Hammond Power Solutions Inc.

Q3 Report 2020

For the nine months ended September 26, 2020

Our Vision

To be a leading global supplier of transformers and magnetics within our chosen markets.

Our Mission

We are a growing and profitable global supplier of transformers and related magnetic products dedicated to satisfying the collective needs of our shareholders, customers, suppliers, employees and community.

Our Values

We value the **safety** and **well-being** of all

We expect **honesty, integrity** and **ethical behaviour**

We embrace **diversity** by nurturing an **inclusive** environment and treating everyone with **dignity** and **respect**

We promote **innovation** and a relentless pursuit of **continuous improvement** through **teamwork**

We believe in **a collaborative approach** to **social** and **environmental sustainability**

Fellow shareholder,

During the most challenging social and economic times that Hammond Power Solutions Inc. ("HPS") has faced in our history, we are pleased to deliver solid financial performance and market share gains in Quarter 3, 2020.

After a very difficult Quarter 2 business environment as much of North America and India were shuttered due to government restrictions, our business robustly rebounded in this last quarter in Canada, the United States ("U.S.") as well as in India. Although our sales are not yet back to the levels of 2019, we have realized record gains both in market share and in margins despite this challenging environment.

This recovery as we know has been uneven in both its breadth and pace. Some resource-related markets such as oil and gas have been devastated by a significant decline in both demand as well as commodity prices. This in turn has had a severe impact on the economic activity in certain parts of the U.S. and Canada. As the U.S. economy gradually comes to life however, our expanded coast-to-coast distributor network is picking up new industrial and commercial business. Our unique advantage of broad diversity in terms of markets, channels, products and geography has been a catalyst in growing our business and strengthening our financial performance during these difficult times.

Our most important and continuing advantage this year has been the incredible passion, support and performance of our employees around the globe. Our focus surrounding the health and safety of our employees and their families has enabled us to continue to operate meeting the needs of our distributors and customers and gaining us a competitive advantage.

We are aware that some challenges may still lie ahead over the next six months due to a resurgence of the pandemic as well as U.S. political uncertainty however we are confident in our continued financial strength and performance, as well as our ability to provide superior service through the continuing efforts of our passionate employees.

William G. Hammond
CHAIRMAN OF THE BOARD & CHIEF EXECUTIVE OFFICER
Grandson of founder Oliver Hammond

Management's Discussion and Analysis

Hammond Power Solutions Inc. (“HPS” or the “Company”) is a North American leader in the design and manufacture of custom electrical engineered magnetics, standard electrical dry-type, cast resin and liquid filled transformers. Advanced engineering capabilities, high quality products, global reach and fast responsive service to customers’ needs have established the Company as a technical and innovative leader serving the electrical and electronic industries. The Company has manufacturing plants in Canada, the United States (“U.S.”), Mexico and India.

The following is Management’s Discussion and Analysis (“MD&A”) of the Company’s consolidated operating results for the nine months ended September 26, 2020, and should be read in conjunction with the accompanying unaudited Condensed Interim Consolidated Financial Statements of the Company for the third quarter of fiscal 2020. This information is based on Management’s knowledge as at November 4, 2020. The Company assumes that the reader of this MD&A has access to and has read the audited Annual Consolidated Financial Statements and MD&A of the Company, contained in our 2019 Annual Report and accordingly, the purpose of this document is to provide a third quarter update to the information contained in the fiscal 2019 MD&A. All amounts are reported under International Financial Reporting Standards (“IFRS”). All amounts in this report are expressed in thousands of Canadian dollars unless otherwise noted. Additional information relating to the Company may be found on SEDAR’s website at www.sedar.com, or on the Company’s website at www.hammondpowersolutions.com.

Caution regarding forward-looking information

This MD&A contains forward-looking statements that involve a number of risks and uncertainties including statements that relate to among other things, HPS’ strategies, intentions, plans, beliefs, expectations and estimates, and can generally be identified by the use of words such as “may”, “will”, “could”, “should”, “would”, “likely”, “expect”, “intend”, “estimate”, “anticipate”, “believe”, “plan”, “objective” and “continue” and words and expressions of similar import. Although HPS believes that the expectations reflected in such forward-looking statements are reasonable, such statements involve risks and uncertainties and undue reliance should not be placed on such statements. Certain material factors or assumptions are applied in making forward-looking statements, and actual results may differ materially from those expressed or implied in such statements. Important factors that could cause actual results to differ materially from expectations include but are not limited to: the impact of the pandemic; general business and economic conditions (including but not limited to currency rates); changes in laws and regulations; legal and regulatory proceedings; and the ability to execute strategic plans. HPS does not undertake any obligation to update publicly or to revise any of the forward-looking statements contained in this document, whether as a result of new information, future events or otherwise, except as required by law.

Additional GAAP and Non-GAAP measures

This document uses the terms "earnings from operations" which represents earnings before finance and other costs/(income) and income taxes. "EBITDA" is also used and is defined as earnings before interest, taxes, depreciation and amortization. "Adjusted EBITDA" from continuing operations represents EBITDA from continuing operations adjusted for foreign exchange gain or loss. Operating earnings, EBITDA and Adjusted EBITDA are some of the measures the Company uses to evaluate the operational profitability. The Company presents EBITDA to show its performance before interest, taxes and depreciation and amortization. Management believes that HPS shareholders and potential investors in HPS use additional GAAP and non-GAAP financial measures, such as operating earnings, EBITDA and Adjusted EBITDA in making investment decisions about the Company and to measure its operational results. A reconciliation of EBITDA and Adjusted EBITDA to net earnings for the quarters ending September 26, 2020 and September 28, 2019 is contained in the MD&A. Earnings from operations, EBITDA and Adjusted EBITDA should not be construed as a substitute for net earnings determined in accordance with IFRS.

"Order bookings" represent confirmed purchase orders for goods or services received from our customers. "Backlog" represents all unshipped customer orders. "Book value per share" is the total shareholders' equity divided by the average outstanding shares. The terms "earnings from operations" "EBITDA", "Adjusted EBITDA", "order bookings", "backlog" and "book value per share" do not have any standardized meaning prescribed within IFRS and may not be comparable to similar measures presented by other companies.

Sales

Sales from continuing operations for the quarter-ended September 26, 2020 were $78,115 versus Quarter 3, 2019 sales of $91,502, a decrease of $13,387 or 14.6%. The sales decline was primarily impacted by the negative effect that the Coronovirus ("COVID-19") global pandemic had on many of our markets and our customers due to the deferment of electrical projects, business interruptions and overall lower economic activity. Year-to-date 2020 sales from continuing operations were $241,928 compared to $268,129 in 2019, a decrease $26,201 or 9.8%.

Sales in the United States ("U.S.") decreased by $8,661 or 16.0%, finishing at $45,608 for Quarter 3, 2020 compared to $54,269 in Quarter 3, 2019. Year-to-date U.S. sales were $153,841 in 2020 and $167,709 in 2019, a decline of $13,868 or 8.3%. The decrease in the Quarter 3, 2020 sales is a result of declines in private branding, a sluggish Original Equipment Manufacturer ("OEM") market, motor control, specialty, mining and power control markets. This was partially offset by solid North American Electrical Distributor ("NAED") sales and increased switchgear and machine building markets.

Third quarter sales were slightly favourably affected by a 0.8% stronger U.S. dollar ("USD") $1.00 USD = $1.33 Canadian dollar ("CAD") compared against $1.00 USD = $1.32 CAD in Quarter 3, 2019. Year-to-date sales were positively impacted by a 1.5% stronger U.S. dollar – $1.00 USD = $1.35 CAD compared against $1.00 USD = $1.33 CAD in 2019.

U.S. sales, when stated in U.S. dollars were $34,174 in Quarter 3, 2020, compared to Quarter 3, 2019 of $41,118, a decline of $6,944 or 16.9%. Year-to-date U.S. sales stated in U.S. dollars were $113,571 in 2020 compared to $126,145 in 2019, a decrease of $12,574 or 10.0%.

Canadian sales were $28,833 for the quarter, realizing a 31.5% increase or $6,911 over Quarter 2, 2020 of sales of $21,922 and decreased $2,658 or 8.4% compared to Quarter 3, 2019 sales of $31,491. Year-to-date Canadian sales were $78,099 in 2020 compared to $87,015 in 2019, a decrease of $8,916 or 10.2%. Canadian sales experienced declines in a number of markets this quarter compared to the same quarter last year, specifically the NAED, capital equipment, utilities and switchgear markets. There were modest increases in the mining, specialty and medical markets during the quarter.

Indian sales for Quarter 3, 2020 finished at $3,674 versus $5,742 in Quarter 3, 2019, a decrease of $2,068 or 36.0% as COVID-19 continues to dramatically constrain the Indian market. Year-to-date Indian sales were $9,988 in 2020 compared to $13,405 in 2019, a decrease of $3,417 or 25.5% due to government imposed COVID-19 100% lockdown of the country during the second quarter.

