EXFO ELECTRO OPTICAL ENGINEERING INC
Form 20-F
November 26, 2008

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

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g)
OF THE SECURITIES EXCHANGE ACT OF 1934; or

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended August 31, 2008; or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the transition period _____ to _____; or

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
Date of event requiring this shell company report

For the transition period from September 1, 2007 to August 31, 2008

Commission File No. 0-30895

EXFO ELECTRO-OPTICAL ENGINEERING INC. /
EXFO INGÉNIERIE ÉLECTRO-OPTIQUE INC.
(Exact name of registrant as specified in its charter)

Canada
(Jurisdiction of Incorporation or organization)

400 Godin Avenue
Quebec, Quebec, G1M 2K2, Canada
(418) 683-0211
(Address, including zip code and telephone number, including area code, of registrant's principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Subordinate Voting Shares without par value	NASDAQ
Subordinate Voting Shares without par value	TSX

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

As of November 3, 2008, the registrant had 30,606,791 Subordinate Voting Shares outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes o No x

If this report is an annual report or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP o International Financial Reporting Standards as issued by the International Accounting Standards Board o Other x

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 x

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 of 15 (d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes o No x

TABLE OF CONTENTS

Table of Contents

DISCLOSURE REGARDING FORWARD-LOOKING INFORMATION

This annual report contains or incorporates by reference statements which constitute forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995 and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition that refer to expectations, projections or other characterizations of future events and circumstances. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including those that are discussed under “Risk Factors” set forth in Item 3D of this annual report. Assumptions relating to forward-looking statements involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. When used in this annual report, the words “believe”, “anticipate”, “plan”, “expect” “intend”, “estimate” or similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure you that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document.

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

PART I.

Item 1. Identity of Directors, Senior Management and Advisors

Not Applicable.

Item 2. Offer Statistics and Expected Timetable

Not Applicable.

Item 3. Key Information

A. Selected Financial Data

The consolidated statements of earnings data for the years ended August 31, 2004 and 2005 and the consolidated balance sheets data as at August 31, 2004, 2005 and 2006 are derived from our audited consolidated financial statements not included in this annual report. The consolidated statements of earnings data for each of the three years ended August 31, 2006, 2007 and 2008 and the consolidated balance sheets data as at August 31, 2007 and 2008 are derived from our audited consolidated financial statements that are included elsewhere in this annual report.

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada (“Canadian GAAP”) and significant differences in measurement and disclosure from generally accepted accounting principles in United States (“U.S. GAAP”) are set out in note 19 to our consolidated financial statements included elsewhere in this annual report. The historical results below are not necessarily indicative of the results to be

expected for any future periods.

1

Table of Contents

The selected financial data should be read in conjunction with our audited consolidated financial statements and the related notes included elsewhere in this annual report, and "Item 5. Operating and Financial Review and Prospects" of this annual report.

