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MANAGEMENT'S DISCUSSION AND ANALYSIS

ON FORM 51-102F1

THREE AND NINE MONTHS ENDED

MAY 31, 2020

July 10, 2020

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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 loss and cash flows for the three and nine months ended May 31, 2020 (Q3 fiscal 2020) 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 2020 (Q3 fiscal 2020 financial statements), our audited annual consolidated financial statements and the accompanying notes for the year ended August 31, 2019 (fiscal 2019), our fiscal 2019 annual MD&A, as well as our 2019 Annual Information Form dated October 24, 2019 (fiscal 2019 AIF). Additional information about NAV CANADA, including our consolidated financial statements for Q3 fiscal 2020 and fiscal 2019, our fiscal 2019 annual MD&A, and our fiscal 2019 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 2020 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 and related travel advisories, 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 2019 AIF. The forward-looking statements contained in this MD&A represent our expectations as of July 10, 2020 and are subject to change after this date. In March 2020, the COVID-19 outbreak was declared a pandemic by the World Health Organization. Refer to "INTRODUCTION – Significant Financial Matters" for further discussion of the impact on NAV CANADA. 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 statement 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").

(millions of Canadian dollars)

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.

Financial Highlights

Results of operations for the three months ended May 31, 2020

The Company recorded a net loss of $14 for the three months ended May 31, 2020 (three months ended May 31, 2019 - $14). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $294 (three months ended May 31, 2019 - $31). 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 three months ended May 31, 2020. Due to the negative impact of the COVID-19 pandemic on air traffic volumes, the Company noted lower than anticipated customer service charges revenues in Q3 fiscal 2020 and it is expected that the normal seasonality pattern, which would see the highest revenue from air traffic experienced in the fourth quarter (June to August), will not occur in fiscal 2020.

	Three months ended May 31		
	2020	2019	Change
Revenue	$ 159	$ 351	$ (192)
Operating expenses	351	367	(16)
Other (income) and expenses	129	15	114
Income tax recovery	(27)	-	(27)
Net loss before net movement in regulatory deferral accounts	(294)	(31)	(263)
Net movement in regulatory deferral accounts [(1)]			
Rate stabilization adjustments:			
Unfavourable variances from planned results	160	6	154
Initial approved adjustment [(2)]	9	5	4
	169	11	158
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	42	21	21
Other employee benefits	(2)	(3)	1
Investment in preferred interests, before tax	97	(14)	111
Investment in equity-accounted investee	-	1	(1)
Income tax	(26)	1	(27)
	111	6	105
	280	17	263
Net loss, after net movement in regulatory deferral accounts	$ (14)	$ (14)	$ -

(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)”).

(millions of Canadian dollars)

(2) In order to achieve breakeven results of operations in the year ending August 31, 2020 (fiscal 2020), the Board approved the fiscal 2020 budget with a reduction of the rate stabilization account as a result of a planned shortfall. As a result, $35 is being transferred out of the rate stabilization account evenly throughout the fiscal year (fiscal 2019 - $18).

Cash flows for the three months ended May 31, 2020

As shown below, cash and cash equivalents increased by $870 during the three months ended May 31, 2020 (three months ended May 31, 2019 - decreased by $15) and the Company experienced negative free cash flow of $129 (three months ended May 31, 2019 - $19), which is a non-GAAP (Generally Accepted Accounting Principle) 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, investments in Aireon and equity related investments and principal payments of lease liabilities. 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		
	2020	2019	Change
Cash flows from (used in):			
Operating [(1)]	$ (102)	$ 10	$ (112)
Investing [(1)]	(26)	(29)	3
Financing [(1)]	997	4	993
Cash flows from (used in) operating, investing and financing activities	869	(15)	884
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase (decrease) in cash and cash equivalents	870	(15)	885
Cash and cash equivalents, beginning of period	48	37	11
Cash and cash equivalents, end of period	$ 918	$ 22	$ 896
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations [(2)]	$ (102)	$ 10	$ (112)
Capital expenditures [(2)]	(26)	(29)	3
Payment of lease liabilities [(2)]	(1)	-	(1)
Free cash flow	$ (129)	$ (19)	$ (110)

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2020" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2020 financial statements.

(millions of Canadian dollars)

Results of operations for the nine months ended May 31, 2020

The Company recorded a net loss of $61 for the nine months ended May 31, 2020 (nine months ended May 31, 2019 - $60). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $420 (nine months ended May 31, 2019 - $109). 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, 2020. Due to the negative impact of the COVID-19 pandemic on air traffic volumes, the Company noted lower than anticipated customer service charges revenues in Q3 fiscal 2020 and it is expected that the normal seasonality pattern, which would see the highest revenue from air traffic experienced in the fourth quarter (June to August), will not occur in fiscal 2020.

	Nine months ended May 31		
	2020	2019	Change
Revenue	$ 845	$ 1,025	$ (180)
Operating expenses	1,107	1,075	32
Other (income) and expenses	185	59	126
Income tax recovery	(27)	-	(27)
Net loss, before net movement in regulatory deferral accounts	(420)	(109)	(311)
Net movement in regulatory deferral accounts [(1)]			
Rate stabilization adjustments:			
Unfavourable (favourable) variances from planned results	144	(4)	148
Initial approved adjustment [(2)]	27	14	13
	171	10	161
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	130	66	64
Other employee benefits	(4)	(5)	1
Investment in preferred interests, before tax	87	(25)	112
Investment in equity-accounted investee	(1)	-	(1)
Income tax	(25)	2	(27)
Realized hedging transactions	1	1	-
	188	39	149
	359	49	310
Net loss, after net movement in regulatory deferral accounts	$ (61)	$ (60)	$ (1)

(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 2020, the Board approved the fiscal 2020 budget with a reduction of the rate stabilization account as a result of a planned shortfall. As a result, $35 is being transferred out of the rate stabilization account evenly throughout the fiscal year (fiscal 2019 - $18).

(millions of Canadian dollars)

Cash flows for the nine months ended May 31, 2020

As shown below, cash and cash equivalents increased by $888 during the nine months ended May 31, 2020 (nine months ended May 31, 2019 - decrease of $16) and the Company experienced negative free cash flow of $147 (nine months ended May 31, 2019 - $45), which is a non-GAAP financial measure as discussed in "INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2020".

	Nine months ended May 31		
	2020	2019	Change
Cash flows from (used in):			
Operating [(1)]	$ (39)	$ 50	$ (89)
Investing [(1)]	(106)	(84)	(22)
Financing [(1)]	1,032	18	1,014
Cash flows from (used in) operating, investing and financing activities	887	(16)	903
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase (decrease) in cash and cash equivalents	888	(16)	904
Cash and cash equivalents, beginning of period	30	38	(8)
Cash and cash equivalents, end of period	$ 918	$ 22	$ 896
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations [(2)]	$ (39)	$ 50	$ (89)
Capital expenditures [(2)]	(106)	(95)	(11)
Payment of lease liabilities [(2)]	(2)	-	(2)
Free cash flow	$ (147)	$ (45)	$ (102)

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2020" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2020 financial statements.