Quarter 3, 2020 sales from continuing operations stated by geographic segment were derived from U.S. sales of 58.4% (Quarter 3, 2019 – 59.3 %) of total sales, Canadian sales of 36.9% (Quarter 3, 2019 – 34.4 %), and Indian sales of 4.7% (Quarter 3, 2019 – 6.3 %).

The negative economic impact of COVID-19 continues to be evident in the Company's third quarter sales where declines were seen across many markets and customers, particularly the OEM market. The Company had experienced market share growth through U.S. distributor channels due to the ability to produce both standard and custom transformers.

Third quarter sales have seen improvement in some markets that had dramatically declined at the beginning of the pandemic. Many companies are finding ways to move forward with business or projects as the end of the pandemic is unknown. While third quarter sales declined due to the impact of the global pandemic, the Company was steadfast in growing market share through its strong NAED and Original Equipment Manufacturer ("OEM") channels. This was achieved through the Company's broad product offerings, strong customer service, organic customer diversity, new customer business development and geographically diverse manufacturing capabilities. The Company's market share continues to be industry leading – distributor conversions, standard and custom transformers manufacturing capabilities and service commitment all allow the Company to be a leader in the electrical transformer market.

The Company's engineering and manufacturing capabilities in dry, liquid filled and cast resin transformer technology is a strength to the Company and fundamental to revenue growth. HPS' growth strategy is evidenced by its business development activities, vertical integration strategies, capital investment and past restructuring actions.

The Company prides itself on building our value proposition as we are unwavering in our commitment to providing exceptional value to our customers through product breadth, custom engineered design and manufacture capabilities, uncompromised quality, service value and ease of doing business.

These factors together with a strong, effective distribution channel, multi-national manufacturing capabilities and global reach will continue to be an advantage for the Company and critical to continued revenue growth. The Company's market diversification strategy is not single-market or industry dependent, resulting in a natural business hedge as some markets grow while others decline.

Order bookings and backlog

Due to the effects of the COVID-19 pandemic, both North America and India experienced decreased bookings of 20.2% as compared to Quarter 3, 2019, primarily in the direct sales/OEM sales channel, which had a decrease of 43.7% while booking rates in the distributor channel were up 2.3%, in spite of the business effects of the pandemic in Quarter 3, 2020. The Company's market position is well anchored in both the U.S. and Canadian distribution markets as the Company continues to hold a strong market share position in our traditional markets through the distribution channel.

Further, as a result of the Quarter 3, 2020 pandemic impact on new order development, the overall year-to-date Company's bookings have decreased 15.4% over the same period as last fiscal year. The distributor channel bookings decreased 6.7% and the direct channel bookings are lower by 27.2%.

The Company order backlog decreased by 9.9% over Quarter 3, 2019, even though bookings rates were lower as product shipments were delayed due to project delays and company closures as a result of the pandemic. Quarter quotation activity was fairly active – a positive indicator of future sales. It is expected the combination of the Company's strategic sales initiatives, service, dominant distributor footprint and new product development will support our booking rates.

HPS is not immune to, and is sensitive to, the volatility and unpredictability of current global economies and the impact that this will have on booking trends. While several markets are seeing positive quotation and order trends, the Company is cognizant that it may see some volatility and unpredictability in longer term booking rates.

Gross margin

The company was successful at delivering an increase in its gross margin rate for Quarter 3, 2020, which was 27.5% compared to a Quarter 3, 2019 gross margin rate of 24.9%, an increase of 2.6% of sales. The year-to-date gross margin rate was 26.4% in 2020 versus 24.1% in 2019, an increase of 2.3%. The margin rate improvement in both the quarter and year-to-date is attributed to a combination of a number of factors: sales mix, market selling price realization, lower raw material commodity costs and receipt of the Canada Emergency Wage Subsidy ("CEWS") benefit in Quarter 2 and 3, 2020. The CEWS program provides an employee wage subsidy for our Canadian entities for periods where there was a significant decline in Canadian trade sales due to the impact of the coronavirus ("COVID-19"). During the quarter, the wage subsidy received for production labour was $2,057 or 2.6% of sales, year-to-date was $4,584 or 1.9% of sales The company did incur extraordinary operating expenses of $287 during the Quarter or 0.4% of sales, year-to-date expenses of $1,576 or 0.7% of sales, relating to wages paid for suspended operational employee wages, non-productive wage support for “at risk” employees, employee transportation, increased cleaning, sanitation and personal protective equipment expenses for the safety of its employees. Excluding the wage subsidy and COVID-19 related expenses, the Company still delivered an increase in gross margin rate of 0.4% during the quarter and 1.1% year-to-date.

The demand for our product is stable, however sales volumes will be determined primarily by which industries and customers are continuing to operate and in what capacity. During the quarter we have seen activity in some markets that had completely shutdown when the pandemic originally started in North America while other markets continue to struggle. As sales decrease, the lower manufacturing throughput will have a dilutive impact on margin rates. The Company will still realize growth in some markets and experience a decline in others underscoring the volatility of markets and sales demand. We are steadfast in our implementation of initiatives to manage the negative volatility impact through our distributor footprint, cost reductions, our product and market breadth as well as our multi-national manufacturing capabilities.

HPS continues to focus on price realization strategies and the achievement of cost reductions in an effort to maintain or increase margin rates. Fluctuating markets, product mix and the effect of COVID-19 on the current global economy will have substantial long-term impact on financial results. Looking forward, the unpredictability of the economic and geopolitical impact of the pandemic and the effect on business activity combined with our backlog decrease, provides an indication of caution for an unknown period of time. HPS was identified as an essential service in all countries that we operate in and was able to continue to manufacture with the exception of India where the country was in lockdown at the end of the first quarter as well as a large portion of the second quarter.

Gross margin rate is impacted by productivity gains, material procurement and engineering cost reduction initiatives. The Company’s ability to flex its manufacturing capacity demand and cost structures is fundamental for future gross margin attainment and improvement. HPS remains focused on its continuous improvement program and cost reductions across the entire organization which will help offset the negative effects of manufacturing load fluctuations and/or reductions. We are confident that these actions going forward will support us in maximizing margin rates during the current economic times. Our diversified market and channel approach will also safeguard some of the impact we’ve experienced during this global pandemic.

Selling and distribution expense

Total selling and distribution expenses were $9,524 in Quarter 3, 2020 or 12.2% of sales versus $10,706 in Quarter 3, 2019 or 11.7% of sales, a decrease of $1,182 but an increase of 0.5% of sales. Year-to-date selling and distribution expenses were $30,015 or 12.4% of sales in 2020 compared to $31,552 or 11.8% of sales in 2019, a decrease of $1,537 but an increase of 0.6% of sales. The increase in the percentage of sales is due to the reduced sales for Quarter 3, 2020. The company did incur lower variable selling costs for commissions and freight expenses due to the lower sales volumes in the quarter, reduced travel expenses and the CEWS benefit of $310 or 0.4% of sales and continued expense management.

The year-over-year decrease in selling and distribution expenses is a result of lower variable freight and commission expenses, reduced travel costs, and the CEWS benefit of $696 or 0.3% of sales. These reductions were partially offset by start-up and operational expenses related to a new distribution centre in Reno, Nevada.

General and administrative expense

General and administrative expenses for Quarter 3, 2020 were $6,525 or 8.4% of sales, compared to Quarter 3, 2019 expenses of $6,604 or 7.2% of sales, a decrease of $79 but an increase of 1.2% of sales. The increases in the percentage of sales is due to the lower sales value for Quarter 3, 2020. Additional provisions for doubtful accounts receivable, were offset by the CEWS benefit in the amount of $657 or 0.8% of sales in the quarter.

Year-to-date general and administrative expenses were $18,786 or 7.8% of sales in 2020, compared to $18,425 or 6.9% of sales in 2019, an increase of $361 or 0.9% of sales. Year-to-date the CEWS benefit was $1,479 or 0.6% of sales. The year-to-date increase in these expenses can be attributed to the continuing costs related to our European business and property holdings in Italy, compensation costs and additional provisions for doubtful accounts receivable, which are partially offset by the CEWS benefit.

Earnings from continuing operations

Quarter 3, 2020 earnings from operations were $5,447, a small decrease of $24 or 0.4% from $5,471 for the same quarter last year. The year-to-date earnings from operations were $14,994 in 2020 compared to $14,681 in 2019, an increase of $313 or 2.1%. The decline in the quarter is mainly a result of the decrease in gross margin dollars due to decreased sales, increased operating expenses related to the pandemic – offset by government wage subsidy support.

Increased year-to-date earnings from operations is due to CEWS benefit support offsetting lower gross margin dollars and increased operating expenses related to the pandemic.

