EXFO ELECTRO OPTICAL ENGINEERING INC
Form 6-K
January 14, 2009

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

FORM 6-K

Report of Foreign Private Issuer Pursuant to Rule 13a-16 or 15d-16
Under the Securities Exchange Act of 1934

For the month of January 2009

EXFO Electro-Optical Engineering Inc.
(Translation of registrant's name into English)

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

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F þForm 40-F o

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes oNo þ

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-______.

TABLE OF CONTENTS

Signatures
Press Release
Interim Consolidated Balance Sheet
Interim Unaudited Consolidated Statements of Earnings
Interim Unaudited Consolidated Statements of Comprehensive Income (Loss) and Accumulated Other Comprehensive Income
Interim Unaudited Consolidated Statements of Retained Earnings and Contributed Surplus
Interim Unaudited Consolidated Statements of Cash Flows
Notes to Consolidated Financial Statements
Management's Discussion and Analysis of Financial Condition and Results of Operations

Table of Contents

On January 13, 2009, EXFO Electro-Optical Engineering Inc., a Canadian corporation, reported its results of operations for the first fiscal quarter ended November 30, 2008. This report on Form 6-K sets forth the news release relating to EXFO's announcement and certain information relating to EXFO's financial condition and results of operations for the first fiscal quarter of the 2009 fiscal year. This press release and information relating to EXFO's financial condition and results of operations for the first fiscal quarter of the 2009 fiscal year are hereby incorporated as a document by reference to Form F-3 (Registration Statement under the Securities Act of 1933) declared effective as of July 30, 2001 and to Form F-3 (Registration Statement under the Securities Act of 1933) declared effective as of March 11, 2002 and to amend certain material information as set forth in these two Form F-3 documents.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

EXFO ELECTRO-OPTICAL ENGINEERING INC.

By: /s/ Germain Lamonde
Name: Germain Lamonde
Title: President and Chief Executive Officer

Date: January 14, 2009

Table of Contents

EXFO Reports Strong Financial Results for First Quarter of 2009

- § Record-high bookings of US$52.3 million, up 19.7% year-over-year
- § Sales increase 13.1% year-over-year to US$46.4 million
- § Gross margin reaches 62.3%, highest level since second quarter of 2001
- § GAAP net earnings amount to US$0.08 per diluted share

QUEBEC CITY, CANADA, January 13, 2009 – EXFO Electro-Optical Engineering Inc. (NASDAQ: EXFO; TSX: EXF) reported today strong financial results for the first quarter ended November 30, 2008.

Sales increased 13.1% to US$46.4 million in the first quarter of fiscal 2009 from US$41.0 million in the first quarter of 2008, but decreased 9.0% from US$50.9 million in the fourth quarter of 2008. Net bookings improved 19.7% year-over-year to a record-high of US$52.3 million for a book-to-bill ratio of 1.13 in the first quarter of fiscal 2009 from US$43.7 million in the same period last year and 14.5% from US$45.7 million in the fourth quarter of 2008.

Gross margin reached 62.3% of sales in the first quarter of fiscal 2009, its highest level since the second quarter of 2001, compared to 55.7% in the first quarter of 2008 and 59.9% in the fourth quarter of 2008.

GAAP net earnings in the first quarter of fiscal 2009 increased to US$5.3 million, or US$0.08 per diluted share, from a GAAP net loss of US$0.1 million, or US$ 0.00 per diluted share, in the same period last year and GAAP net earnings of US$3.3 million, or US$0.05 per diluted share in the fourth quarter of fiscal 2008. GAAP net earnings in the first quarter of 2009 included US$1.1 million in after-tax amortization of intangible assets and US$0.3 million in stock-based compensation costs. It should be noted that EXFO recorded a pre-tax, foreign exchange gain of US$4.6 million in the first quarter of fiscal 2009.

“I am quite pleased with our record-high bookings of US$52.3 million and best gross margin in almost eight years in the last quarter, led by very strong growth from our next-generation, IP test equipment and recent service assurance acquisition that we’re starting to leverage,” said Germain Lamonde, EXFO’s Chairman, President and CEO. “On the strength of a multi-million dollar service assurance contract with a Tier-1 wireless operator, our Protocol business collectively accounted for more than 30% of total bookings in the quarter to significantly contribute to our book-to-bill ratio of 1.13. We also benefited from a weaker Canadian/US exchange rate which positively affected our operating expenses and our earnings.”

“A number of wireline and wireless network operators will likely reduce their capital expenditures in 2009, given the challenging macro-economic conditions,” Mr. Lamonde added. “But we expect many will continue to strategically invest in next-generation IP convergence and broadband deployments in order to add higher-margin revenues, differentiated services and to reduce their operating expenses. EXFO is well positioned to take advantage of these growth segments. We’re also counting on important new products and increased focus to attain our long-term performance metrics. To remain prudent, however, we have implemented a series of measures to control expenses, deferred or cancelled hirings, and fine-tuned our strategies. Finally, our balance sheet remains strong, even after our successful C$30 million share buyback, as we navigate through this tumultuous period.”

Table of Contents

Unaudited Selected Financial Information
(In thousands of US dollars)

Segmented results:	Q1 2009	Q1 2008	Q4 2008
Sales:			
Telecom Division	$ 41,159	$ 35,365	$ 45,338
Life Sciences and Industrial Division	5,204	5,620	5,605
Total	$ 46,363	$ 40,985	$ 50,943
Earnings from operations:			
Telecom Division	$ 1,355	$ 21	$ 2,867
Life Sciences and Industrial Division	738	281	721
Total	$ 2,093	$ 302	$ 3,588
Other selected information:			
GAAP net earnings (loss)	$ 5,287	$ (93)	$ 3,314
After-tax amortization of intangible assets	$ 1,098	$ 499	$ 1,177
Stock-based compensation costs	$ 322	$ 301	$ 368

Operating Expenses
Selling and administrative expenses amounted to US$17.1 million, or 36.9% of sales, in the first quarter of fiscal 2009 compared to US$14.8 million, or 36.2% of sales, in the same period last year and US$17.0 million, or 33.4% of sales, in the fourth quarter of 2008.

Gross research and development expenses totaled US$8.6 million, or 18.6% of sales, in the first quarter of fiscal 2009 compared to US$7.5 million, or 18.3% of sales, in the first quarter of 2008 and US$8.6 million, or 16.8% of sales, in the fourth quarter of 2008.

Net R&D expenses totaled US$7.2 million, or 15.6% of sales, in the first quarter of fiscal 2009 compared to US$6.0 million, or 14.7% of sales, in the same period last year and US$7.3 million, or 14.3% of sales, in the fourth quarter of 2008.

First-Quarter Business Highlights
Market expansion — EXFO delivered sales growth of 13.1% year-over-year, including a combined US$4.5 million revenue contribution from recently acquired Brix Networks and Navtel Communications. Its Protocol business generated record quarterly revenues, accounting for more than 30% of Telecom Division sales for the first time. The company's bookings made significant progress in the wireless market in the first quarter of 2009, while Telecom Division sales increased 16.4% year-over-year and the Life Sciences and Industrial Division experienced a 7.4% drop due to deteriorating end-consumer markets. EXFO's top customer accounted for 3.8% of total sales, while its top three accounts represented 10.4% of sales, demonstrating the company's successful diversification efforts.

Profitability and Gross Margin — EXFO reported GAAP net earnings of US$5.3 million, or US$0.08 per diluted share. An improved gross margin at 62.3%, on account of a weaker Canadian dollar, increased sales of higher-margin Protocol test solutions and the ramp-up of low-cost manufacturing plant in China, also contributed to the company's profitability in the first quarter.

Table of Contents

EXFO launched five new products in the first quarter including amongst others a new software release for the Transport Blazer product line that delivers unprecedented insight into 40 Gbit/s network behavior; new software releases for the IMS InterWatch platform and Packet Blazer product line to support the migration of voice and video applications to the IPv6 (Internet Protocol, version 6) addressing scheme; and expanded Ethernet test capabilities on the Power Blazer product line through multi-stream, quality of service (QoS) support. Products on the market two years or less generated 33.1% of total sales.

Business Outlook

EXFO forecasted sales between US$45 million and US$50 million and GAAP net earnings between US$0.01 per diluted share and US$0.05 per diluted share for the second quarter of 2009. GAAP net earnings include US$0.02 per share in after-tax amortization of intangible assets and stock-based compensation costs.

This guidance was established by management based on existing backlog as of the date of this press release, seasonality, expected bookings for the remaining of the quarter, as well as stability in exchange rates compared to the previous quarter.

Conference Call and Webcast

EXFO will host a conference call today at 5 p.m. (Eastern time) to review its financial results for the first quarter of fiscal 2009. To listen to the conference call and participate in the question period via telephone, dial 1-416-620-2416. Germain Lamonde, Chairman, President and CEO, and Pierre Plamondon, CA, Vice-President of Finance and Chief Financial Officer, will participate in the call. An audio replay of the conference call will be available one hour after the event until 7 p.m. on January 20, 2009. The replay number is 1-402-977-9141 and the reservation number is 21405504. The audio Webcast and replay of the conference call will also be available on EXFO's Website at www.EXFO.com, under the Investors section.

Forward-Looking Statements

This press release 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, anticipate, intend, could, estimate, continue, or the negative or comparable terminology 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 consolidation in the global telecommunications test, measurement and monitoring industry; capital spending levels in the telecommunications, life sciences and high-precision assembly sectors; concentration of sales; fluctuating exchange rates and our ability to execute in these uncertain conditions; the effects of the additional actions we have taken in response to such economic uncertainty (including our ability to quickly adapt cost structures with anticipated levels of business, ability to manage inventory levels with market demand); market acceptance of our new products and other upcoming products; limited visibility with regards to customer orders and the timing of such orders; our ability to successfully integrate our acquired and to-be-acquired businesses; our ability to successfully expand international operations; the retention of key technical and management personnel; and future economic, competitive, financial and market conditions, including any slowdown or recession in the global economy. 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 our Annual Report, on Form 20-F, and our other filings with the U.S. Securities and Exchange Commission and the Canadian securities commissions. 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.

Table of Contents

About EXFO

EXFO is a leading provider of test and service assurance solutions for network service providers and equipment manufacturers in the global telecommunications industry. The Telecom Division offers a wide range of innovative solutions extending across the full technology lifecycle from design to technology deployment and onto service assurance and covering all layers on a network infrastructure to enable triple-play services and next-generation, converged IP networking. The Life Sciences and Industrial Division offers solutions in medical device and opto-electronics assembly, fluorescence microscopy and other life science sectors. For more information, visit www.EXFO.com.