(millions of Canadian dollars)

Financial position as at May 31, 2020

The following table outlines significant changes in our assets, liabilities and regulatory deferral accounts between August 31, 2019 and May 31, 2020:

	May 31 2020	August 31 2019	Change
Assets			
Current assets			
Cash and cash equivalents	$ 918	$ 30	$ 888
Accounts receivable and other	81	98	(17)
Investments	73	72	1
Other current assets	14	13	1
	1,086	213	873
Non-current assets			
Investment in preferred interests	352	439	(87)
Property, plant and equipment	742	750	(8)
Intangible assets	884	906	(22)
Investment in equity-accounted investee	7	6	1
Related party loan receivable	3	3	-
Other non-current assets	2	1	1
	1,990	2,105	(115)
Total assets	3,076	2,318	758
Regulatory deferral account debit balances	2,263	2,087	176
Total assets and regulatory deferral account debit balances	$ 5,339	$ 4,405	$ 934
Liabilities			
Current liabilities			
Bank loan	$ 223	$ 8	$ 215
Trade and other payables	253	242	11
Deferred revenue	16	7	9
Current portion of long-term debt	275	25	250
Other current liabilities	3	1	2
	770	283	487
Non-current liabilities			
Long-term debt	2,013	1,443	570
Employee benefits	2,364	2,226	138
Deferred tax liability	23	48	(25)
Lease liability	4	-	4
Other non-current liabilities	1	1	-
	4,405	3,718	687
Total liabilities	5,175	4,001	1,174
Equity			
Retained earnings (deficit)	(33)	28	(61)
Regulatory deferral account credit balances	197	376	(179)
Total liabilities, equity and regulatory deferral account credit balances	$ 5,339	$ 4,405	$ 934

For a discussion of the changes in cash and cash equivalents (including the bank loan) from August 31, 2019, see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2020".

The change in the investment in preferred interests since August 31, 2019 is discussed in "INTRODUCTION – Significant Financial Matters: Investment in Preferred Interests of Aireon" and the change in long-term debt is discussed in "INTRODUCTION – Significant Financial Matters: Financing Activities".

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

The balance in retained earnings (deficit) as at May 31, 2020 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 fluctuations in revenue and expenses.

Significant Financial Matters

The following items have significant financial importance to the Company:

1. Coronavirus ("COVID-19") pandemic

In March 2020, the COVID-19 outbreak was declared a pandemic by the World Health Organization. The pandemic and the resulting economic contraction has had, and is expected to continue to have, a significant negative impact on global air traffic and on the aviation industry. As a private not-for profit company, our revenues come from our aviation customers, namely airlines, air cargo operators, other commercial air operators and general aviation.

NAV CANADA has seen the number of air traffic movements decline since March 2020 as a result of travel restrictions imposed by governments, the closing of international borders and the economic impact of the pandemic. As a result, the Company's customer service charges revenue has declined significantly as air carriers have reduced their operations, grounded fleets and cancelled flights and routes.

The pandemic is expected to continue to have a negative impact on demand for air travel globally and this will likely continue until such time as travel restrictions are eased and consumer demand for air travel returns. Industry participants are indicating it may be some time before they fully return to pre COVID-19 operating levels. We expect until this occurs that reduced air traffic activity will have a significant negative impact on the Company's operations and revenues.

In response to the impact of the pandemic, the Company will continue to review, monitor and take actions to reduce capital and operating spending and cash outflows, while at the same time ensuring the continued fulfillment of the Company's mandate to safely operate and maintain the Canadian air navigation system as an essential service and to protect the safety of its employees.

To address the significant revenue shortfall, some of the measures the Company has taken include:

- Drawing $225 from its syndicated credit facility to address near-term liquidity needs;
- Issuing a notice of revised service charges, proposing an increase in customer service charge base rates by an average of 29.5% effective September 1, 2020 (See "Air Traffic and Customer Service Charges";

- Raising funds through the issuance of $850 in General Obligation Notes (See “Financing Activities”);
- Implementing cost-cutting measures where possible, including:
  - Reducing the fiscal 2020 capital spending program from a budget of $170 to a forecast of $110;
  - Reducing all non-essential, non-critical activities;
- Accessing the Canada Emergency Wage Subsidy (CEWS) government relief program.

2. Air Traffic and Customer Service Charges[1]

Over the course of fiscal 2020, air traffic volumes, as measured by weighted charging units (WCU) (a measure of the number of flights, aircraft size and distance flown), decreased by 20.3%. Excluding the effect of an extra day for the leap year, air traffic volumes in the first nine months of fiscal 2020 decreased by 20.6% year over year. The approved budget for fiscal 2020 assumed growth of 3.7% for the year. The Company’s current annual forecast for air traffic volumes for fiscal 2020 is negative growth of 35.8% (See “RESULTS OF OPERATIONS – Financial Outlook”).

In accordance with the ANS Act, the Company issued, for consultation, a notice of revised service charges on May 20, 2020, providing details of proposed service charge revisions. The proposed changes would increase customer service charge base rates by an average of 29.5% effective September 1, 2020. The service charge proposal includes provisions to ease the cash flow burden of the increase on customers through payment deferral mechanisms. The consultation period concludes on July 24, 2020.

During the quarter, the International Air Transport Association discontinued, with the consent of Air Canada as intervenor, its application for Judicial Review of the Canadian Transportation Agency’s decision which upheld the Company’s revised service charges implemented September 1, 2019 and January 1, 2020.

3. Rate Stabilization Account

As at May 31, 2020, the rate stabilization account had a debit balance of $78 (see “RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes”).

The rate stabilization account changed by $171 from a credit balance of $93 to a debit balance of $78 during fiscal 2020 due to $144 of unfavourable variances from planned results and the $27 initially approved adjustment to the rate stabilization account. Rate stabilization adjustments are described under “RESULTS OF OPERATIONS – Movements in Rate Stabilization Account”.

4. Salaries and benefits

The Company has taken a number of cost-cutting measures to curb the significant decline in revenue, including management salary reductions, ending the terms of temporary employees, early retirement incentives and concessions from bargaining agents on deferred economic increases. In addition, the Company has availed itself of the CEWS offered by the Government of Canada which is intended to help businesses keep workers on their payroll through the challenges posed by the COVID-19 pandemic. Under CEWS the Company is eligible to receive up to 75% of wages or a maximum of $847 per week per employee for up to 24 weeks, retroactive to March 15, 2020.

Approximately 87% of our workforce is unionized under eight collective agreements. As at May 31, 2020, the Company has ratified collective agreements with seven of its bargaining agents. The Company’s agreement with the Canadian Federal Pilot Association expired on April 30, 2019 and negotiations are ongoing with the union.

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

5. Financing Activities

On May 29, 2020, the Company issued $850 of General Obligation Notes in two series: $550 Series MTN 2020-1 General Obligation Notes with an annual interest rate of 2.924%, maturing on September 29, 2051 and $300 Series MTN 2020-2 General Obligation Notes with an annual interest rate of 2.063%, maturing on May 29, 2030.

As at May 31, 2020, the Company has drawn $225 from its syndicated credit facility in addition to the issue of $850 of General Obligation Notes. The net proceeds of these notes will be used for general corporate purposes, including the repayment of borrowings under the syndicated credit facility which will enhance the Company's liquidity reserves. The Company's syndicated credit facility is described further in section "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy".

6. Pension Plans

The Company continues to meet the funding requirements of its two defined benefit registered pension plans in accordance with the regulations of the Office of the Superintendent of Financial Institutions Canada (OSFI).

The actuarial valuations for funding purposes of the pension plans performed as at January 1, 2020 reported a going concern surplus of $933 (January 1, 2019 – $738).

The regulations governing the funding of federally regulated pension plans include a solvency test, which assumes the plans are terminated as at the valuation date. The actuarial valuations performed as at January 1, 2020 reported a statutory solvency deficiency of $192 (January 1, 2019 - $164).