Earnings from operations are calculated as outlined in the following table:

	Quarter 3, 2020	Quarter 3, 2019	**YTD 2020**	YTD 2019
Net earnings from continuing operations	$ 3,462	$ 3,595	$ 10,030	$ 9,455
Add:				
Income tax expense	1,650	1,434	4,471	4,240
Interest expense	240	419	951	1,060
Foreign exchange gain	(45)	(149)	(524)	(80)
Share of loss (income) of investment in joint venture	107	139	(33)	(86)
Other	33	33	99	92
Earnings from operations	$ 5,447	$ 5,471	$ 14,994	$ 14,681

Net finance and other costs

Interest expense for Quarter 3, 2020 was $240, a decrease of $179 or 42.7% compared to the Quarter 3, 2019 expense of $419. Year-to-date interest cost was $951, a decrease of $109 or 10.3% when compared to the 2019 year-to-date expense of $1,060. A portion of the change in Quarter 3, 2020, $78 in the current year and $73 in the prior year, was due to the accounting standard adoption of IFRS 16 for leases which allocates part of lease costs to interest expense. The year-to-date interest expense related to leases was $257 in 2020 and $228 in 2019. The remainder of the change in the interest expense is a result of lower operating debt levels during the year. Interest expense includes all bank fees.

The foreign exchange gain in Quarter 3, 2020 was $45, a decrease of $104 compared to the gain of $149 in Quarter 3, 2019. The year-to-date foreign exchange gain for 2020 was $524, compared to a gain of $80 for the same period last year, an increase of $444. This gain relates primarily to the transactional exchange pertaining to the Company's U.S. dollar trade accounts payable in Canada. The earnings impact of the foreign exchange gains and losses are related to the increased volatility in the exchange rates during the past year.

As at September 26, 2020, the Company had outstanding foreign exchange contracts in place for 17,400 Euros ("EUR") and $11,000 USD – all of which are implemented as an economic hedge against translation gains and losses on inter-company loans as well as $46,500 USD to economically hedge the U.S. dollar denominated accounts payable in Canadian HPS operations.

Corefficient de R.L. de C.V. ("Corefficient") realized a loss of $107 for Quarter 3, 2020 compared to a loss of $139 for Quarter 3, 2019, a decline of $32. Year-to-date Corefficient has generated income of $33 in 2020 compared to income of $86 in 2019, a decline of $53. While Quarter 1 showed an improvement in the joint venture performance as a result of elevated sales, higher manufacturing throughput, lower material costs and increased selling prices, Quarter 2 and 3 have been impacted by increased costs related to COVID-19 management as well as a decline in sales volume.

Income taxes

Quarter 3, 2020 income tax expense was $1,650 as compared to $1,434 in Quarter 3, 2019, an increase of $216 or 15.1%. Year-to-date income tax expense was $4,471 in 2020 and $4,240 in 2019, an increase of $231 or 5.4%.

The consolidated effective tax rate for Quarter 3, 2020 was 32.3% as compared to 28.5% in 2019, an increase of 3.8%. The year-to-date effective tax rate for the first nine months of 2020 was 30.8% compared to 31.0% for the same period in 2019, a decrease of 0.2%. The changes in the effective tax rates are greatly impacted by changes in the earnings mix of the Company and the share of the loss of investment in joint venture. The Company income is generated from different tax jurisdictions and is subject to different tax rates and regulations.

Deferred tax assets and liabilities consisting mainly of reserves and allowances are related to temporary differences on current assets and liabilities and are not deductible against current year earnings. Deferred tax assets and liabilities relate to temporary differences resulting from intangible assets and the difference between the net book value and undepreciated capital cost of property, plant and equipment.

Net earnings from continuing operations

Net earnings from continuing operations for Quarter 3, 2020 finished at $3,462 compared to net earnings of $3,595 in Quarter 3, 2019, a decline of $133 or 3.7%. Year-to-date net earnings from continuing operations were $10,030 in 2020 compared to $9,455 in 2019, an increase of $575 or 6.1%. The increase in the earnings from continuing operations is a result of the government wage subsidy support and higher foreign exchange gains in the current year offset by decreased gross margin dollar contributions.

Discontinued operations

In Quarter 4, 2018, the Company closed the Italian facility and ceased operations as the entity struggled to generate adequate revenue and profits. The restructuring charges were comprised of severance and benefit costs related to workforce reductions, closure and cancellation costs and write-downs of goodwill, long-lived assets and inventory. The closure of the Italian operations has been presented as discontinued operations in the 2019 financial statements. In 2020 the Italian real estate holding and business development entity is included as part of the continuing operations of the Company.

Earnings per share from continuing operations

The basic earnings per share from continuing operations was $0.30 for Quarter 3, 2020, versus $0.31 in Quarter 3, 2019, a small decline of $0.01 or 3.2%. The year-to-date basic earnings per share from continuing operations was $0.86 in 2020 and $0.81 in 2019, an increase of $0.05 or 6.2%.

EBITDA

EBITDA for Quarter 3, 2020 was $7,466 versus $7,302 in Quarter 3, 2019, an increase of $164 or 2.2%. Year-to-date EBITDA was $21,591 in 2020 and $20,524 in 2019, an increase of $1,067 or 5.2%.

EBITDA and adjusted EBITDA is calculated as outlined in the following table:

	Quarter 3, 2020	Quarter 3, 2019	**YTD 2020**	YTD 2019
Net earnings from continuing operations	$ 3,462	$ 3,595	$ 10,030	$ 9,455
Add:				
Interest expense	240	419	951	1,060
Income tax expense	1,650	1,434	4,471	4,240
Depreciation and amortization	2,114	1,854	6,139	5,769
EBITDA from continuing operations	$ 7,466	$ 7,302	$ 21,591	$ 20,524
Subtract:				
Foreign exchange gain	(45)	(149)	(524)	(80)
Adjusted EBITDA from continuing operations	$ 7,421	$ 7,153	$ 21,067	$ 20,444

Summary of Quarterly Financial Information (Unaudited)

Fiscal 2020 Quarters	Quarter 1, 2020	Quarter 2, 2020	Quarter 3, 2020	YTD Total
Sales	$ 88,420	$ 75,393	$ 78,115	$ 241,928
Net earnings	$ 2,148	$ 4,420	$ 3,462	$ 10,030
Net earnings per share – basic	$ 0.18	$ 0.38	$ 0.30	$ 0.86
Net earnings per share – diluted	$ 0.18	$ 0.38	$ 0.30	$ 0.86
Average U.S. to Canadian exchange rate	$ 1.3388	$ 1.3907	$ 1.3346	$ 1.3547

Fiscal 2019 Quarters	Quarter 1, 2019	Quarter 2, 2019	Quarter 3, 2019	Quarter 4, 2019	Total
Sales	$ 84,690	$ 91,937	$ 91,502	$ 90,653	$ 358,782
Net earnings from continuing operations	$ 2,508	$ 3,352	$ 3,595	$ 3,851	$ 13,306
Net earnings per share from continuing operations – basic	$ 0.21	$ 0.29	$ 0.31	$ 0.32	$ 1.13
Net earnings per share from continuing operations – diluted	$ 0.21	$ 0.29	$ 0.31	$ 0.32	$ 1.13
Average U.S. to Canadian exchange rate	$ 1.3301	$ 1.3379	$ 1.3198	$ 1.3203	$ 1.3270

Quarter 3, 2020 sales declined below prior year levels due to the impact of COVID-19 but have increased from Quarter 2, 2020 levels. There continues to be significant fluctuations of sales volumes in various markets, with some markets being more heavily impacted by COVID-19 than others. Sales for 2020 have been favourably impacted due to small fluctuations in exchange rates.

Gross margin rates for the quarter have increased from the same quarter last year and year-to-date margins have also increased despite a slight decline in the first quarter of the year. This margin improvement can be attributed to sales mix, market specific pricing and raw material commodity costs. HPS Canadian entities received the CEWS government subsidy to partially offset additional costs related to managing COVID-19. While margins have increased, gross margin dollars have decreased in Quarter 3 and year-to-date.

Fluctuations in exchange rates resulted in a gain in foreign exchange in the first nine months of 2020 of $524 compared to a gain of $80 in 2019.

Selling and distribution expenses have decreased in the quarter due to lower variable freight and commission expenses attributed to the decreased sales and receipt of the CEWS reimbursement. General and administrative expense decrease can be attributed to additional provisions for doubtful accounts receiveable, which were offset by the CEWS benefit.

Corefficient, our joint venture that manufactures transformer cores, had a loss for the quarter of $107 in 2020 and loss of $139 in 2019. Year-to-date the joint venture generated income of $33 for 2020 compared to $86 in 2019. While Quarter 1, 2020 showed an improvement in the joint venture performance as a result of elevated sales, higher manufacturing throughput, lower material costs and increased selling prices, Quarter 2 and 3 have been impacted by increased costs related to COVID-19 management as well as a decline in volume.

Changes in volume, product mix, changing economic conditions, fluctuating commodity costs and competitive pricing pressures have all had an impact on the year-over-year quarterly fluctuations for both sales and income.

