MANAGEMENT'S DISCUSSION AND ANALYSIS

ON FORM 51-102F1

THREE AND NINE MONTHS ENDED

MAY 31, 2019

July 12, 2019

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INTRODUCTION

This management's discussion and analysis (MD&A) relates to the unaudited interim consolidated financial position, results of operations, comprehensive income (loss) and cash flows for the nine months ended May 31, 2019 (Q3 fiscal 2019) of NAV CANADA and its subsidiaries (also referred to in this MD&A as we, our, us or the Company). It should be read in conjunction with our unaudited interim condensed consolidated financial statements for Q3 fiscal 2019 (Q3 fiscal 2019 financial statements), our audited annual consolidated financial statements and the accompanying notes for the year ended August 31, 2018 (fiscal 2018), our fiscal 2018 annual MD&A, as well as our 2018 Annual Information Form dated October 25, 2018 (fiscal 2018 AIF). Additional information about NAV CANADA, including our consolidated financial statements for Q3 fiscal 2019 and fiscal 2018, our fiscal 2018 annual MD&A, and our fiscal 2018 AIF are filed on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

Our financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). Our Q3 fiscal 2019 financial statements have been prepared in accordance with International Accounting Standards (IAS) 34 *Interim Financial Reporting*. Our Audit & Finance Committee reviewed this MD&A and our Board of Directors (the Board) approved it before it was filed.

All amounts are presented in Canadian dollars (CDN), which is the Company's functional and reporting currency, unless otherwise indicated. All information presented has been rounded to the nearest million dollars.

Caution Concerning Forward-Looking Information

This MD&A and, in particular, but without limitation, sections "INTRODUCTION – Significant Financial Matters: Air Traffic and Customer Service Charges" and "RESULTS OF OPERATIONS – Financial Outlook" of this MD&A, contain certain statements about NAV CANADA's future expectations. These statements are generally identified by words like "anticipate", "plan", "believe", "intend", "expect", "estimate", "approximate" and the like, as well as future or conditional verbs such as "will", "should", "would" and "could", or negative versions thereof. Because forward-looking statements involve future risks and uncertainties, actual results may be different from those expressed or implied in these statements. Examples include geopolitical unrest, terrorist attacks and the threat of terrorist attacks, war, epidemics or pandemics, natural disasters, weather patterns, environmental concerns, cyber security attacks, labour negotiations, arbitrations, workforce recruitment, training and retention, general aviation industry conditions, air traffic levels, the use of telecommunications and ground transportation as alternatives to air travel, capital market and economic conditions, the ability to collect customer service charges and reduce operating costs, the success of our investment in space-based aircraft surveillance through Aireon LLC (Aireon), changes in interest rates, changes in laws, tax changes, adverse regulatory developments or proceedings and lawsuits. Some of these risks and uncertainties are explained under "Risk Factors" in our fiscal 2018 AIF. The forward-looking statements contained in this MD&A represent our expectations as of July 12, 2019 and are subject to change after this date. Readers of this MD&A are cautioned not to place undue reliance on any forward-looking statement. We disclaim any intention or obligation to update or revise any forward-looking statements included in this document whether as a result of new information, future events or for any other reason, except as required by applicable securities legislation.

Our Business

NAV CANADA is the private sector, non-share capital company that operates Canada's civil air navigation system (ANS). With operations across Canada, we provide air navigation services to aircraft owners and operators within Canadian–controlled airspace. These services include air traffic control, flight information, weather briefings, airport advisories, aeronautical information and electronic navigation aids.

The core business of the Company is to manage and operate the ANS and related services in a safe, efficient and cost effective manner. Our mandate covers both Canadian airspace and airspace delegated to Canada under international agreements.

Financial Strategy and Rate Regulation

In establishing new customer service charges or revising existing charges, we must follow the charging principles set out in our governing legislation, the *Civil Air Navigation Services Commercialization Act* (ANS Act), which prevents us from setting customer service charges higher than what is needed to meet our financial requirements for the provision of air navigation services. Pursuant to these principles, the Board approves the amount and timing of changes to customer service charges. The Board also approves the Company's annual budget where the amounts to be recovered through customer service charges for the ensuing year are determined. Our aim is essentially to achieve breakeven financial results on the consolidated statement of operations on an annual basis. Due to seasonal and other fluctuations in air traffic and given that our costs are predominantly fixed in nature, our quarterly financial results may not achieve a breakeven position, after recording adjustments to the rate stabilization account. This is illustrated in the table under the heading "SUMMARY OF QUARTERLY RESULTS – Quarterly Financial Information (unaudited)".

As noted above, customer service charges are set based on the Company's financial requirements, which take into account estimated air traffic volumes and planned expenses. Since actual revenue and expenses will differ from these estimates, methods to accumulate the variances are required so that they may be taken into account when setting future customer service charges. There is also a need to absorb the immediate effect of unpredictable factors – mainly fluctuations in air traffic volumes resulting from unforeseen events. We meet these objectives through the use of a "rate stabilization" mechanism.

In preparing our consolidated financial statements we reflect the impact of rate regulation. As such, the timing of recognition of certain revenue and expenses differs from what would otherwise be expected for companies that are not subject to regulatory statutes governing the level of charges. For example, we adjust our net income (loss) through transfers to or from the rate stabilization account, based on variations from the amounts that were used when establishing customer service charges. If our actual revenue exceeds actual expenses, the excess is reflected as a credit to the rate stabilization account and is returnable to customers through future customer service charges. Similarly, if actual revenue is less than actual expenses, the revenue shortfall is reflected as a debit to the rate stabilization account and is recoverable from customers through future customer service charges (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account").

In addition, for certain transactions where the timing of the cash flows differs significantly from the accounting recognition, the Company recognizes regulatory deferral account debits and credits in order to adjust the accounting recognition to the period in which they will be considered for rate setting. These transactions are generally considered for rate setting when the amounts are expected to be realized in cash.

When determining the level of customer service charges, we consider the Company's current and future financial requirements (see "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)" and "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

Our financial strategy is to fulfil our essential services mandate based on a sound financial foundation, reflected in part through high credit ratings in the financial markets. Maintaining this strong foundation requires a prudent approach that balances the interests of our key stakeholders while complying with our statutory and contractual obligations.

(millions of Canadian dollars)

Financial Highlights

Results of operations for the three months ended May 31, 2019

The Company recorded a net loss of $14 in the three months ended May 31, 2019 (three months ended May 31, 2018 - net loss of $8). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $31 (three months ended May 31, 2018 - $8).

	Three months ended May 31		
	2019	2018	Change
Revenue	$ 351	$ 349	$ 2
Operating expenses	367	361	6
Other (income) and expenses	15	(14)	29
Income tax expense	-	10	(10)
Net loss, before net movement in regulatory deferral accounts	(31)	(8)	(23)
Net movement in regulatory deferral accounts [(1)]			
Rate stabilization adjustments:			
Unfavourable variances from planned results	6	11	(5)
Initial approved adjustment [(2)]	5	2	3
	11	13	(2)
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	21	24	(3)
Other employee benefits	(3)	(2)	(1)
Investment in preferred interests, before tax	(14)	(46)	32
Investment in equity-accounted investee	1	-	1
Income tax	1	10	(9)
Realized hedging transactions	-	1	(1)
	6	(13)	19
	17	-	17
Net loss, after net movement in regulatory deferral accounts	$ (14)	$ (8)	$ (6)

(1) The Company is subject to legislation that regulates the level of its charges (see "INTRODUCTION – Financial Strategy and Rate Regulation"). The timing of the recognition of certain revenue and expenses recovered through charges is recorded through movements in regulatory deferral accounts (see "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)").

(2) In order to achieve breakeven results of operations in fiscal 2019, the Board approved a reduction of the rate stabilization account as a result of a planned shortfall. As a result, $18 is being transferred out of the rate stabilization account evenly throughout the fiscal year (fiscal 2018 - $10).