For more information
Vance Oliver
Manager, Investor Relations
(418) 683-0913, Ext. 3733
vance.oliver@exfo.com

Table of Contents

EXFO Electro-Optical Engineering Inc.
Interim Consolidated Balance Sheet

(in thousands of US dollars)

	As at November 30, 2008 (unaudited)	As at August 31, 2008
Assets		
Current assets		
Cash	$ 5,441	$ 5,914
Short-term investments	65,915	81,626
Accounts receivable		
Trade (note 4)	33,018	31,473
Other	4,859	4,753
Income taxes and tax credits recoverable	3,541	4,836
Inventories (note 5)	30,125	34,880
Prepaid expenses	1,993	1,774
Future income taxes	8,895	9,140
	153,787	174,396
Tax credits recoverable	19,264	20,657
Property, plant and equipment	17,475	19,875
Intangible assets	16,121	19,945
Goodwill	36,634	42,653
Future income taxes	14,297	15,540
	$ 257,578	$ 293,066
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 6)	$ 24,440	$ 24,713
Deferred revenue	4,560	5,079
	29,000	29,792
Deferred revenue	3,388	3,759
Forward exchange contracts (note 4)	2,275	–

	34,663	33,551
Contingency (note 7)		
Shareholders’ equity		
Share capital (note 8)	141,991	142,786
Contributed surplus	5,921	5,226
Retained earnings	65,781	60,494
Accumulated other comprehensive income	9,222	51,009
	222,915	259,515
	$ 257,578	$ 293,066

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

Table of Contents

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Earnings

(in thousands of US dollars, except share and per share data)

	Three months ended November 30,	
	2008	2007
Sales	$ 46,363	$ 40,985
Cost of sales (note 5) (1, 2)	17,480	18,144
Gross margin	28,883	22,841
Operating expenses		
Selling and administrative(1)	17,091	14,817
Net research and development(1) (note 9)	7,221	6,012
Amortization of property, plant and equipment	1,159	976
Amortization of intangible assets	1,319	734
Total operating expenses	26,790	22,539
Earnings from operations	2,093	302
Interest income	466	1,483
Foreign exchange gain (loss)	4,568	(616)
Earnings before income taxes	7,127	1,169
Income taxes (note 10)		
Current	(61)	1,181
Future	1,901	81
	1,840	1,262
Net earnings (loss) for the period	$ 5,287	$ (93)
Basic and diluted net earnings (loss) per share	$ 0.08	$ (0.00)
Basic weighted average number of shares outstanding (000's)	67,340	69,000
Diluted weighted average number of shares outstanding (000's) (note 11)	67,717	69,672
(1) Stock-based compensation costs included in:		
Cost of sales	$ 29	$ 37
Selling and administrative	201	197
Net research and development	92	67

	$	322	$	301

(2) The cost of sales is exclusive of amortization, shown separately.

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

Table of Contents

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Comprehensive Income (Loss)
and Accumulated Other Comprehensive Income

(in thousands of US dollars)

Comprehensive income (loss)

	Three months ended November 30,	
	2008	2007
Net earnings (loss) for the period	$ 5,287	$ (93)
Foreign currency translation adjustment	(36,933)	13,906
Changes in unrealized losses on short-term investments	22	39
Unrealized gains (losses) on forward exchange contracts	(6,929)	1,948
Reclassification of realized gains on forward exchange contracts in net earnings (loss)	(137)	(759)
Future income tax effect of the above items	2,190	(380)
Comprehensive income (loss)	$ (36,500)	$ 14,661

Accumulated other comprehensive income

	Three months ended November 30,	
	2008	2007
Foreign currency translation adjustment		
Cumulative effect of prior periods	$ 51,129	$ 53,418
Current period	(36,933)	13,906
	14,196	67,324
Unrealized gains (losses) on forward exchange contracts		
Cumulative effect of prior periods	(96)	1,948
Current period, net of realized gains and future income taxes	(4,876)	809
	(4,972)	2,757
Unrealized losses on short-term investments		
Cumulative effect of prior periods	(24)	(55)
Current period, net of future income taxes	22	39
	(2)	(16)
Accumulated other comprehensive income	$ 9,222	$ 70,065

Total retained earnings and accumulated other comprehensive income amounted to $112,263 and $75,003 as at November 30, 2007 and 2008, respectively.

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

Table of Contents

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Retained Earnings and Contributed Surplus

(in thousands of US dollars)

Retained earnings

	Three months ended November 30,	
	2008	2007
Balance – Beginning of the period	$ 60,494	$ 42,330
Add (deduct)		
Net earnings (loss) for the period	5,287	(93)
Premium on redemption of share capital (note 8)	–	(39)
Balance – End of the period	$ 65,781	$ 42,198

Contributed surplus

	Three months ended November 30,	
	2008	2007
Balance – Beginning of the period	$ 5,226	$ 4,453
Add (deduct)		
Stock-based compensation costs	321	316
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	(2)
Discount on redemption of share capital (note 8)	374	–
Balance – End of the period	$ 5,921	$ 4,767

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

Table of Contents

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Three months ended November 30,	
	2008	2007
Cash flows from operating activities		
Net earnings (loss) for the period	$ 5,287	$ (93)
Add items not affecting cash		
Change in discount on short-term investments	456	902
Stock-based compensation costs	322	301
Amortization	2,478	1,710
Deferred revenue	353	351
Future income taxes	1,901	81
Change in unrealized foreign exchange gain	(3,456)	–
	7,341	3,252
Change in non-cash operating items		
Accounts receivable	(7,325)	1,166
Income taxes and tax credits	(696)	(458)
Inventories	(367)	(87)
Prepaid expenses	(542)	(612)
Accounts payable and accrued liabilities	(1,087)	(5,694)
	(2,676)	(2,433)
Cash flows from investing activities		
Additions to short-term investments	(122,100)	(211,453)
Proceeds from disposal and maturity of short-term investments	126,605	214,571
Additions to capital assets (1)	(1,514)	(1,573)
	2,991	1,545
Cash flows from financing activities		
Change in bank loan	–	699
Exercise of stock options	26	–
Redemption of share capital (note 8)	(447)	(174)
	(421)	525
Effect of foreign exchange rate changes on cash	(367)	343
Change in cash	(473)	(20)
Cash – Beginning of the period	5,914	5,541
Cash – End of the period	$ 5,441	$ 5,521

(1) As at November 30, 2007 and 2008, unpaid purchases of capital assets amounted to $852 and $312, respectively.

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

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

1 Interim Financial Information

The financial information as at November 30, 2008, and for the three-month periods ended November 30, 2007 and 2008, is unaudited. In the opinion of management, all adjustments necessary to present fairly the results of these periods in accordance with generally accepted accounting principles (GAAP) in Canada have been included. The adjustments made were of a normal and recurring nature. Interim results may not necessarily be indicative of results anticipated for the entire year.

These interim consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada and use the same accounting policies and methods used in the preparation of the company's most recent annual consolidated financial statements, except for changes as described in note 2. However, all disclosures required for annual financial statements have not been included in these financial statements. Consequently, these interim consolidated financial statements should be read in conjunction with the company's most recent annual consolidated financial statements.

2 New Accounting Standards and Pronouncements

Adopted in fiscal 2009

In December 2006, the Canadian Institute of Chartered Accountants (CICA) issued three new sections, which provide a complete set of disclosure and presentation requirements for financial instruments: Section 3862, "Financial Instruments – Disclosures"; Section 3863, "Financial Instruments – Presentation"; and Section 1535, "Capital Disclosures".

Section 3862 replaces the disclosure portion of Section 3861, "Financial Instruments – Disclosure and Presentation". The new standard places increased emphasis on disclosures regarding risks associated with both recognized and unrecognized financial instruments and how these risks are managed. It is also intended to remove any duplicate disclosures and simplify the disclosures about concentrations of risk, credit risk, liquidity risk and price risk previously found in Section 3861.

Section 3863 carries forward the presentation requirements from Section 3861, unchanged.

Section 1535 applies to all entities, regardless of whether they have financial instruments or are subject to external capital requirements. The new section requires disclosure of information about an entity's objectives, policies and processes for managing capital, as well as quantitative data about capital and whether the entity has complied with any capital requirements.

The company adopted these new standards on September 1, 2008 (notes 3 and 4).

In June 2007, the CICA issued Section 3031, "Inventories". This standard requires the measurement of inventories at the lower of cost and net realizable value and includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either first-in, first-out (FIFO) or weighted average cost formula to measure the cost of inventories and requires the reversal of previous write-downs

to net realizable value when there is a subsequent increase in the value of inventories. The new standard applies to fiscal years beginning on or after January 1, 2008. The company adopted this new standard on September 1, 2008, and its adoption had no effect on its consolidated financial statements.

In June 2007, the CICA amended Section 1400, “General Standards of Financial Statement Presentation” to include new requirements regarding an entity’s ability to continue as a going concern. These amendments apply to fiscal years beginning on or after January 1, 2008. The company adopted these amendments on September 1, 2008, and their adoption had no effect on its consolidated financial statements.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

To be adopted after fiscal 2009

In February 2008, the CICA issued Section 3064, "Goodwill and intangible assets", which supersedes Section 3062, "Goodwill and other intangible assets" and Section 3450, "Research and development costs". Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill remain unchanged from the standards included in Section 3062. This new section applies to fiscal years beginning on or after October 1, 2008. The company will adopt this new standard on September 1, 2009, and has not yet determined the effects its adoption will have on its consolidated financial statements.

3 Capital Disclosures

The company is not subject to any external restrictions on its capital.

The company's objectives when managing capital are:

- To maintain a flexible capital structure, which optimizes the cost of capital at acceptable risk;
- To sustain future development of the company, including research and development activities and potential acquisitions of complementary businesses or products; and
- To provide the company's shareholders with an appropriate return on their investment.

The company defines its capital as shareholders' equity, excluding accumulated other comprehensive income. Accumulated other comprehensive income's main component is the cumulative foreign currency translation adjustment, which is solely the result of the translation of the company's consolidated financial statements into US dollars (the reporting currency).

The capital of the company amounted to $208,506,000 and $213,693,000 as at August 31, 2008 and November 2008, respectively.

Of this capital, as at November 30, 2008, an amount of $71,356,000 represented cash and short-term investments ($87,540,000 as at August 31, 2008), a portion of which can be considered in excess of the company's current and expected needs. The company has consequently been actively repurchasing shares from the open market via a normal course issuer bid through the facilities of the Toronto Stock Exchange and the NASDAQ. Furthermore, as at November 30, 2008, the company had an outstanding substantial issuer bid to purchase for cancellation up to 8,823,529 subordinate voting shares for an aggregate purchase price not to exceed CA$30,000,000 (note 14).

4 Financial Instruments

Market risk

Currency risk

The principal measurement currency of the company is the Canadian dollar. The company is exposed to currency risks as a result of its export sales of products manufactured in Canada and China, the majority of which are denominated in US dollars and euros. These risks are partially hedged by forward exchange contracts (US dollars) and certain operating expenses (US dollars and euros).

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

As at November 30, 2008, the company held contracts to sell US dollars for Canadian dollars at various forward rates, which are summarized as follows:

Expiry dates	Contractual amounts (unaudited)	Weighted average contractual forward rates
December 2008 to August 2009	$ 28,300	1.0616
September 2009 to August 2010	24,200	1.0760
September 2010 to August 2011	14,600	1.1221
September 2011	1,000	1.1278
Total	$ 68,100	1.0807

These contracts are designated and accounted for as cash flow hedges.

The fair value of forward exchange contracts, which represents the amount that the company would receive or pay to settle the contracts based on the forward exchange rate at period end, amounted to net gains of $62,000 as at August 31, 2008 and net losses of $7,973,000 as at November 30, 2008, following the significant decrease in the value of the Canadian dollar compared to the US dollar during the quarter. As at November 30, 2008, forward exchange contracts, in the amount of $4,877,000, are presented in the accounts payable and accrued liabilities (note 6) in the balance sheet, and forward exchange contracts, in the amount of $2,275,000, are presented in forward exchange contracts in the balance sheet.

The following table summarizes significant financial assets and liabilities that are subject to currency risk as at November 30, 2008:

		Carrying amount (in thousands of US dollars) (unaudited)		Carrying amount (in thousands of euros)
Financial Assets				
Cash	$	2,773	€	505
Accounts receivable		26,742		2,225
		29,515		2,730
Financial Liabilities				
Accounts payable and accrued liabilities		5,982		356
Forward exchange contracts		68,100		–
		74,082		356
Net exposure	$	(44,567)	€	2,374

The period-end value of the Canadian dollar compared to the US dollar was CA$1.2372 = US$1.00 as at November 30, 2008.