Capital resources and liquidity

Net cash generated by operating activities for Quarter 3, 2020 was $10,419 versus net cash used for operating activities of $1,460 in Quarter 3, 2019, an improvement of $11,879. This change has been generated by positive cash from working capital during the Quarter. Year-to-date net cash generated by operating activities was $11,610 compared to $1,363 in 2019, an increase of $10,247. The year-to-date increase is a result of higher earnings and lower cash used for working capital during the year.

During the quarter, non-cash working capital generated cash of $7,131 compared to cash used of $3,869 for the same quarter last year, an increase of $11,000. The year-to-date change in non-cash working capital was cash usage of $4,167 in 2020 compared to $14,300 in 2019, a decrease of usage of $10,133. The year-to-date working capital changes are primarily related to a decrease in accounts receivable.

Cash used in investing activities decreased by $583 from $1,055 in the first nine months of 2019 to $472 in the same period of 2020. Capital expenditures were $472 in Quarter 3, 2020 compared to $1,054 for Quarter 3, 2019, a decrease of $582. Year-to-date capital expenditures were $2,002 in the current year compared to $2,615 in 2019. The Company continues to invest in the areas of manufacturing processes and capabilities, information technology and new product development.

Total cash used in financing activities for Quarter 3, 2020 was $723 as compared to $865 in Quarter 3, 2019, a decrease of $142. The source of this change was higher advance of operating debt in Quarter 3, 2020 offset by higher dividend payments and lease payments. Year-to-date financing activities used cash of $11,182 compared to $7,576 in the first nine months of 2019, an increase of $3,606. Higher repayment of operating debt was $2,781 of the year-to-date change.

Bank operating lines of credit have decreased from prior year levels finishing Quarter 3, 2020 at $27,322 compared to $30,007 at the end of Quarter 3, 2019, a decrease of $2,685. The bank operating lines of credit have decreased $5,375 since the year-end balance of $32,697 and decreased $6,895 since the Quarter 1, 2020 balance of $34,217.

The company's liquidity is solid. The Company's overall operating debt balance net of cash was $4,790 in Quarter 3, 2020 compared to $22,678 in Quarter 3, 2019, a decrease in debt position of $17,888 primarily reflective of increased profitability and receipt of CEWS payments.

All bank covenants continue to be met as at September 26, 2020.

The Company will utilize its cash generated from operations combined with the existing available credit facilities to finance ongoing operational cash requirements for working capital, capital expenditures and investing activities going forward.

Contractual obligations

	2020	2021	2022	2023	2024	Total
Accounts payable and accrued liabilities	$ 46,485	–	–	–	–	$ 46,485
Capital expenditure purchase commitments	3,298	–	–	–	–	3,298
Bank operating lines	–	27,322	–	–	–	27,322
Lease liabilities	1,700	2,111	2,217	1,730	1,389	9,147
Total	$ 51,483	$ 29,433	$ 2,217	$ 1,730	$ 1,389	$ 86,252

Regular quarterly dividend declaration

During Quarter 3, 2020 the Board of Directors of HPS declared a quarterly cash dividend of eight and a half cents ($0.085) per Class A Subordinate Voting Share of HPS and a quarterly cash dividend of eight and a half cents ($0.085) per Class B Common Share of HPS payable on September 28, 2020 to shareholders of record at the close of business on September 18, 2020. The ex-dividend date was September 26, 2020. The Company has paid a cash dividend of twenty-five and a half cents ($0.255) per Class A Subordinate Voting Share and twenty-five and a half cents ($0.255) per Class B Common Share year-to-date. The dividend yield is 5.5%.

Controls and procedures

The Chief Executive Officer and the Chief Financial Officer are responsible for establishing and maintaining disclosure controls and procedures and for establishing and maintaining adequate internal controls over financial reporting. The control framework used in the design of disclosure controls and procedures and internal control over financial reporting is the 2013 Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("2013 COSO Framework"). Our internal control system was designed to provide reasonable assurance to our Management and Board of Directors regarding the preparation and fair presentation of published financial statements in accordance with International Financial Reporting Standards. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

During Quarter 3, 2020 there were no material changes identified in HPS' internal controls over financial reporting that had materially affected, or was reasonably likely to materially affect HPS' internal control over financial reporting. HPS does carry out ongoing improvements to its internal controls over financial reporting but nothing considered at a material level.

Risks and uncertainties

The Company's goal is to proactively manage risks in a structured approach in conjunction with strategic planning, with the intent to preserve and enhance shareholder value. However as with most businesses HPS is subject to a number of market place, industry and economic-related business risks, which could cause our results to vary materially from anticipated future results. The Company is acutely cognizant of these risks and continually assesses the current and potential impacts that they have on the business. HPS continuously strives to curtail the negative impact of these risks through diversification of its core business, market channel expansion, breadth of product offering, geographic diversity of its operations and business hedging strategies.

Coronavirus ("COVID-19") – Business Disruption

Markets, governments and health organizations around the world are working to contain the outbreak of the COVID-19. COVID-19 presents a wide range of potential issues or complications for the Company, most of which the Company is not able to know the full extent of.

The following is a summary of what the Company believes may impact their business as a result of COVID-19:

- Disruptions to business operations resulting from quarantines of employees, customers, suppliers and third party service providers in areas affected by the outbreak;
- Disruptions to business operations resulting from travel restrictions;
- Uncertainty around the duration of the virus' impact; and
- Change in classification of essential services, requiring HPS to shut down operations.

Currently, COVID-19 will be a material disruption to the Company's business. Our operations in Canada, the U.S. and Mexico have been designated as "essential services" businesses. Our Indian operations were not operating from March 24, 2020 to May 2, 2020 as the government had imposed a 100% lockdown of the country, shutting down all businesses. Although the company's U.S. markets remain steady, it appears that the company will see significant reductions in sales in the Canadian and Indian markets. Due to the uncertainty and unpredictability of the impacts of the COVID-19 pandemic on the business operations, the uncertainty of governmental and health authorities legislation, the negative financial impact of the unprecedented pandemic will be more clearly determinable over the next few quarters.

Other Business Risks

If any of the following risks were to occur they could materially adversely affect HPS' financial condition, liquidity or results of operations.

We may not realize all of the anticipated benefits of our acquisitions, divestures, joint ventures or strategic initiatives, or these benefits may take longer to realize than expected.

In order to be profitable, the Company must successfully execute upon its strategic initiatives and effectively manage the resulting changes in its operations. The Company's assumptions underlying its strategic plans may be subjective, the market may react negatively to these plans and HPS may not be able to successfully execute these plans, and even if successfully executed, its actions may not be effective or may not lead to the anticipated benefits within the expected time frame.

These strategic initiatives can include acquisitions and joint ventures. To be successful, management will conduct due diligence to identify valuation issues and potential loss contingencies, negotiate transaction terms, complete complex transactions and manage post-closing matters such as the integration of acquired startup businesses. Management's due diligence reviews are subject to the completeness and accuracy of disclosures made by third parties. The Company may incur unanticipated costs or expenses following a completed acquisition, including post-closing asset impairment charges, expenses associated with eliminating duplicate facilities, litigation or other liabilities.

Many of the factors that could have an adverse impact will be outside of management's control and could result in increased costs and decreases in the amount of expected revenues and diversion of management's time and attention. Failure to implement an acquisition strategy, including successfully integrating acquired businesses, could have an adverse effect on our business, financial condition and result of operations.

We sell to customers around the world and have global operations and, therefore, are subject to the risks of doing business in many countries.

We do business in a host of countries around the world. Approximately 75% of our sales were to customers outside of Canada. In addition, a number of our manufacturing operations, suppliers and employees are located in many places around the world. The future success of our business depends in large part on growth in our sales in non-Canadian markets. Our global operations are subject to numerous financial, legal and operating risks, such as political and economic instability; prevalence of corruption in certain countries; enforcement of contract and intellectual property rights and compliance with existing and future laws, regulations and policies, including those related to tariffs, investments, taxation, trade controls, product content and performance, employment and repatriation of earnings.

Our global business translates into conducting business in various currencies, all of which are subject to fluctuations.

HPS' global footprint exposes the Company to currency fluctuations and volatility and at times, has had a significant impact on the financial results of the Company. The Company's functional currency is the Canadian dollar with its operating results reported in Canadian dollars. A significant portion of Company's sales and material purchases are denominated in U.S. dollars. There is a natural hedge as sales denominated in U.S. dollars are partially offset by the cost of raw materials purchased from the U.S. and commodities tied to U.S. dollar pricing. A change in the value of the Canadian dollar against the U.S. dollar will impact earnings significantly at times. Generally, a lower value for the Canadian dollar compared to the U.S. dollar will have a beneficial impact on the Company's results while a higher value for the Canadian dollar compared to the U.S. dollar will have a corresponding negative impact on the Company's profitability.

HPS has partially reduced the impact of foreign exchange fluctuations by increasing our U.S. dollar driven manufacturing output, periodically instituting price increases to help offset negative changes and entering into forward foreign exchange contracts.