(millions of Canadian dollars)

Cash flows for the three months ended May 31, 2019

As shown below, cash and cash equivalents decreased by $15 during the three months ended May 31, 2019 (three months ended May 31, 2018 - $106) and the Company experienced negative free cash flow of $19 (three months ended May 31, 2018 - $30), which is a non- Generally Accepted Accounting Principle (non-GAAP) financial measure. Non-GAAP financial measures do not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers. The Company defines free cash flow as cash generated from operations, less capital expenditures and investments in Aireon and equity related investments. Management places importance on this indicator as it assists in measuring the impact of its investment program on the Company's financial resources.

	Three months ended May 31		
	2019	2018	Change
Cash flows from (used in):			
Operations [(1)]	$ 10	$ 9	$ 1
Investing [(1)]	(29)	(48)	19
Financing [(1)]	4	(67)	71
Decrease in cash and cash equivalents	(15)	(106)	91
Cash and cash equivalents, beginning of period	37	134	(97)
Cash and cash equivalents, end of period	$ 22	$ 28	$ (6)
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations [(2)]	$ 10	$ 9	$ 1
Capital expenditures [(2)]	(29)	(39)	10
Free cash flow	$ (19)	$ (30)	$ 11

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2019" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2019 financial statements.

(millions of Canadian dollars)

Results of operations for the nine months ended May 31, 2019

The Company recorded a net loss of $60 for the nine months ended May 31, 2019 (nine months ended May 31, 2018 - $50). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $109 (nine months ended May 31, 2018 - $65). Given the normal seasonality of air traffic and the fact that our costs are predominantly fixed in nature, a net loss is expected for the nine months ended May 31, 2019.

	Nine months ended May 31		
	2019	2018	Change
Revenue	$ 1,025	$ 1,001	$ 24
Operating expenses	1,075	1,041	34
Other (income) and expenses	59	34	25
Income tax (recovery) expense	-	(9)	9
Net loss, before net movement in regulatory deferral accounts	(109)	(65)	(44)
Net movement in regulatory deferral accounts [(1)]			
Rate stabilization adjustments:			
Unfavourable (favourable) variances from planned	(4)	2	(6)
Initial approved adjustment [(2)]	14	7	7
	10	9	1
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	66	78	(12)
Other employee benefits	(5)	(4)	(1)
Investment in preferred interests, before tax	(25)	(62)	37
Income tax	2	(7)	9
Realized hedging transactions	1	1	-
	39	6	33
	49	15	34
Net loss, after net movement in regulatory deferral accounts	$ (60)	$ (50)	$ (10)

(1) See "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)"

(2) In order to achieve breakeven results of operations in fiscal 2019, the Board approved a reduction of the rate stabilization account as a result of a planned shortfall. As a result, $18 is being transferred out of the rate stabilization account evenly throughout the fiscal year (fiscal 2018 - $10).

(millions of Canadian dollars)

Cash flows for the nine months ended May 31, 2019

As shown below, cash and cash equivalents decreased by $16 during the nine months ended May 31, 2019 (nine months ended May 31, 2018 - $194) and the Company experienced negative free cash flow of $45 (nine months ended May 31, 2018 - $145), which is a non-GAAP financial measure as discussed in "INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2019".

	Nine months ended May 31		
	2019	2018	Change
Cash flows from (used in):			
Operations (1)	$ 50	$ (26)	$ 76
Investing (1)	(84)	(126)	42
Financing (1)	18	(42)	60
Decrease in cash and cash equivalents	(16)	(194)	178
Cash and cash equivalents, beginning of period	38	222	(184)
Cash and cash equivalents, end of period	$ 22	$ 28	$ (6)
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations (2)	$ 50	$ (26)	$ 76
Capital expenditures (2)	(95)	(124)	29
Income tax refund on investment in preferred interests (2)	-	5	(5)
Free cash flow	$ (45)	$ (145)	$ 100

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2019" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2019 financial statements.

(millions of Canadian dollars)

Financial position as at May 31, 2019:

The following table outlines significant changes in our assets and liabilities between August 31, 2018 and May 31, 2019:

	May 31 2019	August 31 2018	Change
Assets			
Current assets			
Cash and cash equivalents	$ 22	$ 38	$ (16)
Accounts receivable and other	97	102	(5)
Investments	72	71	1
Other current assets	12	17	(5)
	203	228	(25)
Non-current assets			
Investment in preferred interests	443	418	25
Property, plant and equipment	736	735	1
Intangible assets	909	932	(23)
Related party loans receivable	2	12	(10)
Investment in equity-accounted investee	6	6	-
Employee benefits	2	2	-
Other non-current assets	2	1	1
	2,100	2,106	(6)
Total assets	2,303	2,334	(31)
Regulatory deferral account debit balances	1,023	954	69
Total assets and regulatory deferral account debit balances	**$ 3,326**	**$ 3,288**	**$ 38**
Liabilities			
Current liabilities			
Bank loans	$ 55	$ -	$ 55
Trade and other payables	222	247	(25)
Deferred revenue	7	4	3
Current portion of long-term debt	25	275	(250)
	309	526	(217)
Non-current liabilities			
Long-term debt	1,442	1,219	223
Employee benefits	1,151	1,070	81
Deferred tax liability	52	50	2
Other non-current liabilities	1	1	-
	2,646	2,340	306
Total liabilities	2,955	2,866	89
Equity			
Retained earnings (deficit)	(32)	28	(60)
Regulatory deferral account credit balances	403	394	9
Total liabilities, equity and regulatory deferral account credit balances	**$ 3,326**	**$ 3,288**	**$ 38**

For a discussion of the changes in cash and cash equivalents from August 31, 2018, see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2019".

The change in related party loans receivable is due to the repayment of the bridge financing by Aireon in December 2018.

The changes in the current portion of long-term debt and long-term debt are due to the settlement of the MTN 2009-1 General Obligation Notes and the issuance of the MTN 2019-1 General Obligation Notes.

The change in non-current employee benefits liability is the result of the impact of current service costs, net finance costs and contributions on each of the Company's benefit plans.

The changes in regulatory deferral account debit and credit balances are discussed further in "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)".

The balance in retained earnings (deficit) as at May 31, 2019 reflects the earnings up to that date. We plan our operations to essentially be in an annual financial breakeven position after expenses are met through customer service charges and other revenue sources, and after adjustments are made to the rate stabilization account. As a result, the balance in the retained earnings account at the end of each fiscal year has remained stable at $28. Any variation from this amount at the end of any interim period reflects seasonal or other planned fluctuations in revenue and expenses.

Significant Financial Matters

The following items have significant financial importance to the Company:

1. Rate Stabilization Account

As at May 31, 2019, the rate stabilization account (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account") had a credit balance of $114 (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

The rate stabilization account decreased by $10 during the nine months ended May 31, 2019 due to $4 of favourable variances from planned results, offset by the $14 initially approved adjustment to the rate stabilization account. Rate stabilization adjustments are described under "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account".

2. Air Traffic and Customer Service Charges[1]

Over the course of Q3 fiscal 2019, air traffic volumes, as measured by weighted charging units (WCU) (a measure of the number of flights, aircraft size and distance flown), increased by 2.4% year-over-year. The approved budget for fiscal 2019 assumed growth of 3.6% for the year and the Company's current annual forecast for air traffic growth for fiscal 2019 is 2.3%.

We continuously monitor our financial requirements and air traffic, and regularly update our financial forecasts to account for changes in the economic environment. On a quarterly basis, we review the most current information available from aviation industry sources as well as forecasts of macro-economic indicators; we then modify our forecast assumptions accordingly and consider the need for a change in rates.

In accordance with the ANS Act, the Company issued a notice of revised service charges for consultation on June 4, 2019, providing the details of proposed revisions. The consultation period concludes on August 6, 2019.

[1] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

(millions of Canadian dollars)

The proposed service charges would be implemented in two phases, taking effect on September 1, 2019 and January 1, 2020, respectively.

Overall, proposed customer service charge rate revisions, effective September 1, 2019, will represent an average 0.8% increase in base rates, which recovers the cost of domestic space-based Automatic Dependent Surveillance-Broadcast (SB ADS-B) data services.