Once the valuations are filed, pension contributions are based on the January 1, 2020 actuarial valuations. The valuations will be filed with OSFI by September 30, 2020, in line with a filing extension provided by OSFI in response to the pandemic. The Company has the option of meeting its pension solvency funding requirements with letters of credit or cash contributions, with the maximum letters of credit based on 15% of solvency liabilities. At January 1, 2020, outstanding letters of credit represent 7% of solvency liabilities (January 1, 2019 - 8%).

On April 15, 2020, the Minister of Finance announced a moratorium on solvency special payments for the remainder of calendar 2020 which came into force on May 27, 2020. Under this moratorium, defined benefit plan sponsors are not required to make solvency special payments due for the months of March to November 2020. Plan sponsors who had already met their March and April solvency funding requirements through letters of credit, were permitted to reduce the face value of letters of credit by the amount of these payments. Accordingly, subsequent to May 31, 2020, the Company decreased its outstanding letters of credit to $533.

(millions of Canadian dollars)

7. Investment in Preferred Interests of Aireon

During Q3 fiscal 2020 (as discussed in note 6 of the Q3 fiscal 2020 financial statements), the Company updated the fair value of its investment in preferred interests of Aireon to reflect the impact of the COVID-19 pandemic as it relates to the number and frequency of air traffic movements in the aviation sector in general and the resulting impact on Aireon's operations and revenues. While not all of Aireon's revenue will be impacted, overall revenue levels are expected to decline and the reduction in air traffic may delay the signing by Aireon of new customers for space-based air traffic surveillance data services. As at May 31, 2020, the Company adjusted the fair value of its investment in preferred interests to $255 U.S. ($352 CDN) from $330 U.S. ($439 CDN) as at August 31, 2019. Included in the fair value presented in the statement of financial position are dividends receivable of $55 U.S ($76 CDN) (August 31, 2019 - $47 U.S. ($63 CDN)).

In addition, as a result of the decrease in the fair value, the related net deferred tax liability decreased to $23 CDN as at May 31, 2020 (August 31, 2019 - $48 CDN).

RESULTS OF OPERATIONS

Revenue

The following table provides a breakdown of our revenue by category. Our fiscal 2019 AIF and the notes to our Q3 fiscal 2020 financial statements provide more information about the different categories of our customer service charges.

	Three months ended May 31			
	2020	2019	Change	%
Enroute	$ 72	$ 171	$ (99)	(58%)
Terminal	56	133	(77)	(58%)
Daily / annual / quarterly	6	23	(17)	(74%)
North Atlantic and international communication	7	11	(4)	(36%)
Total customer service charges	141	338	(197)	(58%)
Other (1)	18	13	5	38%
	$ 159	$ 351	$ (192)	(55%)

	Nine months ended May 31			
	2020	2019	Change	%
Enroute	$ 404	$ 495	$ (91)	(18%)
Terminal	314	389	(75)	(19%)
Daily / annual / quarterly	49	68	(19)	(28%)
North Atlantic and international communication	31	34	(3)	(9%)
Total customer service charges	798	986	(188)	(19%)
Other (1)	47	39	8	21%
	$ 845	$ 1,025	$ (180)	(18%)

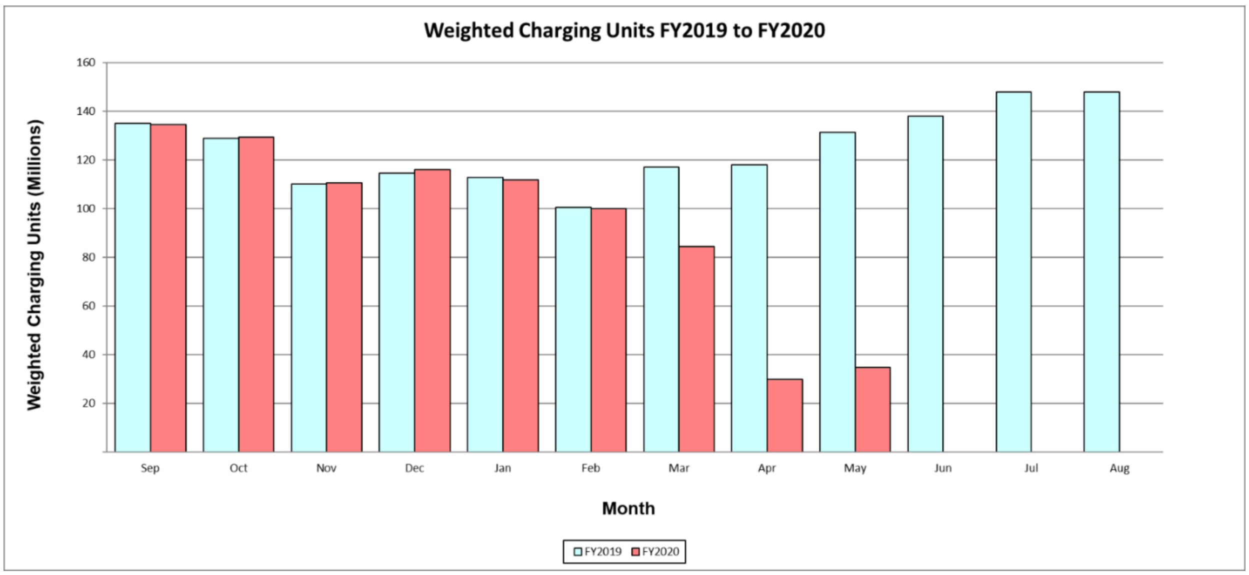
(1) Other revenue consists of service and development contracts, conference centre services at our facility in Cornwall (Ontario), the sale of civil aeronautical publications and other miscellaneous revenue.

Revenue for the three and nine months ended May 31, 2020 decreased by $192 and $180, respectively, compared to the same periods in fiscal 2019, primarily due to the COVID-19 pandemic which had a significant negative impact on global air traffic and on air traffic in Canadian controlled air space managed by the Company. The Company saw negative air traffic growth of 59.4% and 20.3%, respectively, year-over-year, as measured by WCUs.

Other revenue for the three and nine months ended May 31, 2020 increased $5 and $8, respectively, compared to the same periods in fiscal 2019, primarily due to a large service and development contract that commenced in fiscal 2020 and is expected to continue through fiscal 2026.

Air Traffic

Negative air traffic growth for the first nine months of fiscal 2020 reflects the impact of the COVID-19 pandemic on air traffic volumes and decreased by 20.3% when compared to the first nine months of fiscal 2019. The chart below shows traffic in WCUs.



Future air traffic volumes may be influenced by numerous factors, including the speed of recovery of air traffic following the COVID-19 pandemic, other epidemics or pandemics, 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, government interventions, travel restrictions and closings of borders to air travel, weather patterns, natural disasters, environmental concerns and demographic patterns.

(millions of Canadian dollars)

Operating Expenses

	Three months ended May 31			
	2020	2019	Change	%
Salaries and benefits	$ 244	$ 261	$ (17)	(7%)
Technical services	37	29	8	28%
Facilities and maintenance	15	18	(3)	(17%)
Depreciation and amortization	41	39	2	5%
Other	14	20	(6)	(30%)
	$ 351	$ 367	$ (16)	(4%)

Salaries and benefits expense in the three months ended May 31, 2020 decreased by $17 compared to 2019 primarily due to reduced overtime costs as a result of the significant decrease in air traffic volume and a reduction in non-essential activities and travel. In addition, the Company received $12 from the CEWS government relief program, offsetting compensation costs. These decreases were partially offset by increased compensation levels and increased pension current service costs as a result of a 90 basis point decrease in the discount rate at August 31, 2019 compared to August 31, 2018.