Worldwide HPS is subject to, and required to comply with, multiple income and other taxes, regulations and is exposed to uncertain tax liabilities risk.
The Company operates and is subject to income tax and other forms of taxation in numerous tax jurisdictions. Taxation laws and rates which determine taxation expenses may vary significantly in different jurisdictions and legislation governing taxation laws and rates is also subject to change. Therefore, the Company's earnings may be impacted by changes in the proportion of earnings taxed in different jurisdictions, changes in taxation rates, changes in estimates of liabilities and changes in the amount of other forms of taxation. Tax structures are subject to review by both domestic and foreign taxation authorities. The determination of the consolidated tax provision and liabilities requires significant judgment. Tax filings are subject to audits which could materially change the amount of current and deferred income tax assets and liabilities.

We face the potential harms of natural disasters, acts of war, terrorism, international conflicts or other disruptions to our operations.
Our business depends on the movement of goods around the world. Natural disasters, pandemics, acts or threats of war or terrorism, international conflicts, political instability and the actions taken by governments could cause damage to or disrupt our business operations, our suppliers or our customers and could create economic instability. Although it is not possible to predict such events or their consequences, these events could decrease demand for our products or make it difficult or impossible to deliver our products.

The U.S. political uncertainty and potential for changes in the business environment can lead to legislative changes that could impact business.
The U.S. has a number of geopolitical risks that could be challenging for the Company. The impact of these political changes can be difficult to predict and can have a pervasive impact on the global business climate. Changes in political leaders can impact trade relations as well as taxes and/or duties. The Company's current structure includes a significant amount of business that crosses borders and any changes in the current trade structure could have a material impact for the Company. The Company's global footprint will be critical to mitigating any impact for political changes that would modify the current trade relationships.

Our industry is highly competitive.
HPS faces competition in all of our market segments. Current and potential competitors may have greater brand name recognition, more established distribution networks, access to larger customer bases and substantially greater financial, distribution, technical, sales and market, manufacturing and other resources than HPS. As a result, those competitors may have advantages relative to HPS; including stronger bargaining power with suppliers that may result in more favourable pricing, the ability to secure supplies at time of shortages, economies of scale in production, the ability to respond more quickly to changing customer demands and the ability to devote great resources to the development, promotion and sales of their products and services. If the Company is unable to compete effectively, it may experience a loss of market share or reduced profitability. We expect the level of competition to remain high in the future.

Our business is highly sensitive to global and regional economic conditions in the industries we serve.
Current global economic conditions influence the Company's focus, direction, strategic initiatives and financial performance. To address the current uncertainty, we are focusing our efforts on projects that will increase our market reach, advance our cost competiveness, expand capacity and improve our manufacturing flexibility.

The Company believes that being an agile organization will hold even greater importance in order to respond quickly to both unexpected opportunities and challenges. HPS' management believes that the key to expanding our market share during this economic slowdown is growing our access to a variety of domestic and global markets. This will be achieved through our current and new OEM and distributor channels.

The disruption to businesses that can come from unpredictable weather can have an impact on sales volume as customer projects can be delayed or cancelled.
Extreme weather conditions such as heavy rains, flooding, snowfall, tornadoes and hurricanes can potentially have a negative impact on the Company's sales trends and booking rates. When these conditions are present the Company may see short-term effects of such occurrences due to their unpredictability. This may impact delivery and capacity requirements.

The business practice of extending credit to customers can lead to a risk of uncollectability.
A substantial portion of the Company's accounts receivable are with customers in manufacturing sectors and are subject to credit risks normal to those industries. The Company's expansion into emerging markets increases

DOLLARS IN THOUSANDS UNLESS OTHERWISE STATED

credit risk which is partially mitigated by progress payments. Approvals are based on trade information, payment history, credit rating and financial analysis. Although the Company has historically incurred very low bad debt expense, the current economic environment conditions elevate this exposure.

Market supply and demand impact on commodity prices
An area that has a definite impact on the Company's costs and earnings is the cyclical effects and unprecedented market cost pressures of both copper commodity and steel pricing in the global markets. This risk is mitigated through strategic supply line agreements and alliances in place with major steel suppliers to ensure adequate supply and competitive market pricing.

Off-balance sheet arrangements

The Company has no off-balance sheet arrangements other than capital expenditure commitments disclosed in Notes to the Consolidated Financial Statements contained in our 2019 Annual Report.

Transactions with related parties

The Company had no transactions with related parties in 2020, other than transactions disclosed in Note 12 in the Condensed Notes to the Condensed Consolidated Interim Financial Statements contained in our Quarter 3, 2020 Report.

Proposed transactions

The Company continues to evaluate strategic business development initiatives and has no firm transactions as at September 26, 2020.

Financial instruments

As at September 26, 2020, the Company had outstanding foreign exchange contracts in place for 17,400 EUR and $11,000 USD – all of which are implemented as a hedge against translation gains and losses on inter-company loans as well as $46,500 USD to hedge the U.S. dollar denominated accounts payable in Canadian operations of HPS.

Critical accounting estimates

The preparation of the Company's condensed consolidated interim financial statements requires Management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. These estimates are based upon Management's historical experience and various other assumptions that are believed by Management to be reasonable under the circumstances.

Such assumptions and estimates are evaluated on an ongoing basis and form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

The Company assesses the carrying value of its property, plant and equipment, intangible assets and goodwill every year, or more often if necessary. If it is determined that we cannot recover the carrying value of an asset or goodwill, the unrecoverable amount is written off against current earnings. The Company bases its assessment of recoverability on assumptions and judgments about future prices, demand and manufacturing costs. A material change in any of these assumptions could have a significant impact on the potential impairment and/or useful lives of these assets.

Outstanding share data

Details of the Company's outstanding share data:

8,966,624	Class A Shares
2,778,300	Class B Common Shares
11,744,924	Total Class A and B Shares

Adopted accounting pronouncements

Definition of a Business (Amendments to IFRS 3)
On October 22, 2018, the IASB issued amendments to IFRS 3 Business Combinations that seeks to clarify whether a transaction results in an asset or a business acquisition. The amendments apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020.

The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or as a group of similar identifiable assets. If the preparer chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process.

The Company adopted the amendments in its financial statements for the annual period beginning on January 1, 2020. The adoption of the amendments did not have a material impact on the consolidated financial statements.

Strategic direction and outlook

HPS has undergone significant growth and expansion over the past few years:

- Escalating growth of the NAED channel;
- New global customers;
- Expanded relationships with existing customers;
- Compliance with regulatory changes;
- New product development;
- Expanded product offering using cast resin technology;
- Capital investment in North American manufacturing facilities in Canada, the U.S. and Mexico;
- Establishment of a state-of-the-art core manufacturing facility in Mexico; and
- Development and further implementation of our ERP system to enhance availability of information and streamline processes.

HPS has a history of strength, perseverance and resilience. The Company has navigated through fluctuating and challenging economic times, increased globalization, regulatory changes, changes in customers and markets and significant advances in technology. HPS has framed these challenges as opportunities and developed strategies to address them.

We are aware that the global economy is vital to maintaining competitiveness and market share growth. Our international ventures have allowed us to expand product offerings and open up additional markets and customers that were previously not accessible. These acquisitions also provided us with cast resin technology which has introduced new markets.

The COVID-19 pandemic continues to have an unprecedented impact on the global economy. The full impact or timeline is not yet known but governmental decisions to declare a state of emergency in a number of countries in which we operate had an immediate impact on the economies of such countries. The demand for our transformers particularly in North America continues, but sales volumes have been and are expected to be, tempered due to the economic impact caused by the pandemic. Based on the foregoing, HPS expects to see continued moderation and fluctuation of revenues as well as a continuation of increases in operational costs which will have the effect of reducing HPS' financial performance in 2020 and into 2021. Our Canadian entities received a government subsidy for eligible wages in Quarter 2 and Quarter 3, 2020 which offset some additional wages and operational COVID-19 related costs and supported operational and financial performance. The wage subsidy has been extended into 2021 and the Company will continue to monitor eligibility. HPS will remain cognizant of further programs that may be announced.

HPS is committed to managing the impact the pandemic will have on our financial performance. The Company will maintain its liquidity and balance sheet strength.

HPS has implemented robust health and safety precautions dedicated to providing a safe working environment for our employees while continuing to manufacture and serve our customers during this volatile and unpredictable time.

The implementation of the ERP system has allowed HPS to enhance the availability and quality of information accessible to support operational performance, supplement strategic decision making, improve customer service and audit and control. The ERP system implementation was completed in our Indian facility in Quarter 2, 2019 and an implementation project began in Quarter 3, 2019 for the Company's remaining operation that will be converted to our ERP platform. It is expected to be fully implemented in early 2021. The consolidation to the ERP platform is an important step towards providing one global, integrated, consistent source of information and data.