	Years ended August 31,				
	2008	2007	2006	2005	2004
	(in thousands of US dollars, except share and per share data)				
Consolidated Statements of Earnings Data:					
Amounts under Canadian GAAP					
Sales	$ 183,790	$ 152,934	$ 128,253	$ 97,216	$ 74,630
Cost of sales (1)	75,624	65,136	57,275	44,059	34,556
Gross margin	108,166	87,798	70,978	53,157	40,074
Operating expenses					
Selling and administrative	61,153	49,580	40,298	31,782	25,890
Net research and development	26,867	16,668	15,404	12,190	12,390
Amortization of property, plant and equipment	4,292	2,983	3,523	4,256	4,935
Amortization of intangible assets	3,871	2,864	4,394	4,836	5,080
Impairment of long-lived assets	–	–	604	–	620
Government grants	–	(1,079)	(1,307)	–	–
Restructuring and other charges	–	–	–	292	1,729
Total operating expenses	96,183	71,016	62,916	53,356	50,644
Earnings (loss) from operations	11,983	16,782	8,062	(199)	(10,570)
Interest income	4,639	4,717	3,253	2,524	1,438
Foreign exchange gain (loss)	442	(49)	(595)	(1,336)	(278)
Earnings (loss) before income taxes and extraordinary gain	17,064	21,450	10,720	989	(9,410)
Income taxes	1,676	(20,825)	2,585	2,623	(986)
Earnings (loss) before extraordinary gain	15,388	42,275	8,135	(1,634)	(8,424)
Extraordinary gain	3,036	–	–	–	–
Net earnings (loss) for the year	$ 18,424	$ 42,275	$ 8,135	$ (1,634)	$ (8,424)
Basic and diluted earnings (loss) before extraordinary gain per share	$ 0.22	$ 0.61	$ 0.12	$ (0.02)	$ (0.13)
Basic and diluted earnings (loss) per share	$ 0.27	$ 0.61	$ 0.12	$ (0.02)	$ (0.13)
Basic weighted average number of shares used in per share calculations (000's)	68,767	68,875	68,643	68,526	66,020
Diluted weighted average number of shares used in per share calculations (000's)	69,318	69,555	69,275	68,981	66,615
Other consolidated statements of earnings data:					
Gross research and development	$ 32,454	$ 25,201	$ 19,488	$ 15,878	$ 15,668
Net research and development	$ 26,867	$ 16,668	$ 15,404	$ 12,190	$ 12,390
Amounts under U.S. GAAP					
Net earnings (loss) for the year	$ 18,424	$ 42,257	$ 8,135	$ (2,920)	$ (9,571)
Basic and diluted net earnings (loss) per share	$ 0.27	$ 0.61	$ 0.12	$ (0.04)	$ (0.14)
Basic weighted average number of shares used in per share calculations (000's)	68,767	68,875	68,643	68,526	66,020
	69,318	69,555	69,275	68,981	66,615

Diluted weighted average number of shares used in per share calculations (000's)					

	As at August 31,				
	2008	2007	2006	2005	2004
	(in thousands of US dollars)				
Consolidated Balance Sheets Data:					
Amounts under Canadian GAAP					
Cash	$ 5,914	$ 5,541	$ 6,853	$ 7,119	$ 5,159
Short-term investments	81,626	124,217	104,437	104,883	83,969
Total assets	293,066	279,138	219,159	190,957	172,791
Long-term debt (excluding current portion)	–	–	354	198	332
Share capital	142,786	150,019	148,921	521,875	521,733
Shareholders' equity	$ 259,515	$ 250,165	$ 196,234	$ 173,400	$ 157,327
Amounts under U.S. GAAP					
Cash	$ 5,914	$ 5,541	$ 6,853	$ 7,119	$ 5,159
Short-term investments	81,626	124,217	104,437	104,883	83,969
Total assets	280,426	268,389	212,702	182,852	164,758
Long-term debt (excluding current portion)	–	–	354	198	332
Share capital	568,917	599,519	598,421	597,664	596,309
Shareholders' equity	$ 246,802	$ 239,343	$ 189,777	$ 165,295	$ 149,294

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

Table of Contents

B. Capitalization and Indebtedness

Not Applicable.

C. Reasons for the Offer and Use of Proceeds

Not Applicable.

D. Risk Factors

We must continue to overcome significant competition in our targeted industries in order to gain market share and achieve our growth strategy.

The market for our primary business activity namely designing, manufacturing, marketing and selling telecommunications test, measurement and service assurance equipment is rapidly evolving and is marked by intense competition and technical innovation. Likewise, the market for our selected life sciences and industrial solutions is very competitive. We anticipate the pace of change to remain high or even accelerate for our targeted industries in the future. We might see the emergence of new competitors or the consolidation of current competitors, as the markets for telecommunications test, measurement and service assurance equipment as well as for life sciences and industrial solutions might evolve in response to technical innovations and economic conditions. Achieving a compound annual growth rate of 20% for sales in the next three years, as defined in our new corporate performance metrics, will largely depend on our ability to gain market share by increasing sales of current products at existing accounts, expanding into new accounts, introducing new products and product enhancements, and exploiting new market opportunities.