The period-end value of the Canadian dollar compared to the euro was CA$1.5706 = €1.00 as at November 30, 2008.

The following sensitivity analyse summarizes the effect that a change in the value of the Canadian dollar (compared to US dollar and euro) would have on financial assets and liabilities denominated in US dollars and euros, as well as on net earnings, net earnings per diluted share and comprehensive income, based on the foreign exchange rates as at November 30, 2008:

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the US dollar would decrease (increase) net earnings by $1,832,000, or $0.03 per diluted share.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the euro would decrease (increase) net earnings by $333,000, or $0.00 per diluted share.

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the US dollar would increase (decrease) comprehensive income by $4,500,000.

The impact of the change in the value of the Canadian dollar compared to the US dollar and the euro on these financial assets and liabilities is recorded in the foreign exchange gain or loss line item in the consolidated statements of earnings, except for outstanding forward contracts, which impact is recorded in comprehensive income. The change in the value of the Canadian dollar compared to the US dollar and the euro also impacts the company's balances of income tax and tax credits recoverable or payable and future income tax assets and liabilities related to integrated foreign subsidiaries; this may result in additional and significant foreign exchange gain or loss. However, these assets and liabilities are not considered financial instruments, and are excluded from the sensitivity analysis above. The foreign exchange rate fluctuations also flow through the statements of earnings line items, as a significant portion of the company's operating expenses are denominated in Canadian dollars, and the company reports its results in US dollars; that effect is not reflected in the sensitivity analysis above.

Interest rate risk

The company is exposed to interest rate risks through its short-term investments. As at November 30, 2008, the company's short-term investments, in the amount of $65,915,000, bear interest at rates ranging between 2.36% to 3.16% and mature between December 2008 and April 2009.

- An increase (decrease) of 0.5% in the interest rate of the company's short-term investments would increase (decrease) net earnings by $57,000, or $0.00 per diluted share on a quarterly basis.

Due to their short-term maturity of usually three months or less, the company's short-term investments are not subject to significant fair value interest rate risk. Accordingly, change in fair value has been nominal to the degree that amortized cost has historically approximated the fair value. Any change in fair value of the company's short-term investments, all of which are classified as available for sale, is recorded in comprehensive income.

Cash, accounts receivable and accounts payable and accrued liabilities are non-interest-bearing financial assets and liabilities.

Credit risk

Financial instruments that potentially subject the company to credit risk consist primarily of cash, short-term investments, accounts receivable and forward exchange contracts (with a positive fair value). As at November 30, 2008, the company's short-term investments consist of debt instruments issued by 13 (10 as at August 31, 2008) high-credit quality corporations and trusts. None of these debt instruments are expected to be affected by a liquidity risk, and none of them represent asset-backed commercial paper. The company's cash and forward exchange contracts are held with or issued by high-credit quality financial institutions; therefore, the company considers the risk of non-performance on these instruments to be limited.

Generally, the company does not require collateral or other security from customers for trade accounts receivable; however, credit is extended to customers following an evaluation of creditworthiness. In addition, the company performs ongoing credit reviews of all its customers and establishes an allowance for doubtful accounts receivable when accounts are determined to be uncollectible. Allowance for doubtful accounts amounted to $305,000 and $331,000 as at August 31, 2008 and November 30, 2008, respectively and bad debt expense amounted to $39,000 and $40,000 for the three months ended November 30, 2007 and 2008, respectively.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

For the three months ended November 30, 2008, no customer represented more than 10% of global sales.

The following table summarizes the age of trade accounts receivable as at November 30, 2008:

	(unaudited)
Current	$ 23,855
Past due since less than 30 days	6,720
Past due, 31 to 60 days	1,969
Past due, more than 61 days	805
Total accounts receivable	33,349
Allowance for doubtful accounts	(331)
	$ 33,018

Liquidity risk

Liquidity risk is defined as the potential that the company cannot meet its obligations as they become due.

The following table summarizes the contractual maturity of the company's financial liabilities as at November 30, 2008:

	0-12 months	13-24 months	25-36 months
		(unaudited)	
Accounts payable and accrued liabilities	$ 19,563	$ –	$ –
Forward exchange contracts			
Outflow	36,400	19,500	12,200
Inflow	(31,277)	(17,144)	(11,062)
Total	$ 24,686	$ 2,356	$ 1,138

In addition to these contractual liabilities, the company has a cash contingent consideration payable for the acquisition of Brix Networks, up to a maximum of $7,537,000, and any amount payable will be paid during fiscal 2009. Also, the company has share repurchase programs that may require additional cash outflows during fiscal 2009 and 2010 (notes 8 and 14).

As at November 30, 2008, the company had $71,356,000 in cash and short-term investments. In addition to these financial assets, the company has unused available lines of credit totalling $9,509,000 for working capital and other general corporate purposes, including potential acquisitions and share repurchase programs as well as unused lines of credit of $10,227,000 for foreign currency exposure related to its forward exchange contracts.

5 Inventories

	As at	As at

	November 30, 2008	August 31, 2008
	(unaudited)	
Raw materials	$ 14,355	$ 17,651
Work in progress	1,601	1,961
Finished goods	14,169	15,268
	$ 30,125	$ 34,880

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The cost of sales comprised almost exclusively the amount of inventory recognized as an expense during the reporting periods, except for the related amortization, that is shown separately in operating expenses.

Inventory write-down amounted to $351,000 and $794,000 for the three months ended November 30, 2007 and 2008, respectively.

6 Accounts Payable and Accrued Liabilities

	As at November 30, 2008	As at August 31, 2008
	(unaudited)	
Trade	$ 8,273	$ 10,303
Salaries and social benefits	7,027	8,888
Warranty	696	974
Commissions	782	761
Tax on capital	849	923
Restructuring charges	195	292
Forward exchange contracts (note 4)	4,877	714
Other	1,741	1,858
	$ 24,440	$ 24,713

Changes in the warranty provision are as follows:

	Three months ended November 30,	
	2008	2007
	(unaudited)	
Balance – Beginning of period	$ 974	$ 800
Provision	142	159
Settlements	(420)	(109)
Balance – End of period	$ 696	$ 850

7 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.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

On April 19, 2002, the plaintiffs filed an amended complaint containing master allegations against all of the defendants in all of the 310 cases included in this class action and also filed an amended complaint containing allegations specific to four of the company's underwriters, the company and two of its executive officers. In addition to the allegations mentioned above, the amended complaint alleges that the underwriters (i) used their analysts to manipulate the stock market; and (ii) implemented schemes that allowed issuer insiders to sell their shares rapidly after an initial public offering and benefit from high market prices. As concerns the company and its two executive officers in particular, the amended complaint alleges that (i) the company's registration statement was materially false and misleading because it failed to disclose the additional commissions and compensation to be received by underwriters; (ii) the two named executive officers learned of or recklessly disregarded the alleged misconduct of the underwriters; (iii) the two named executive officers had motive and opportunity to engage in alleged wrongful conduct due to personal holdings of the company's stock and the fact that an alleged artificially inflated stock price could be used as currency for acquisitions; and (iv) the two named executive officers, by virtue of their positions with the company, controlled the company and the contents of the registration statement and had the ability to prevent its issuance or cause it to be corrected. The plaintiffs in this suit seek an unspecified amount for damages suffered.

In July 2002, the issuers filed a motion to dismiss the plaintiffs' amended complaint and a decision was rendered on February 19, 2003. Only one of the claims against the company was dismissed. On October 8, 2002, the claims against its officers were dismissed pursuant to the terms of Reservation of Rights and Tolling Agreements entered into with the plaintiffs.

In June 2004, an agreement of partial settlement was submitted to the court for preliminary approval. The proposed partial settlement was between the plaintiffs, the issuer defendants in the consolidated actions, the issuer officers and directors named as defendants, and the issuers' insurance companies. The court granted the preliminary approval motion on February 15, 2005, subject to certain modifications. On August 31, 2005, the court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The court also appointed the notice administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members by January 15, 2006. The settlement fairness hearing occurred on April 24, 2006, and the court reserved decision at that time.

While the partial settlement was pending approval, the plaintiffs continued to litigate against the underwriter defendants. The district court directed that the litigation proceed within a number of "focus cases" rather than in all of the 310 cases that have been consolidated. The company's case is not one of these focus cases. On October 13, 2004, the district court certified the focus cases as class actions. The underwriter defendants appealed that ruling, and on December 5, 2006, the Court of Appeals for the Second Circuit reversed the district court's class certification decision.

On April 6, 2007, the Second Circuit denied the plaintiffs' petition for rehearing of that decision and, on May 18, 2007, the Second Circuit denied the plaintiffs' petition for rehearing en banc. In light of the Second Circuit's opinion, liaison counsel for all issuer defendants, including the company, informed the court that this settlement cannot be approved, because the defined settlement class, like the litigation class, cannot be certified. On June 25, 2007, the district court entered an order terminating the settlement agreement. On August 14, 2007, the plaintiffs filed their second consolidated amended class-action complaints against the focus cases and, on September 27, 2007, again moved for class certification. On November 12, 2007, certain of the defendants in the focus cases moved to dismiss the second consolidated amended class-action complaints. On March 26, 2008, the district court denied the motions to dismiss, except as to Section 11 claims raised by those plaintiffs who sold their securities for a price in excess of the initial

offering price and those who purchased outside of the previously certified class period. Briefing on the class certification motion was completed in May 2008. That motion was withdrawn without prejudice on October 10, 2008.

Due to the inherent uncertainties of litigation, the final outcome of the case is uncertain and it is not possible to determine the amount of any possible losses. The company will continue to defend its position in this litigation that the claims against it, and its officers, are without merit. Accordingly, no provision for this case has been made in the interim consolidated financial statements as at November 30, 2008.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

8 Share Capital

On November 6, 2008, the company announced that its Board of Directors had authorized a renewal of its share repurchase program, by way of a normal course issuer bid on the open market, of up to 10% of its public float (as defined by the Toronto Stock Exchange), or 2,738,518 subordinate voting shares, at the prevailing market price. The company expects to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The period of the normal course issuer bid commenced on November 10, 2008, and will end on November 9, 2009, or on an earlier date if the company repurchases the maximum number of shares permitted under the bid. The program does not require the company to 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.

On November 10, 2008, the company announced that its Board of Directors had authorized a substantial issuer bid (the “Offer”) to purchase for cancellation up to 8,823,529 subordinate voting shares for an aggregate purchase price not to exceed CA$30,000,000. The Offer is being made by way of a “modified Dutch Auction” pursuant to which shareholders might tender all or a portion of their shares (i) at a price not less than CA$3.40 per share and not more than CA$3.90 per share, in increments of CA$0.05 per share, or (ii) without specifying a purchase price, in which case their shares would be purchased at the purchase price determined in accordance with the Offer. The Offer expired on December 16, 2008 (note 14).

Upon the announcement of the Offer, the company suspended the normal course issuer bid referred to above, until 20 business days following the expiration of the Offer.

The following tables summarize changes in share capital for the three months ended November 30, 2007 and 2008.