Charges related to SB ADS-B data services within the North Atlantic oceanic airspace will begin January 1, 2020 and will be recovered through an increase in the existing North Atlantic Enroute (NAT) service charge.

3. Collective Agreements

Approximately 88% of our workforce is unionized under eight collective agreements.

As at May 31, 2019, the Company has expired agreements with four unions, comprising 72% of our represented workforce, whose collective agreements expired March 31, 2019 and April 30, 2019, respectively. The Company is currently in negotiations with two of these unions, comprising 60% of our represented workforce.

Negotiations have commenced with one union, comprising approximately 6% of our represented workforce, whose contract expired on June 30, 2019.

4. Financing Activities

On March 29, 2019, the Company issued $250 Series MTN 2019-1 General Obligation Notes due on September 29, 2050. The notes have an annual interest rate of 3.209%. The proceeds from these notes were used to repay the Company's $250 Series MTN 2009-1 General Obligation Notes that matured on April 17, 2019. The Company also closed the related bond forward agreement that had been entered into in June 2018 to hedge the interest rate risk related to the refinancing at a loss of $9.

RESULTS OF OPERATIONS

Revenue

The following table provides a breakdown of our revenue by category. Our fiscal 2018 AIF and the notes to our Q3 fiscal 2019 financial statements provide more information about the different categories of our customer service charges.

	Three months ended May 31			
	2019	2018	Change	%
Enroute	$ 171	$ 172	$ (1)	(1%)
Terminal	133	127	6	5%
Daily / annual / quarterly	23	24	(1)	(4%)
North Atlantic and international communication	11	11	-	-
Total customer service charges	338	334	4	1%
Other [(1)]	13	15	(2)	(13%)
	$ 351	$ 349	$ 2	1%

(millions of Canadian dollars)

	Nine months ended May 31			
	2019	2018	Change	%
Enroute	$ 495	$ 492	$ 3	1%
Terminal	389	371	18	5%
Daily / annual / quarterly	68	67	1	1%
North Atlantic and international communication	34	32	2	6%
Total customer service charges	986	962	24	2%
Other (1)	39	39	-	-
	$ 1,025	$ 1,001	$ 24	2%

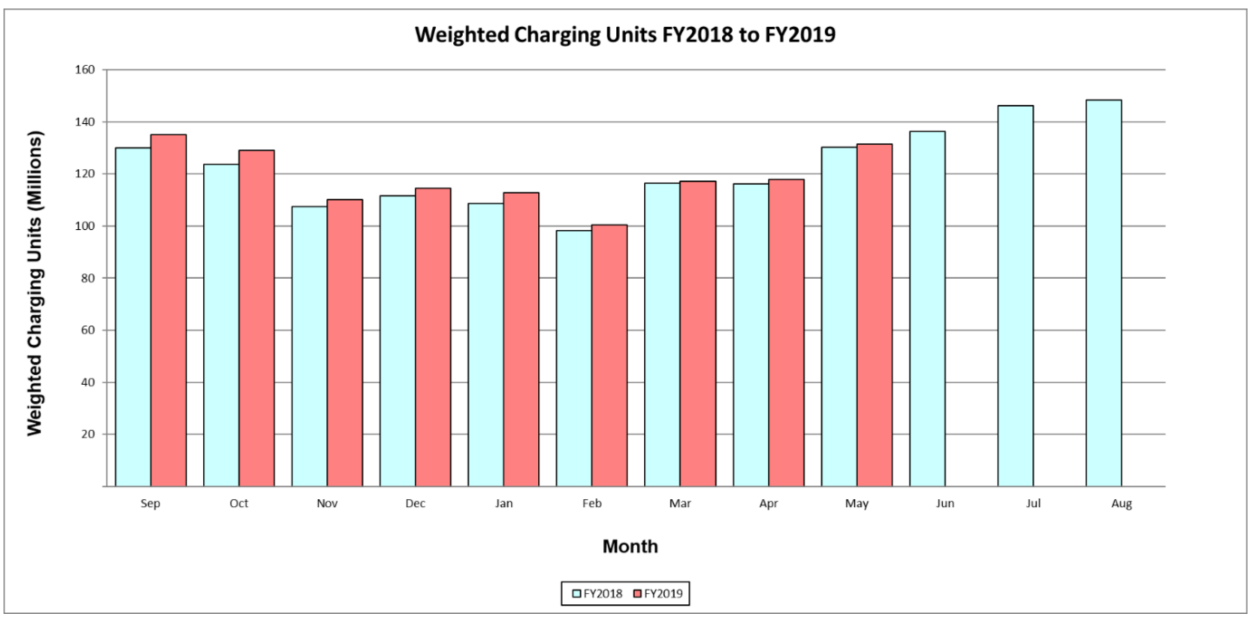
(1) Other revenue consists of service and development contracts, conference centre services at our facility in Cornwall (Ontario), the sale of civil aeronautical publications and other miscellaneous revenue.

Revenue for the three and nine months ended May 31, 2019 increased by $2 and $24 respectively primarily due to a 1.0% and 2.4% growth in WCUs during the three and nine months ended May 31, 2019.

Effective September 1, 2018, the Company implemented revisions to its service charges resulting in a decrease on average of 0.4% to existing base rates. This effectively continues the 0.4% one-year temporary rate reduction that was implemented on September 1, 2017.

Air Traffic

Air traffic growth for the first nine months of fiscal 2019 reflects normal seasonality and increased by 2.4% when compared to the first nine months of fiscal 2018. The chart shows traffic in WCUs.



Future air traffic volumes may be influenced by numerous factors, including the rate of economic growth or decline, changing air passenger demand, aircraft capacity utilization levels, fuel costs, changes in air carrier operations and behaviours, general aviation industry conditions, air carrier competition, airline restructurings and insolvencies, terrorist activities, epidemics or pandemics, weather patterns, natural disasters, environmental concerns, demographic patterns and other factors.

(millions of Canadian dollars)

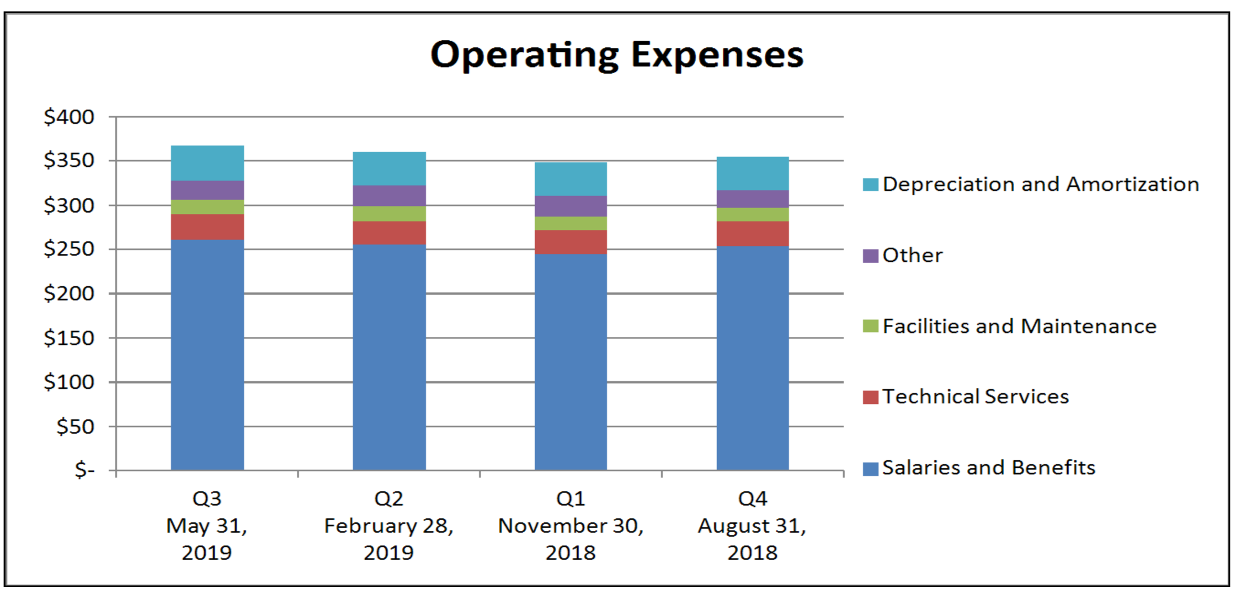
Operating Expenses

	Three months ended May 31			
	2019	2018	Change	%
Salaries and benefits	$ 261	$ 256	$ 5	2%
Technical services	29	28	1	4%
Facilities and maintenance	16	16	-	-
Depreciation and amortization	39	39	-	-
Other	22	22	-	-
	$ 367	$ 361	$ 6	2%

