief Executive Officer for two of Nortel's key joint ventures, first in the Middle East and later in Germany. Prior to his time at Nortel, Mr. Edwards spent 13 years at GEC-Plessey Telecommunications where he worked in engineering, quality assurance and international sales. Mr. Edwards has held a number of chairs, including Chairman of the Board of Nortel's interests in Turkey, Nortel Netas, which was listed on the Istanbul Stock Exchange. He also was a member of the Advisory Counsel to the Turkish government between 2004 and 2008, and previously served on the UK Government Broadband Stakeholders Group and the Information Age Partnership. Darryl Edwards holds a Higher National Certificate (Physics) from Birmingham Polytechnic in the UK.

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Étienne Gagnon was appointed Vice-President, Test and Measurement Division in June 2010. He is responsible for EXFO's wireline and wireless test and measurement business units (Optical, Transport and Datacom, Access, Simulators and Analyzers) and Corporate Marketing (CTO Office and Marketing-Communications). In May 2003, he had been named EXFO's Vice-President, Optical Business Unit and Customer Service, and in May 2007, he had taken on the responsibility of all of EXFO's telecom business units (Optical, Transport and Datacom, Navtel Product Group, Access). Mr. Gagnon began his career as a design engineer for Bombardier/Canadair, where he worked on the Canadian Regional Jet project between 1990 and 1993. Later, he held the position of Business Development Manager for France Telecom in Hungary. In 1994, he joined EXFO's European office as a Regional Sales Manager, and in 1996, he was brought back to Quebec City to head the OSP marketing group. Mr. Gagnon then went on to become the director of EXFO's Outside Plant division in 1998, and remained in that function until 2000, when he joined TeraXion, an optical component manufacturer based in Quebec City, as Vice-President of Sales and Marketing until returning to EXFO in early 2003. Étienne Gagnon holds a bachelor's degree in mechanical engineering from the University of Montreal's School of Engineering, and a master's degree in European business from the École nationale supérieure des télécommunications in France.

Luc Gagnon was appointed Vice-President, Manufacturing Operations in May 2003 and, in May 2007, he also took on the vice-presidency of the Customer Service department. He is responsible for ensuring the smooth operation of all manufacturing activities, which include production, purchasing, product engineering, quality assurance, planning, manufacturing engineering, product configuration, transportation and customs, as well as material resources. In addition, he must ensure that there is an ongoing and efficient relation between the manufacturing process and the end customer. Prior to his nomination in 2003, Mr. Gagnon held the position of Production Director since 2000. Before joining EXFO, he had similar roles in several other high-technology companies. He worked for Mendes from 1999 to 2000, for C-MAC from 1997 to 1999, for STERIS from 1993 to 1997 and for MITEL from 1985 to 1993. Luc Gagnon holds a bachelor's degree in electrical engineering and master's degree in engineering, both from the Université de Sherbrooke, in Canada.

Germain Lamonde, a company founder, has been President and Chief Executive Officer of EXFO since its inception in 1985. He has also been Chairman of the Board since EXFO went public in 2000. Responsible for the overall management and strategic direction of EXFO, Mr. Lamonde has grown the company from the ground up into a global leader in the test and measurement and systems and service assurance industry. Mr. Lamonde has served on the board of directors of several organizations such as the Canadian Institute for Photonic Innovations, the POLE QCA Economic Development Corporation, the National Optics Institute of Canada (INO) and Laval University, to name a few. Germain Lamonde holds a bachelor's degree in physics engineering from the University of Montreal's School of Engineering (École Polytechnique), a master's degree in optics from Université Laval in Quebec City, and is also a graduate of the Ivey Executive Management Program offered by the University of Western Ontario.