During the past few years, the telecommunications test, measurement and service assurance industry has witnessed consolidation. Danaher Corporation acquired Tektronix, Inc., in November 2007. Anritsu Corporation acquired NetTest A/S in August 2005 and JDS Uniphase Corporation (JDSU) completed its acquisition of Acterna Corporation during the same month. Agilent Technologies Inc. divested itself of its semiconductor division to refocus its efforts on test and measurement. With the exception of JDSU (which also sells optical components), these competitors are global test, measurement and service assurance vendors who complement their broad range of products with telecommunications test, measurement and service assurance equipment. Similarly, Spirent plc. and Yokagawa are global test, measurement and service assurance vendors who compete against us. Other competitors, such as Digital Lightwave Inc., Fluke Networks and Tektronix, operating divisions within Danaher Corporation, IXIA, Sunrise Telecom Inc., and VeEX Inc. compete against us in separate niche markets. Some competitors in both groups may have greater financial, technical and/or marketing resources than us. Consequently, they may be able to devote greater resources to the development, marketing, manufacturing, selling and support of their products in order to capture market share.

Competitors also may be better positioned than us to capture market share or to acquire companies and new technologies that would potentially displace our products or render them obsolete. We cannot predict whether current or future competitors will develop or market products that offer higher performance, more features, or are more cost-effective than our current or future products. To remain competitive and achieve our growth strategy, we must increase our sales and develop cost-effective products and product enhancements that offer higher performance and more functionality, in current and new sectors, so that we can increase our market share. Our failure to do so may harm our business, results of operations and financial condition.

Table of Contents

Fluctuations in the exchange rates between the Canadian dollar, US dollar and other currencies may adversely affect our operating results.

Most of our sales are denominated in currencies other than the Canadian dollar (principally US dollars and Euros). However, a large portion of our operating expenses and capital expenditures are denominated in Canadian dollars. As a result, even though we manage to some extent our exposure to currency risks with forward-exchange contracts and certain operating expenses denominated in currencies other than the Canadian dollar, we are exposed to fluctuations in the exchange rates between the Canadian dollar on one hand and the US dollar and Euro on the other. For example, the average exchange rate of the Canadian dollar versus the US dollar was 1.0071 in fiscal 2008 compared to 1.1215 in 2007. During the period from September 1, 2008 to October 31, 2008, the Canadian dollar fluctuated significantly, mainly due to the turmoil in financial markets. Any increase in the value of the Canadian dollar relative to other currencies, especially the US dollar, and any variance between the value of the Canadian dollar and the contractual rate of our forward-exchange contracts, could have a material adverse effect on our operating results and provide competitive advantages to our competitors.

Our business may be adversely affected by unfavorable general economic and market conditions

Our business is subject to the effects of general economic conditions in North America and throughout the world and, more particularly, market conditions in the telecommunications industry. During fiscal 2008, a weaker global macro-economic environment prompted many network service providers to carefully scrutinize their capital expenditures. Even if network service providers (“NSPs”) reduce their capital expenditures amidst a challenging environment, we believe that it will accelerate the fundamental shift in their capital spending budgets from legacy to next-generation, IP networking as the latter maximizes revenue-generating services and reduces operating costs. We believe that we are very well positioned to enable the deployment of next-generation, IP-based networks. It should be noted, however, that the turmoil in financial markets has rendered it more difficult for NSPs to secure financing for their deployments. In the past, our operating results were adversely affected by reduced telecom capital spending in North America, Europe and Asia and by general unfavorable economic conditions. In particular, sales to network service providers in North America were significantly and adversely affected by a downturn in 2001 in the telecommunications industry. If there is a recession or slowdown in key geographic regions or markets, we may experience a material adverse impact on our business, operating results and financial condition.

One of our customers has accounted for a high percentage of our sales in the past several years, and any adverse factor affecting this customer or our relationship with this customer could cause our sales to decrease.

A Tier-1 carrier in the US accounted for 7.4% of our sales in fiscal 2008, 14.7% in fiscal 2007, 13.8% in 2006 and 23.3% in 2005. Although we have reduced our exposure to this customer in recent years, we may not be able to offset lower sales at this particular account in the future. Even if this customer has a supply contract with us, it could change its purchasing practice, force us to renegotiate prices and is not obligated to purchase a specific amount of products from us or provide us with binding purchase forecasts for any period. In addition, our customers typically purchase our products under individual purchase orders and may cancel or defer purchases on short notice without significant penalties.