	Nine months ended May 31			
	2020	2019	Change	%
Salaries and benefits	$ 786	$ 761	$ 25	3%
Technical services	103	83	20	24%
Facilities and maintenance	51	54	(3)	(6%)
Depreciation and amortization	117	115	2	2%
Other	50	62	(12)	(19%)
	$ 1,107	$ 1,075	$ 32	3%

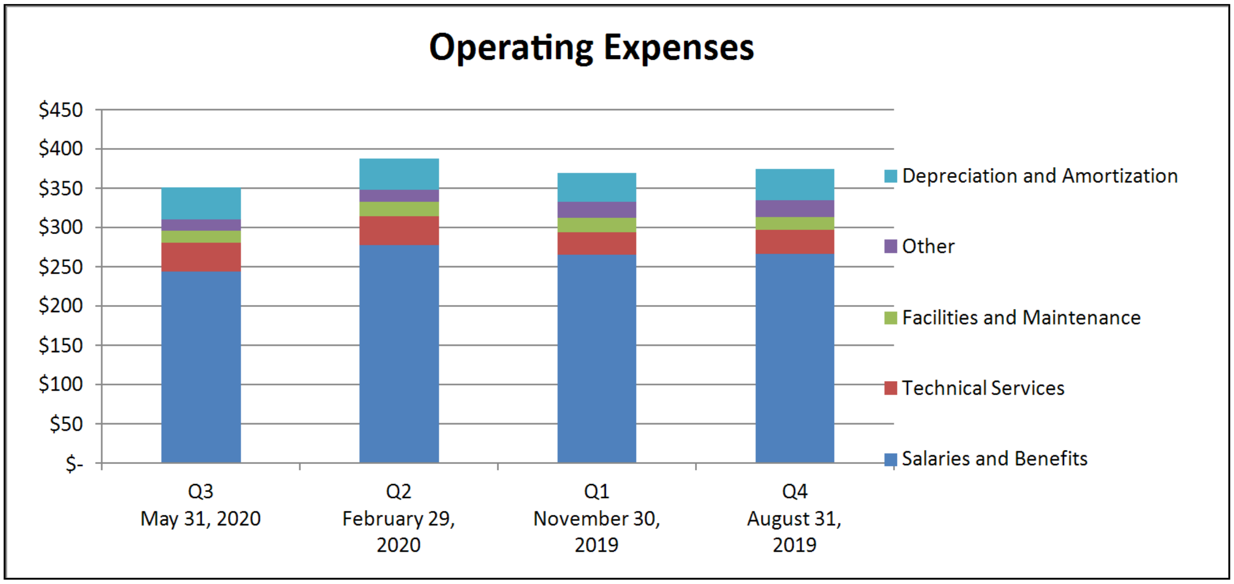
Salaries and benefits expense in the nine months ended May 31, 2020 increased by $25 compared to 2019 primarily due to increased pension current service costs as a result of a 90 basis point decrease in the discount rate at August 31, 2019 compared to August 31, 2018 and increased compensation levels. These increases were partially offset by reduced overtime costs as a result of the significant decrease in air traffic volume in Q3 fiscal 2020 and reduction in non-essential activities and travel as a result of the COVID-19 pandemic, along with the receipt of $12 from the CEWS government relief program, offsetting compensation costs.

Technical services expense in the three and nine months ended May 31, 2020 increased by $8 and $20 respectively, compared to May 31, 2019 primarily due to the cost of domestic and oceanic space-based surveillance data services of $12 and $25, respectively, in fiscal 2020.

Other expenses decreased in the three and nine months ended May 31, 2020 by $6 and $12 respectively, compared to May 31, 2019 primarily due to Company-wide efforts to reduce discretionary spending to offset the impact of decreased customer service charges revenue due to the COVID-19 pandemic.

(millions of Canadian dollars)

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



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

	Three months ended May 31		
	2020	2019	Change
Finance income			
Interest income	$ (1)	$ -	$ 1
Net change in fair value of financial assets at FVTPL (1)			
Investment in preferred interests	-	(3)	(3)
Other investments	(1)	-	1
Total finance income	(2)	(3)	(1)
Net interest expense relating to employee benefits	16	9	(7)
Other finance costs			
Interest expense	18	19	1
Net change in fair value of financial assets at FVTPL (1)			
Investment in preferred interests	109	-	(109)
	127	19	(108)
Other gains, net of losses			
Foreign exchange gains	(12)	(11)	1
Other losses	-	1	1
	(12)	(10)	2
	$ 129	$ 15	$ (114)
Income tax recovery	$ (27)	$ -	$ 27

(millions of Canadian dollars)

	Nine months ended May 31		
	2020	2019	Change
Finance income			
Interest income	$ (2)	$ (2)	$ -
Net change in fair value of financial assets at FVTPL (1)			
Investment in preferred interests	-	(9)	(9)
Other investments	(3)	-	3
	(3)	(9)	(6)
Total finance income	(5)	(11)	(6)
Net interest expense relating to employee benefits	47	28	(19)
Other finance costs			
Interest expense	55	56	1
Net change in fair value of financial assets at FVTPL (1)			
Investment in preferred interests	103	-	(103)
	158	56	(102)
Other gains, net of losses			
Foreign exchange gains	(14)	(14)	-
Share of net gain of equity-accounted investee	(1)	-	1
	(15)	(14)	1
	$ 185	$ 59	$ (126)
Income tax recovery	$ (27)	$ -	$ 27

(1) The net change in fair value of financial assets at FVTPL includes interest and dividend income related to those financial assets.

Net interest expense relating to employee benefits increased by $7 and $19, respectively during the three and nine months ended May 31, 2020 compared to the three and nine months ended May 31, 2019 primarily due to lower interest income, partially offset by lower interest expense due to the decrease in discount rates at August 31, 2019 compared to August 31, 2018.

During the three and nine months ended May 31, 2020, the net change in fair value of the investment in preferred interests was a loss of $109 and $103, respectively, as compared to a gain of $3 and $9 for the three and nine months ended May 31, 2019, primarily due to the $112 write-down of the fair value of the investment in preferred interests of Aireon as discussed in section "INTRODUCTION – Significant Financial Matters: Investment in Preferred Interests of Aireon".

The write-down of the fair value of the investment in preferred interests of Aireon resulted in an income tax recovery of $27 for the three and nine months ended May 31, 2020 as a result of the reduction in the net deferred tax liability.

(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		
	2020	2019	Change
Rate stabilization account [1]	$ 169	$ 11	$ 158
Other regulatory deferral accounts			
Employee benefit pension contributions	42	21	21
Other employee benefits	(2)	(3)	1
Investment in preferred interests, before tax	97	(14)	111
Investment in equity-accounted investee	-	1	(1)
Income tax	(26)	1	(27)
	$ 280	$ 17	$ 263

	Nine months ended May 31		
	2020	2019	Change
Rate stabilization account [1]	$ 171	$ 10	$ 161
Other regulatory deferral accounts			
Employee benefit pension contributions	130	66	64
Other employee benefits	(4)	(5)	1
Investment in preferred interests, before tax	87	(25)	112
Investment in equity-accounted investee	(1)	-	(1)
Income tax	(25)	2	(27)
Realized hedging transactions	1	1	-
	$ 359	$ 49	$ 310

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

To adjust the total pension benefit expense to reflect the cash amount of contributions to be recovered through rate setting, the net movement in the employee benefit pension contributions regulatory deferral account for the three and nine months ended May 31, 2020 were $42 and $130, respectively, compared to $21 and $66 for the three and nine months ended May 31, 2019. The increase is largely due to the increase in pension current service costs and net interest expense as a result of a decrease in the discount rate at August 31, 2019 compared to August 31, 2018.