Pierre Marcouiller has served as our Director since May 2000. Mr. Marcouiller is Chairman of the Board and CEO of Camoplast Solideal, a world leader in the design, manufacturing and distribution of off-road tires, rubber tracks, undercarriage systems and wheels, as well as a North-American leader in under-the-hood plastic components and assemblies for the automotive industry. Prior to joining Camoplast Solideal, Mr. Marcouiller was President and General Manager of Venmar Ventilation Inc. (1988-1996), where he was the controlling shareholder from 1991 to 1996. He is also a Director of Canam Group Inc., an industrial company specialized in the design and fabrication of construction products and solutions in the commercial, industrial, institutional, residential, and bridge and highway infrastructure markets. Mr. Marcouiller also holds directorships in other privately held companies. Pierre Marcouiller holds a bachelor's degree in business administration from Université du Québec à Trois-Rivières and an MBA from Université de Sherbrooke.

Guy Marier has served as our Director since January 2004. President of Bell Québec between 1999 and 2003, Mr. Marier completed his successful 33-year career at Bell as Executive Vice-President of the Project Management Office, before retiring at the end of 2003. From 1988 to 1990, Mr. Marier headed Bell Canada International's investments and projects in Saudi Arabia and, for the three following years, served as President of Télébec, limited partnership, a member of the Bell group of companies. He then returned to the parent company to hold various senior management positions. Guy Marier holds a Bachelor of Arts from the University of Montreal and a Bachelor of Business Administration from Université du Québec à Montréal.

Claudio Mazzuca was appointed Vice-President, Systems and Service Assurance Division in March 2012. Prior to this appointment, he held the role of Director of EXFO's Transport and Datacom business unit since 2006. In this role, he was responsible for the development and execution of business and product strategy for this business unit, which now is a leading player in the Ethernet and next-generation packet transport test market segments. Mr. Mazzuca began his career as a systems engineer for Nortel Networks, where he worked on the launch of the highly successful 10G High-Speed Transport and DWDM product line, and later on Nortel's Preside Network Management solution. He then moved to technology startup Hyperchip Systems as Senior Product Manager, focusing on the development of large-scale metro and core IP routers and switches, and associated OEM components. In 2004, he joined EXFO's Transport and Datacom business unit as Product Line Manager for the next-generation SONET/SDH products, and in 2005, was promoted to Group Manager for the entire Transport and Datacom product line. Claudio Mazzuca holds a bachelor's degree in electrical engineering from Concordia University and a master's degree in business from McGill University in Montreal.

Pierre Plamondon was appointed Vice-President, Finance and Chief Financial Officer (CFO) of EXFO in January 1996. He is responsible for accounting, financial reporting, legal services, investor relations and information technology services. Prior to joining EXFO, Mr. Plamondon served as Senior Manager for Price Waterhouse, now PricewaterhouseCoopers LLP, from September 1981 to December 1995, in Canada and France. Pierre Plamondon holds a bachelor's degree in business administration and a license in accounting, both from Université Laval in Quebec City. Mr. Plamondon has been a member of the Canadian Institute of Chartered Accountants since 1983. He is currently a director of Urbanimmersive Inc., a public company listed on the TSX Venture Exchange Inc. and has been a member of the Board of Directors of SOVAR Inc. (Société de valorisation des applications de la recherche de l'Université Laval) from 2000 to 2011. Over the years, he also served on the Board of Directors of several non-profit organizations, and is currently a Board member for the Fondation de l'Université Laval.

Benoit Ringuette has been our in-house Legal Counsel and Corporate Secretary since April 2004. Prior to joining EXFO, Mr. Ringuette practiced mainly in commercial, corporate and securities law from 1998 to 2003 as an associate in the law firms of O'Brien, Flynn Rivard in Quebec City and Desjardins Ducharme Stein Monast in Quebec City. Mr. Ringuette has been a member of the Quebec Bar since 1998. Mr. Ringuette holds a bachelor's degree in Civil Law and a master's degree in Business Administration (MBA) from Laval University in Quebec City, Canada.