	Three months ended November 30, 2007				
	Multiple voting shares		Subordinate voting shares		
	Number	Amount	Number	Amount	Total amount
			(unaudited)		
Balance as at August 31, 2007	36,643,000	$ 1	32,361,561	$ 150,018	$ 150,019
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	2	2
Redemption of share capital	–	–	(29,200)	(135)	(135)
Balance as at November 30, 2007	36,643,000	$ 1	32,332,361	$ 149,885	$ 149,886

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

	Three months ended November 30, 2008				
	Multiple voting shares		Subordinate voting shares		
	Number	Amount	Number	Amount	Total amount
			(unaudited)		
Balance as at August 31, 2008	36,643,000	$ 1	30,783,705	$ 142,785	$ 142,786
Exercise of stock options	–	–	12,500	26	26
Redemption of share capital	–	–	(176,914)	(821)	(821)
Balance as at November 30, 2008	36,643,000	$ 1	30,619,291	$ 141,990	$ 141,991

9 Net Research and Development Expenses

Net research and development expenses comprise the following:

	Three months ended November 30,	
	2008	2007
	(unaudited)	
Gross research and development expenses	$ 8,612	$ 7,486
Research and development tax credits	(1,391)	(1,474)
	$ 7,221	$ 6,012

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

10 Income Taxes

For the three months ended November 30, 2007 and 2008, the reconciliation of the income tax provision calculated using the combined Canadian federal and provincial statutory income tax rate with the income tax provision in the financial statements is as follows:

	Three months ended November 30,	
	2008	2007
	(unaudited)	
Income tax provision at combined Canadian federal and provincial statutory tax rate (31% in 2008 and 32% in 2007)	$ 2,203	$ 374
Increase (decrease) due to:		
Foreign income taxed at different rates	(19)	88
Non-taxable income	(48)	(81)
Non-deductible expenses	172	222
Foreign exchange effect of translation of foreign integrated subsidiaries	(836)	127
Other	177	157
Unrecognized future income tax assets on temporary deductible differences and unused tax losses and deductions	191	375
	$ 1,840	$ 1,262

The income tax provision consists of the following:

	2008	2007
Current	$ (61)	$ 1,181
Future	1,710	(294)
Valuation allowance	191	375
	1,901	81
	$ 1,840	$ 1,262

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

11 Earnings per Share

The following table summarizes the reconciliation of the basic weighted average number of shares outstanding and the diluted weighted average number of shares outstanding:

	Three months ended November 30,	
	2008	2007
	(unaudited)	
Basic weighted average number of shares outstanding (000's)	67,340	69,000
Plus dilutive effect of:		
Stock options (000's)	125	401
Restricted share units (000's)	173	201
Deferred share units (000's)	79	70
Diluted weighted average number of shares outstanding (000's)	67,717	69,672
Stock awards excluded from the calculation of the diluted weighted average number of shares because their exercise price was greater than the average market price of the common shares (000's)	2,045	1,118

12 Segment Information

The company is organized under two reportable segments: the Telecom Division and the Life Sciences and Industrial Division. The Telecom Division offers integrated test solutions and network monitoring systems to network service providers, cable TV operators, system vendors and component manufacturers throughout the global telecommunications industry. The Life Sciences and Industrial Division offers solutions in medical-device and opto-electronics assembly, fluorescence microscopy and other life sciences sectors.

The following tables present information by segment:

	Three months ended November 30, 2008		
	Telecom Division	Life Sciences and Industrial Division	Total
		(unaudited)	
Sales	$ 41,159	$ 5,204	$ 46,363

Earnings from operations	$	1,355	$	738	$	2,093
Unallocated items						
Interest income						466
Foreign exchange gain						4,568
Earnings before income taxes						7,127
Income taxes						1,840
Net earnings for the period					$	5,287

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

	Three months ended November 30, 2007		
	Telecom Division	Life Sciences and Industrial Division	Total
		(unaudited)	
Sales	$ 35,365	$ 5,620	$ 40,985
Earnings from operations	$ 21	$ 281	$ 302
Unallocated items			
Interest income			1,483
Foreign exchange loss			(616)
Earnings before income taxes			1,169
Income taxes			1,262
Net loss for the period			$ (93)

Total assets by reportable segment are detailed as follows:

	As at November 30, 2008	As at August 31, 2008
	(unaudited)	
Total assets		
Telecom Division	$ 132,021	$ 145,168
Life Sciences and Industrial Division	8,204	9,571
Unallocated assets	117,353	138,327
	$ 257,578	$ 293,066

Unallocated assets are comprised of cash, short-term investments, other receivables on forward exchange contracts, income taxes and tax credits recoverable and future income tax assets.

13 Differences between Canadian and U.S. GAAP

These interim consolidated financial statements are prepared in accordance with Canadian GAAP and significant differences in measurement and disclosure from U.S. GAAP are set out in note 19 to the company's most recent annual consolidated financial statements. This note describes significant changes occurring since the most recent annual consolidated financial statements and provides a quantitative analysis of all significant differences. All disclosures

required in annual financial statements under U.S. GAAP and Regulation S-X of the Securities and Exchange Commission in the United States have not been provided in these interim consolidated financial statements.

Statements of earnings

For the three months ended November 30, 2007 and 2008, there were no significant differences between the net earnings (loss) under Canadian GAAP as compared to U.S. GAAP.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Reconciliation of shareholders' equity to conform to U.S. GAAP

The following summary sets out the significant differences between the company's reported shareholders' equity under Canadian GAAP as compared to U.S. GAAP:

	As at November 30, 2008 (unaudited)	As at August 31, 2008
Shareholders' equity in accordance with Canadian GAAP	$ 222,915	$ 295,515
Goodwill	(10,856)	(12,640)
Stock appreciation rights	(73)	(73)
Shareholders' equity in accordance with U.S. GAAP	$ 211,986	$ 246,802

Research and development tax credits

Under Canadian GAAP, all research and development tax credits are recorded as a reduction of gross research and development expenses. Under U.S. GAAP, tax credits that are utilizable against income taxes payable are recorded in the income taxes. These tax credits amounted to $980,000 and $896,000 for the three months ended November 30, 2007 and 2008, respectively. This difference has no impact on the net earnings (loss) and the net earnings (loss) per share for the reporting periods.

Statements of cash flows

For the three months ended November 30, 2007 and 2008, there were no significant differences between the statements of cash flows under Canadian GAAP as compared to U.S. GAAP, except for the subtotal before change in non-cash operating items, whose presentation is not permitted under U.S. GAAP.

New accounting standards and pronouncements

Adopted in fiscal 2009

In September 2006, the Financial Accounting Standard Board (FASB) issued SFAS 157, "Fair Value Measurements", which establishes a framework for measuring fair value in GAAP and is applicable to other accounting pronouncements, in which fair value is considered to be the relevant measurement attribute. SFAS 157 also expands disclosures about fair value measurement. In February 2008, the FASB amended SFAS 157 to exclude leasing transactions and to delay the effective date by one year for non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a non-recurring basis. This statement is effective for fiscal years beginning after November 15, 2007. The company adopted this statement on September 1, 2008, and its adoption had no effect on its consolidated financial statements.

In February 2007, the FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of FASB Statement No. 115", which permits entities to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of this statement apply only to entities that elect the fair value option. However, the amendment to SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", applies to all entities with available-for-sale and trading securities. This statement is effective for fiscal years beginning after November 15, 2007. The company adopted this statement on September 1, 2008, and it did not elect to use the fair value option as of the date of adoption.

Table of Contents

EXFO Electro-Optical Engineering Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

To be adopted after fiscal 2009

In December 2007, the FASB issued SFAS 141(R), "Business Combinations", and SFAS 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51". These new standards will significantly change the accounting and reporting for business combination transactions and noncontrolling (minority) interests in consolidated financial statements. SFAS 141(R) and SFAS160 are required to be adopted simultaneously and are effective for the first annual reporting period beginning on or after December 15, 2008. Earlier adoption is prohibited. The company will adopt this statement on September 1, 2009, and is currently evaluating the impact the adoption of SFAS 141(R) and SFAS 160 will have on its consolidated financial statements.

In March 2008, the FASB issued SFAS 161, "Disclosure about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133", which will require entities to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flow. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The company will adopt this statement on September 1, 2009, and is currently evaluating the impact its adoption will have on its note disclosures related to derivative instruments and hedging activities.

In April 2008, the FASB issued the FASB staff position (FSP) FAS 142-3, "Determination of the Useful Lives of Intangible Assets". This FSP amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS 142, "Goodwill and Other Intangible Assets". The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset under SFAS 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS 141 (revised 2007), "Business Combinations", and other U.S. generally accepted accounting principles (GAAP). This FSP shall be effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. The guidance for determining the useful life of a recognized intangible asset in paragraphs 7–11 of this FSP shall be applied prospectively to intangible assets acquired after the effective date. The disclosure requirements in paragraphs 13–15 shall be applied prospectively to all intangible assets recognized as of, and subsequent to, the effective date. The company will adopt this FSP on September 1, 2009, and is currently evaluating the impact its adoption will have on its consolidated financial statements.

In May 2008, the FASB issued SFAS 162, "The Hierarchy of Generally Accepted Accounting Principles". The new standard is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with U.S. GAAP for non-governmental entities. For non-governmental entities, the guidance in SFAS 162 replaces that prescribed in Statement on Auditing Standards (SAS) No. 69, "The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles" and will become effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board's amendments to AU Section 411, "The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles". The company is currently evaluating the impact the adoption of SFAS 162 will have on its consolidated financial statements.

14 Subsequent Event

On December 18, 2008, pursuant to its substantial issuer bid (note 8), the company purchased for cancellation 7,692,307 subordinated voting shares for an aggregate purchase price of CA$30,000,000, excluding related fees. The company used cash and short-term investments to fund the repurchase of shares.

Table of Contents

Management's Discussion and Analysis of Financial Condition
and Results of Operations

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, anticipate, intend, could, estimate, continue, or the negative or comparable terminology 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 consolidation in the global telecommunications test, measurement and monitoring industry; capital spending levels in the telecommunications, life sciences and high-precision assembly sectors; concentration of sales; fluctuating exchange rates and our ability to execute in these uncertain conditions; the effects of the additional actions we have taken in response to such economic uncertainty (including our ability to quickly adapt cost structures with anticipated levels of business, ability to manage inventory levels with market demand); market acceptance of our new products and other upcoming products; limited visibility with regards to customer orders and the timing of such orders; our ability to successfully integrate our acquired and to-be-acquired businesses; our ability to successfully expand international operations; the retention of key technical and management personnel; and future economic, competitive, financial and market conditions, including any slow-down or recession in the global economy. 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 our Annual Report, on Form 20-F, and our other filings with the U.S. Securities and Exchange Commission and the Canadian securities commissions. 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 January 8, 2009.

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

INDUSTRY OVERVIEW

The fundamental drivers for increased bandwidth and convergence towards IP-based networks in the global telecommunications industry remain solid for the moment. However, it is still unknown what impact the current recession will have on global telecom investment levels, particularly in the United States and Western Europe. The growth in bandwidth demand, the intense competition between telecom operators (telcos) and cable companies (cablecos), as well as the various benefits of new converged IP networks (attracting new applications and revenues while reducing cost of operation) are reasons several operators may continue investing in broadband deployments and IP convergence.

Table of Contents

Global Internet bandwidth demand is fuelled by a wide range of applications like video streaming, Web gaming, etc. TeleGeography Research estimated that global Internet bandwidth increased at a compound annual growth rate (CAGR) of 54% from 2004 to 2008. This trend will likely remain strong in the years to come with upcoming deployments of Internet protocol television (IPTV), high-definition Internet protocol television (HD-IPTV) and increased online video streaming, since these applications, among others, will consume a colossal amount of additional bandwidth. As a result, telcos and cablecos will likely maintain significant investments in their access networks in order to provide differentiated, revenue-generating services to attract and retain consumers, who are increasingly relying on broadband network services for their work, entertainment and everyday activities.

As the volume of IP traffic, number of applications and quantity of consumers are increasing, so is the need for a 24/7, real-time service assurance solution that monitors IP traffic at the application level, from the access to the core network, as this is the best method for wireline and wireless operators to minimize the cost to operate their networks and provide a superior customer experience.