The net movement in regulatory deferral accounts of the Company's investment in preferred interests of $111 and $112 during the three and nine months ended May 31, 2020, before tax are primarily due to the decrease in the fair value of the investment in preferred interests of Aireon as at May 31, 2020, as discussed in "INTRODUCTION – Significant Financial Matters: Investment in Preferred Interests of Aireon".

The $27 decrease in net movement in regulatory deferral of income tax during the three and nine months ended May 31, 2020 reflects the decrease in the net deferred tax liability as a result of the decrease in fair value of the investment in preferred interests of Aireon as at May 31, 2020.

(millions of Canadian dollars)

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 7 of our fiscal 2019 annual consolidated financial statements. The table below shows the movements in the rate stabilization account.

	Three months ended May 31		
	2020	2019	Change
Credit balance on the statement of financial position, beginning of period	$ 91	$ 125	$ (34)
Variances from planned results:			
Revenue lower than planned	(216)	(3)	(213)
Operating expenses lower than planned	50	1	49
Other (income) and expenses (higher) lower than planned	(77)	13	(90)
Net movement in other regulatory deferral accounts	83	(17)	100
Total variances from planned results	(160)	(6)	(154)
Initial approved adjustment	(9)	(5)	(4)
Net movement in rate stabilization account recorded in net loss	(169)	(11)	(158)
Credit (debit) balance on the statement of financial position, end of period	$ (78)	$ 114	$ (192)

The $169 change in the rate stabilization account during Q3 fiscal 2020 is primarily due to:

- revenue that was $216 lower than planned primarily due to the negative impact of the COVID-19 pandemic on air traffic volumes;
- other expenses that were $77 higher than planned primarily due to the decrease in the fair value of the investment in preferred interests of Aireon of $112, partially offset by income tax recovery of $27 and foreign exchange gains of $11 on our investment in preferred interests of Aireon; and
- the planned adjustment of $9, representing the Q3 fiscal 2020 portion of the anticipated $35 annual net loss at the time the fiscal 2020 budget was approved;

partially offset by:

- net movement of $83 in other regulatory deferral accounts that was higher than planned primarily due to:
    - a regulatory adjustment of $112 to offset the decrease in fair value in the investment in preferred interests of Aireon;
    - a regulatory expense for pension benefits that was $9 higher than planned primarily due to higher pension current service costs as a result of a decrease in the discount rate at August 31, 2019 compared to that used to prepare the fiscal 2020 budget; partially offset by

(millions of Canadian dollars)

- a regulatory adjustment of $27 related to the deferral of income tax recoveries due to the decrease in fair value of the investment in preferred interests of Aireon; and
- a regulatory adjustment of $11 related to the deferral of foreign exchange gains on our investment in preferred interests of Aireon; and

- operating expenses that were $50 lower than planned primarily as a result of the Company's actions taken to reduce spending and cash outflow amid the COVID-19 pandemic.

	Nine months ended May 31		
	2020	2019	Change
Credit balance on the statement of financial position, beginning of period	$ 93	$ 124	$ (31)
Variances from planned results:			
Revenue lower than planned	(231)	(4)	(227)
Operating expenses lower than planned	65	14	51
Other (income) and expenses (higher) lower than planned	(82)	27	(109)
Net movement in other regulatory deferral accounts	104	(33)	137
Total variances from planned results	(144)	4	(148)
Initial approved adjustment	(27)	(14)	(13)
Net movement in rate stabilization account recorded in net loss	(171)	(10)	(161)
Credit (debit) balance on the statement of financial position, end of period	$ (78)	$ 114	$ (192)

The $171 decrease in the rate stabilization account during the nine months ended May 31, 2020 is primarily due to:

- revenue that was $231 lower than planned primarily due to the negative impact of the COVID-19 pandemic on air traffic volumes;
- other expenses that were $82 higher than planned primarily due to decrease in fair value of the investment in preferred interests of Aireon of $112, partially offset by an income tax recovery of $27 relating to the decrease in fair value of the investment in preferred interests of Aireon; and
- the planned adjustment of $27, representing three quarters of the anticipated $35 annual net loss at the time the fiscal 2020 budget was approved;

partially offset by:

- net movement of $104 in other regulatory deferral accounts that was higher than planned primarily due to:
  - a regulatory adjustment of $112 as a result of the decrease in fair value in the investment in preferred interests of Aireon;

(millions of Canadian dollars)

  - a regulatory expense for pension benefits that was $30 higher than planned primarily due to higher pension current service costs as a result of a decrease in the discount rate at August 31, 2019 compared to that used to prepare the fiscal 2020 budget; partially offset by
  - a regulatory adjustment of $27 related to the deferral of income tax recoveries due to the decrease in fair value of the investment in preferred interests of Aireon; and
  - a regulatory adjustment of $14 related to the deferral of foreign exchange gains on our investment in preferred interests of Aireon; and
- operating expenses that were $65 lower than planned, primarily as a result of the Company's actions taken to reduce spending and cash outflow amid the COVID-19 pandemic.

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		
	2020	2019	Change
Items that will be reclassified to income or (loss):			
Changes in fair value of cash flow hedges	$ -	$ (6)	$ 6
Net movement in regulatory deferral accounts	-	6	(6)
Total other comprehensive income (loss)	$ -	$ -	$ -

	Nine months ended May 31		
	2020	2019	Change
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)	10
Net movement in regulatory deferral accounts	(1)	10	(11)
Total other comprehensive income (loss)	$ -	$ -	$ -

There were no significant events or changes to the Company's defined benefit pension and other post-employment benefit plans that would require a revaluation during the three and nine months ended May 31, 2020 and May 31, 2019.

During the three and nine months ended May 31, 2019, negative fair value adjustments of $6 and $10, respectively, were recorded on the Company's interest rate hedges related to the re-financing of debt instruments that matured in fiscal 2019.

(millions of Canadian dollars)

Amounts Considered for Rate Setting Purposes

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

(a) air traffic results and forecasts;

(b) our financial and operating requirements, including our current and anticipated balance in the rate stabilization account and the extent to which our operating costs are variable and can be contained;

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

(d) updates to our financial forecasts, debt servicing and financial requirements, and resulting financial coverage ratios.

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

	May 31 2020	August 31 2019	Change
Rate stabilization account debit (credit) balance	$ 78	$ (93)	$ 171
Regulatory pension cash contributions to be recovered at a later date	$ 34	$ 34	$ -

Financial Outlook[2]

As noted previously under "INTRODUCTION - Caution Concerning Forward-Looking Information" and "INTRODUCTION - Significant Financial Matters", the Company has seen a significant decline in the number of air traffic movements as compared to the same period in fiscal 2019 as a result of travel restrictions imposed by governments, the closing of international borders and the economic impact of the pandemic. As a result, the Company's customer service charges revenue has declined significantly as air carriers have reduced their operations, grounded fleets and cancelled flights and routes. The pandemic is expected to continue to have a negative impact on air travel globally and this will likely continue until such time as travel restrictions are eased and consumer demand for air travel returns. Industry participants are indicating it may be some time before they fully return to pre COVID-19 operating levels. We expect until this occurs that reduced air traffic activity will have a significant negative impact on the Company's operations and revenues.