Sylvain Rouleau was appointed Vice-President, Human Capital at EXFO in January 2012. As such, his main responsibility is overseeing the human resources department, and, more specifically, his mandate is to transform EXFO into an organization that optimizes its human capital and, in turn, surpasses its objectives. Mr. Rouleau has over 25 years' experience in human resources and has held several executive positions in a variety of international organizations. Namely, before joining EXFO, he was Senior Vice-President, Human Capital at Kruger since February 2009. From 2003 to 2009, he worked for the Alcan Group   Bauxite & Alumina as Vice-President, Human Resources, Communications and Corporate Affairs. Prior to that, he managed human resources teams for Nortel Networks as well as several divisions of the General Electric Company, such as GE Power Systems, GE Medical Systems and GE Aircraft Engines, both in Canada and abroad. Mr. Rouleau's international perspective and his proven expertise as a business partner and as a change agent serve as a reference in human resources management. Sylvain Rouleau holds a master's degree in organizational psychology (O.D. and Complex Systems) from the Université de Sherbrooke in Canada, and he has given several conferences on leading-edge organizations.

Joseph Soo was appointed EXFO's Vice-President of Asia Sales in December 2011. He is responsible for managing telecom sales, both direct and indirect, and for the execution of sales strategies in the Asian market. As a member of the Strategy and Management Committees, he also develops corporate strategy for EXFO. Mr. Soo has extensive market knowledge and sales experience in the telecom industry, as he has been leading Asia Pacific sales teams for major test and measurement providers for the last 15 years. Namely, he was Vice-President of Asia Pacific Sales at

Fluke Networks from 2010 to 2011. Prior to that, he was Executive Vice-President of Rohde & Schwarz Asia Pacific Regional, where he held various management and sales positions at different Rohde & Schwarz locations since he began there in 1997. Earlier on, Mr. Soo began his career as a Senior EMC Engineer at Astec Power Pte Ltd in 1990. Joseph Soo is fluent in English and Chinese and has lived both in Asia and the US. He holds a Bachelor of Science degree from the University of Minnesota Twin Cities and has attended several executive MBA courses at the Singapore Institute of Management.

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Susan Spradley was appointed to EXFO's Board of Directors in October 2011. Ms. Spradley is Executive Director of US Ignite, a public-private partnership. She brings to EXFO more than 20 years of experience in the wireless telecommunications industry in which she has held senior executive positions in sales, product line management, operations, services and customer support. Most recently she was Head of the North American Region at Nokia Siemens Networks and also a member of the company's Executive Board. Prior to joining Nokia Siemens Networks, Ms. Spradley held prominent leadership roles at Nortel Networks including President of Global Services and Operations, President of Global Product Line Management and North American Sales, and Vice-President of Customer Service and Operations. She also served as Vice-President of Marketing and Product Development for North America at Siemens Communications. In addition, she previously was a member of the National Security Telecommunications Advisory Committee reporting to the President of the United States.Susan Spradley holds a bachelor's degree in Computer Science from the University of Kansas and completed the Advanced Management Program at Harvard University Business School.

Dana Yearian was appointed EXFO's Vice-President, Sales, Americas in March 2007. Prior to this appointment, Mr. Yearian held the position of Vice-President, Telecom Sales, North America. He is responsible for managing telecom sales, both direct and indirect, and the execution of sales strategies across North, Central and South America. Mr. Yearian oversees all sales-related functions for the EXFO sales organization throughout this territory, including sales operations, global account management and partner programs. As a member of the Strategy and Management committees, he also helps develop corporate strategy. From 2005 to 2006, Mr. Yearian held senior executive sales positions at Spirent Communications Service Assurance Division. In 2003, Mr. Yearian founded The Katrixx Group, which provided consulting and contracting services to high-technology companies. Before founding his company, Mr. Yearian worked as Vice-President of Sales at Acterna Corp. (from 1991 to 2003), where he led both North American and International sales and support operations. Prior to working for Acterna, Mr. Yearian held various executive positions, namely at Toshiba America, Silicon Sensors (Advanced Photonix, Inc.) and Impell Corporation (ABB Ltd.). Dana Yearian holds a bachelor's degree in electrical engineering from the Illinois Institute of Technology in Chicago, and has completed MBA course work at DePaul University, also in Chicago, Illinois, USA.