As well, it is now clear from a telco perspective, that fiber-to-the-home (FTTH) is becoming the access network architecture of choice for network operators. It allows them to meet heightened bandwidth requirements and future-proof their access networks, as residential bandwidth requirements are growing from the 1 to 5 Mbit/s (megabits per second) of the past to the 30 to 100 Mbit/s required in the long-term to assure multiple HD-IPTV channels, online gaming, high-speed content-rich Internet, VoIP (voice-over-Internet protocol) telephony and a myriad of other IP-based applications. Some projects, however, might be delayed based on the ability to fund such projects. Hybrid architectures, combining copper and fiber (fiber-to-the-curb, or FTTC, and fiber-to-the-node, or FTTN), will also keep expanding in the short term, since they are less-expensive methods to increase bandwidth and can be mass-deployed faster.

These investment decisions are applicable not only to green-field deployments and high-rise buildings, but also to larger-scale rollouts as long-term operating costs are less than FTTC and FTTN. It is noteworthy to mention that the cost of deploying FTTH has largely fallen over the last four years as volume increased and deployment tools, like those we offer, are making the task increasingly simple and efficient. We are only at the early stages of fiber deployments in access networks, both in the Americas and around the world. It is also worth noting that Western Europe and even China have become increasingly committed to deploying FTTH networks, given their high population density.

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 now seeing early deployments and becoming mainstream, while the upcoming 100 Gbit/s Ethernet is in the early stage of field trials by a selected few operators. The deployment of these solutions is expected to be significantly more economical, especially if trenches need to be dug in order to deploy new fiber in metro or long-distance routes.

As telecommunication networks are being transformed to provide IP-based voice, video and data capabilities, legacy SONET/SDH standards, which were first established in the mid-1980s and implemented until 2005, do not have the payload flexibility to seamlessly and efficiently mix and transport video with voice and data. These networks will not be capable to efficiently carry these emerging IP-based services as they are designed for public switched telephone network (PSTN), point-to-point voice transmission only. As a result, with new SONET/SDH standards, which are part of what the industry is calling next-gen networks, telco operators are increasingly turning to next-generation, IP-based networks to allow for more flexible and efficient transport of applications and services, and to offer customers higher-margin triple-play services and even quadruple-play services as wireline and wireless technologies become increasingly interconnected. Finally, as subscribers of these new services reach a critical mass, telcos are relying on service assurance solutions to ensure that the quality of service (QoS) and quality of experience (QoE) demanded by

users are optimal in the post-deployment phase.

These market dynamics positively affected telecom test and monitoring suppliers in the first quarter of fiscal 2009. However, deteriorating macro-economic conditions in the United States and Western Europe could instigate a slowdown in capital spending among customers that would necessarily reduce demand for our test and monitoring solutions.

Table of Contents

COMPANY OVERVIEW

We reported sales of $46.4 million in the first quarter of fiscal 2009, which represented an increase of 13.1% year-over-year. We also reported record-high net accepted orders of $52.3 million in the first quarter of fiscal 2009 for a book-to-bill ratio of 1.13. Total sales for the first quarter of fiscal 2009 included $4.5 million from newly acquired Brix Networks Inc. and Navtel Communications Inc. Excluding the impact of theses two acquisitions, we would have posted year-over-year organic sales growth of 2.1% in the first quarter of fiscal 2009.

Looking at the bottom line, we generated GAAP net earnings of $5.3 million, or $0.08 per diluted share, in the first quarter of fiscal 2009, compared to a net loss of $93,000, or $0.00 per share, for the same period last year. Net earnings for the first quarter of fiscal 2009 were positively and significantly affected by the weaker value of the Canadian dollar compared to the US dollar. During the first quarter of fiscal 2009, we reported a foreign exchange gain of $4.6 million, compared to a foreign exchange loss of $616,000 for the same period last year. Net earnings per diluted share in the first quarter of 2009 included charges of $0.02 for stock-based compensation costs and the after-tax amortization expense for intangible assets. EBITDA (earnings before interest, income taxes, depreciation and amortization) reached $9.1 million, or 19.7% of sales in the first quarter of fiscal 2009, compared to $1.4 million, or 3.4% of sales for the same period last year (see further in this document for a complete reconciliation of EBITDA to GAAP net earnings/loss).

During the first quarter of fiscal 2009, we faced a substantial and sudden decrease in the value of the Canadian dollar versus the US dollar, which had a two-fold positive impact on our financial results. Firstly, the average value of the Canadian dollar decreased 13.9% in the first quarter of fiscal 2009, compared to the same period last year. Given that most of our sales are denominated in US dollars but a significant portion of our expenses are denominated in Canadian dollars, our financial resulted were positively affected as these expenses (denominated in Canadian dollars) were reduced when translated in US dollars for reporting purposes. Secondly, we recorded an exchange gain of $4.6 million, which represents the effect of the 14.1% decrease (compared to August 31, 2008) in the value of the Canadian dollar versus the US dollar on our balance sheet items denominated in foreign currencies. In comparison, for the same period last year, we reported a foreign exchange loss of $616,000. During that period, the average value of the Canadian dollar increased 13.8% compared to the US dollar year-over-year and the period-end value of the Canadian dollar increased 5.6% compared to August 31, 2007.

On November 6, 2008, we announced that our Board of Directors had authorized a renewal of our share repurchase program, by way of a normal course issuer bid on the open market, of up to 10% of our public float (as defined by the Toronto Stock Exchange), or 2.7 million subordinate voting shares, at the prevailing market price. We expect to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The period of the normal course issuer bid started on November 10, 2008, and will end on November 9, 2009, 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.

On November 10, 2008, we announced that our Board of Directors had authorized a substantial issuer bid (the "Offer") to purchase for cancellation up to 8.8 million subordinate voting shares for an aggregate purchase price not to exceed CA$30 million. The Offer is being made by way of a "modified Dutch Auction" pursuant to which shareholders may tender all or a portion of their shares (i) at a price not less than CA$3.40 per share and not more than CA$3.90 per share, in increments of CA$0.05 per share, or (ii) without specifying a purchase price, in which case their shares will be purchased at the purchase price determined in accordance with the Offer. The Offer expired on December 16, 2008, and, on December 18, 2008, we purchased for cancellation 7.7 million subordinated voting shares for an aggregate purchase price of CA$30 million, excluding related fees. We used cash and short-term investments to fund the repurchase of shares.

Upon the approval of the Offer, we suspended the normal course issuer bid referred to above, until 20 business days following the expiration of the Offer.

Table of Contents

During the first quarter of fiscal 2009, we launched five new products, including a new software release for the Transport Blazer product line that delivers unprecedented insight into 40 Gbit/s network behavior; new software releases for the InterWatch platform and Packet Blazer product line to support the migration of voice and video applications to the IPv6 (Internet Protocol, version 6) addressing scheme; and expanded Ethernet test capabilities on the Power Blazer product line through multistream, quality of service (QoS) support. Sales from products that have been on the market two years or less represented 33.1% of total sales in the first quarter of fiscal 2009.

OUR STRATEGY, KEY PERFORMANCE INDICATORS AND CAPABILITY TO DELIVER RESULTS

For a complete description of our strategy and the related key performance indicators, as well as our capability to deliver results in fiscal 2009, please refer to the corresponding sections in our most recent Annual Report, filed with the securities commissions.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

For a complete description of our critical accounting policies and estimates, please refer to the corresponding section in our most recent Annual Report, filed with the securities commissions. The following details the changes in critical accounting policies that were adopted in fiscal 2009 and those to be adopted after 2009.

Adopted in fiscal 2009

In December 2006, the Canadian Institute of Chartered Accountants (CICA) issued three new sections, which provide a complete set of disclosure and presentation requirements for financial instruments: Section 3862, “Financial Instruments – Disclosures”; Section 3863, “Financial Instruments – Presentation”; and Section 1535, “Capital Disclosures”.

Section 3862 replaces the disclosure portion of Section 3861, “Financial Instruments – Disclosure and Presentation”. The new standard places increased emphasis on disclosures regarding risks associated with both recognized and unrecognized financial instruments and how these risks are managed. It is also intended to remove any duplicate disclosures and simplify the disclosures about concentrations of risk, credit risk, liquidity risk and price risk previously found in Section 3861.

Section 3863 carries forward the presentation requirements from Section 3861, unchanged.

Section 1535 applies to all entities, regardless of whether they have financial instruments and are subject to external capital requirements. The new section requires disclosure of information about an entity’s objectives, policies and processes for managing capital, as well as quantitative data about capital and whether the entity has complied with any capital requirements.

We adopted these new standards on September 1, 2008 and provided the required disclosure in our interim consolidated financial statements.

In June 2007, the CICA issued Section 3031, “Inventories”. This standard requires the measurement of inventories at the lower of cost and net realizable value and includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either first-in, first-out (FIFO) or weighted average cost formula to measure the cost of inventories and requires the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. The new standard applies to fiscal years beginning on or after January 1, 2008. We adopted this new standard on September 1, 2008, and its

adoption had no effect on our consolidated financial statements.

In June 2007, the CICA amended Section 1400, "General Standards of Financial Statement Presentation" to include new requirements regarding an entity's ability to continue as a going concern. These amendments apply to fiscal years beginning on or after January 1, 2008. We adopted these amendments on September 1, 2008, and their adoption had no effect on our consolidated financial statements.

Table of Contents

To be adopted after fiscal 2009

In February 2008, the CICA issued Section 3064, "Goodwill and intangible assets", which supersedes Section 3062, "Goodwill and other intangible assets" and Section 3450, "Research and development costs". Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill remain unchanged from the standards included in Section 3062. This new section applies to fiscal years beginning on or after October 1, 2008. We will adopt this new standard on September 1, 2009, and have not yet determined the effects its adoption will have on our consolidated financial statements.

Table of Contents

RESULTS OF OPERATIONS

The following discussion and analysis of our consolidated financial condition and results of operations for the three months ended November 30, 2007 and 2008, should be read in conjunction with our interim consolidated financial statements and the related notes thereto. Our interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP) and significant differences in measurement and disclosure from United States generally accepted accounting principles (U.S. GAAP) are set out in note 13 to our interim consolidated financial statements. Our measurement currency is the Canadian dollar, although we report our financial statements in US dollars. The following table sets forth interim consolidated statements of earnings data in thousands of US dollars, except per share data, and as a percentage of sales for the periods indicated:

	Three months ended November 30,		Three months ended November 30,	
	2008	2007	2008	2007
	(unaudited)		(unaudited)	
Consolidated statements of earnings data:				
Sales	$ 46,363	$ 40,985	100.0%	100.0%
Cost of sales (1)	17,480	18,144	37.7	44.3
Gross margin	28,883	22,841	62.3	55.7
Operating expenses				
Selling and administrative	17,091	14,817	36.9	36.2
Net research and development	7,221	6,012	15.6	14.7
Amortization of property, plant and equipment	1,159	976	2.5	2.3
Amortization of intangible assets	1,319	734	2.8	1.8
Total operating expenses	26,790	22,539	57.8	55.0
Earnings from operations	2,093	302	4.5	0.7
Interest income	466	1,483	1.0	3.7
Foreign exchange gain (loss)	4,568	(616)	9.9	(1.5)
Earnings before income taxes	7,127	1,169	15.4	2.9
Income taxes				
Current	(61)	1,181	(0.1)	2.9
Future	1,901	81	4.1	0.2
	1,840	1,262	4.0	3.1
Net earnings (loss) for the period	$ 5,287	$ (93)	11.4%	(0.2)%
Basic and diluted net earnings (loss) per share	$ 0.08	$ (0.00)		
Segment information:				
Sales:				
Telecom Division	$ 41,159	$ 35,365	88.8%	86.3%
Life Sciences and Industrial Division	5,204	5,620	11.2	13.7
	$ 46,363	$ 40,985	100.0%	100.0%
Earnings from operations:				
Telecom Division	$ 1,355	$ 21	2.9%	0.1%
Life Sciences and Industrial Division	738	281	1.6	0.6
	$ 2,093	$ 302	4.5%	0.7%

Research and development data:				
Gross research and development	$ 8,612	$ 7,486	18.6%	18.3%
Net research and development	$ 7,221	$ 6,012	15.6%	14.7%

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

Table of Contents

SALES

For the three months ended November 30, 2008, our global sales increased 13.1% to $46.4 million from $41.0 million for the same period last year, with an 89%-11% split in favor of our Telecom Division (86%-14% for the same period last year).