Given the evolving situation, Management continues to analyze the extent of the financial impact, which is expected to be material, depending on the duration of the pandemic. The Company has already taken steps to reduce operating costs as well as its ongoing and future capital program spending. The Company has also accessed its available syndicated credit facility to address near-term liquidity requirements in the amount of $225 and issued $850 of General Obligation Notes. In addition, the Company has accessed the CEWS government relief program.

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

(millions of Canadian dollars)

Presented below are the Company's current projected annual consolidated results before rate stabilization for fiscal 2020 compared to fiscal 2019 actual results. These projections reflect the assumption that air traffic movements will remain depressed at approximately 70-75% of fiscal 2019 levels through the end of fiscal 2020.

	Fiscal 2020	Fiscal 2019	Change	%
Before rate stabilization				
Revenue	$ 973	$ 1,437	$ (464)	(32%)
Operating expenses and other (income) and expenses, including other regulatory adjustments	1,382	1,468	(86)	(6%)
Net loss before rate stabilization adjustments	$ (409)	$ (31)	$ (378)	

Revenue

Revenue in fiscal 2020 is expected to decrease by approximately 32% or $464 from $1,437 in fiscal 2019 primarily due to the significant reduction in air traffic volumes as a result of the COVID-19 pandemic, resulting in forecasted negative air traffic growth of 35.8%. The reduction in customer service charge revenue is partially offset by increased revenue from technology sales and services.

Operating Expenses and Other (Income) and Expenses

Operating expenses and other (income) and expenses before rate stabilization for fiscal 2020 are expected to be $1,382. This is a decrease of 6% or $86 compared to fiscal 2019 primarily due to:

- targeted measures to decrease spending and cash outflows to help offset the significant decrease in customer service charge revenue, including reducing discretionary costs where possible and accessing the CEWS government relief program; and
- reduction in overtime costs as a result of the decrease in air traffic movements;

partially offset by:

- increased compensation levels arising largely from inflationary increases in collective agreements; and
- a full year of domestic satellite surveillance charges and the first partial year of oceanic satellite surveillance charges commencing in January 2020.

Cash Flows

Given the expected net cash outflows from operations and investing activities and net cash inflows from financing activities in fiscal 2020, the Company's cash position is currently anticipated to be $763 as at August 31, 2020 (August 31, 2019 - $30). This cash outlook is based on anticipated annual cash inflows from financing activities of $1,031, partially offset by cash outflows from operating activities of $166, largely due to the reduction in customer service charge revenue and cash outflows from investing activities of $133 related to the Company's capital program. Cash inflows from financing activities are largely due to net proceeds from the issuance of $850 of General Obligation Notes and net proceeds from bank loans of $225 at August 31, 2020 (offset by the associated interest costs and repayment of the $8 balance as at August 31, 2019), partially offset by the annual $25 principal repayment of the Series 97-2 amortizing revenue bonds.

Rate Stabilization Account

The Company currently anticipates that the rate stabilization account will have a debit balance of $316 at the end of fiscal 2020 (August 31, 2019 – credit balance of $93), resulting from the significant decrease in customer service charge revenue as a result of the COVID-19 pandemic, partially offset by decisive cost-cutting measures. The current and anticipated balance in the rate stabilization account (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes"), is a consideration in the setting of rates as well as future cost containment measures to be taken.

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, 2020, the Company had a net loss of $1. Our interest costs were $73. Consolidated earnings (after rate stabilization) before interest costs were $72, which is 0.99 times our interest requirement for the fiscal year and just under our one-to-one target. Depreciation and amortization expense for this period was $156. Our cash flow coverage was 3.12 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 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, 2020, 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.

(millions of Canadian dollars)

Related Party Transactions

The Company's related parties include its key management personnel, subsidiaries, joint ventures, entities in which it has a significant influence and registered pension plans for its employees. The transactions with these related parties are not materially different from what was reported in the fiscal 2019 annual MD&A with the exception of an agreement with Aireon to provide a subordinated loan, up to a total of $11 U.S. ($15 CDN), which was entered into during the nine months ended May 31, 2020.

SUMMARY OF QUARTERLY RESULTS

Quarterly Financial Information (unaudited)

	Three months ended			
	Q3 May 31 2020	Q2 February 29 2020	Q1 November 30 2019	Q4 August 31 2019
Revenue	$ 159	$ 322	$ 364	$ 412
Operating expenses	351	387	369	374
Other (income) and expenses	129	25	31	32
	(321)	(90)	(36)	6
Income tax recovery	(27)	-	-	(3)
Net income (loss) before net movement in regulatory deferral accounts	(294)	(90)	(36)	9
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	169	2	-	21
Other regulatory deferral account adjustments	111	38	39	30
	280	40	39	51
Net income (loss) after net movement in regulatory deferral accounts	$ (14)	$ (50)	$ 3	$ 60

	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

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. Given the negative impact of the COVID-19 pandemic on air traffic volumes, it is expected that the normal seasonality pattern will not occur in fiscal 2020. The Company's air traffic volumes decreased 59.4% over the course of Q3 fiscal 2020, as measured in WCU.

The majority of our operating expenses are incurred evenly throughout the year. To offset the significant reduction in revenue as a result of the pandemic, the Company will continue to review, monitor and take actions to reduce capital and operating spending and cash outflows.

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 long-term disability (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 2019 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, 2020.

As at May 31, 2020, we had $918 of cash and cash equivalents and committed credit facilities of $1,390, of which $309 was available for unrestricted use (see "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

Cash flows for the three months ended May 31, 2020

	Three months ended May 31		
	2020	2019	Change
Cash flows from (used in):			
Operating	$ (102)	$ 10	$ (112)
Investing	(26)	(29)	3
Financing	997	4	993
Cash flows from (used in) operating, investing and financing activities	869	(15)	884
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase (decrease) in cash and cash equivalents	870	(15)	885
Cash and cash equivalents, beginning of period	48	37	11
Cash and cash equivalents, end of period	$ 918	$ 22	$ 896
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations	$ (102)	$ 10	$ (112)
Capital expenditures (1)	(26)	(29)	3
Payment of lease liabilities (1)	(1)	-	(1)
Free cash flow	$ (129)	$ (19)	$ (110)

(1) See the statement of cash flows in our Q3 fiscal 2020 financial statements.

As shown above, cash and cash equivalents increased by $870 for the three months ended May 31, 2020 and the Company experienced negative free cash flow of $129, which is a non-GAAP financial measure as discussed in "INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2020".

Cash flows from operations for the three months ended May 31, 2020 were outflows of $102 compared to inflows of $10 for the three months ended May 31, 2019. The variance of $112 was primarily due to lower receipts from customer service charges of $157 as a result of the negative impact of COVID-19 pandemic on air traffic volumes, partially offset by lower payments to employees and suppliers of $35 and $6 received under the CEWS government relief program to offset compensation costs.

Cash outflows from investing activities for the three months ended May 31, 2020 were $26 compared to $29 for the three months ended May 31, 2019 and related to the Company's capital spending program.

Cash flows from financing activities for the three months ended May 31, 2020 were inflows of $997 compared to inflows of $4 for the three months ended May 31, 2019. The increase in Q3 fiscal 2020 was primarily a result of net proceeds of $845 from the issuance of the General Obligation Notes and $179 net proceeds from bank loans, partially offset by $25 to repay the Series 97-2 amortizing revenue bonds.