Term of Executive Officers

Executive officers are appointed annually by the Board of Directors and serve until their successors are appointed and qualified or until earlier resignation or removal. There are no family relations among directors and officers and no arrangements with third parties (customers, suppliers) pursuant to which they were appointed as officers or directors.

B. Compensation

COMPENSATION OF DIRECTORS AND EXECUTIVE OFFICERS

Compensation Discussion and Analysis

This Compensation Discussion and Analysis focuses primarily on: (i) significant elements of the Corporation’s executive compensation program; (ii) principles on which the Corporation makes compensation decisions and determines the amount of each element of executive and director compensation; and (iii) an analysis of the material compensation decisions made by the Human Resources Committee for the financial year ended August 31, 2012.

The following is a discussion of the compensation arrangements with the Corporation’s Chief Executive Officer (“CEO”), Chief Financial Officer (“CFO”) and each of the three most highly compensated executive officers whose total

compensation was, individually, more than CA$150,000, (the "Named Executive Officers" or "NEOs"). The Corporation's NEOs for the financial year ended August 31, 2012 were Mr. Germain Lamonde (CEO), Mr. Pierre Plamondon (CFO), Mr. Stephen Bull, Vice-President, Research and Development, Mr. Sylvain Rouleau, Vice-President, Human Capital and Mr. Dana Yearian, Vice-President, Sales — Americas.

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Members of the Human Resources Committee

During the financial year ended August 31, 2012, the Human Resources Committee was composed of:

Mr. Guy Marier (Chairman)
Mr. Pierre-Paul Allard
Mr. Darryl Edwards
Mr. Pierre Marcouiller
Ms. Susan Spradley
Mr. David A. Thompson (until January 12, 2012);

None of these members were officers or employees, or former officers or employees of the Corporation or its subsidiaries. All of the members of the Human Resources Committee are considered "independent", as defined in NASDAQ National Market listing requirements and applicable securities legislation and regulations. They each have experience in executive compensation either as a chief executive officer or a senior executive officer of a publicly-traded corporation. Mr. Guy Marier has held various senior management and executive positions in the last 25 years. Mr. Pierre-Paul Allard has held management and executive positions for the last 30 years. Mr. Darryl Edwards has held a number of senior executive leadership positions in the last 30 years. Mr. Pierre Marcouiller has 25 years of experience in management. Ms. Susan Spradley has been a senior executive for 20 years. Over the course of their careers, all members have been exposed at various degrees to the complexity of balancing efficient executive compensation strategies with the evolution of business requirements, having to manage directly or indirectly impacts and consequences of executive compensation decisions. The Board of Directors believes that the Human Resources Committee collectively has the knowledge, experience and background required to fulfill its mandate.

Mandate of the Human Resources Committee

The Human Resources Committee of the Board of Directors is responsible for establishing the annual compensation and assessing the risks related thereto and overseeing the assessment of the performance of all the Corporation's executive officers, including the President and Chief Executive Officer. This Human Resources Committee also reviews and submits to the Board of Directors the salary structure and the short-term and long-term incentive compensation programs for all employees of the Corporation. The Human Resources Committee also evaluates and makes recommendations to the Board of Directors regarding the compensation of directors, including the number of Deferred Share Units credited to the non-employee directors pursuant to the Deferred Share Unit Plan. The Human Resources Committee's goal is to develop and monitor executive compensation programs that are consistent with strategic business objectives and shareholders' interests. Though the Human Resources Committee is responsible for the review and approval of the employees that will receive Restricted Share Units or options to purchase shares of the Corporation, in accordance with policies established by the Board of Directors and the terms of the Long-Term Incentive Plan, these functions may be shared between the Board of Directors and the Human Resources Committee. During the period from September 1, 2011 to August 31, 2012, these functions have been shared by the Board of Directors and the Human Resources Committee but have mainly been performed by the Human Resources Committee.