	Nine months ended May 31			
	2019	2018	Change	%
Salaries and benefits	$ 761	$ 731	$ 30	4%
Technical services	83	81	2	2%
Facilities and maintenance	48	47	1	2%
Depreciation and amortization	115	114	1	1%
Other	68	68	-	-
	$ 1,075	$ 1,041	$ 34	3%

Salaries and benefits expense for the three and nine months ended May 31, 2019 increased by $5 and $30, respectively, compared to the three and nine months ended May 31, 2018 primarily due to increased compensation levels and overtime costs arising from negotiated increases in collective agreements, increased staffing requirements to meet air traffic growth and activities related to supporting projects and maintaining optimum staffing levels across the country.

As illustrated in the table below, the majority of our operating expenses are incurred evenly throughout the year.



(millions of Canadian dollars)

Other (Income) and Expenses (Including Income Tax (Recovery) Expense)

	Three months ended May 31		
	2019	2018	Change
Finance income			
Interest income	$ -	$ (1)	$ (1)
Net change in fair value of financial assets at FVTPL [1]			
Investment in preferred interests	(3)	(42)	(39)
Other investments	-	(1)	(1)
	(3)	(43)	(40)
Total finance income	(3)	(44)	(41)
Net interest expense relating to employee benefits	9	14	5
Other finance costs			
Interest expense	19	20	1
Other gains, net of losses			
Foreign exchange losses	(11)	(4)	7
Other (gains) and losses	1	-	(1)
	(10)	(4)	6
	$ 15	$ (14)	$ (29)
Income tax expense	$ -	$ 10	$ 10

[1] The net change in fair value of financial assets at fair value through profit or loss (FVTPL) includes interest and dividend income related to those financial assets.

The decrease in net change in fair value of the investment in preferred interests is due to positive fair value adjustments of $39 recorded in Q3 fiscal 2018, based on the price paid by NATS for an investment in the preferred interests of Aireon.

Net interest expense relating to employee benefits decreased by $5 in Q3 fiscal 2019 compared to Q3 fiscal 2018 primarily due to higher interest income, partially offset by an increase in finance costs.

The income tax expense of $10 recorded in Q3 fiscal 2018 relates to the fair value increase in the Company's investment in preferred interests, recorded during the same period.

(millions of Canadian dollars)

	Nine months ended May 31		
	2019	2018	Change
Finance income			
Interest income	$ (2)	$ (3)	$ (1)
Net change in fair value of financial assets at FVTPL			
Investment in preferred interests	(9)	(48)	(39)
Other investments	-	(2)	(2)
	(9)	(50)	(41)
Total finance income	(11)	(53)	(42)
Net interest expense relating to employee benefits	28	41	13
Other finance costs			
Interest expense	56	58	2
Other gains, net of losses			
Foreign exchange gains	(14)	(12)	2
	(14)	(12)	2
	$ 59	$ 34	$ (25)
Income tax recovery	$ -	$ (9)	$ (9)

Net interest expense relating to employee benefits decreased by $13 in fiscal 2019 compared to fiscal 2018 primarily due to higher interest income, partially offset by an increase in finance costs.

The Company recorded an income tax recovery of $9 in fiscal 2018 compared to $nil in fiscal 2019 as a result of a $19 decrease in net deferred tax liabilities related to the Company's investment in preferred interests of Aireon due to the change in the U.S. federal corporate income tax rate from 35% to 21%, partially offset by a $10 increase in net deferred tax liabilities related to the same investment due to the fair value increase recorded based on the price paid by NATS for its investment in the preferred interests of Aireon (as discussed above).

(millions of Canadian dollars)

Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)

The net movement in regulatory deferral accounts related to net income (loss) represents the regulatory accounting adjustments, including the rate stabilization mechanism, to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting.

	Three months ended May 31		
	2019	2018	Change
Rate stabilization account [1]	$ 11	$ 13	$ (2)
Other regulatory deferral accounts			
Employee benefit pension contributions	21	24	(3)
Other employee benefits	(3)	(2)	(1)
Investment in preferred interests, before tax	(14)	(46)	32
Investment in equity-accounted investee	1	-	1
Income tax	1	10	(9)
Realized hedging transactions	-	1	(1)
	$ 17	$ -	$ 17

[1] The movements in the rate stabilization account are detailed in the table below under "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account".

The net movement in the employee benefit pension contributions regulatory deferral account for Q3 fiscal 2019 decreased by $3 compared to Q3 fiscal 2018. Regulatory adjustments to adjust the total pension benefit expense to the level of pension contributions to be recovered through rate setting were $21 in Q3 fiscal 2019 compared to $24 in Q3 fiscal 2018.

The $32 net movement in regulatory deferral of the Company's investment in preferred interests before tax is primarily due to the regulatory deferral of the $39 increase in the fair value of the investment in Q3 fiscal 2018, with no similar regulatory deferral in Q3 fiscal 2019.

The net movement in the income tax regulatory deferral account of $9 is a result of the fair value increase related to the investment in preferred interests of Aireon recorded in fiscal 2018.

	Nine months ended May 31		
	2019	2018	Change
Rate stabilization account	$ 10	$ 9	$ 1
Other regulatory deferral accounts			
Employee benefit pension contributions	66	78	(12)
Other employee benefits	(5)	(4)	(1)
Investment in preferred interests, before tax	(25)	(62)	37
Income tax (recovery)	2	(7)	9
Realized hedging transactions	1	1	-
	$ 49	$ 15	$ 34

The net movement in the employee benefit pension contributions regulatory deferral account for the nine months ended May 31, 2019 decreased by $12 compared to the same period in fiscal 2018. Regulatory adjustments required to the total pension benefit expense to reflect the cash amount of contributions to be recovered through rate setting were $66 in fiscal 2019 compared to $78 in fiscal 2018.

(millions of Canadian dollars)

The $37 decrease in the investment in preferred interests regulatory deferral account for the nine months ended May 31, 2019 is primarily due to the regulatory deferral of the $9 increase in fair value of the investment, compared to an increase of $48 recorded in the same period in fiscal 2018.

The net movement in the income tax regulatory deferral account includes the deferral of future income tax liabilities related to the Company's investment in preferred interests of Aireon. The $9 increase in fiscal 2019 compared to fiscal 2018 is a result of the decrease in net deferred tax liabilities related to the investment in preferred interests of Aireon which is due to the change in the U.S. federal corporate income tax rate from 35% to 21%, partially offset by the increase in fair value of the investment recorded in fiscal 2018.

Movements in Rate Stabilization Account

Our rate stabilization mechanism and accounting are described at the beginning of this MD&A and in notes 1 and 8 of our fiscal 2018 annual consolidated financial statements. The table below shows the movements in the rate stabilization account.

