

**EXFO Inc.**  
**Condensed Unaudited Interim Consolidated Balance Sheets**

(in thousands of US dollars)

	<b>As at February 28, 2014</b>	<b>As at August 31, 2013</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash	\$ 47,064	\$ 45,386
Short-term investments	4,641	4,868
Accounts receivable		
Trade	43,511	50,117
Other	2,525	2,778
Income taxes and tax credits recoverable	5,511	6,525
Inventories	37,280	35,705
Prepaid expenses	3,035	2,561
	143,567	147,940
<b>Tax credits recoverable</b>	40,994	41,719
<b>Property, plant and equipment</b>	42,852	45,523
<b>Intangible assets</b>	5,539	7,543
<b>Goodwill</b>	25,969	27,313
<b>Deferred income taxes</b>	11,136	10,807
<b>Other assets</b>	693	693
	\$ 270,750	\$ 281,538
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	\$ 31,267	\$ 26,253
Provisions	638	756
Income taxes payable	337	679
Current portion of long-term debt	–	296
Deferred revenue	8,625	9,467
	40,867	37,451
<b>Deferred revenue</b>	3,501	3,932
<b>Deferred income taxes</b>	3,373	3,226
<b>Other liabilities</b>	922	477
	48,663	45,086
<b>Shareholders' equity</b>		
Share capital (note 4)	111,337	109,837
Contributed surplus	15,787	17,186
Retained earnings	110,766	112,852
Accumulated other comprehensive loss	(15,803)	(3,423)
	222,087	236,452
	\$ 270,750	\$ 281,538

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

# EXFO Inc.

## Condensed Unaudited Interim Consolidated Statements of Earnings

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

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
<b>Sales</b>	\$ 51,179	\$ 107,182	\$ 62,576	\$ 122,397
Cost of sales <sup>(1)</sup> (note 5)	20,073	41,258	23,664	47,321
Selling and administrative (note 5)	21,537	43,245	23,074	45,364
Net research and development (note 5)	10,973	22,254	11,960	23,562
Depreciation of property, plant and equipment (note 5)	1,243	2,518	1,504	3,109
Amortization of intangible assets (note 5)	1,074	2,256	1,922	3,884
Interest (income) expenses	(49)	(76)	25	(8)
Foreign exchange gain	(2,292)	(3,094)	(1,700)	(2,456)
<b>Earnings (loss) before income taxes</b>	<u>(1,380)</u>	<u>(1,179)</u>	<u>2,127</u>	<u>1,621</u>
<b>Income taxes</b> (note 6)	<u>(41)</u>	<u>907</u>	<u>2,088</u>	<u>3,220</u>
<b>Net earnings (loss) for the period</b>	<u>\$ (1,339)</u>	<u>\$ (2,086)</u>	<u>\$ 39</u>	<u>\$ (1,599)</u>
<b>Basic and diluted net earnings (loss) per share</b>	\$ (0.02)	\$ (0.03)	\$ 0.00	\$ (0.03)
<b>Basic weighted average number of shares outstanding (000's)</b>	60,414	60,316	60,392	60,391
<b>Diluted weighted average number of shares outstanding (000's)</b> (note 7)	60,414	60,316	61,175	60,391

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

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

# EXFO Inc.

## Condensed Unaudited Interim Consolidated Statements of Comprehensive Loss

(in thousands of US dollars)

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
<b>Net earnings (loss) for the period</b>	\$ (1,339)	\$ (2,086)	\$ 39	\$ (1,599)
Other comprehensive income (loss), net of income taxes				
Items that will not be reclassified subsequently to net earnings				
Foreign currency translation adjustment	(9,580)	(11,528)	(9,184)	(10,892)
Items that may be reclassified subsequently to net earnings				
Unrealized gains/losses on forward exchange contracts	(1,289)	(1,529)	(679)	(762)
Reclassification of realized gains/losses on forward exchange contracts in net earnings (loss)	191	365	(130)	(329)
Deferred income tax effect of gains/losses on forward exchange contracts	294	312	217	293
Other comprehensive loss	<u>(10,384)</u>	<u>(12,380)</u>	<u>(9,776)</u>	<u>(11,690)</u>
<b>Comprehensive loss for the period</b>	<u>\$ (11,723)</u>	<u>\$ (14,466)</u>	<u>\$ (9,737)</u>	<u>\$ (13,289)</u>