Telecom Division

For the three months ended November 30, 2008, our Telecom Division sales increased 16.4% to $41.2 million from $35.4 million for the same period last year.

In the first quarter of fiscal 2009, we posted year-over-year sales growth mainly due to the market acceptance as well as market share gain of our next-generation IP test solutions, and due to the inclusion of the sales of newly acquired Brix Networks and Navtel Communications' products. In fact, sales of Brix Network and Navtel Communications amounted to $4.5 million together for the quarter. Excluding these sales, our telecom sales would have increased 3.6% organically year-over-year. During the first quarter of fiscal 2009, we posted record-high sales and bookings of protocol test solutions and, unsurprisingly, our protocol test solutions represented our fastest-growing product line. Also, they represented more than 30% of our telecom sales in the first quarter of fiscal 2009, compared to more than 10% for the same period last year.

On the other hand, sales of optical test solutions slightly decreased during the first quarter of fiscal 2009, compared to the same period last year. This mainly results from lower sales in the Americas including Verizon's Fiber Optic Service (FIOS). Global sales to this top customer represented 4.0% ($1.6 million) of our telecom sales in the first quarter of fiscal 2009, compared to 13.1% ($4.6 million) for the same period last year. Excluding sales to this customer, our telecom sales would have increased 28.6% in the first quarter of fiscal 2009, compared to the same period last year. This shows that we have successfully diversified our customer base year-over-year. It should be noted that this customer was not our top customer during the first quarter of fiscal 2009 (second largest).

Finally, in the first quarter of fiscal 2009, foreign exchange losses on our forward exchange contracts, which are included in our telecom sales, amounted to $211,000 compared to foreign exchange gains of $1.3 million for the same period last year. In the first quarter of fiscal 2009, the average value of the Canadian dollar versus the US dollar decreased 13.9% compared to the same period last year.

Sales of our copper-access test solutions were slightly up in the first quarter of fiscal 2009, compared to the same period last year. During fiscal 2008, we launched the AXS-200 SharpTESTER, a new added-value product that integrates Consultronics (copper-access) core knowledge and intellectual property; the AXS-200 SharpTESTER platform also houses a new test module, the AXS-200/630 Triple-Play Test Set, which differentiates our access network offering from that of other vendors. These new, innovative products have yet to contribute to our sales for this market segment.

Life Sciences and Industrial Division

For the three months ended November 30, 2008, our Life Sciences and Industrial Division sales decreased 7.4% to $5.2 million from $5.6 million for the same period last year.

A significant portion of sales of that division are conducted through original equipment manufacturer (OEM) agreements. Consequently, we are dependent, to some extent, on the buying pattern of our customers. Moreover, a significant part of our product offering is related to manufacturing applications of consumer goods, which have been more susceptible to the state of the global economy.

Net bookings

Overall, for the two divisions, net accepted orders increased 19.7% year-over-year to a record-high $52.3 million in the first quarter of fiscal 2009 from $43.7 million for the same period last year, for a book-to-bill ratio of 1.13.

Table of Contents

This increase of bookings year-over-year is due to significant order acceleration in our Protocol test segment, lead by a major order amounting up to $4 million that was announced in the first quarter of fiscal 2009 when a Tier-1 wireless operator in North America has selected our converged service assurance solution to provide real-time monitoring of the quality of voice-over-IP (VoIP) and IP multimedia subsystem (IMS) services over its converged network.

Geographic distribution

In the first quarter of fiscal 2009, sales to the Americas, Europe, Middle-East and Africa (EMEA) and Asia-Pacific (APAC) accounted for 56%, 27% and 17% of global sales, respectively, compared to 58%, 24% and 18%, respectively for the same period last year.

In the first quarter of fiscal 2009, we reported year-over-year sales increases (in dollars) in every geographic area. In fact, sales to the Americas, EMEA and APAC increased (in dollars) 11.1%, 24.9% and 3.6%, respectively, which resulted in a slightly larger percentage of sales coming from international markets.

In the Americas, the increase in sales in the first quarter of fiscal 2009, compared to the same period last year, comes from every region; we posted a sales growth of 43.3%, 6.3% and 8.9% in Canada, United States and Latin America, respectively. In the United States, despite the decrease in sales to our top customer year-over-year, we were able to increase our sales in this region partially thanks to the contribution of Brix Networks and Navtel Communications whose sales were traditionally in that region. As mentioned above, during the first quarter of fiscal 2008, we benefited from aggressive FTTH rollouts from our top customer, and sales to this customer represented 11.3% ($4.6 million) of our global sales in the first quarter of fiscal 2008, compared to 3.5% ($1.6 million) for the same period this year. We believe that we did not lose market share with this particular customer in the first quarter of fiscal 2009. We believe we have expanded market share as we successfully got additional product-line approvals to partially offset the decline in optical business and came out to a significant growth in booking at that account during the last quarter. Excluding sales to this customer, sales to the United States would have increased 31.3% in dollars year-over-year; this shows that, overall, we have diversified our customer base and product mix year-over-year in this region. Finally, sales to Latin America fluctuate depending on the timing and scope of our customers' projects.

The increase in sales in the EMEA market, in dollars, in the first quarter of fiscal 2009, compared to the same period last year, is a result of our continued strategy from the last few years to aggressively develop this market in the past several years, to consistently invest in sales resources, and to develop stronger support and service operations in this region. In addition, many Tier-1 carriers in EMEA are migrating their traditional circuit-switched core networks to higher-speed, dense wavelength-division multiplexing (DWDM) and next-generation packet-based architectures, which is creating a market demand for our protocol test solutions as well as our DWDM, ROADM and fiber characterization test kits. Furthermore, we are leveraging our FTTx leadership gained in the United States to provide consultancy with many of the early adopters in this field in EMEA.

In the APAC market, we are seeing the continued return on investment of some specific optical, protocol as well as life sciences and industrial products developed and targeted for this important market. This increasingly competitive range, coupled with our steadily expanding market presence, is responsible for the higher sales in this region in the first quarter of fiscal 2009, compared to the same period last year.

Through our two divisions, we sell our products to a broad range of customers, including network service providers, network equipment manufacturers, wireless operators, cable TV operators, optical system and component manufacturers, as well as customers in the life sciences and high-precision assembly sectors. In the first quarter of fiscal 2009, no customer accounted for more than 10% of our global sales, and our top three customers accounted for 10.4% of our global sales. In the corresponding period last year our top customer accounted for 11.3% ($4.6 million) of our global sales, and our top three customers accounted for 16.5% of our global sales.

Table of Contents

GROSS MARGIN

Gross margin reached 62.3% of sales for the three months ended November 30, 2008, compared to 55.7% for the same period last year.

In the first quarter of fiscal 2009, gross margin reached its highest level since the second quarter of fiscal 2001. The increase in our gross margin in the first quarter of fiscal 2009, compared to the same period last year, can be explained by the following factors.

First, the impact of the fluctuations in the value of the Canadian dollar compared to the US dollar was twofold in the first quarter of fiscal 2009. Indeed, over the last several quarters, our procurement costs decreased as the Canadian dollar strengthen compared to the US dollar and as a significant portion of our raw material purchases is denominated in US dollars. This allowed us to improve our gross margin continually over the last quarters, as our raw material costs of parts purchased in US dollar are measured in Canadian dollar in our financial statements. In addition, the sudden decrease in the value of the Canadian dollar versus the US dollar resulted in a lower cost of goods sold expressed in US dollars in the statements of earnings. However, the increase of our procurement cost of raw materials purchased in US dollars, as a result of the sudden and recent decrease in the value of the Canadian dollar compared to the US dollar, will be seen in the next quarters, as these raw materials will be included in the cost of goods sold of products manufactured with these parts.

Secondly, in the first quarter of fiscal 2009, our gross margin was positively affected by the significant increase in sales of our protocol test solutions year-over-year, including those of Brix Networks and Navtel Communications, as these products have better margins than our other test solutions. Sales of protocol test solutions reached their highest level in the first quarter of fiscal 2009.

In addition, the significant increase in global sales year-over-year resulted in an increase in manufacturing activities, allowing us to better absorb our fixed manufacturing costs.

Finally, the operation of our manufacturing facility in China resulted in a larger portion of our sales coming from products manufactured in China; those products have a lower cost of goods than those manufactured in our facilities in Canada, thus resulting in an improvement in gross margin year-over-year.

Considering the expected sales growth in fiscal 2009, the expected increase in sales of protocol products and the full contribution of Brix Networks and Navtel Communications (which tend to generate higher margins), the cost-effective design of our products, our 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 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 costs, shifts in customer and product mix, under-absorption of fixed manufacturing costs, challenges encountered in the operation of our manufacturing facility in China and increases in product offerings by other suppliers in our industry. Finally, any increase in the strength of the Canadian dollar, compared to the US dollar, would have a negative impact on our gross margin in fiscal 2009 and beyond.

SELLING AND ADMINISTRATIVE

For the three months ended November 30, 2008, selling and administrative expenses were $17.1 million, or 36.9% of sales, compared to $14.8 million, or 36.2% of sales for the same period last year.

Brix Networks and Navtel Communications, which were acquired in the third quarter of fiscal 2008, contributed for the whole period to our selling and administrative expenses in the first quarter of fiscal 2009, which caused these expenses to increase compared to the same period last year. In addition, selling expenses for Brix Networks and Navtel Communications tend to be higher in percentage of sales than the rest of the business, as their sales cycle is much longer and complex than our other product lines.

In addition, during the first quarter of fiscal 2009, we continued intensifying our sales and marketing activities to develop our markets and leverage our significant research and development investments; this resulted in higher sales and marketing expenditures (including additional employees and expenses to support the launch of several new products and to increase brand name recognition), compared to the corresponding period last year.

However, during the first quarter of fiscal 2009, the substantial and sudden decrease in the average value of the Canadian dollar compared to the US dollar had a significant positive impact on our selling and administrative expenses, since a significant portion of these expenses are denominated in Canadian dollars and since these expenses increased year-over-year as our sales grew.

Also, during the first quarter of fiscal 2008, we discontinued certain product lines, which led to the lay-off of some of our sales and marketing personnel, resulting in severance expenses during that period.

For fiscal 2009, considering the expected increase in sales and the significant impact of the acquisitions of Brix Networks and Navtel Communications on our selling and administrative expenses—whose selling expenses tend to be higher, as their products deliver better margins compared to the rest of our product lines—we expect our selling and administrative expenses to increase in dollars and range between 32% and 34%. In particular, in fiscal 2009, we expect our commission expenses to increase as sales volume increases. Furthermore, considering our goal of becoming the leading player in the telecom test, measurement and monitoring space, we plan to continue intensifying our sales and marketing efforts, both domestic and international, which will also cause our expenses to rise. Finally, any increase in the strength of the Canadian dollar would also cause our selling and administrative expenses to increase, as a significant portion of these expenses are incurred in Canadian dollars.