HPS continues to have a strong reputation of being an industry leader and is both operationally and financially strong. We are positioned to meet the evolving needs of our traditional markets while becoming a leading player in a growing number of market sectors. Historically, HPS has navigated through long-term economic uncertainty and we continue to remain confident in our vision of the future. HPS continues to be focused on escalation of market share, sales growth from product development, geographic diversification, productivity gains, cost reduction and capacity flexibility.

While there have been many successes and challenges, the unpredictable and fluctuating global economic climate has had a pervasive and persistent impact on HPS' profitability over a number of years. The Company has also experienced the adverse impact of unpredictability of foreign currency exchange rates, variability of raw material commodity costs, fluctuating manufacturing throughput and market pricing pressures. These deterrents are being prudently managed through our operational plans and strategic initiatives and projects.

HPS is confronting these challenges and continuously building our competitive and strategic advantage by focusing on:

- Investing in capital and employees;
- Disciplined cost management initiatives;
- Sales development;
- NAED channel expansion;
- Broadened product offering;
- Bringing quality and value to all stakeholders of the Company;
- Identifying and pursuing additional sales opportunities with both existing as well as new customers;
- Cash flow generation;
- Product development;
- Capital investment; and
- Strategic planning.

The combination of our decades of experience, commitment, engineering expertise, solid supplier relationships and a broad and unique business perspective gained through our diverse products, customers and markets are all key success factors critical to our success. These factors have also created a resilient organization that can navigate challenges.

HPS has performed very well during these erratic and unpredictable times and remains steadfast in its execution of its operational and strategic plans. The Company remains a market leader that is committed to all stakeholders, achieving industry leading results, financial strength and solid liquidity.

Selected Annual and Quarterly Information

(tabular amounts in thousands of dollars)

The information contained in the following table presents the historic audited annual financial information as at December 31 and the unaudited financial information for the previous eight quarters up to, and including the Third Quarter of 2020. The quarterly information has been extracted from our unaudited consolidated financial statements, which in the opinion of Management are prepared in accordance with the IFRS accounting framework as noted.

Annual Information (1)	2015	2016	2017	2018	**2019**
Sales	274,639	274,793	301,750	314,082	358,792
Earnings from operations	12,644	10,873	14,470	13,779	20,543
EBITDA	18,748	14,356	23,069	17,915	28,175
Net earnings (loss)	6,320	1,793	6,114	(12,917)	11,607
Total assets	222,969	205,177	192,449	205,527	214,953
Non-current liabilities	5,454	4,131	3,641	2,528	11,271
Total liabilities	90,668	84,524	77,438	96,793	105,186
Total shareholders' equity attributable to equity holders of the Company	129,665	120,441	114,848	108,734	109,767
Operating debt, net of cash	(13,202)	(11,318)	(16,983)	(17,056)	(9,326)
Cash provided by operations	16,065	15,216	1,032	6,474	17,810
Basic earnings (loss) per share	0.53	0.16	0.53	(1.10)	0.99
Diluted earnings (loss) per share	0.53	0.16	0.52	(1.10)	0.99
Dividends declared and paid	2,807	2,808	2,809	2,818	3,287
Average exchange rate (USD$=CAD$)	1.274	1.325	1.298	1.294	1.327
Book value per share	11.08	10.29	9.80	9.26	9.36

	2018		**2019**				**2020**	
Quarterly Information	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Sales	86,714	84,690	91,937	91,502	90,653	88,420	75,393	78,115
Earnings from operations	4,780	4,479	4,731	5,471	5,862	3,033	6,514	5,447
EBITDA	8,221	6,111	7,111	7,302	7,651	5,678	8,447	7,466
Net (loss) earnings	(14,833)	2,508	3,352	3,595	2,152	2,148	4,420	3,462
Total assets	205,527	206,554	205,059	206,586	214,953	212,929	197,895	203,443
Non-current liabilities	2,528	10,914	10,558	9,947	11,271	9,729	9,039	8,558
Total liabilities	96,793	99,939	99,640	96,870	105,186	97,156	81,375	87,215
Total shareholders' equity attributable to equity holders of the Company	108,734	106,615	105,419	109,716	109,767	115,773	116,520	116,228
Operating debt, net of cash	(17,056)	(16,588)	(18,582)	(22,678)	(9,326)	(18,356)	(12,906)	(4,790)
Cash provided by (used in) operations	4,941	2,316	507	(1,460)	16,447	(6,038)	7,229	10,419
Basic (loss) earnings per share	(1.27)	0.20	0.25	0.27	0.27	0.18	0.38	0.30
Diluted (loss) earnings per share	(1.27)	0.20	0.25	0.27	0.27	0.18	0.38	0.30
Dividends declared and paid	706	822	821	821	823	998	999	998
Average exchange rate (USD$=CAD$)	1.319	1.330	1.338	1.320	1.320	1.339	1.390	1.335
Book value per share	9.26	9.09	8.99	9.33	9.36	9.86	9.92	9.90

(1) Balances for 2015-2017 not restated to reflect discontinued operations

Consolidated Statements of Financial Position

(unaudited) (tabular amounts in thousands of dollars)	As at September 26, 2020	As at December 31, 2019
Assets		
Current assets		
Cash	$ 22,532	$ 23,371
Accounts receivable	60,167	64,004
Inventories	49,219	50,926
Income taxes receivable	1,355	1,626
Prepaid expenses and other assets	2,320	2,657
Total current assets	$ 135,593	$ 142,584
Non-current assets		
Long-term lease receivable	3,254	3,180
Property, plant and equipment (note 4 and 7)	28,636	32,468
Investment in properties	3,893	3,709
Investment in joint venture (note 5)	13,857	13,428
Deferred tax assets	1,463	1,944
Intangible assets (note 6)	5,438	6,331
Goodwill	11,309	11,309
Total non-current assets	67,850	72,369
Total assets	$ 203,443	$ 214,953
Liabilities		
Current liabilities		
Bank operating lines of credit	$ 27,322	$ 32,697
Accounts payable and accrued liabilities	46,485	56,216
Income tax liabilities	1,814	1,055
Provisions	824	1,710
Current portion of lease liabilities (note 7)	2,212	2,237
Total current liabilities	$ 78,657	$ 93,915
Non-current liabilities		
Provisions	280	285
Deferred tax liabilities	1,343	1,819
Long-term portion of lease liabilities (note 7)	6,935	9,167
Total non-current liabilities	8,558	11,271
Total liabilities	$ 87,215	$ 105,186
Shareholders' Equity		
Share capital	14,491	14,491
Contributed surplus	2,498	2,498
Accumulated other comprehensive income (note 9)	6,865	7,439
Retained earnings	92,374	85,339
Total shareholders' equity	$ 116,228	$ 109,767
Total liabilities and shareholders' equity	$ 203,443	$ 214,953

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Operations

(unaudited) (tabular amounts in thousands of dollars, except per share amounts)

	Quarter Ending		Nine Months Ending	
	September 26, 2020	September 28, 2019	**September 26, 2020**	September 28, 2019
Sales (note 10)	$ 78,115	$ 91,502	$ 241,928	$ 268,129
Cost of sales (note 11)	56,619	68,721	178,133	203,471
Gross margin	21,496	22,781	63,795	64,658
Selling and distribution (note 11)	9,524	10,706	30,015	31,552
General and administrative (note 11)	6,525	6,604	18,786	18,425
Earnings from operations	5,447	5,471	14,994	14,681
Finance and other costs (income):				
Interest expense	240	419	951	1,060
Foreign exchange gain	(45)	(149)	(524)	(80)
Share of loss (income) of investment in joint venture (note 5)	107	139	(33)	(86)
Other	33	33	99	92
Net finance and other costs	335	442	493	986
Earnings before income taxes	5,112	5,029	14,501	13,695
Income tax expense	1,650	1,434	4,471	4,240
Net earnings from continuing operations	$ 3,462	$ 3,595	$ 10,030	$ 9,455
Loss from discontinued operations, net of tax	–	(472)	–	(1,059)
Net earnings	$ 3,462	$ 3,123	$ 10,030	$ 8,396
Earnings per share				
Basic earnings per share	$ 0.30	$ 0.27	$ 0.86	$ 0.72
Diluted earnings per share	$ 0.30	$ 0.27	$ 0.86	$ 0.72
Basic earnings per share from continuing operations	$ 0.30	$ 0.31	$ 0.86	$ 0.81
Diluted earnings per share from continuing operations	$ 0.30	$ 0.31	$ 0.86	$ 0.81

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Comprehensive Income

(unaudited) (tabular amounts in thousands of dollars)

	Quarter Ending		Nine Months Ending	
	September 26, 2020	September 28, 2019	**September 26, 2020**	September 28, 2019
Net earnings	$ 3,462	$ 3,123	$ 10,030	$ 8,396
Other comprehensive income (loss)				
Foreign currency translation differences for foreign operations (note 9)	(2,756)	1,935	(574)	(2,288)
Total comprehensive income for the period	$ 706	$ 5,058	$ 9,456	$ 6,108