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

# EXFO Inc.

## Condensed Unaudited Interim Consolidated Statements of Changes in Shareholders' Equity

(in thousands of US dollars)

	<b>Six months ended February 28, 2013</b>				
	<b>Share capital</b>	<b>Contributed surplus</b>	<b>Retained earnings</b>	<b>Accumulated other comprehensive income</b>	<b>Total shareholders' equity</b>
Balance as at September 1, 2012	\$ 110,965	\$ 17,298	\$ 111,511	\$ 13,507	\$ 253,281
Exercise of stock options (note 4)	87	-	-	-	87
Redemption of share capital (note 4)	(913)	(227)	-	-	(1,140)
Reclassification of stock-based compensation costs (note 4)	1,261	(1,261)	-	-	-
Stock-based compensation costs	-	878	-	-	878
Net loss for the period	-	-	(1,599)	-	(1,599)
Other comprehensive loss					
Foreign currency translation adjustment	-	-	-	(10,892)	(10,892)
Changes in unrealized gains/losses on forward exchange contracts, net of deferred income taxes of \$293	-	-	-	(798)	(798)
Total comprehensive loss for the period	<u>-</u>	<u>-</u>	<u>(1,599)</u>	<u>(11,690)</u>	<u>(13,289)</u>
Balance as at February 28, 2013	<u>\$ 111,400</u>	<u>\$ 16,688</u>	<u>\$ 109,912</u>	<u>\$ 1,817</u>	<u>\$ 239,817</u>

	<b>Six months ended February 28, 2014</b>				
	<b>Share capital</b>	<b>Contributed surplus</b>	<b>Retained earnings</b>	<b>Accumulated other comprehensive loss</b>	<b>Total shareholders' equity</b>
Balance as at September 1, 2013	\$ 109,837	\$ 17,186	\$ 112,852	\$ (3,423)	\$ 236,452
Exercise of stock options (note 4)	195	-	-	-	195
Redemption of share capital (note 4)	(831)	(106)	-	-	(937)
Reclassification of stock-based compensation costs (note 4)	2,136	(2,136)	-	-	-
Stock-based compensation costs	-	843	-	-	843
Net loss for the period	-	-	(2,086)	-	(2,086)
Other comprehensive loss					
Foreign currency translation adjustment	-	-	-	(11,528)	(11,528)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes of \$312	-	-	-	(852)	(852)
Total comprehensive loss for the period	<u>-</u>	<u>-</u>	<u>(2,086)</u>	<u>(12,380)</u>	<u>(14,466)</u>
Balance as at February 28, 2014	<u>\$ 111,337</u>	<u>\$ 15,787</u>	<u>\$ 110,766</u>	<u>\$ (15,803)</u>	<u>\$ 222,087</u>