The loss of such a customer or the reduction, delay, or cancellation of orders from this customer or other significant customers could cause our sales and, therefore, net earnings to decline.

We have faced pricing pressure on our existing products and expect that this pressure will continue. If we do not keep lowering our manufacturing costs or introduce new products with higher margins, our gross margins may decrease and our operating results may be adversely affected.

We continue to implement measures to protect our gross margin, despite the negative impact of the exchange rate between US and Canadian currencies. In addition, since September 2007, we began transferring and ramping the manufacturing of our higher-volume, lower-complexity telecom products at a wholly-owned production facility in Shenzhen, China, with a goal of lowering our production costs. However, increased competitiveness in the telecommunications test, measurement and service assurance industry will likely result in continuing downward pressure on average selling prices, which may in turn negatively affect our gross margins. Pricing pressure can result from a number of factors such as:

Table of Contents

- increased competition for business;
- reduced demand;
- limited number of potential customers;
- competition from companies with lower production costs, including companies operating in lower cost environments;
- introduction of new products by competitors;
- greater economies of scale for higher-volume competitors;
- large customers, who buy in high volumes, can exert substantial negotiating leverage over us; and
- resale of used equipment.

In addition, gross margins may also be negatively affected by increased costs of raw materials as well as obsolescence and excess costs, product and customer mix and under-absorption of fixed manufacturing costs.

As pricing pressure will likely continue to affect our existing products, we may have to increase the number of units sold to maintain our existing sales levels. If we are unable to increase our sales levels, lower our manufacturing costs, or introduce new products with higher margins, our gross margins may decline and our operating results may suffer.

Our products may have unforeseen defects that could harm our reputation, impede market acceptance of our products and negatively impact our business, results of operations and financial condition.

As a result of their complexity, our products may contain undetected software or hardware defects, inaccurate calibration or compatibility problems or regulatory compliance issues, particularly when they are first introduced or when new versions are released. There can be no assurance that, despite our testing and diligent effort, defects will not be found in new products after they have been fully deployed and operated under peak stress conditions or that customized products meet customer sign-off acceptance requirements. If we are unable to fix defects or other problems or meet custom requirements, we could experience, among other things:

- costly repairs;
- product returns or recalls;
- damage to our brand reputation;
- loss of customers, failure to attract new customers or achieve market acceptance;
- diversion of development and engineering resources;
- legal actions by our customers, including claims for consequential damages and loss of profits; and
- legal actions by governmental entities, including actions to impose product recalls and/or forfeitures.

The occurrence of any one or more of the foregoing could seriously harm our business, results of operations and financial condition.

We may not be able to make the necessary acquisitions or strategic alliances needed for the development of our business or, if we do make such acquisitions or strategic alliances, we cannot assure you that we will successfully integrate the businesses, products, technologies and personnel. In addition, such acquisitions could distract management's attention from our day-to-day business and operations. Ultimately, the failure to make strategic acquisitions or the inability to carry out effective integrations could disrupt our overall business and harm our financial condition.

We intend to carefully seek businesses, whose products and technologies are complementary to ours, or which will enable us to expand our markets and/or our market share. There can be no assurance that we will ultimately make any such transactions. Our competitors may be in a better position to acquire the same businesses, products and technologies that we wish to acquire. In addition, our fluctuating stock price, our cash position or our ability to raise

capital or issue debt on favorable terms or at all at the time of an acquisition may affect our ability to complete such an acquisition.

We made two strategic acquisitions in fiscal 2008, namely of Navtel Communications and Brix Networks, and we intend to continue making acquisitions of businesses, products and technologies as part of our overall growth strategy. In the event of any future acquisition, we could:

Table of Contents

- issue shares that would dilute individual shareholder percentage ownership;
- incur debt;
- assume liabilities and commitments;
- incur significant expenses related to amortization of additional intangible assets;
- incur significant impairment losses of goodwill and intangible assets related to such acquisitions; and
- incur losses from operations.