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Changes in Equity

(unaudited) For the nine months ended September 26, 2020

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2020	$ 14,491	$ 2,498	$ 7,439	$ 85,339	$ 109,767
Total comprehensive income for the year					
Net earnings	–	–	–	10,030	10,030
Other comprehensive loss					
Foreign currency translation differences related to joint venture (note 5)	–	–	396	–	396
Foreign currency translation differences (note 9)	–	–	(970)	–	(970)
Total other comprehensive loss	–	–	(574)	–	(574)
Total comprehensive (loss) income for the year	–	–	(574)	10,030	9,456
Transactions with owners, recorded directly in equity					
Dividends to equity holders (note 8)	–	–	–	(2,995)	(2,995)
Total transactions with shareholders	–	–	–	(2,995)	(2,995)
Balance at September 26, 2020	$ 14,491	$ 2,498	$ 6,865	$ 92,374	$ 116,228

*AOCI – Acculated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Changes in Equity

(unaudited) For the six months ended September 28, 2019

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2019	$ 14,217	$ 2,559	$ 12,740	$ 79,218	$ 108,734
Impact of application of new accounting standard	–	–	–	(2,603)	(2,603)
Adjusted balances as of January 1, 2019	14,217	2,559	12,740	76,615	106,131
Total comprehensive income for the year					
Net earnings	–	–	–	8,396	8,396
Other comprehensive loss					
Foreign currency translation differences related to joint venture (note 5)	–	–	(343)	–	(343)
Foreign currency translation differences (note 9)	–	–	(1,945)	–	(1,945)
Total other comprehensive loss	–	–	(2,288)	–	(2,288)
Total comprehensive (loss) income for the year	–	–	(2,288)	8,396	6,108
Transactions with owners, recorded directly in equity					
Repurchase of shares	(65)	(12)	–	(239)	(316)
Stock options exercised	300	(43)	–	–	257
Dividends to equity holders (note 8)	–	–	–	(2,464)	(2,464)
Total transactions with owners	235	(55)	–	(2,703)	(2,523)
Balance at September 28, 2019	$ 14,452	$ 2,504	$ 10,452	$ 82,308	$ 109,716

*AOCI – Acculated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Cash Flows

(unaudited) (tabular amounts in thousands of dollars)	Nine Months Ending September 26, 2020	Nine Months Ending September 28, 2019
Cash flows from operating activities		
Net earnings	$ 10,030	$ 8,396
Adjustments for:		
Share of income of investment in joint venture	(33)	(86)
Amortization of property, plant and equipment	5,623	5,229
Amortization of intangible assets	516	540
Provisions	(139)	(1,053)
Interest expense	951	1,060
Income tax expense	4,471	4,240
Change in unrealized (loss) gain on derivatives included in accounts payable and accrued liabilities	(2,201)	1,464
	19,218	19,790
Change in non-cash working capital (note 13)	(4,167)	(14,300)
Cash generated in operating activities	15,051	5,490
Income tax paid	(3,441)	(4,127)
Net cash generated by operating activities	11,610	1,363
Cash flows from investing activities		
Acquisition of property, plant and equipment (note 4)	(2,002)	(2,615)
Acquisition of intangible assets (note 6)	(3)	(2)
Cash used in investing activities	(2,005)	(2,617)
Cash flows from financing activities		
Repayments of borrowings	(5,375)	(2,594)
Receipt of lease receivable payments	140	137
Issue of common shares	–	257
Share repurchase	–	(316)
Payment of lease liabilities (note 7)	(2,001)	(1,536)
Cash dividends paid (note 8)	(2,995)	(2,464)
Interest paid	(951)	(1,060)
Cash used in financing activities	(11,182)	(7,576)
Foreign exchange on cash held in a foreign currency	738	614
Decrease in cash	(839)	(8,216)
Cash and cash equivalents at beginning of period	23,371	15,545
Cash and cash equivalents at end of period	$ 22,532	$ 7,329

See accompanying notes to condensed consolidated interim financial statements

Nine months ended September 26, 2020 and September 28, 2019 (amounts in thousands of dollars except share and per share amounts)

The accompanying unaudited interim financial statements of Hammond Power Solutions Inc., ("HPS" or the "Company") have been prepared by and are the responsibility of the Company's Management. The Company's independent auditor has not performed a review of these financial statements in accordance with standards adopted by the Canadian Institute of Chartered Accountants ("CICA") for a review of interim financial statements by an entity's auditor.

1. Reporting entity

Hammond Power Solutions Inc. is a company domiciled in Canada. The address of the Company's registered office is 595 Southgate Drive Guelph, Ontario. The Company's Class A subordinate voting shares are listed on the Toronto Stock Exchange and trade under the symbol HPS.A.

The Condensed Consolidated Interim Financial Statements of the Company as at and for the third quarter ended September 26, 2020 comprise the Company and its subsidiaries (together referred to as the "Group" and individually as "Group entities"). The Group is primarily involved in the design and manufacture of custom electrical magnetics, cast resin, custom liquid filled distribution and power transformers and standard electrical transformers, serving the electrical and electronic industries. The Group has manufacturing plants in Canada, the United States ("U.S."), Mexico, Italy, and India. The Company also holds a 55% economic interest in a joint venture located in Mexico called Corefficient de R.L. de C.V. ("Corefficient").

2. Basis of preparation

(a) Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with requirements of IAS 34, Interim Financial Reporting and do not include all of the information required for full annual financial statements. These condensed consolidated interim financial statements were approved by the Board of Directors on November 4, 2020.

(b) Use of estimates and judgments

The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In preparing these condensed consolidated interim financial statements, the significant judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended December 31, 2019.

3. Summary of significant accounting policies:

These condensed consolidated interim financial statements should be read in conjunction with the Group's 2019 annual audited financial statements, which are available on the System for Electronic Document Analysis and Retrieval ("SEDAR"). The significant accounting policies applied by the Company in these condensed consolidated interim financial statements are the same as those applied by the Company in its Consolidated Financial Statements as at and for the year ended December 31, 2019, with the exception of items noted below:

Changes to accounting policies

Definition of a Business (Amendments to IFRS 3)

On October 22, 2018, the IASB issued amendments to IFRS 3 Business Combinations, that seeks to clarify whether a transaction results in an asset or a business acquisition. The amendments apply to businesses acquired in annual

Nine months ended September 26, 2020 and September 28, 2019 (amounts in thousands of dollars except share and per share amounts)

reporting periods beginning on or after January 1, 2020.

The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or as a group of similar identifiable assets. If the preparer chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process.

The Company adopted the amendments in its financial statements for the annual period beginning on January 1, 2020. The adoption of the amendments did not have a material impact on the consolidated financial statements.

4. Property, plant and equipment

Property, plant and equipment comprise owned and leased assets that do not meet the definition of investment property.

	September 26, 2020	December 31, 2019
Property, plant and equipment owned	$ 21,550	$ 23,415
Right-of-use assets (note 7)	7,086	9,053
	$ 28,636	$ 32,468

The Group had acquisitions of fixed assets for the nine months ended September 26, 2020 in the amount of $2,002,000 of machinery and equipment (2019 – $2,615,000).

5. Joint venture

The Company has a 55% economic and voting interest in Corefficient, whose principal place of business is in Monterrey, Mexico. The Company treats its investment in Corefficient as a joint arrangement. The carrying value of the Company's interest in Corefficient is as follows:

	September 26, 2020	December 31, 2019
Cost of investment in joint venture	$ 20,032	$ 20,032
Cumulative share of loss in investment in joint venture, net of tax	(3,362)	(3,395)
Foreign currency translation differences related to the joint venture	(2,813)	(3,209)
	$ 13,857	$ 13,428

Selected financial information relating to Corefficient is as follows:

	September 26, 2020	December 31, 2019
Cash	$ 2,547	$ 4,341
Trade and other receivables	11,100	11,286
Inventories	2,653	3,047
Other current assets	76	118
Total current assets	$ 16,376	$ 18,792
Non-current assets	17,694	19,697
Total assets	$ 34,070	$ 38,489
Current liabilities	$ 8,140	$ 12,744
Non-current liabilities	1,008	1,603
Total liabilities	$ 9,148	$ 14,347

Nine months ended September 26, 2020 and September 28, 2019 (amounts in thousands of dollars except share and per share amounts)

	Nine Months Ending	
	September 26, 2020	September 28 2019
Revenue	$ 42,997	$ 41,937
Income for the period	60	157

The income for the nine months ended September 26, 2020 includes depreciation and amortization expense of $2,402,000 (2019 – $1,750,000), interest expense of $46,000 (2019 – interest income of $15,000) and an income tax expense of $5,000 (2019 – $85,000) related to Corefficient.

6. Intangible assets

The Group had acquisitions of intangible assets for the nine months ended September 26, 2020 in the amount of $3,000 (2019 – $2,000), for the addition of software. None of the intangible assets have been developed internally.