The Human Resources Committee has reviewed and discussed with the CEO and Vice-President, Human Capital of the Corporation, the compensation disclosure in this document, and has recommended to the Board of Directors that the disclosure be included in this Annual Report.

From September 1, 2011 to November 1, 2012, the Human Resources Committee held five (5) meetings and at four (4) of those meetings executive compensation was discussed. The Human Resources Committee meetings were attended by all the members of the Human Resources Committee, except Mr. Allard and Mr. Marcouiller who were each absent at one meeting. The following table outlines the main activities of the Human Resources Committee during the last financial year:

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Meeting	Main activities of the Human Resources Committee
October 11, 2011	Review and approval of the Short-Term Incentive Plan for the financial year started September 1, 2011; Review of the proposed salary scales and salary increases for the year started September 1, 2011; Review and approval of the compensation plans of executive officers for the financial year started September 1, 2011 being the Base Salary, the Short-Term Incentive Plan and the stock-based compensation delivered through the Long-Term Incentive Plan; Review and approval of the stock-based compensation plan for the sales force delivered through the Long-Term Incentive Plan for the financial year started September 1, 2011; Review and approval of the quantum for the stock-based compensation plan for the performing employees delivered through the Long-Term Incentive Plan for the financial year started September 1, 2011; Review and approval of the executive compensation section of the management proxy circular for the financial year ended August 31, 2011 during a Board of Directors meeting; Review of the succession planning program; Review of the Mobilization / Motivation Plan; Review of a coaching program for the CEO; Review and approval of the CEO objectives; Review of the 2012 executive compensation disclosure obligations; Review of the Management Improvement Performance Program.
January 11, 2012	Review of the quarterly payments under the Short-Term Incentive Plan for the financial year started September 1, 2011 and being part of the Short-Term Incentive Plan; Review and approval of the stock-based compensation plan for the performing employees delivered through the Long-Term Incentive Plan for the financial year started September 1, 2011; Review and approval of the CEO objectives and compensation plan; Review of the Mobilization / Motivation Plan; Review of the Management Improvement Performance Program; Review of the sales forces commissions plans; Review of the succession planning program.
March 27, 2012	Review of the quarterly payments under the Short-Term Incentive Plan for the financial year started September 1, 2011 and being part of the Short-Term Incentive Plan; Review and approval of the stock-based compensation delivered through the Long-Term Incentive Plan;

	Review of the sales compensation plans; Review of the employee mobilization survey; Review of the succession planning program.
June 28, 2012	Review of the quarterly payments under the Short-Term Incentive Plan for the financial year started September 1, 2011 and being part of the Short-Term Incentive Plan; Confirmation of the members' biographies; Introduction to the Risk Assessment of Executive Compensation; Status update on the employee mobilization survey; Review of the Structure Realignment; Review of the Restructuring Activities; Review of the Management Framework Renewal; Review of the sales forces commissions plans; Determination by the Members of their respective DSU percentage of their Annual Retainer.
October 9, 2012	Review and approval of the Short-Term Incentive Plan for the financial year started September 1, 2012; Review of the proposed salary scales and salary increases for the year started September 1, 2012; Review and approval of the compensation plans of executive officers for the financial year started September 1, 2012 being the Base Salary, the Short-Term Incentive Plan and the stock-based compensation delivered through the Long-Term Incentive Plan; Review and approval of the stock-based compensation plan for the sales force delivered through the Long-Term Incentive Plan for the financial year started September 1, 2012; Review and approval of the quantum for the stock-based compensation plan for the performing employees delivered through the Long-Term Incentive Plan for the financial year started September 1, 2012; Review and approval of the executive compensation section of the management proxy circular for the financial year ended August 31, 2012; Review of the succession planning program; Review of the Mobilization / Motivation Plan; Review and approval of the CEO objectives and compensation plan; Review of the Risk Assessment of Executive Compensation disclosure obligations.