These acquisitions also involve numerous risks, including:

- risk of not realizing the expected benefits or synergies of such acquisitions;
- problems integrating the acquired operations, technologies, products and personnel;
- risks associated with the transfer of acquired know-how and technology;
- unanticipated costs or liabilities;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience; and
- potential loss of key employees, particularly those of acquired organizations.

If we fail to adapt appropriately to the challenges associated with operating internationally, the expected growth of our business may be impeded and our operating results may be affected.

For the fiscal year ended August 31, 2008, customers outside of the United States and Canada accounted for 49.0% of our sales. Our international sales will be limited if we cannot establish and maintain relationships with international distributors, set up additional foreign operations, expand international sales channel management, hire additional personnel, develop relationships with international service providers and operate adequate after-sales support internationally.

In the third quarter of fiscal 2007, we established a software development center in Pune, India, to supplement the efforts of our R&D centers in Quebec City, Canada, Montreal, Canada, Concord, Canada, and since the third quarter of fiscal 2008, Boston, United States. We also began manufacturing high-volume, low-complexity telecom products at our wholly-owned production facility in Shenzhen, China, in the first quarter of fiscal 2008 with the goal of lowering our manufacturing costs.

Even if we are able to successfully expand our international operations, we may not be able to maintain or increase international market demand for our products. Our international operations are subject to a number of risks, including:

- challenges in staffing and managing foreign operations due to the limited number of qualified candidates, employment laws and business practices in foreign countries, any of which could increase the cost and reduce the efficiency of operating in foreign countries;
- our inability to comply with import/export, environmental and other trade compliance regulations of the countries in which we do business, together with unexpected changes in such regulations;
- measures to ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future, especially in light of setting up new operating companies in India and China or the likely future acquisition of companies;
- failure to adhere to laws, regulations and contractual obligations relating to customer contracts in various countries;
- difficulties in establishing and enforcing our intellectual property rights;
- inability to maintain a competitive list of distributors for indirect sales;
- tariffs and other trade barriers;
- economic instability in foreign markets;

- wars, acts of terrorism and political unrest;
- language and cultural barriers;
- lack of integration of foreign operations;
- currency fluctuations;

Table of Contents

- potential foreign and domestic tax consequences;
- technology standards that differ from those on which our products are based, which could require expensive redesign and retention of personnel familiar with those standards;
- longer accounts receivable payment cycles and possible difficulties in collecting payments which may increase our operating costs and hurt our financial performance; and
- failure to meet certification requirements.

Any of these factors could harm our international operations and negatively affect our business, results of operations and financial condition. The recurrence of weakness in these economies or of weakness in other foreign economies could have a significant negative effect on our future operating results.

We may make misjudgments in our strategic planning that could have material adverse effects on our business, results of operations and financial condition.

We devise a three-year strategic business plan, which is prepared by management and approved by our Board of Directors. This strategic plan, reviewed by management on a regular basis, is mainly based on market research and analysis related to future market trends and demands. In our strategic plan, we have made and will continue to make judgments based on our analysis of future market trends and requirements. These decisions may involve substantial investments in the development of new product lines, diversification of our business on a geographic basis, as well as expansion into new market segments — either organically or through acquisitions. We may make misjudgments in our strategic planning that could have material adverse effects on our business, results of operations and financial condition.

Our quarterly revenues and operating results are subject to significant fluctuations and you should not rely on them as an indication of our future performance.

Our sales and operating results have fluctuated from quarter to quarter in the past and significant fluctuations may occur in the future, especially following the acquisition of Brix Networks (renamed EXFO Service Assurance Inc.). EXFO Service Assurance Inc. offers service assurance systems that monitor next-generation, converged IP networks. Given that these systems are more complex and mission-critical than traditional test equipment, the orders are much larger and the sales cycles are relatively longer.

In addition, our sales and operating results generally depend on the volume and timing of the orders we receive from customers as well as our ability to fulfill received orders. Our operating expenses, which include manufacturing overhead costs, selling and administrative, research and development, and amortization expenses, are relatively fixed in the short term. If we sell fewer products than anticipated, if there is a delay in the launch of new products, or if prices for our products decline, we may not be able to quickly reduce our operating expenses in response to lower sales. Factors that could affect the amount and timing of our sales, and cause quarterly fluctuations in our revenue and operating results include:

- length of the product sales cycle for certain products, especially those that are higher priced and more complex;
- timing of product launches and market acceptance of new products for us as well as our competitors;
- our ability to sustain product volumes and high levels of quality across all product lines;
- timing of shipments for large orders;
- effect of seasonality on sales and bookings; and
- losing key accounts and not successfully developing new ones.