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

# EXFO Inc.

## Condensed Unaudited Interim Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
<b>Cash flows from operating activities</b>				
Net earnings (loss) for the period	\$ (1,339)	\$ (2,086)	\$ 39	\$ (1,599)
Add (deduct) items not affecting cash				
Changes in discount on short-term investments	–	–	(3)	(1)
Stock-based compensation costs	402	865	468	916
Depreciation and amortization	2,317	4,774	3,426	6,993
Deferred revenue	1,024	(728)	111	(1,420)
Deferred income taxes	(324)	301	988	1,721
Changes in foreign exchange gain/loss	(793)	(901)	(775)	(798)
	<u>1,287</u>	<u>2,225</u>	<u>4,254</u>	<u>5,812</u>
Changes in non-cash operating items				
Accounts receivable	6,182	4,525	2,016	(6,088)
Income taxes and tax credits	(1,686)	(943)	(1,313)	(3,186)
Inventories	(1,221)	(3,533)	1,213	1,053
Prepaid expenses	(787)	(616)	(414)	(55)
Other assets	(40)	(34)	–	–
Accounts payable, accrued liabilities and provisions	(94)	5,391	(3,687)	(50)
Other liabilities	(17)	(43)	(15)	(210)
	<u>3,624</u>	<u>6,972</u>	<u>2,054</u>	<u>(2,724)</u>
<b>Cash flows from investing activities</b>				
Additions to short-term investments	(4,790)	(14,571)	(10,236)	(34,769)
Proceeds from disposal and maturity of short-term investments	4,790	14,562	13,283	37,810
Additions to capital assets	(1,695)	(2,396)	(2,504)	(4,493)
	<u>(1,695)</u>	<u>(2,405)</u>	<u>543</u>	<u>(1,452)</u>
<b>Cash flows from financing activities</b>				
Repayment of long-term debt	(307)	(307)	(293)	(293)
Exercise of stock options	89	195	36	87
Redemption of share capital	(937)	(937)	(167)	(1,140)
	<u>(1,155)</u>	<u>(1,049)</u>	<u>(424)</u>	<u>(1,346)</u>
<b>Effect of foreign exchange rate changes on cash</b>				
	<u>(1,475)</u>	<u>(1,840)</u>	<u>(1,566)</u>	<u>(1,921)</u>
<b>Change in cash</b>	(701)	1,678	607	(7,443)
<b>Cash – Beginning of the period</b>	<u>47,765</u>	<u>45,386</u>	<u>50,818</u>	<u>58,868</u>
<b>Cash – End of the period</b>	<u>\$ 47,064</u>	<u>\$ 47,064</u>	<u>\$ 51,425</u>	<u>\$ 51,425</u>
<b>Supplementary information</b>				
Interest paid	\$ 7	\$ 9	\$ 17	\$ 26
Income taxes paid	\$ 229	\$ 871	\$ 552	\$ 937
Additions to capital assets	\$ 1,196	\$ 2,680	\$ 1,021	\$ 2,261

As at February 28, 2013 and 2014, unpaid purchases of capital assets amounted to \$677 and \$515 respectively.

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

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

### 1 Nature of Activities and Incorporation

EXFO Inc. and its subsidiaries (together “EXFO” or the company) design, manufacture and market test and service assurance solutions for wireless and wireline network operators and equipment manufacturers in the global telecommunications industry. The company offers core-to-edge solutions to assess the performance and reliability of converged Internet protocol (IP) fixed and mobile networks.

EXFO is a company incorporated under the Canada Business Corporations Act and domiciled in Canada. The address of its headquarters is 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2.

These condensed interim consolidated financial statements were authorized for issue by the Board of Directors on March 25, 2014.

### 2 Basis of Presentation

These condensed interim consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB) applicable to the preparation of interim financial statements, including IAS 34, “*Interim Financial Reporting*”, and using the same accounting policies and methods used in the preparation of the company’s most recent annual consolidated financial statements except for the changes in accounting policies described below. Consequently, these condensed interim consolidated financial statements should be read in conjunction with the company’s most recent annual consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB.

#### New IFRS Pronouncements and Amendments

The company has adopted the following amended and new standards, effective September 1, 2013. These changes were made in accordance with the applicable transitional provisions.

##### *Consolidation*

IFRS 10, “*Consolidated Financial Statements*”, requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. IFRS 10 replaces Standing Interpretations Committee (“SIC”) 12, “*Consolidation — Special Purpose Entities*”, and parts of IAS 27, “*Consolidated and Separate Financial Statements*”. The adoption of IFRS 10 had no impact on the company’s consolidated financial statements.

##### *Joint arrangements*

IFRS 11, “*Joint Arrangements*”, requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operations. Joint ventures are accounted for using the equity method of accounting whereas for a joint operation, the venture recognizes its share of the assets, liabilities, revenues and expenses of the joint operation. IFRS 11 replaces IAS 31, “*Interests in Joint Ventures*” and SIC 13, “*Jointly Controlled Entities — Non-Monetary Contributions by Venturers*”. The adoption of IFRS 11 had no impact on the company’s consolidated financial statements.