(millions of Canadian dollars)

Cash flows for the nine months ended May 31, 2020

	Nine months ended May 31		
	2020	2019	Change
Cash flows from (used in):			
Operating	$ (39)	$ 50	$ (89)
Investing	(106)	(84)	(22)
Financing	1,032	18	1,014
Cash flows from (used in) operating, investing and financing activities	887	(16)	903
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase (decrease) in cash and cash equivalents	888	(16)	904
Cash and cash equivalents, beginning of period	30	38	(8)
Cash and cash equivalents, end of period	$ 918	$ 22	$ 896
Free cash flow (non-GAAP financial measure):			
Cash flows from (used in):			
Operations	$ (39)	$ 50	$ (89)
Capital expenditures [(1)]	(106)	(95)	(11)
Payment of lease liabilities [(1)]	(2)	-	(2)
Free cash flow	$ (147)	$ (45)	$ (102)

(1) See the statements of cash flows of our Q3 fiscal 2020 financial statements.

As shown above, cash and cash equivalents increased by $888 during the nine months ended May 31, 2020 and the Company experienced negative free cash flow of $147, which is a non-GAAP financial measure as discussed in "INTRODUCTION – Financial Highlights: Cash flows for the three months ended May 31, 2020".

Cash flows from operations for the nine months ended May 31, 2020 were outflows of $39 compared to inflows of $50 for the nine months ended May 31, 2019, primarily due to lower receipts from customer service charges of $156 as a result of the negative impact of COVID-19 pandemic on air traffic volumes, partially offset by lower payments to employees and suppliers of $51, lower interest payments of $7 and $6 received under the CEWS government relief program to offset compensation costs.

Cash outflows from investing activities for the nine months ended May 31, 2020 were $106 compared to $84 in the nine months ended May 31, 2019. The Company invested $106 in capital projects during the nine months ended May 31, 2020 compared to $95 in the nine months ended May 31, 2019 which was partially offset by $11 cash inflows from the repayment of the bridge financing from Aireon.

Cash inflows from financing activities for the nine months ended May 31, 2020 were $1,032 compared to $18 for the nine months ended May 31, 2019. The inflows in fiscal 2020 were primarily a result of net proceeds of $845 from the issuance of the General Obligation Notes and $215 net proceeds from bank loans, partially offset by $25 to repay the Series 97-2 amortizing revenue bonds.

(millions of Canadian dollars)

Liquidity and Financing Strategy

Our liquidity and financing strategy remains unchanged from that disclosed in our fiscal 2019 annual MD&A.

We are exposed to refinancing 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 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, 2020, the credit facilities are utilized as follows:

Credit facilities:	
Credit facility with a syndicate of Canadian financial institutions (1) (2)	$ 850
Letter of credit facilities for pension funding purposes (3)	540
Total available credit facilities	1,390
Less: Outstanding letters of credit for pension funding purposes (3)	538
Less: Outstanding letters of credit for other purposes (2)	10
Less: Bank loan (net of interest costs)	223
Undrawn committed borrowing capacity	619
Less: Operations and maintenance reserve fund allocation (4)	310
Credit facilities available for unrestricted use	$ 309

(1) The Company's credit facility with a syndicate of Canadian financial institutions in the amount of $850 is comprised of two equal tranches maturing on September 12, 2022 and September 12, 2024. 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, 2020.

(2) At May 31, 2020, $10 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 $850 committed credit facility.

(3) The letter of credit facilities for pension funding purposes are comprised of four facilities with Canadian financial institutions totalling $540. Two of the credit facilities, representing $250, are set to mature on December 31, 2020 and the remaining facilities will expire on December 31, 2021. At May 31, 2020, $538 was drawn for pension solvency funding purposes. As discussed in "INTRODUCTION – Significant Financial Matters: Pension Plans", subsequent to May 31, 2020, the Company requested a decrease of $5 to our outstanding letters of credit.

(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").

(millions of Canadian dollars)

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

	May 31 2020	August 31 2019
LONG-TERM DEBT:		
Bonds and notes payable		
Under the Master Trust Indenture	$ 425	$ 450
Under the General Obligation Indenture	1,875	1,025
	2,300	1,475
Adjusted for deferred financing costs and discounts	(12)	(7)
Total bonds and notes payable	2,288	1,468
Less: current portion of long-term debt	(275)	(25)
Total long-term debt	$ 2,013	$ 1,443
LIQUIDITY:		
Cash and cash equivalents	$ 918	$ 30
Debt service reserve fund	73	72
	$ 991	$ 102
Undrawn committed borrowing capacity (1)	$ 619	$ 684

(1) $309 of this borrowing capacity is available as described in the previous table (August 31, 2019 - $374).

Credit Ratings

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

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

As a result of the COVID-19 pandemic, on April 1, 2020, S&P revised its outlook on the Company to negative from stable and affirmed its 'AA' long-term issuer credit and senior secured debt ratings, and 'AA-' senior subordinated debt rating. In revising its outlook to negative, S&P noted that the revision reflects a one-in-three chance that they could lower the ratings over the next 12 to 24 months. S&P indicated they would consider doing so should a prolonged traffic downturn or slow traffic recovery post-pandemic lead to large and sustained deterioration in financial metrics.

S&P noted that they "expect NAV CANADA to withstand the significant pressure that the traffic decline is exerting on its cash flows, as it possesses adequate liquidity and no large debt issues until February 2021".

S&P stated that they expect NAV CANADA will preserve strong relationships with domestic financial institutions, maintaining its track record of access to external liquidity. In assessing our ability to manage external shocks, S&P points to the Company's legislated ability to fully adjust user charges to meet our financial obligations with the view that good debt service metrics provide additional financial capacity.

On April 8, 2020, Moody's affirmed NAV CANADA's ratings and stable outlook. The ratings action reflects NAV CANADA's strong liquidity profile. The "liquidity sources, combined with cost management measures, planned liquidity enhancement measures and capital expenditure reductions that are being considered, will provide NAV CANADA with the ability to withstand the material declines in passenger traffic that we expect in 2020 and possibly still into 2021."

Moody's stated that "the stable rating outlook reflects our expectation that NAV CANADA will implement the necessary rate increases to compensate for lower levels of activity as a result of the coronavirus outbreak."

On April 17, 2020, 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; and
- Manageable capital expenditure program.

They also noted the following credit challenges:

- Material short-term negative impact of the coronavirus outbreak on revenues due to reduced air traffic activity; and
- Defined benefit pension plan creates recurring calls on cash.

Moody's stated that "the rating outlook is stable, reflecting our expectation that NAV CANADA will ultimately implement the necessary rate increases to compensate for lower levels of activity as a result of the coronavirus outbreak."

On May 26, 2020, S&P and Moody's affirmed NAV CANADA's credit ratings ahead of the Company's issuance of General Obligation Notes.

(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 2019 annual MD&A.

Contractual Obligations

A breakdown of contractual obligations as at May 31, 2020 for the next five fiscal years and thereafter is presented in the following table. 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.

	Remaining payments – for years ending August 31						
	Total	2020	2021	2022	2023	2024	Thereafter
Bank loan	$ 223	$ 223	$ -	$ -	$ -	$ -	$ -
Long-term debt (including current portion) (1), (2)	2,300	-	275	25	25	25	1,950
Interest payments (2)	1,495	18	83	78	76	74	1,166
Capital commitments	120	77	15	11	3	3	11
Operating contract commitments	16	1	4	3	3	2	3
Future lease liabilities(3)	59	-	-	-	2	3	54
Lease liability	7	1	3	3	-	-	-
Related party loan (4)	15	15	-	-	-	-	-
Total contractual obligations	$ 4,235	$ 335	$ 380	$ 120	$ 109	$ 107	$ 3,184

(1) Payments represent principal of $2,300. 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.