Our sales and operating results could also be affected by the following factors, some of which we have little or no control over:

- fluctuating demand for telecommunications test, measurement and service assurance equipment as well as life sciences and industrial solutions;
- changes in the capital spending and operating budgets of our customers, which may cause seasonal or other fluctuations in product mix, volume, timing and number of orders we receive from our customers;
- order cancellations or rescheduled delivery dates;

Table of Contents

- pricing changes by our competitors or suppliers;
- customer bankruptcies and difficulties in collecting accounts receivable;
- restructuring and impairment charges;
- foreign exchange rate fluctuations, as a portion of our operating expenses are denominated in Canadian dollars; and
- general economic conditions, including a slowdown or recession.

We may in the future choose to reduce prices, increase spending, or modify our product portfolio in response to actions by competitors or as an effort to pursue new market opportunities. These actions may also adversely affect our business and operating results and may cause our quarterly results to be lower than the results of previous quarters. Due to these factors, you should not rely on quarter-to-quarter comparisons of our results of operations as an indication of our future performance.

If we are unable to adapt to current and future changes in technology or if we are unable to introduce new and enhanced products on a timely basis, our products may become obsolete, which could prevent us from achieving our growth strategy and adversely affect our operating results.

The industries that we target are characterized by rapidly evolving technology and industry standards that result in frequent new product introductions. Any failure by us to anticipate or respond to new technological developments, customer requirements or evolving standards could have a material adverse effect on our business, results of operations and financial condition. The development of proprietary technology entails significant technical and business risks and requires substantial expenditures and lead-time. The success of our new product introductions will depend on several factors, including our ability to:

- properly identify and anticipate customer needs;
- innovate and develop new products;
- gain timely market acceptance for new products;
- manufacture and deliver our new products on time, in sufficient volume and with adequate quality;
- price our products competitively;
- continue investing in our research and development programs; and
- anticipate competitors’ announcements of new products.

Failure to do the above could be exploited by our competitors. If we lose market share as a result of lapses in our product development, our business would suffer.

Our intellectual property and proprietary technology are important to the continued success of our business. Our failure to protect this proprietary technology may significantly impair our competitive position.

Our success and ability to compete depend to a significant extent on our proprietary technology, with which we attempt to keep others from using the innovations that are central to our existing and future products. We currently hold 41 actively-maintained granted patents from the United States (including one “design” patent), seven from Canada, four from Germany (including one "Utility Model"), four from the United Kingdom, three from France, and two from China. In addition, EXFO has twenty US patent applications in process, eleven Canadian patents applications in process, three European applications in process, three in China, two direct national entries (not via the European application) in Germany, and one in Russia, these applications being either direct national or regional submissions or submissions as applications under the Patent Cooperation Treaty. We also rely on a combination of copyright and trademark laws, trade secrets, confidentiality procedures, contractual provisions and license agreements to protect our proprietary technology. We may have to engage in litigation in order to protect our patents and other intellectual property rights, or to determine the validity or scope of the proprietary rights of others. Such litigation can be time-consuming and expensive, regardless of whether we win or lose.

8

Table of Contents

The process of seeking patent protection can be long and expensive and we cannot be certain that any currently pending or future applications will actually result in issued patents, or that, even if patents are issued, they will be of sufficient scope or strength to provide meaningful protection or any commercial advantage to us. We also rely on trade secret protection for our technology, in part through confidentiality agreements with our employees, consultants, distributors and third parties. However, these agreements may be breached or otherwise not effective and we may not have adequate remedies for any breach or shortfall of these agreements. In any case, others may come to know about our trade secrets through a variety of methods. In addition, the laws of some territories in which we sell our products may not protect our intellectual property rights to the same extent as do the laws of Canada and the United States.