##### *Disclosure of interests in other entities*

IFRS 12, “*Disclosure of Interests in Other Entities*”, establishes disclosure requirements for interests in other entities, such as subsidiaries, joint arrangements, associates and structured entities. This standard carries forward existing disclosures and introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity’s interests in other entities. The adoption of IFRS 12 had no impact on the company’s consolidated financial statements.

# EXFO Inc.

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### *Fair value measurement*

IFRS 13, “*Fair Value Measurement*”, is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and, in many cases, does not reflect a clear measurement basis or consistent disclosures. The adoption of IFRS 13 did not require any adjustment to the valuation techniques used by the company to measure fair value. The company provided the required additional disclosure in its consolidated financial statements (note 3).

### *Financial instruments*

IFRS 7, “*Financial Instruments: Disclosures*”, has been amended to enhance disclosure requirements related to offsetting of financial assets and liabilities. The adoption of these amendments had no impact on the company’s consolidated financial statements.

## 3 Financial Instruments

### *Fair Value of Financial Instruments*

The company classifies its derivative and non-derivative financial assets and liabilities measured at fair value using the fair value hierarchy as follows:

Level 1: Quoted prices (unadjusted) in active market for identical assets or liabilities;

Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset and liability, either directly or indirectly;

Level 3: Unobservable inputs for the asset or liability.

The company’s short-term investments are classified within level 1 of the fair value hierarchy because they are valued using quoted market prices in active markets. The company’s forward exchange contracts are classified within level 2 of the fair value hierarchy because they are valued using quoted prices and forward exchange rates at the balance sheet dates.

The fair value of forward exchange contract represents the amount at which they could be settled based on estimated current market rates.

The fair value of derivative and non-derivative financial assets and liabilities by level of hierarchy is as follows:

	<b>As at February 28, 2014</b>		<b>As at August 31, 2013</b>	
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 1</b>	<b>Level 2</b>
<b>Financial assets</b>				
Short-term investments	\$ 4,641	\$ –	\$ 4,868	\$ –
<b>Financial liabilities</b>				
Forward exchange contracts	\$ –	\$ 1,847	\$ –	\$ 722

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

### **Derivative Financial Instruments**

The functional currency of the company is the Canadian dollar. The company is exposed to a currency risk as a result of its export sales of products manufactured in Canada, China and Finland, the majority of which are denominated in US dollars and euros. This risk is partially hedged by forward exchange contracts (US dollars) and certain operating expenses (US dollars and euros). Forward exchange contracts, which are designated as cash flow hedging instruments, qualify for hedge accounting.

As at February 28, 2014, the company held contracts to sell US dollars for Canadian dollars at various forward rates, which are summarized as follows:

Expiry dates	Contractual amounts	Weighted average contractual forward rates
March 2014 to August 2014	\$ 10,800	1.0308
September 2014 to August 2015	18,200	1.0589
September 2015 to August 2016	13,400	1.0923
September 2016 to December 2016	3,400	1.1063
Total	\$ 45,800	1.0656

The carrying amount of forward exchange contracts is equal to fair value, which is based on the amount at which they could be settled based on estimated current market rates. The fair value of forward exchange contracts amounted to net losses of \$808,000 as at August 31, 2013 and \$2,111,000 as at February 28, 2014.

Based on the portfolio of forward exchange contracts as at February 28, 2014, the company estimates that the portion of the net unrealized losses on these contracts as of that date, which will be realized and reclassified from accumulated other comprehensive income to net earnings over the next 12 months, amounts to \$1,196,000.

As at February 28, 2014, forward exchange contracts in the amount of \$1,196,000 are presented as current liabilities in accounts payable and accrued liabilities and forward exchange contracts of \$651,000 are presented as long-term liabilities in other long-term liabilities in the balance sheet. These forward exchange contracts are not yet recorded within sales.