	Nine months ended May 31		
	2019	2018	Change
Credit balance on the statement of financial position, beginning of period	$ 124	$ 131	$ (7)
Variances from planned results:			
Revenue higher (lower) than planned	(4)	10	(14)
Operating expenses (higher) lower than planned	14	(7)	21
Other (income) and expenses lower than planned	27	61	(34)
Net movement in other regulatory deferral accounts	(33)	(66)	33
Total variances from planned results	4	(2)	6
Initial approved adjustment	(14)	(7)	(7)
Net movement in rate stabilization account recorded in net income (loss)	(10)	(9)	(1)
Credit balance on the statement of financial position, end of period	$ 114	$ 122	$ (8)

The $10 decrease in the rate stabilization account during the nine months ended May 31, 2019 is primarily due to:

- net movement of $33 in regulatory deferral accounts that was more favourable than planned primarily due to:
    - a net regulatory income $14 higher than planned related to the Company's investment in preferred interests of Aireon, to defer the unrealized foreign exchange gains due to the fluctuation of the Canadian dollar against the U.S. dollar;
    - a regulatory expense for pensions and other employee benefits that was $21 lower than planned primarily due to lower pension contributions expense;

  partially offset by:

    - a regulatory adjustment of $3 to recognize a surplus on long-term disability (LTD) benefits;

(millions of Canadian dollars)

- revenue that was $4 lower than planned; and
- the planned adjustment of $14, representing three quarters of the anticipated $18 annual net loss at the time the fiscal 2019 budget was approved;

partially offset by:

- operating expenses that were $14 lower than planned, primarily due to lower non-compensation operating expenses; and
- other (income) and expenses that were $27 lower than planned primarily due to higher foreign exchange gains on our investment in preferred interests of Aireon and lower than planned net finance costs relating to employee benefits.

Other Comprehensive Income (Loss)

The accounting recognition of other comprehensive income (loss) amounts are offset by regulatory deferrals in order to defer the accounting recognition to the periods in which they will be considered for rate setting. These transactions are generally considered for rate setting when the amounts are expected to be realized in cash, with the exception of the cash flows related to hedging instruments, which are considered for rate setting in the same period as the underlying hedged transaction, and re-measurements of unfunded defined employee benefit plans, which are considered for rate setting over the employees' average expected remaining service period.

	Three months ended May 31		
	2019	2018	Change
Items that will be reclassified to income or (loss):			
Changes in fair value of cash flow hedges	(6)	(4)	(2)
Net movement in regulatory deferral accounts	6	4	2
Total other comprehensive income (loss)	$ -	$ -	$ -

There were no significant events or changes to the Company's defined pension and other post-employment benefit plans that would require a revaluation during Q3 fiscal 2019 and Q3 fiscal 2018.

During Q3 fiscal 2019, negative fair value adjustments of $6 were recorded on the Company's interest rate hedges related to the re-financing of debt instruments that matured in fiscal 2019. The negative fair value adjustment of $4 recorded during Q3 fiscal 2018 relates to the Company's interest rate hedges for the refinancing of these same debt instruments.

(millions of Canadian dollars)

	Nine months ended May 31		
	2019	2018	Change
Items that will not be reclassified to income or (loss):			
Re-measurements of employee defined benefit plans	$ -	$ 100	$ (100)
Net movement in regulatory deferral accounts	-	(100)	100
	-	-	-
Items that will be reclassified to income or (loss):			
Amortization of loss on cash flow hedge	-	1	(1)
Changes in fair value of cash flow hedges	(10)	4	(14)
Net movement in regulatory deferral accounts	10	(5)	15
	-	-	-
Total other comprehensive income (loss)	$ -	$ -	$ -

For the nine months ended May 31, 2019, there were no significant events or changes to the Company's defined pension and other post-employment benefit plans that would require a revaluation. Re-measurement gains on employee defined benefit plans in the nine months ended May 31, 2018 of $100 were recorded during Q1 fiscal 2018 and are a result of a return on plan assets $226 greater than the expected return based on the discount rate of 3.60% at August 31, 2018, partially offset by actuarial losses of $126 from a 10 basis point decrease in the discount rate to 3.50%.

In fiscal 2019, negative fair value adjustments of $10 were recorded primarily on the Company's interest rate hedges related to the re-financing of debt instruments that matured during fiscal 2019. In fiscal 2018, positive fair value adjustments of $4 were recorded primarily on the Company's interest rate hedges related to the financing of the same debt instruments.

Amounts Considered for Rate Setting Purposes

As discussed under "INTRODUCTION – Financial Strategy and Rate Regulation", when establishing customer service charges the Board considers, among other things:

(a) the Company's financial requirements and the extent to which operating costs are variable;

(b) the current and anticipated balance in the rate stabilization account;

(c) the recovery of pension contributions on a cash basis.

The table below shows the balance of the rate stabilization account and the amount of regulatory pension cash contribution to be recovered at a later date:

	May 31 2019	August 31 2018	Change
Rate stabilization account credit balance	$ 114	$ 124	$ (10)
Regulatory pension cash contribution to be recovered at a later date	$ (34)	$ (34)	$ -

(millions of Canadian dollars)

Financial Outlook[2]

Presented below are the Company's current projected annual consolidated results before rate stabilization for fiscal 2019 compared to fiscal 2018 actual results.

	Fiscal 2019	Fiscal 2018	Change	%
Before rate stabilization				
Revenue	$ 1,443	$ 1,415	$ 28	2%
Operating expenses and other (income) and expenses, including other regulatory adjustments	1,463	1,422	41	3%
Net income (loss) before rate stabilization adjustments	$ (20)	$ (7)	$ (13)	

Revenue

Revenue in fiscal 2019 is expected to increase by approximately 2.0% or $28 from $1,415 in fiscal 2018 primarily due to forecasted air traffic growth of 2.3%, partially offset by a decrease in other revenue. As discussed in "RESULTS OF OPERATIONS – Revenue", the revised charges, effective September 1, 2018, effectively continue the 0.4% temporary rate reduction that was implemented in fiscal 2018.

In our Q2 fiscal 2019 MD&A, we had disclosed anticipated revenue of $1,443 for fiscal 2019 and forecasted air traffic growth of 2.4%. The decrease in expected air traffic growth to 2.3% at Q3 fiscal 2019 is offset by an increase in other revenue.

Operating Expenses and Other (Income) and Expenses

Operating expenses and other (income) and expenses before rate stabilization for fiscal 2019 are expected to be $1,463. This is an increase of 2.9% or $41 compared to fiscal 2018 primarily due to:

- increased compensation levels and overtime costs arising from inflationary increases in collective agreements, increased staffing requirements to meet air traffic growth and to support projects, and the maintenance of optimum staffing levels across the country;
- first partial year of satellite surveillance charges commencing in March 2019;
- increased operational requirements impacting facilities and maintenance, technical services and other expenses; and
- the effects of inflation,

partially offset by:

- lower pension current service costs due to an increase in discount rates.

[2] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

Across the Company, we remain focused on cost saving measures that are consistent with safety, which is our top priority. Our efforts are aimed at managing staffing levels and discretionary expenses, as well as continuing to implement process improvement initiatives and efficiencies.

In our Q2 fiscal 2019 MD&A, we had disclosed anticipated operating expenses and other (income) and expenses, before rate stabilization of $1,466 for fiscal 2019. The decrease of $3 is primarily related to lower operational requirements, partially offset by lower regulatory deferral of LTD expenses as a result of negative experience.

Cash Flows

Given the expected net cash flows from operations and cash flows from investing and financing activities in fiscal 2019, the Company's cash position is currently expected to decrease to $31 as at August 31, 2019 from $38 as at August 31, 2018. This cash outlook is based on anticipated annual cash inflows from operating activities of $172, partially offset by cash outflows from investing activities of $157 and financing activities of $22. Financing net cash outflows are primarily comprised of $275 for the repayment of long-term debt and the disbursement of $9 on settlement of a bond forward, partially offset by the issuance of $250 and proceeds from bank loans of $15. Investing activities include cash outflows for capital expenditures of $168, partially offset by the repayment of the bridge loan to Aireon of $11. As discussed below, the Company has adequate existing sources of financing to cover all of its anticipated cash flow requirements.

In our Q2 fiscal 2019 annual MD&A, we had disclosed an anticipated cash position of $30 by the end of fiscal 2019. The increase of $1 is primarily due to an increase in cash flows from operating activities from $157 to $172, reducing the requirement for proceeds from bank loans from $28 to $15.