7. Lease liabilities

The Group leases many assets including buildings, vehicles and office equipment. Information about leases for which the Group is a lessee is presented below.

	Buildings	Vehicles	Office Equipment	Total
Balance at January 1, 2020	$ 8,503	$ 523	$ 27	$ 9,053
Additions	–	263	–	263
Depreciation	(1,456)	(233)	(16)	(1,705)
Effect of movements in exchange rates	(529)	5	(1)	(525)
Balance at September 26, 2020	$ 6,518	$ 558	$ 10	$ 7,086

Maturity analysis – contractual undiscounted cash flows	**September 26, 2020**	December 31, 2019
Less than one year	$ 2,760	$ 2,602
One to five years	8,097	9,318
More than five years	254	696
Total undiscounted lease liabilities	$ 11,111	$ 12,616
Less: effect of discounting	$ (1,964)	$ (1,212)
Lease liabilities included in the statement of financial position	$ 9,147	$ 11,404
Current	$ 2,212	$ 2,237
Non-current	$ 6,935	$ 9,167

Nine months ended September 26, 2020 and September 28, 2019 (amounts in thousands of dollars except share and per share amounts)

Amounts recognized in statement of operations	Nine Months Ending September 26, 2020		September 28 2019	
Interest on lease liabilities	$	257	$	228

Amounts recognized in statement of cash flows	Nine Months Ending September 26, 2020		September 28 2019	
Payment of lease liabilities	$	2,001	$	1,536

8. Share capital

(a) Dividends

The following dividends were declared and paid by the Company:

	Nine Months Ending September 26, 2020		September 28 2019	
25.5 cents per Class A subordinate voting shares (2019: 21 cents)	$	2,287	$	1,881
25.5 cents per Class B common shares (2019: 21 cents)		708		583
	$	2,995	$	2,464

(b) Deferred Share Units

The Company maintains a deferred share unit plan in order to issue deferred share units ("DSUs") to non-employee directors and senior-executives of HPS.

The movement in DSUs for the nine months ended September 26, 2020 was as follows:

	Number of DSUs	Closing Share Price	
Balance at January 1, 2020	121,571	$	7.68
DSUs Issued	39,440		7.17
DSUs exercised	(14,788)		6.24
Balance at September 26, 2020	146,223	$	6.42

An expense of $38,000 (2019 – $262,000) for the nine months ended September 26, 2020 was recorded in general and administrative expenses. The liability of $867,000 (December 31, 2019 – $829,000) related to these DSUs is included in accounts payable and accrued liabilities.

9. Accumulated other comprehensive income

Changes to the accumulated other comprehensive income ("AOCI") balance include foreign currency translation differences relating to the net assets of foreign operations which have been determined to have functional currencies under IFRS that are their respective domestic currencies. Total other comprehensive loss for the nine months ended September 26, 2020 was $574,000 (2019 –$2,288,000), of which $970,000 (2019 – $1,945,000) relates to the translation of wholly-owned subsidiaries, resulting in an ending balance of accumulated other comprehensive income of $6,865,000 (September 28, 20192019 – $10,452,000).

Nine months ended September 26, 2020 and September 28, 2019 (amounts in thousands of dollars except share and per share amounts)

10. Sales

	Three Months Ending		Nine Months Ending	
	September 26, 2020	**September 28, 2019**	**September 26, 2020**	**September 28, 2019**
Canada	$ 28,833	$ 31,491	$ 78,099	$ 87,015
United States and Mexico	45,608	54,269	153,841	167,709
India	3,674	5,742	9,988	13,405
	78,115	91,502	241,928	268,129
Italy – discontinued operations	–	–	–	281
	$ 78,115	$ 91,502	$ 241,928	$ 268,410

As at September 26, 2020, the Company has deferred revenue of $NIL (December 31, 2019 – $197,000).

11. Government Subsidy

The Government of Canada implemented the Canada Emergency Wage Subsidy program (CEWS) that provided a subsidy of 75% of eligible remuneration, paid by an eligible entity that experienced significant revenue declines due to the COVID-19 global pandemic. Year-to-date in 2020 the Company has qualified for subsidy payments. The subsidy amounts relating to the quarter have been recorded as a reduction in expenses as follows: cost of sales $2,057, selling and distribution $310 and general and administrative expenses $657 for a total of $3,024. Year-to-date the Company has recorded reduction in expenses as follows: cost of sales $4,584, selling and distribution $696 and general administrative expenses of $1,479 for a total of $6,759.

12. Related party transactions

Arathorn Investments Inc. beneficially owns 2,778,300 (2019 – 2,778,300) Class B common shares of the Company, representing 100% of the issued and outstanding Class B common shares of the Company and 1,064,108 (2019 – 1,062,202) Class A subordinate voting shares of the Company, representing approximately 11.9% (2019 – 11.9%) of the issued and outstanding Class A subordinate voting shares of the Company and as a result controls the Company. William G. Hammond, Chief Executive Officer and Chairman of the Company, owns all of the issued and outstanding shares of Arathorn Investments Inc. Total dividends paid during the quarter, directly and indirectly to William G. Hammond were $327,000 (Quarter 3 2019 – $269,000).

13. Change in operating working capital

The table below depicts the receipt of (use of) cash for working capital purposes by the Company:

	Nine Months Ending	
	September 26, 2020	September 28, 2019
Accounts receivable	$ 3,837	$ (3,656)
Inventories	1,707	(4,310)
Prepaid expenses	1,161	362
Accounts payable and accrued liabilities	(8,339)	(2,927)
Provisions	(752)	(3,108)
Foreign exchange	(1,781)	(661)
	$ (4,167)	$ (14,300)

HPS Offices, Manufacturing Facilities and Warehouse Locations

Canada
Hammond Power Solutions Inc.

Corporate Head Office
595 Southgate Drive
Guelph, Ontario N1G 3W6

15 Industrial Road
Walkerton, Ontario N0G 2V0

10 Tawse Place
Guelph, Ontario N1H 6H9

Delta Transformers Inc.

795 Industriel Boul.
Granby, Quebec J2G 9A1

3850 place de Java
Suite 200
Brossard, Québec J4Y 0C4

India
Hammond Power Solutions Private Limited

2nd Floor
Icon Plaza, H. No. 5-2/222/IP/B
Allwyn X-Roads
Miyapur, Hyderabad – 500049

Italy
Hammond Power Solutions S.p.A.

Via Amedeo Avogadro 26
10121 Torino, Italy
at R & P Legal

Mexico
Hammond Power Solutions S.A. de C.V.

Ave. Avante #810
Parque Industrial Guadalupe
Guadalupe, Nuevo Leon, C.P. 67190
Monterrey, Mexico

Ave. Avante #900
Parque Industrial Guadalupe
Guadalupe, Nuevo Leon, C.P. 67190
Monterrey, Mexico

Mexico
Corefficient, S. de R.L. de C.V.

Ave. Avante #840
Parque Industrial Guadalupe
Guadalupe, Nuevo León, México
C.P. 67190

United States
Hammond Power Solutions, Inc.

1100 Lake Street
Baraboo, Wisconsin 53913

17715 Susana Road
Compton, California 90224

6550 Longley Lane, Suite 135
Reno, Nevada 89511

Corporate Officers and Directors

William G. Hammond *
Chairman of the Board and
Chief Executive Officer

Chris R. Huether
Corporate Secretary and
Chief Financial Officer

Donald H. MacAdam *+
Director

Grant C. Robinson *+
Director

David J. FitzGibbon *+
Director

Dahra Granovsky *+
Director

Fred M. Jaques *+
Director

Anne Marie Turnbull *+
Director

David M. Wood *+
Director

* Corporate Governance Committee
+ Audit and Compensation Committee

Stock Exchange Listing

Toronto Stock Exchange (TSX)
Trading Symbol: HPS.A

Registrar and Transfer Agent

Computershare Investor Share Services Inc.
100 University Avenue
Toronto, Ontario
Canada M5J 2Y1

Auditors

KPMG LLP
115 King Street South
Waterloo, Ontario N2J 5A3

Legal Representation

Dentons Canada LLP
77 King Street West, Suite 400
Toronto Dominion Centre
Toronto, Ontario M5K 0A1

Banking Institution

JP Morgan Chase
Bank N.A. 66 Wellington Street West,
Suite 4500
Toronto, Ontario M5K 1E7

Investor Relations

Contact: Dawn Henderson,
Manager Investor Relations
Phone: 519.822.2441 x414
Email: ir@hammondpowersolutions.com

The Hammond Museum of Radio is one of North America's premiere wireless museums. It is home to thousands of receivers and transmitters dating back to the turn of the century. The museum is open regular business hours Monday to Friday; evenings and weekends by special appointment.

Tours can be arranged by calling:
519-822-2441 x 590

A STRATEGY IS NECESSARY
BECAUSE THE FUTURE
IS UNPREDICTABLE.

Hammond Power
Solutions Inc.

HAMMONDPOWERSOLUTIONS.COM