Compensation Plan Control - Compensation Consultant and Internal Review

As a general practice, the Corporation's relative position in terms of compensation levels is determined periodically through studies performed by independent consulting firms using a selected reference market of comparable companies. The benchmarking activities are further detailed below under the heading – "Benchmarking".

In 2007, the Corporation engaged two human resources consultants, Mercer (Canada) Ltd. ("Mercer") and Aon Corporation ("Aon"), to advise whether the compensation positioning of the Corporation was still aligned with the comparative market. Further to recommendations from Mercer and Aon, the Corporation decided to gradually align the compensation positioning (for the base salary, short-term and long-term incentives) from the fiftieth percentile to the sixtieth percentile for selected positions (the "Target Compensation Positioning") over the following three years.

In 2008, the Corporation engaged Hewitt Associates LLC to conduct a world-wide market analysis for selected international positions. The survey included annual base salary, bonuses and commission plans.

In 2009, the Corporation appointed Mercer to review the compensation positioning of the Corporation. Mercer confirmed that the Corporation's compensation scheme (base salary, short-term compensation, long-term compensation) was still aligned with the comparative market but some adjustments were proposed to be made for certain executive officers. Considering the overall economic situation, the adjustments proposed by Mercer were postponed.

In 2010, the Corporation engaged Mercer to conduct a study of the Corporation's executive compensation plans. The study examined the total compensation including the fix components (i.e., base salary, pension, benefits and perquisites) and the variable components (i.e., short-term and long-term incentives). The analysis of Mercer indicated that adjustments were required primarily to base salary levels and the long-term incentive plan, as well as pension value. Any adjustments were made from a total compensation perspective. Mercer has suggested modifying the compensation philosophy to progressively align the executive compensation toward a total compensation to the fiftieth percentile for expected performance with an opportunity, conditional on performance, to exceed the fiftieth percentile total compensation (the "Target Total Compensation"). Further to such recommendations, the Corporation has decided to gradually align over the following three (3) years the compensation positioning according to the Target Total Compensation scheme proposed by Mercer for the compensation plans of the financial year starting September 1, 2010 ("Mercer Three Year Compensation Plan").

In 2011 and 2012, the Corporation pursued its Mercer Three Year Compensation Plan described above and therefore the Corporation did not conduct any study of the Corporation's executive compensation plans during those two years. The Corporation is planning to conduct such study in 2013 to adjust, as the case may be, its Mercer Three Year Compensation Plan.

In addition, internal pay equity studies are a key factor to complete the compensation review process and indicate where necessary adjustments may be required. During the financial year ended August 31, 2012, this practice continued and certain compensation adjustments were made.

The Human Resources Committee has the authority to retain any independent consultants of its choice to advise its members on total executive compensation policy matters, and to determine the fees and the terms and conditions of the engagement of these consultants. The Human Resources Committee is ultimately responsible for its own decisions, which may take into consideration more than the information and recommendations provided by its compensation consultants or management.

For the financial year that ended on August 31, 2012, the Human Resource Committee retained the services of Mercer for an opinion on CEO compensation. The Corporation also retained the services of Aon, Mercer and Optimum Actuaires & Conseillers Inc. for services non-related to executive compensation. The services provided by Aon concerned the access to compensation data for sales employees. The Corporation consulted Mercer for assistance in maintenance of pay equity for unionized employees and other general inquiries concerning compensation. The services provided by Optimum Actuaires & Conseillers Inc. concerned an analysis on financial impacts of the benefits provided by the Corporation to its employees. Fees for the services performed that are not related to executive compensation are not required to be approved by the Human Resource Committee.