Rate Stabilization Account

The Company currently anticipates that the rate stabilization account will have a credit balance of $104 at the end of fiscal 2019, resulting from estimated revenue of $1,443 and total operating expenses and other (income) and expense (including other regulatory adjustments) of $1,463 (before rate stabilization).

In our Q2 fiscal 2019 MD&A, we had forecast a rate stabilization account credit balance of $101 at the end of fiscal 2019. The increase of $3 is due to the forecasted decrease in operating expenses and other (income) and expenses (including other regulatory adjustments).

Earnings and Cash Flow Coverage

During a fiscal year, quarterly revenue will reflect seasonal or other fluctuations in the airline industry and therefore our net results vary from quarter to quarter. Our mandate to operate on essentially a financial breakeven basis results in a planned earnings coverage ratio – calculated on the basis of earnings before interest divided by interest expense – that is close to one-to-one. However, the seasonal nature of our revenue may result in an earnings coverage ratio of less than one-to-one for any interim period.

For the twelve months ended May 31, 2019, the Company had a net loss of $10. Our interest costs were $75. Consolidated earnings (after rate stabilization) before interest were $65, which is 0.87 times our interest requirement for this period and just below our one-to-one target. Depreciation and amortization expense for this period was $153. Our cash flow coverage was 2.91 times our interest requirement for this period.

Earnings coverage ratio and cash flow coverage are non-GAAP financial measures and do not have any standardized meaning prescribed by IFRS. The earnings coverage ratio and cash flow coverage are provided pursuant to and in compliance with National Instrument 44-102 *Shelf Distributions* of the Canadian Securities Administrators. The Company calculates the earnings coverage ratio on the basis of earnings before interest expense on financial liabilities at amortized cost (interest expense) divided by interest expense. Cash flow coverage is calculated on the basis of earnings (after rate stabilization) before interest expense, depreciation and amortization divided by interest expense. Under the *Income Tax Act* (Canada), NAV CANADA, excluding its subsidiaries, is not subject to income taxes and accordingly, no deduction for income taxes has been made. After the application of rate regulated accounting, the provision for income taxes related to our taxable subsidiaries is not significant.

We maintain a debt service reserve fund and an operations and maintenance reserve fund under our Master Trust Indenture and we are subject to liquidity covenants under our General Obligation Indenture, designed to cover 12 months interest on borrowings and 25% of our annual operating and maintenance expenses. As at May 31, 2019, we were in full compliance with our debt indentures, including the Master Trust Indenture's requirements regarding the reserve funds, the flow of funds and with the rate covenants, as well as the liquidity and other provisions of the General Obligation Indenture.

Related Party Transactions

The Company's related parties include its key management personnel, subsidiaries, joint ventures and registered pension plans for its employees. The transactions with these related parties are not materially different from what was reported in the fiscal 2018 annual MD&A.

(millions of Canadian dollars)

SUMMARY OF QUARTERLY RESULTS

Quarterly Financial Information (unaudited)

	Three months ended			
	Q3 May 31 2019	Q2 February 28 2019	Q1 November 30 2018	Q4 August 31 2018
Revenue	$ 351	$ 317	$ 357	$ 414
Operating expenses	367	360	348	355
Other (income) and expenses	15	27	17	26
	(31)	(70)	(8)	33
Income tax (recovery) expense	-	-	-	1
Net income (loss) before net movement in regulatory deferral accounts	(31)	(70)	(8)	32
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	11	3	(4)	(2)
Other regulatory deferral account adjustments	6	23	10	20
	17	26	6	18
Net income (loss) after net movement in regulatory deferral accounts	$ (14)	$ (44)	$ (2)	$ 50

	Three months ended			
	Q3 May 31 2018	Q2 February 28 2018	Q1 November 30 2017	Q4 August 31 2017
Revenue	$ 349	$ 305	$ 347	$ 332
Operating expenses	361	340	340	348
Other (income) and expenses	(14)	30	18	16
	2	(65)	(11)	(32)
Income tax (recovery) expense	10	(19)	-	3
Net income (loss) before net movement in regulatory deferral accounts	(8)	(46)	(11)	(35)
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	13	(7)	3	2
Other regulatory deferral account adjustments	(13)	8	11	25
	-	1	14	27
Net income (loss) after net movement in regulatory deferral accounts	$ (8)	$ (45)	$ 3	$ (8)

Discussion of Quarterly Results

The quarterly variations in revenue mainly reflect seasonal fluctuations. Typically, revenue is highest in our fourth quarter (June to August) as a result of increased air traffic in the summer months, and the second quarter (December to February) has the lowest air traffic volumes. Air traffic for Q3 fiscal 2019 was 1.0% higher on average than in Q3 fiscal 2018. Strong traffic results in fiscal 2018 along with traffic growth projections for fiscal 2019 have enabled the Company to implement revised service charges, whereby existing base rates decreased by an average of 0.4% on September 1, 2018. This effectively continues the one-year temporary rate reduction implemented on September 1, 2017. On average, customers will pay the same rates in fiscal 2019 as they did in fiscal 2018.

The majority of our operating expenses are incurred evenly throughout the year.

Other (income) and expenses fluctuate primarily due to:

- fair value adjustments on investments, including the investment in preferred interests of Aireon, which change based on market factors and changes in expectations of credit losses;
- changes in net interest expense relating to employee benefits as a result of changes in annual discount rates; and
- changes in foreign exchange (gains) or losses as a result of the strengthening or weakening of the Canadian dollar compared to foreign currencies in which the Company transacts, mainly the U.S. dollar.

Net movement in regulatory deferral accounts related to net income (loss) fluctuates due to:

- changes in the rate stabilization account based on variances from planned results and the initial approved adjustment;
- the recovery of pension solvency deficiency contributions made;
- changes in employee benefit pension contributions and expense;
- changes in other employee benefits, including positive or negative LTD experience and funding requirements;
- changes in the investment in preferred interests of Aireon, before tax;
- changes in the investment in equity-accounted investee;
- changes in income taxes; and
- changes in unrealized hedging transactions.

(millions of Canadian dollars)

LIQUIDITY AND CAPITAL RESOURCES

Our fiscal 2018 annual MD&A explains how we manage our cash and capital resources. There have been no changes in that approach for the nine months ended May 31, 2019.

As at May 31, 2019, we had $22 of cash and cash equivalents and committed credit facilities of $1,215, of which $355 was available for unrestricted use (see "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

Cash flows for the three months ended May 31, 2019

	Three months ended May 31		
	2019	2018	Change
Cash flows from (used in):			
Operations	$ 10	$ 9	$ 1
Investing	(29)	(48)	19
Financing	4	(67)	71
Decrease in cash and cash equivalents	(15)	(106)	91
Cash and cash equivalents, beginning of period	37	134	(97)
Cash and cash equivalents, end of period	$ 22	$ 28	$ (6)
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations	$ 10	$ 9	$ 1
Capital expenditures (1)	(29)	(39)	10
Free cash flow	$ (19)	$ (30)	$ 11

(1) See the statement of cash flows in our Q3 fiscal 2019 financial statements.

As shown above, cash and cash equivalents decreased by $15 for the three months ended May 31, 2019 and the Company experienced negative free cash flow of $19, which is a non-GAAP financial measure as discussed in "INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2019".

Cash flows from operations for the three months ended May 31, 2019 were inflows of $10 compared to inflows of $9 for the three months ended May 31, 2018, primarily due to $9 higher receipts from customer service charges, partially offset by $8 higher payments to employees and suppliers.

Cash outflows from investing activities for the three months ended May 31, 2019 were $29 compared to $48 for the three months ended May 31, 2018. In Q3 fiscal 2019, investment in capital projects was $28 (cash outflows of $29), compared to $46 in Q3 fiscal 2018 (cash outflows of $39). In addition, the Company provided bridge financing of $9 to Aireon in Q3 fiscal 2018.