(2) Further details on interest rates and maturity dates on long-term debt are provided in note 9 of the Q3 fiscal 2020 financial statements and note 14 of the 2019 annual consolidated financial statements.

(3) The Company has entered into a commitment for the lease of head office space commencing in the fiscal year ending August 31, 2023. The annual commitment is approximately $3 with a term of 20 years. The current head office lease is set to expire on October 31, 2022.

(4) During the nine months ended May 31, 2020, the Company entered into an agreement with Aireon to provide a subordinated loan up to a total of $11 U.S. ($15 CDN).

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 2019 annual MD&A.

(millions of Canadian dollars)

Capital Management

The Company views capital as the sum of its issued long-term debt, retained earnings (deficit) and accumulated other comprehensive income, regulatory deferral accounts and balances under certain employee benefit plans, 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 2020	August 31 2019
Bonds and notes payable	$ 2,288	$ 1,468
Equity:		
Retained earnings (deficit)	(33)	28
Regulatory deferral accounts:		
Debit balances	(2,263)	(2,087)
Credit balances	197	376
Employee benefits:		
LTD liability	2	3
Liability for funded pension benefits	1,943	1,813
Liability for accumulating sick leave	17	17
Total capital	$ 2,151	$ 1,618

Management's approach and objectives when managing capital remain unchanged from those described in our fiscal 2019 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 2019 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 2019 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, 2020, except as discussed below and as noted under the heading "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy".

Interest Rate Risk: We are exposed to the risk that net interest expense will increase as a result of changes in market interest rates. As at May 31, 2020, the Company has $991 invested in financial assets that bear interest at floating rates (August 31, 2019 - $102). A 100 basis point change in variable interest rates would result in an annual difference of approximately $8 in the Company's earnings before rate stabilization adjustments (August 31, 2019 - $1).

Foreign Exchange Risk: As at May 31, 2020, the Company's net exposure to foreign exchange risk related to the U.S. dollar has decreased, largely due to the decrease in the fair value of the investment in preferred interests of Aireon. If the Canadian dollar strengthened or weakened by 10% against the U.S. dollar as at May 31, 2020, all other variables remaining constant, net income (loss) before net movement in regulatory deferral accounts would have been impacted by $32 (August 31, 2019 - $40).

Other Price Risk: During Q3 fiscal 2020, the Company reviewed the fair value of its investment in preferred interests of Aireon. The fair value was determined using a discounted cash flow model. The estimated fair value of the investment in preferred interests of Aireon may change in subsequent periods. Any such changes could be material and would be reflected in the statement of operations as they occur. A sensitivity analysis with respect to changes in the unobservable inputs to the valuations is discussed in note 10 of the Q3 fiscal 2020 financial statements.

Aireon provides global satellite-based surveillance capability for air navigation service providers around the world. The following risks have been identified with respect to the Company's investment in preferred interests of Aireon:

- The reduction in air traffic across the globe as a result of the COVID-19 pandemic and travel restrictions put in place;
- The expectation that air traffic may not return to pre COVID-19 levels for some time, which will impact Aireon's revenue where billings are volumetric and reflect air traffic movements; and
- The expectation that the Company's receipt of dividends will therefore be delayed.

Insurance

Our aviation liability insurance program was last renewed on November 15, 2019 for one year. This insurance covers all of our ANS 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

Significant accounting policies used in these interim condensed consolidated financial statements are disclosed in note 3 of the 2019 annual consolidated financial statements, except for the application of new standards, amendments and interpretations effective September 1, 2019 as described in note 2 (f) of the Company's November 30, 2019 interim condensed consolidated financial statements. The note details the impact and changes in accounting policies as a result of the adoption of IFRS 16 – *Leases*, effective September 1, 2019. 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. At this time, the Company does not expect to adopt any of these standards or amendments before their effective dates.

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

<u>IAS 37 Provisions, Contingent Liabilities and Contingent Assets: Onerous Contracts - Cost of Fulfilling a Contract</u>

In May 2020, the IASB published *Onerous Contracts - Cost of Fulfilling a Contract* amending the standard regarding costs a company should include as the cost of fulfilling a contract when assessing whether a contract is onerous. The amendment clarifies that for the purpose of assessing whether a contract is onerous, the cost of fulfilling the contract includes both the incremental costs of fulfilling that contract and allocation of other costs that relate directly to fulfilling contracts.

The amendment is effective for annual periods beginning on or after January 1, 2022 with early application permitted. The extent of the impact of the changes have not yet been determined.

<u>IAS 1 Presentation of Financial Statements: Classification of Liabilities as Current or Non-current</u>

In January 2020, the IASB published *Classification of Liabilities as Current or Non-current* providing a more general approach to the classification of liabilities based on the contractual arrangements in place at the reporting date.

The amendment is effective for annual periods beginning on or after January 1, 2022 with early application permitted. In April 2020, the IASB published an exposure draft proposing to delay the effective date to annual periods beginning on or after January 1, 2023. The extent of the impact of the changes have not yet been determined.

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of these interim condensed consolidated financial statements requires management to make estimates and judgments about the future.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Accounting estimates will, by definition, seldom equal actual results.

Critical judgments and key sources of estimation uncertainty are disclosed in note 2 (d) of the 2019 annual consolidated financial statements.

The Company's critical accounting estimates and judgments applied in the preparation of the Company's Q3 fiscal 2020 financial statements are consistent with those applied and disclosed in our fiscal 2019 annual consolidated financial statements and as described in the fiscal 2019 annual MD&A, with the exception of those related to the Company's investment in preferred interests of Aireon as discussed below.

Investment in Preferred Interests of Aireon

The Company's investment in Aireon is in preferred interests, which are redeemable and convertible to common equity interests. Until the Company exercises its right to convert its preferred interests to common interests, it does not have access to Aireon's residual net assets and accordingly this investment is accounted for as a financial instrument classified and measured at FVTPL.

During Q3 fiscal 2020, the Company updated the fair value of its investment in preferred interests of Aireon to reflect the impact of the COVID-19 pandemic and related travel restrictions on Aireon's operations and the aviation sector in general as discussed in section "INTRODUCTION – Significant Financial Matters: Investment in Preferred Interests of Aireon".

The fair value of the Company's investment in preferred interests of Aireon as at May 31, 2020 was determined using a discounted cash flow model, where the valuation model considers the present value of expected future payments, discounted using a risk-adjusted discount rate. The critical assumptions and estimates used when determining the fair value are:

- discount rates – the discount rate range used is 15% - 17%, which is generally consistent with discount rates used by other investors in preferred and common equity interests of Aireon; and
- expected timing of future dividend payments – the timing of the payments based on Aireon's forecasted after-tax dividend payment schedule has been delayed to reflect the impact of COVID-19.

The Company continues to monitor the status of Aireon in order to determine whether there are any indicators that would impact Aireon's fair value. Changes in the valuation of Aireon as a whole could materially affect the valuation of the investment in preferred interests, with changes reflected in the statement of operations as required. The investment in preferred interests of Aireon is subject to price risk. The fair value may fluctuate over time due to, among other things, economic conditions and the cash flows of Aireon.

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, 2020 that have materially affected or are reasonably likely to materially affect the Company's ICFR.