RESEARCH AND DEVELOPMENT

Gross research and development expenses

For the three months ended November 30, 2008, gross research and development expenses totalled $8.6 million, or 18.6% of sales, compared to $7.5 million, or 18.3% of sales for the same period last year.

Brix Networks and Navtel Communications, which were acquired in the third quarter of fiscal 2008, contributed for the whole period to our gross research and development expenses in the first quarter of fiscal 2009, which caused these expenses to increase compared to the same period last year. In addition, Brix Networks and Navtel Communications tend to incur a higher percentage of sales for research and development expenses compared to our other product lines as their products are more software-intensive, although they deliver higher margins than most of our other product lines.

In addition, we intensified our research and development activities, namely in our software development center in Pune, India, which resulted in increased gross research and development expenses in the first quarter of fiscal 2009, compared to the same period last year.

However, during the first quarter of fiscal 2009, the significant and rapid decrease in the average value of the Canadian dollar compared to the US dollar also had a substantial positive effect on our gross research and development expenses as an important portion of these expenses are denominated in Canadian dollars and also because these expenses increased year-over-year.

Also, in the first quarter of fiscal 2008, we closed down our R&D operations in Budapest, Hungary, and certain R&D projects, which resulted in severance expenses during that period.

Tax credits

For the three months ended November 30, 2008, tax credits from the Canadian federal and provincial governments for research and development activities were $1.4 million, or 16.2% of gross research and development expenses, compared to $1.5 million, or 19.7% of gross research and development expenses for the same period last year.

Table of Contents

All our research and development tax credits are denominated in Canadian dollars. The significant and sudden decrease in the value of the Canadian dollar compared to the US dollar during the first quarter of fiscal 2009 had a negative impact on these tax credits expressed in US dollars.

However, that decrease in tax credits was offset in part by increased research and development activities in Canada where we are eligible to tax credits.

The decrease in research and development tax credits as a percentage of gross research and development expenses is mainly due to the fact that the portion of gross research and development incurred in Canada, where we are entitled to tax credits, was lower than last year following the establishment of our new software development center in India as well as the acquisition of Brix Networks, which is located in the United States. Our research and development activities conducted outside Canada do not entitle us to tax credits.

For fiscal 2009, we expect that our net research and development expenses will increase in dollars, and range between 14% and 16% of sales, given our focus on innovation, the addition of Brix Networks and Navtel Communications, whose products are software-intensive, the addition of software features in our products, our desire to gain market share and our goal to exceed customer expectations. Also, we are increasingly taking advantage of talent pools around the world with the establishment of a research and development center focused on software development in Pune, India. Finally, any increase in the strength of the Canadian dollar in the upcoming quarters would cause our net research and development expenses to increase, as a significant portion of these are incurred in Canadian dollars.

AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

For the three months ended November 30, 2008, amortization of property, plant and equipment was $1.2 million, compared to $976,000 for the same period last year.

The recent startup of our own manufacturing and research and development facilities in China and India, the upgrade of our IT systems, and the impact of the acquisition of Brix Networks and Navtel Communications in the third quarter of fiscal 2008 resulted in an increase in our amortization expenses in the first quarter of fiscal 2009, compared to the same period last year. However, the significant decrease in the average value of the Canadian dollar versus the US dollar in the first quarter of fiscal 2009, compared to the same period last year, limited the increase in our amortization expenses year-over-year as a significant portion of these expenses are denominated in Canadian dollars.

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. These intangible assets resulted in amortization expense of $1.3 million during the first quarter of fiscal 2009, compared to $734,000 for the same period last year.

The increase in amortization expenses in the first quarter of fiscal 2009, compared to the same period last year, is mainly due to the acquisition of Brix Networks core technology in the third quarter of 2008.

INTEREST INCOME

Our interest income mainly resulted from our short-term investments, less interests and bank charges. For the three months ended November 30, 2008, interest income amounted to $466,000, compared to $1.5 million for the same

period last year.

Table of Contents

The decrease in interest income in the first quarter of fiscal 2009, compared to the same period last year, is mainly due to the decrease of our cash and short-term investments following the cash payment of $41.0 million for the acquisitions of Brix Networks and Navtel Communications in the third quarter of fiscal 2008, the redemption of share capital for $8.5 million over the last 12 months, in accordance with our share buy-back program as well as the general reduction in interest rates year-over-year. In addition, the significant decrease in the average value of the Canadian dollar, compared to the US dollar year-over-year, contributed to the decrease in our interest income in the first quarter of fiscal 2009, compared to the same period last year, as it is denominated in Canadian dollars.

FOREIGN EXCHANGE GAIN (LOSS)

Foreign exchange gains and losses are mainly the result of the translation of operating activities denominated in currencies other than the Canadian dollar.

For the three months ended November 30, 2008, the foreign exchange gain amounted to $4.6 million compared to a foreign exchange loss of $616,000 for the same period last year.

During the first quarter of fiscal 2009, the value of the Canadian dollar significantly and rapidly decreased versus the US dollar compared to the previous quarter, which resulted in a foreign exchange gain in the first quarter of fiscal 2009. In fact, the period-end value of the Canadian dollar decreased 14.1% to CA$1.2372 = US$1.00 in the first quarter of fiscal 2009, compared to CA$1.0626 = US$1.00 at the end of the previous quarter. This represents the largest quarterly change in the value of the Canadian dollar compared to the US dollar in the history of the company. We also have to consider that the volume of operations denominated in foreign currency increased year-over-year, further increasing the exchange gain compared to the same period last year.

On the other hand, during the first quarter of fiscal 2008, the value of the Canadian dollar significantly and rapidly increased versus the US dollar compared to the previous quarter, which resulted in a significant foreign exchange loss in the first quarter of fiscal 2008. In fact, the period-end value of the Canadian dollar increased 5.6% to CA$1.0008 = US$1.00 in the first quarter of fiscal 2008, compared to CA$1.0564 = US$1.00 at the end of the previous quarter.

It should be noted that foreign exchange rate fluctuations also flow through the P&L line items as a significant portion of our operating items are denominated in Canadian dollars, and we report our results in US dollars. Consequently, the significant decrease in the average value of the Canadian dollar in the first quarter of fiscal 2009, compared to the same period last year, resulted in a significant and positive impact on our financial results. This was amplified by the fact that our operating activities incurred in Canadian dollars increased year-over-year. In fact, the average value of the Canadian dollar in the first quarter of fiscal 2009 was CA$1.1501 = US$1.00 versus CA$0.9901 = US$1.00 for the same period last year, representing a decrease of 13.9% in the average value of the Canadian dollar year-over-year.

We manage our exposure to currency risks with forward exchange contracts. In addition, some of our Canadian entities' operating activities are denominated in US dollars or other currencies, which further hedges these risks. However, any increase in the value of the Canadian dollar, compared to the US dollar, would have a negative impact on our operating results.

INCOME TAXES

For the three months ended November 30, 2008, our income tax expense totaled $1.8 million compared to $1.3 million for the same period last year.

For the three months ended November 30, 2008, we reported income tax expenses of $1.8 million on earnings before income taxes of $7.1 million, for an effective income tax rate of 25.8%. Our combined Canadian and provincial statutory tax rate is 31%. This situation mainly results from the fact that a significant portion of our foreign exchange gain is created by the translation of financial statements of our foreign integrated subsidiaries, and is therefore non-taxable. On the other hand, we continue to maintain a valuation allowance for some of our subsidiaries at loss and we have some non-deductible expenses, such as stock-based compensation costs. Otherwise, the actual tax rate would have been closer to the statutory tax rate.

Table of Contents

For the three months ended November 30, 2007, we reported income tax expenses of $1.3 million on earnings before income taxes of $1.2 million, for an effective income tax rate of 108%. This unusual situation mainly resulted from the fact that some expenses were non-deductible for tax purposes (mainly stock-based compensation expenses and foreign exchange losses created by the translation of financial statements of our foreign integrated subsidiaries) and the fact that we continue to maintain a valuation allowance for some of our subsidiaries at loss. In addition, we recorded income tax expenses for minimum taxes payable in certain tax jurisdictions, which taxes are not related to pre-tax earnings. Otherwise, the actual tax rate would have been closer to the statutory tax rate.

Please refer to note 10 to our interim consolidated financial statements for details on income taxes and a full reconciliation of the income tax provision.

LIQUIDITY AND CAPITAL RESOURCES

Cash requirements and capital resources

As at November 30, 2008, cash and short-term investments totalled $71.4 million, while our working capital was at $124.8 million. Our cash and short-term investments decreased $16.2 million in the first quarter of fiscal 2009, compared to the previous quarter, mainly due to the significant decrease in the value of the Canadian dollar compared to the US dollar. Indeed, we recorded an unrealized foreign exchange loss on our cash and short-term investments of $11.6 million. 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. In addition, we paid $1.5 million and $447,000 for the purchases of capital assets and the redemption of share capital, respectively. Finally, operating activities used cash flows of $2.7 million.

Our short-term investments consist of commercial paper issued by 13 (ten as at August 31, 2008) high-credit quality corporations and trusts; therefore, we consider the risk of non-performance of these financial instruments to be limited. None of these debt instruments are expected to be affected by a liquidity risk, and none of them represent asset-backed commercial paper. For the purposes of managing our cash position, we have established a cash management policy, which we follow and monitor on a regular basis. These short-term investments will be used for working capital and other general corporate purposes, including other potential acquisitions and our share repurchase programs.

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 cash contingent consideration payable for the acquisition of Brix Networks, the cash payment of CA$30 million (US$25.1 million) required in December 2008 under our substantial issuer bid, and the effect of our normal course issuer bid. In addition to these assets, we have unused available lines of credit totaling $9.5 million for working capital and other general corporate purposes and unused lines of credit of $10.2 million for foreign currency exposure related to forward exchange contracts. However, possible operating losses 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.

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

Cash flows used by operating activities were $2.7 million for the three months ended November 30, 2008, compared to $2.4 million for the same period last year.

Table of Contents

Cash flows used by operating activities in the first quarter of fiscal 2009 were mainly attributable to the net earnings after items not affecting cash of $7.3 million, offset by the negative net change in non-cash operating items of $10.0 million mainly due to the negative effect on cash of the increase of $7.3 million in our accounts receivable (due to timing of sales, as sales mainly occurred at the end of the quarter), the increase of $696,000 in our income taxes and tax credits recoverable (mainly tax credits earned during the quarter and not yet recovered), the increase of $542,000 in our prepaid expenses (fees paid for the substantial issuer bid), and the decrease of $1.1 million in our accounts payable and accrued liabilities, mainly due to timing of purchases and payments.

Cash flows used by operating activities in the first quarter of fiscal 2008 were mainly attributable to the net earnings after items not affecting cash of $3.3 million, offset by the negative net change in non-cash operating items of $5.7 million mainly due to the negative effect on cash of the increase of $458,000 in our income taxes and tax credits recoverable (mainly tax credits earned during the quarter and not yet recovered), the increase of $612,000 in our prepaid expenses, and the decrease of $5.7 million in our accounts payable and accrued liabilities, mainly due to timing of purchases and payments. The decrease of $1.2 million in our accounts receivable (timing and sequential decrease of sales) offset in part these negative effects on cash.