Cash inflows from financing activities for the three months ended May 31, 2019 were $4 compared to outflows of $67 for the three months ended May 31, 2018. The inflow in Q3 fiscal 2019 was primarily a result of $248 proceeds from the issue of the MTN 2019-1 General Obligation Notes and $40 proceeds from bank loans, partially offset by $275 outflows to repay the MTN 2009-1 General Obligation Notes and the Series 97-2 amortizing revenue bonds and $9 to settle derivative liabilities related to the MTN 2019-1 interest rate hedge.

(millions of Canadian dollars)

Cash flows for the nine months ended May 31, 2019

	Nine months ended May 31		
	2019	2018	Change
Cash flows from (used in):			
Operations	$ 50	$ (26)	$ 76
Investing	(84)	(126)	42
Financing	18	(42)	60
Decrease in cash and cash equivalents	(16)	(194)	178
Cash and cash equivalents, beginning of period	38	222	(184)
Cash and cash equivalents, end of period	$ 22	$ 28	$ (6)
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations	$ 50	$ (26)	$ 76
Capital expenditures (1)	(95)	(124)	29
Income tax refund on investment in preferred interests (1)	-	5	(5)
Free cash flow	$ (45)	$ (145)	$ 100

(1) See the statements of cash flows of our Q3 fiscal 2019 financial statements.

As shown above, cash and cash equivalents decreased by $16 for the nine months ended May 31, 2019 and the Company experienced negative free cash flow of $45, which is a non-GAAP financial measure as discussed in “INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2019”.

Cash flows from operations for the nine months ended May 31, 2019 were inflows of $50 compared to outflows of $26 for the nine months ended May 31, 2018, primarily due to higher receipts from customer service charges of $47 and higher other receipts of $8; $33 of payments to refund customer service charges and the payment of $42 to settle curtailed severance benefits both made in fiscal 2018 with none made in 2019; partially offset by higher payments to employees and suppliers of $53.

Cash outflows from investing activities for the nine months ended May 31, 2019 were $84 compared to $126 in the nine months ended May 31, 2018. The Company invested $94 in capital projects during the nine months ended May 31, 2019 (cash outflows of $95), partially offset by $11 cash inflows from the repayment of the bridge financing from Aireon compared to $123 in the nine months ended May 31, 2018 (cash outflows of $124) and loans to related parties of $10. The cash outflows in fiscal 2018 were partially offset by an income tax refund of $5 on the Company's investment in preferred interests of Aireon.

Cash inflows from financing activities for the nine months ended May 31, 2019 were $18 compared to outflows of $42 for the nine months ended May 31, 2018. The inflows in fiscal 2019 were primarily due to $248 of proceeds from the issue of the MTN 2019-1 Notes and $55 net proceeds from bank loans, partially offset by $275 outflows to repay the MTN 2009-1 General Obligation Notes and the Series 97-2 amortizing revenue bonds and $9 to settle derivative liabilities related to the MTN 2019-1 interest rate hedge.

(millions of Canadian dollars)

Liquidity and Financing Strategy

Our liquidity and financing strategy remains unchanged from that disclosed in our fiscal 2018 annual MD&A.

We are exposed to re-financing risk with respect to our bond and note maturities, including the $25 annual amortizing payment due on the Series 97-2 amortizing revenue bonds. We mitigate this risk by maintaining committed credit facilities in an amount sufficient to meet our refinancing needs in the event of temporary capital market disruptions or lack of access to the market for any reason. The Company issued a Base Shelf Prospectus on November 9, 2017 that is valid for a 25-month period.

On March 29, 2019, the Company issued $250 Series MTN 2019-1 General Obligation Notes due on September 29, 2050. The notes have an annual interest rate of 3.209%. The proceeds from these notes were used to repay the Company's $250 Series MTN 2009-1 General Obligation Notes that matured on April 17, 2019. The Company also closed the related bond forward agreement that had been entered into in June 2018 to hedge the interest rate risk related to the refinancing at a loss of $9.

The Company has a revolving credit facility with a syndicate of Canadian financial institutions and separate letter of credit facilities for pension funding purposes. As at May 31, 2019, the credit facilities are utilized as follows:

Credit facilities:	
Credit facility with a syndicate of Canadian financial institutions (1) (2)	$ 675
Letter of credit facilities for pension funding purposes (3)	540
Total available credit facilities	1,215
Less: Outstanding letters of credit for pension funding purposes (3)	501
Less: Outstanding letters of credit for other purposes (2)	9
Less: Bank loan	55
Undrawn committed borrowing capacity	650
Less: Operations and maintenance reserve fund allocation (4)	295
Credit facilities available for unrestricted use	$ 355

(1) The Company's credit facility with a syndicate of Canadian financial institutions in the amount of $675 is comprised of two equal tranches maturing on September 12, 2021 and September 12, 2023. The credit facility agreement provides for loans at varying rates of interest based on certain benchmark interest rates, specifically the Canadian prime rate and the Canadian bankers' acceptance rate, and on the Company's credit rating at the time of drawdown. The Company is required to pay commitment fees, which are dependent on the Company's credit rating. The Company is in compliance with the credit facility covenants as at May 31, 2019.

(2) At May 31, 2019, $9 was drawn from an uncommitted revolving credit facility. In connection with this facility, an allocation of $25 with a Canadian financial institution has been made under its $675 committed credit facility.

(3) The letter of credit facilities for pension funding purposes are comprised of four facilities with Canadian financial institutions totalling $540, which will mature on December 31, 2019, unless extended. During the nine months ended May 31, 2019, the Company increased these facilities by $25. At May 31, 2019, $501 was drawn for pension solvency funding purposes.

(millions of Canadian dollars)

(4) The operations and maintenance reserve fund may be used to pay operating and maintenance expenses, if required (see also "LIQUIDITY AND CAPITAL RESOURCES – Financial Instruments and Risk Management: Reserve Funds and Financial Instruments").

The table below shows our long-term debt, liquidity and investments profile.

	May 31 2019	August 31 2018
LONG-TERM DEBT:		
Bonds and notes payable		
Under the Master Trust Indenture	$ 450	$ 475
Under the General Obligation Indenture	1,025	1,025
	1,475	1,500
Adjusted for deferred financing costs and discounts	(8)	(6)
Total bonds and notes payable	1,467	1,494
Less: current portion of long-term debt	(25)	(275)
Total long-term debt	$ 1,442	$ 1,219
LIQUIDITY:		
Cash and cash equivalents	$ 22	$ 38
Debt service reserve fund	72	71
	$ 94	$ 109
Undrawn committed borrowing capacity (1)	$ 650	$ 683

(1) $355 of this borrowing capacity is available as described in the previous table (August 31, 2018 - $388).

Credit Ratings

The Company's debt obligations have been assigned the following credit ratings:

Rating Agency	Senior Debt	General Obligation Notes	Outlook
DBRS Limited (DBRS)	AA	AA (low)	Stable
Moody's Investors Service (Moody's)	Aa2	Aa2	Stable
Standard & Poor's (S&P)	AA	AA-	Stable

On March 8, 2019, S&P issued a press release affirming the Company's ratings and stable outlook. The press release noted the Company's credit strengths as holding a monopoly over an essential transportation service, legislated ability to levy user charges on airlines to meet financial requirements and strong financial performance. They noted that the Company's debt metrics continue to improve thanks to a declining debt level.

S&P stated that NAV CANADA has "adequate liquidity and financial flexibility, thanks to a stable level of unrestricted reserves and available lines of credit, and very strong debt capacity." S&P noted the Company's legislated perpetual monopoly over civil air navigation services in Canadian-controlled airspace and the fact that its air traffic volumes depend not on any one region, but the entire country and international airspace assigned to Canada by treaty. S&P therefore considers the Company's service area to be more diversified than that of airport operators.

On February 28, 2019, Moody's issued a credit opinion affirming NAV CANADA's base line credit assessment at Aa2 and its senior and subordinated ratings at Aa2. Moody's noted the Company's following credit strengths:

- Essential infrastructure asset for the Canadian air transportation system;
- Monopoly provider of civil air navigation services over a very large airspace;
- Legislated right to establish and levy rates and charges as needed to meet financial requirements resulting in good degree of cash flow predictability;
- Continued solid traffic growth;
- Manageable capital expenditure program.