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The aggregate fees paid to Aon, Mercer and Optimum Actuaires & Conseillers Inc. for consulting services provided to the Human Resources Committee for services related to determining compensation for any of the Corporation's directors and executive officers and to the Corporation for all other services provided during the financial years ended August 31, 2011 and 2012 are as follows:

Type of Fee	Financial 2011 Fees	Percentage of Financial 2011 Fees	Financial 2012 Fees	Percentage of Financial 2012 Fees
Executive Compensation Related Fees	CA$7,035	43%	CA$1,780	3%
All Other Fees	CA$9,245	57%	CA$57,314	97%
Total	CA$16,280	100%	CA$59,094	100%

Benchmarking

The Target Total Compensation of senior executives has been reviewed with guidance and advice from Mercer, using a peer group of companies as reference point for determining a competitive total compensation package. The comparator group included private and publicly-traded companies evolving in high technologies, telecommunications and durable-manufacturing goods industries. The selection was based on a number of factors including comparable size, similar service business and relationship to the telecommunications and life science industries. For certain executives, we emphasized certain comparative companies more than others in determining total compensation based on the responsibilities of such executives. When drawing comparisons to companies significantly larger than the Corporation, in particular those in the manufacturing goods industry, we did not examine compensation arrangements of the most senior executive of that comparator but instead looked to the roles and responsibilities of individuals within those companies with equivalent business experience.

Mercer used three primary comparator groups in matching the Corporation's incumbent senior executives to positions of similar responsibility within comparable private and publicly-traded companies:

(1) 2009 Mercer Benchmark Database, which contains compensation data for selected Canadian companies with median annual revenues of CA$325 million. The following is a list of the main companies, with a particular emphasis on the high-technology/telecommunications and manufacturing-durable goods industries, servicing industries, revenue categories and geography, used for the purposes of setting 2010 compensation: Arcan Resources Ltd.; Linamar Corporation; Arsenal Energy Inc.; Livingston International; Baytex Energy Trust; Logistec Corporation; Canadian Hydro Developers Inc.; MacDonald, Dettwiler and Associates Corporation – Quebec; Canadian Pacific; Pason Systems Inc.; CE Franklin Ltd.; Precision Drilling Trust; Centerra Gold Inc.; RDM Corporation; Compton Petroleum Corporation; SNC-Lavalin; Computer Modelling Group Ltd.; Softchoice Corp.; Crew Energy Inc.; Stantec Inc.; Enerflex Systems Ltd.; Teck Resources Limited; Labopharm Inc.; TeraGo Networks Inc.; and Velan Inc. Mercer can only disclose the identities of the publicly-traded participating organizations due to confidentiality covenants with survey participants;

(2) 2009 US Mercer Benchmark Database (2,771 participants); and

(3) 2009 UK Mercer Benchmark Database (193 participants), which contains compensation data for companies in all industries of all sizes and scopes. Focuses on companies with revenues lower than CA$500 million.

For the executives based outside Canada, their total compensation was aligned at the median of the local market. Mercer cannot disclose the identities of participating organizations within a specific revenue range

due to confidentiality covenants with survey participants. Local laws forbid the disclosure of company names when a sampling of companies is extracted from a local database.

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Guiding Principles for Compensation of Executive Officers

The Corporation's executive compensation plans are designed to attract, retain and motivate key executives who directly impact the Corporation's long-term success and the creation of shareholder value. In determining executive compensation, the Human Resources Committee considers the following four principles:

Performance-based: Executive compensation levels reflect both the results of the Corporation and individual results based on specific quantitative and qualitative objectives established at the beginning of each financial year in keeping with the Corporation's long-term strategic objectives.

Aligned with shareholder interests: An important portion of incentive compensation for executives is composed of equity awards to ensure that executives are aligned with the principles of sustained long-term shareholder value growth.

Market competitive: Compensation of executives is designed to be externally competitive when compared against executives of comparable peer companies, and in consideration of the Corporation's results.