Investing activities

Cash flows provided by investing activities were $3.0 million for the three months ended November 30, 2008, compared to $1.5 million for the same period last year. In the first quarter of fiscal 2009, we disposed (net of acquisitions) of $4.5 million worth of short-term investments but paid $1.5 million for the purchase of capital assets. For the corresponding period last year, we disposed (net of acquisitions) $3.1 million worth of short-term investments and paid $1.6 million for the purchase of capital assets.

Financing activities

Cash flows used by financing activities were $421,000 for the three months ended November 30, 2008, compared to cash flows provided by financing activities of $525,000 for the same period last year. During the first quarter of fiscal 2009, we paid $447,000 for the redemption of share capital under our normal course issuer bid program and received $26,000 from the exercise of stock options. For the corresponding period last year, cash flows provided by financing activities were due to changes in bank loan of $699,000, offset by the cash payment of $174,000 for the redemption of share capital under our normal course issuer bid program.

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, 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 November 30, 2008, 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

December 2008 to August 2009	$	28,300,000	1.0616
September 2009 to August 2010		24,200,000	1.0760
September 2010 to August 2011		14,600,000	1.1221
September 2011		1,000,000	1.1278
Total	$	68,100,000	1.0807

Table of Contents

The fair value of forward exchange contracts, which represents the amount that the company would receive or pay to settle the contracts based on the forward exchange rate at period end, amounted to net gains of $62,000 as at August 31, 2008 and net losses of $8.0 million as at November 30, 2008, following the significant decrease in the value of the Canadian dollar compared to the US dollar during the quarter.

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 EXFO, four of the underwriters of our Initial Public Offering and some of our 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 EXFO'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 EXFO's Initial Public Offering; and (ii) the underwriters allegedly entering into agreements with customers whereby shares issued in connection with EXFO'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 19, 2002, the plaintiffs filed an amended complaint containing master allegations against all of the defendants in all of the 310 cases included in this class action and also filed an amended complaint containing allegations specific to four of EXFO's underwriters, EXFO and two of our executive officers. In addition to the allegations mentioned above, the amended complaint alleges that the underwriters (i) used their analysts to manipulate the stock market; and (ii) implemented schemes that allowed issuer insiders to sell their shares rapidly after an initial public offering and benefit from high market prices. As concerns EXFO and our two executive officers in particular, the amended complaint alleges that (i) EXFO's registration statement was materially false and misleading because it failed to disclose the additional commissions and compensation to be received by underwriters; (ii) the two named executive officers learned of or recklessly disregarded the alleged misconduct of the underwriters; (iii) the two named executive officers had motive and opportunity to engage in alleged wrongful conduct due to personal holdings of EXFO's stock and the fact that an alleged artificially inflated stock price could be used as currency for acquisitions; and (iv) the two named executive officers, by virtue of their positions with EXFO, controlled it and the contents of the registration statement and had the ability to prevent its issuance or cause it to be corrected. The plaintiffs in this suit seek an unspecified amount for damages suffered.

In July 2002, the issuers filed a motion to dismiss the plaintiffs' amended complaint and a decision was rendered on February 19, 2003. Only one of the claims against EXFO was dismissed. On October 8, 2002, the claims against its officers were dismissed pursuant to the terms of Reservation of Rights and Tolling Agreements entered into with the plaintiffs.

In June 2004, an agreement of partial settlement was submitted to the court for preliminary approval. The proposed partial settlement was between the plaintiffs, the issuer defendants in the consolidated actions, the issuer officers and directors named as defendants, and the issuers' insurance companies. The court granted the preliminary approval motion on February 15, 2005, subject to certain modifications. On August 31, 2005, the court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The court also appointed the notice administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members by January 15, 2006. The settlement fairness hearing occurred on April 24, 2006, and the court reserved decision at that time.

While the partial settlement was pending approval, the plaintiffs continued to litigate against the underwriter defendants. The district court directed that the litigation proceed within a number of "focus cases" rather than in all of the 310 cases that have been consolidated. EXFO's case is not one of these focus cases. On October 13, 2004, the district court certified the focus cases as class actions. The underwriter defendants appealed that ruling, and on December 5, 2006, the Court of Appeals for the Second Circuit reversed the district court's class certification decision.

Table of Contents

On April 6, 2007, the Second Circuit denied the plaintiffs' petition for rehearing of that decision and, on May 18, 2007, the Second Circuit denied the plaintiffs' petition for rehearing en banc. In light of the Second Circuit's opinion, liaison counsel for all issuer defendants, including EXFO, informed the court that this settlement could not be approved, because the defined settlement class, like the litigation class, could not be certified. On June 25, 2007, the district court entered an order terminating the settlement agreement. On August 14, 2007, the plaintiffs filed their second consolidated amended class action complaints against the focus cases and, on September 27, 2007, again moved for class certification. On November 12, 2007, certain of the defendants in the focus cases moved to dismiss the second consolidated amended class action complaints. On March 26, 2008, the district court denied the motions to dismiss, except as to Section 11 claims raised by those plaintiffs who sold their securities for a price in excess of the initial offering price and those who purchased outside of the previously certified class period. Briefing on the class certification motion was completed in May 2008. That motion was withdrawn without prejudice on October 10, 2008.

Due to the inherent uncertainties of litigation, the final outcome of the case is uncertain and it is not possible to determine the amount of any possible losses. We will continue to defend our position in this litigation that the claims against EXFO, and our officers, are without merit. Accordingly, no provision for this case has been made in the interim consolidated financial statements as at November 30, 2008.

SHARE CAPITAL AND STOCK-BASED COMPENSATION PLANS

Share capital

As at January 8, 2009, EXFO had 36,643,000 multiple voting shares outstanding, entitling to ten votes each and 22,930,178 subordinate voting shares outstanding. The multiple voting shares and the subordinate voting shares are unlimited as to number and without par value. On December 18, 2008, we redeemed 7.7 million subordinated voting shares for a total consideration of CA$30 million, plus related fees, based on our substantial issuer bid program.

Long-Term Incentive Plan and Deferred Share Unit Plan

The aggregate number of subordinate voting shares covered by stock options, restricted share units (RSUs) and deferred share units (DSUs) granted under the Long-Term Incentive Plan and the Deferred Share Unit Plan was 3,112,200 as at November 30, 2008. The maximum number of subordinate voting shares issuable under these two plans cannot exceed 6,306,153 shares. The following tables summarize information about stock options, RSUs and DSUs granted to the members of the Board of Directors and to Management and Corporate Officers of the company and its subsidiaries as at November 30, 2008:

Stock Options	Number	% of issued and outstanding	Weighted average exercise price
Chairman of the Board, President and CEO (one individual)	179,642	10%	$9.05
Board of Directors (four individuals)	148,807	8%	$6.19
Management and Corporate Officers (eight individuals)	212,139	12%	$14.49
	540,588	30%	$10.40

Restricted Share Units (RSUs)	Number	% of issued

		and outstanding
Chairman of the Board, President and CEO (one individual)	150,714	12%
Management and Corporate Officers (eleven individuals)	525,084	43%
	675,798	56%

Table of Contents

Deferred Share Units (DSUs)	Number	% of issued and outstanding
Board of Directors (five individuals)	90,517	100%

OFF-BALANCE SHEET ARRANGEMENTS

As at November 30, 2008, our off-balance sheet arrangements consisted of letters of guarantee. As at November 30, 2008, our letters of guarantee amounted to $5.4 million; these letters of guarantee expire at various dates through fiscal 2011. From this amount, we had $1.1 million worth of letters of guarantee for our own selling and purchase requirements, which were reserved from one of our lines of credit. The remainder in the amount of $4.3 million was used to secure our line of credit in Chinese currency. This line of credit was unused as at November 30, 2008. This $4.3 million letter of guarantee is secured by short-term investments.

VARIABLE INTEREST ENTITY

As of November 30, 2008, we did not have interests in any variable interest entities.

RISKS AND UNCERTAINTIES

Over the past several years, we have managed our business in a difficult environment; focused on research and development programs for new and innovative products aimed at expected growth pockets in our sector; continued the development of our domestic and international markets; and made strategic acquisitions. However, we operate in a highly competitive sector that is in constant evolution and, as a result, we encounter various risks and uncertainties that must be given appropriate consideration in our strategic management policies.

We are exposed to currency risks due to the export of our Canadian-manufactured products, the large majority of which are denominated in US dollars. These risks are partially hedged by operating expenses denominated in US dollars and forward exchange contracts. The increased strength of the Canadian dollar, compared to the US dollar, over the last few years, has caused our operating expenses to increase significantly. Any further increase in the value of the Canadian dollar in the coming months would negatively affect our results of operations.

In addition, risks and uncertainties related to the telecommunications test, measurement and monitoring industry involve the rapid development of new products that may have short life cycles and require extensive research and development; the difficulty of adequately predicting market size and trends; the difficulty of retaining highly skilled employees; and the ability to quickly adapt our cost structure to changing market conditions in order to achieve profitability.

Furthermore, given our strategic goals for growth and competitive positioning in our industry, we are continuously expanding into international markets, including our manufacturing facilities in China and our software development center in India. This exposes us to certain risks and uncertainties, namely changes in local laws and regulations, multiple technological standards, protective legislation, pricing pressure, cultural differences and the management of operations in China and India.

Also, while strategic acquisitions, like those we have made in the past, those closed in fiscal 2008 and possibly others in the future, are essential to our long-term growth, they also expose us to certain risks and uncertainties related to the rapid and effective integration of these businesses as well as their products, technologies and personnel. Finally, integration requires the dedication of management resources, which may detract their attention from our day-to-day business and operations.

Table of Contents

Our business is subject to the effects of general economic conditions in North America and throughout the world and, more particularly, market conditions in the telecommunications industry. In the past, our operating results were adversely affected by reduced telecom capital spending in North America, Europe and Asia and by general unfavorable economic conditions. In particular, sales to network service providers in North America were significantly and adversely affected by a downturn in 2001 in the telecommunications industry. With a recession or slowdown in key geographic regions or markets, we may experience a material adverse impact on our business, operating results and financial condition.

The economic environment of our industry could also result in some of our customers experiencing difficulties and, consequently, this could have a negative effect on our results, especially in terms of future sales and recoverability of accounts receivable. However, the sectorial and geographic diversity of our customer base provides us with a reasonable level of protection in this area. Finally, other financial instruments, which potentially subject us to credit risks, consist mainly of cash, short-term investments and forward exchange contracts. Our short-term investments consist of debt instruments issued by high-credit quality corporations and trusts. Our cash and forward exchange contracts are held with or issued by high-credit quality financial institutions; therefore, we consider the risk of non-performance on these instruments to be limited.

For a more complete understanding of risk factors that may affect us, please refer to the risk factors set forth in our disclosure documents published with securities commissions at www.EXFO.com or www.sedar.com in Canada or www.sec.gov/edgar.shtml in the U.S.

Non-GAAP financial measure

We provide a non-GAAP financial measure (EBITDA*) as supplemental information regarding our operational performance. We use EBITDA for the purposes of evaluating our historical and prospective financial performance, as well as our performance relative to our competitors. This measure also helps 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 GAAP 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 GAAP. 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 GAAP.

The following table summarizes the reconciliation of EBITDA to GAAP net earnings (loss):

	Three months ended November 30,	
	2008	2007
GAAP net earnings (loss) for the period	$ 5,287	$ (93)
Add (deduct):		
Amortization of property, plant and equipment	1,159	976
Amortization of intangible assets	1,319	734
Interest income	(466)	(1,483)
Income taxes	1,840	1,262
EBITDA for the period	$ 9,139	$ 1,396

EDITDA in percentage of sales	19.7%	3.4%

*EBITDA is defined as net earnings (loss) before interest, income taxes, amortization of property, plant and equipment and amortization of intangible assets.