They also noted the following credit challenges:

- Defined benefit pension plan creates recurring calls on cash;
- Periods of weak debt service coverage ratio when the Company depletes its rate stabilization account.

Moody's stated that "the rating outlook is stable, reflecting our expectation that NAV CANADA will be prudent and take into account its overall financial position and upcoming obligations when contemplating a rate decrease and, vice versa, that it will implement the necessary rate increases if traffic growth slows down and/or expenses increase."

Our credit ratings provided by DBRS remain unchanged from those described in our fiscal 2018 annual MD&A.

(millions of Canadian dollars)

Cash Requirements

The following information about our contractual obligations and other commitments summarizes certain of our liquidity and capital resource requirements that have changed from that reported in our fiscal 2018 annual MD&A.

Contractual Obligations

A breakdown of contractual obligations as at May 31, 2019 for the next five fiscal years and thereafter is presented in the following table.

	Remaining payments – for years ending August 31						
	Total	2019	2020	2021	2022	2023	Thereafter
Bank loan	$ 55	$ 55	$ -	$ -	$ -	$ -	$ -
Long-term debt (including current portion) (1), (2)	1,475	-	25	275	25	25	1,125
Interest payments (2)	1,000	18	70	63	56	54	739
Capital commitments	101	33	26	6	4	13	19
Operating lease commitments	84	1	7	5	5	6	60
Total contractual obligations	$ 2,715	$ 107	$ 128	$ 349	$ 90	$ 98	$ 1,943

Total contractual obligations exclude commitments for goods and services in the ordinary course of business. Also excluded are other long-term liabilities mainly due to reasons of uncertainty of timing of cash flows and items that are non-cash in-nature.

(1) Payments represent principal of $1,475. The Company intends to refinance principal maturities at their maturity dates. The Company may choose to repay a portion of these maturities with available cash, and/or may increase the size of a re-financing to generate additional liquidity or for other purposes, and/or may choose to redeem, in whole or in part, an issue in advance of its scheduled maturity date.

(2) Further details on interest rates and maturity dates on long-term debt are provided in note 8 to our Q3 fiscal 2019 interim financial statements.

The Company's letters of credit are discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy".

The Company's contributions to its pension plans are discussed in the fiscal 2018 annual MD&A.

(millions of Canadian dollars)

Capital Management

The Company views capital as the sum of its issued long-term debt, retained earnings and accumulated other comprehensive income, regulatory deferral accounts and certain employee benefits, as depicted in the following table. This definition of capital is used by management and may not be comparable to measures presented by other companies.

	May 31 2019	August 31 2018
Bonds and notes payable	$ 1,467	$ 1,494
Equity:		
Retained earnings (deficit)	(32)	28
Regulatory deferral accounts:		
Debit balances	(1,023)	(954)
Credit balances	403	394
Employee benefits:		
LTD asset	(2)	(2)
Liability for funded pension benefits	773	707
Liability for accumulating sick leave	18	18
Total capital	$ 1,604	$ 1,685

Management's approach and objectives when managing capital remain unchanged from those described in our fiscal 2018 annual MD&A.

Financial Instruments and Risk Management

Reserve Funds and Financial Instruments

Under the Master Trust Indenture, we maintain a debt service reserve fund and an operations and maintenance reserve fund. We are also required to meet certain minimum liquidity levels under the General Obligation Indenture. The requirements of the debt service reserve fund and the operations and maintenance reserve fund remain unchanged from that described in our fiscal 2018 annual MD&A.

Financial Risk Management

The Company is exposed to several risks as a result of holding financial instruments, including interest rate risk, foreign exchange risk, price risk, credit risk and liquidity risk. The Company's exposure to financial risks and how the Company manages each of those risks are described in the Company's fiscal 2018 annual MD&A. There were no significant changes to those risks or to the Company's management of exposure to those risks during the nine months ended May 31, 2019, except as noted below:

(1) Liquidity risk

As at May 31, 2019, the Company's credit facilities available for unrestricted use are $355 (August 31, 2018 - $388). The decrease is largely due to the bank loan of $55 outstanding at May 31, 2019, partially offset by an increase of $25 in letter of credit facilities for pension funding purposes.

Insurance

Our aviation liability insurance program was last renewed on November 15, 2018. This insurance covers all of our ANS operations liabilities to third parties. The Company also carries other lines of insurance at levels deemed to be appropriate by management for the nature of our business. The cost of this insurance is not significant to the Company.

The Company is contractually obligated to indemnify the Government of Canada for any loss suffered by or claimed against it which is covered by the Company's aviation operations liability insurance.

Legal Proceedings

The Company is party to certain legal proceedings in the ordinary course of its business. Management does not expect the outcome of any of these proceedings to have a material adverse effect on the consolidated financial position or results of operations of the Company.

CHANGES IN ACCOUNTING POLICIES

The Company's Q3 fiscal 2019 financial statements were prepared in accordance with IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board (IASB). Significant accounting policies used in the Q3 fiscal 2019 financial statements are disclosed in note 3 of the Company's fiscal 2018 annual consolidated financial statements, except for the application of new standards, amendments and interpretations effective or early adopted September 1, 2018 as described in note 2 (e) to the Company's Q1 fiscal 2019 financial statements, which details the impact and changes in accounting policies as a result of the adoption of IFRS 15 – *Revenue from Contracts with Customers* (IFRS 15) and IFRIC 22 *Foreign Currency Transactions and Advance Consideration* (IFRIC 22), both effective September 1, 2018. No other changes to significant accounting policies have been made subsequently. The accounting policies have been applied consistently to all periods presented, unless otherwise indicated.

Future Accounting Pronouncements

The IASB has issued a number of standards and amendments that are not yet effective. The Company continues to analyze these standards and amendments to determine the extent of their impact on its consolidated financial statements.

The Company has the following update regarding its progress in implementing future standards:

<u>IFRS 16 – Leases (IFRS 16)</u>

In January 2016, the IASB issued IFRS 16, completing its project to improve the financial reporting of leases. The new standard will replace IAS 17 – Leases (IAS 17), and sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract. For lessees, IFRS 16 eliminates the classification of leases as either operating or finance leases that exist under IAS 17, and requires recognition of assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. IFRS 16 substantially carries forward the lessor accounting requirements under IAS 17, maintaining the classification of leases as operating or finance leases, and accounting for the lease according to its classification. IFRS 16 is to be applied retrospectively, using either a full retrospective approach or a modified retrospective approach, for annual periods beginning on or after January 1, 2019. Earlier application is permitted, but only if IFRS 15 has also been adopted.

The Company has completed a detailed review of those contracts in the scope of IFRS 16 to determine the accounting impacts and has determined that the impact is expected to be minimal. We are now reviewing disclosure requirements. The Company anticipates using the modified retrospective approach on transition to IFRS 16. For any lease that meets the definition of a lease in accordance with IFRS 16 and was previously classified as an operating lease, the Company anticipates measuring its right of use asset at an amount equal to the lease liability upon adoption of IFRS 16 on September 1, 2019.

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires management to make estimates and judgments that affect the reported amounts of revenue and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of commitments and contingencies at the date of the financial statements. These estimates and judgments are based on historical experience, current conditions and various other assumptions made by management that are believed to be reasonable under the circumstances. By their nature, these estimates and judgments are subject to uncertainty and the amounts currently reported in the Company's consolidated financial statements could, in future, prove to be inaccurate. Any changes from those estimates and judgments could have a material impact on our consolidated financial statements. The estimates and judgments are reviewed on an ongoing basis.

The Company's critical accounting estimates and judgments applied in the preparation of the Company's Q3 fiscal 2019 financial statements are consistent with those applied and disclosed in our fiscal 2018 annual consolidated financial statements and as described in the fiscal 2018 annual MD&A.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes to the Company's internal control over financial reporting (ICFR) during the three months ended May 31, 2019 that have materially affected or are reasonably likely to materially affect the Company's ICFR.