During the three and six months ended February 28, 2013 and 2014, the company recognized within its sales the following gains or losses on forward exchange contracts:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Gains (losses) on forward exchange contracts	\$ (285)	\$ (369)	\$ 153	\$ 355



# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

### 4 Share Capital

On January 8, 2014, the company announced that its Board of Directors approved the renewal of its share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of the issued and outstanding subordinate voting shares, representing 2,043,101 subordinate voting shares at the prevailing market price. The company expects to use cash, short-term investments or future cash flow from operations to fund the repurchase of shares. The normal course issuer bid started on January 13, 2014, and will end on January 12, 2015, or on an earlier date if the company repurchases the maximum number of shares permitted under the bid. The program does not require that the company repurchases any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled.

The following tables summarize changes in share capital for the six months ended February 28, 2013 and 2014.

	<b>Six months ended February 28, 2013</b>				
	<b>Multiple voting shares</b>		<b>Subordinate voting shares</b>		<b>Total Amount</b>
	<b>Number</b>	<b>Amount</b>	<b>Number</b>	<b>Amount</b>	
Balance as at September 1, 2012	31,643,000	\$ 1	28,710,891	\$ 110,964	\$ 110,965
Exercise of stock options	-	-	23,275	51	51
Redemption of restricted share units	-	-	127,949	-	-
Redemption of share capital	-	-	(205,123)	(793)	(793)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	612	612
Balance as at November 30, 2012	31,643,000	1	28,656,992	110,834	110,835
Exercise of stock options	-	-	7,400	36	36
Redemption of restricted share units	-	-	141,725	-	-
Redemption of deferred share units	-	-	37,054	-	-
Redemption of share capital	-	-	(31,210)	(120)	(120)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	649	649
Balance as at February 28, 2013	<u>31,643,000</u>	<u>\$ 1</u>	<u>28,811,961</u>	<u>\$ 111,399</u>	<u>\$ 111,400</u>

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

	Six months ended February 28, 2014				
	Multiple voting shares		Subordinate voting shares		Total Amount
	Number	Amount	Number	Amount	
Balance as at September 1, 2013	31,643,000	\$ 1	28,401,790	\$ 109,836	\$ 109,837
Exercise of stock options	-	-	25,800	106	106
Redemption of restricted share units	-	-	315,583	-	-
Redemption of deferred share units	-	-	38,010	-	-
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	1,435	1,435
Balance as at November 30, 2013	31,643,000	1	28,781,183	111,377	111,378
Exercise of stock options	-	-	20,500	89	89
Redemption of restricted share units	-	-	95,882	-	-
Redemption of share capital	-	-	(214,470)	(831)	(831)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	701	701
Balance as at February 28, 2014	<u>31,643,000</u>	<u>\$ 1</u>	<u>28,683,095</u>	<u>\$ 111,336</u>	<u>\$ 111,337</u>

### 5 Statements of Earnings

Net research and development expenses comprise the following:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Gross research and development expenses	\$ 13,046	\$ 26,355	\$ 14,126	\$ 28,024
Research and development tax credits and grants	(2,073)	(4,101)	(2,166)	(4,462)
	<u>\$ 10,973</u>	<u>\$ 22,254</u>	<u>\$ 11,960</u>	<u>\$ 23,562</u>

Gross research and development expenses for the three months and the six months ended February 28, 2013, include \$89,000 in restructuring charges.

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

Depreciation and amortization expenses by functional area are as follows:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Cost of sales				
Depreciation of property, plant and equipment	\$ 380	\$ 764	\$ 422	\$ 867
Amortization of intangible assets	497	1,062	1,257	2,531
	<u>877</u>	<u>1,826</u>	<u>1,679</u>	<u>3,398</u>
Selling and administrative expenses				
Depreciation of property, plant and equipment	234	481	275	572
Amortization of intangible assets	380	775	432	874
	<u>614</u>	<u>1,256</u>	<u>707</u>	<u>1,446</u>
Net research and development expenses				
Depreciation of property, plant and equipment	629	1,273	807	1,670
Amortization of intangible assets	197	419	233	479
	<u>826</u>	<u>1,692</u>	<u>1,040</u>	<u>2,149</u>
	<u>\$ 2,317</u>	<u>\$ 4,774</u>	<u>\$ 3,426</u>	<u>\$ 6,993</u>
Depreciation of property, plant and equipment	\$ 1,243	\$ 2,518	\$ 1,504	\$ 3,109
Amortization of intangible assets	<u>1,074</u>	<u>2,256</u>	<u>1,922</u>	<u>3,884</u>
	<u>\$ 2,317</u>	<u>\$ 4,774</u>	<u>\$ 3,426</u>	<u>\$ 6,993</u>

Inventory write-down is as follows:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Inventory write-down	\$ <u>1,251</u>	\$ <u>2,438</u>	\$ 924	\$ <u>1,937</u>

Employee compensation comprises the following:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Salaries and benefits	\$ 30,700	\$ 60,720	\$ 32,183	\$ 63,230
Stock-based compensation costs	<u>402</u>	<u>865</u>	<u>468</u>	<u>916</u>
Total employee compensation for the period	<u>\$ 31,102</u>	<u>\$ 61,585</u>	<u>\$ 32,651</u>	<u>\$ 64,146</u>

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

Stock-based compensation costs by functional area are as follows:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Cost of sales	\$ 45	\$ 100	\$ 57	\$ 112
Selling and administrative expenses	259	592	310	623
Net research and development expenses	98	173	101	181
	<u>\$ 402</u>	<u>\$ 865</u>	<u>\$ 468</u>	<u>\$ 916</u>

### 6 Income taxes

For the three months and the six months ended February 28, 2013 and 2014, the reconciliation of the income tax provision calculated using the combined Canadian federal and provincial statutory income tax rate with the income tax provision in the financial statements is as follows:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Income tax provision (recovery) at combined Canadian federal and provincial statutory tax rate (27%)	\$ (372)	\$ (318)	\$ 574	\$ 437
Increase (decrease) due to:				
Foreign income taxed at different rates	(209)	(295)	(97)	(278)
Non-taxable (income)/loss	(471)	(893)	(372)	(1,164)
Non-deductible expenses	181	407	222	423
Foreign exchange effect of translation of foreign subsidiaries	(34)	212	(74)	284
Utilization of previously unrecognized deferred income tax assets	12	(3)	-	-
Unrecognized deferred income tax assets on temporary deductible differences and unused tax losses	974	1,961	1,062	2,694
Other	(122)	(164)	773	824
	<u>\$ (41)</u>	<u>\$ 907</u>	<u>\$ 2,088</u>	<u>\$ 3,220</u>

# EXFO Inc.

## Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

The income tax provision (recovery) consists of the following:

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Current	\$ 283	\$ 606	\$ 1,100	\$ 1,499
Deferred	(324)	301	988	1,721
	<u>\$ (41)</u>	<u>\$ 907</u>	<u>\$ 2,088</u>	<u>\$ 3,220</u>

### 7 Earnings per Share

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

	Three months ended February 28, 2014	Six months ended February 28, 2014	Three months ended February 28, 2013	Six months ended February 28, 2013
Basic weighted average number of shares outstanding (000's)	60,414	60,316	60,392	60,391
Plus dilutive effect of (000's):				
Stock options	2	17	33	32
Restricted share units	491	645	641	651
Deferred share units	90	102	109	121
	<u>\$ 60,997</u>	<u>\$ 61,080</u>	<u>\$ 61,175</u>	<u>\$ 61,195</u>
Diluted weighted average number of shares outstanding (000's)				
Stock awards excluded from the calculation of diluted weighted average number of shares because their exercise price was greater than the average market price of the common shares (000's)	<u>\$ 259</u>	<u>\$ 129</u>	<u>\$ 84</u>	<u>\$ 102</u>

For the six months ended February 28, 2013 and the three and six months ended February 28, 2014, the diluted amount per share was the same amount as the basic amount per share since the dilutive effect of stock options, restricted share units and deferred share units was not included in the calculation; otherwise, the effect would have been antidilutive. Accordingly, the diluted amount per share for these periods was calculated using the basic weighted average number of shares outstanding.