Our intellectual property rights, particularly our existing or future patents, may be invalidated, circumvented, challenged or required to be licensed to others. Furthermore, others may develop technologies that are similar or superior to our technology, duplicate or reverse engineer our technology, or design around the patents owned or licensed by us. We cannot be sure that the steps that we take to protect our technology will prevent misappropriation or infringement. If we fail to protect our technology so that others may copy or use it, we will be less able to differentiate our products and our sales may decline.

Others may claim that our products infringe upon their intellectual property rights, or they may infringe our intellectual property, and we may expend significant resources enforcing or defending our rights or suffer competitive injury.

Litigation regarding intellectual property rights is common in the technology industry and for this reason we expect that third-party infringement claims involving technologies may increase. If an infringement claim is filed against us, we may be prevented from using some of our technologies and may incur significant costs to resolve the claim. Conversely, we may be required to spend significant resources to monitor and enforce our intellectual property rights.

We could incur substantial costs in defending ourselves and our customers against infringement claims or in bringing infringement claims against others. Litigation could also adversely affect sales of the challenged product or technology and divert the efforts of our management and technical personnel. In the event of an infringement claim, we may be required to obtain one or more licenses from third parties. We cannot assure you that we, or our customers, could obtain necessary licenses from third parties at a reasonable cost or at all. If we fail to obtain a license where one is required, we could incur substantial liabilities and be forced to suspend the marketing of the challenged products.

If customers fail to meet their financial commitments to us, it could have a material adverse effect on our business, results of operations and financial condition.

Some of our customers may experience cash flow problems. Consequently, we may have customers who delay payments or may not be able to meet their financial commitments to us. Furthermore, they may not order as many products from us as originally forecasted or they may cancel their orders outright. The failure of customers to order products would result in decreased revenues for us. If customers fail to meet their financial commitments to us, it could have a material adverse effect on our business, results of operations and financial condition.

As our customers consolidate, they may reduce or halt purchases of our products, which would harm our sales and operating results.

Consolidation in the telecommunications industry could reduce the number of customers to which our products are sold. Some of our customers have been subject to consolidation and could obtain products from a vendor other than us, or demand more favorable terms and conditions from us, which would harm our sales and operating results. In addition, some customers may merge with or acquire our competitors and discontinue their relationships with us.

9

Table of Contents

If we fail to predict our supply requirements accurately, we may have excess inventory or insufficient inventory, either of which could cause us to incur additional costs and/or experience manufacturing delays.

We provide non-binding forecasts of our requirements to some of our suppliers up to six months prior to scheduled delivery of products to our customers. If we overestimate our forecasted requirements, we may have excess inventory, which could harm our relationships with our suppliers due to reduced future orders, increase our costs and require inventory write-offs. If we underestimate our requirements, we may have an inadequate inventory of parts, which could interrupt manufacturing of our products and result in shipment delays. The likelihood of misjudging our inventory requirements increased in the past year with the opening of a telecom manufacturing facility in Shenzhen, China, for high-volume, low-complexity products. This manufacturing facility complements the low-volume, high-complexity telecom products produced at our plant in Quebec City, Canada. In addition, lead times for materials and parts that we order may be long and depend on factors such as the procedures of, or supply terms with, a specific supplier and demand for each part at a given time.

We depend on a single supplier or a limited number of suppliers for some key components and materials in our products, which makes us susceptible to supply shortages or price fluctuations that could adversely affect our operating results.

We depend on a limited number of suppliers for some of the parts used to manufacture our products for which alternative sources may not be readily available. In addition, all our orders are placed through individual purchase orders and, therefore, our suppliers may stop supplying parts to us at any time. The reliance on a single source or limited number of suppliers could result in increased costs, delivery problems and reduced control over product pricing and quality. Financial difficulties of suppliers could also affect our ability to obtain necessary parts in a timely manner. Any interruption or delay in the supply of any of these parts could significantly harm our ability to meet scheduled product deliveries to our customers and cause us to lose sales. Furthermore, the process of qualifying a new manufacturer for complex parts, designed to our specifications, such as our optical and mechanical parts, is lengthy and would consume a substantial amount of time of our technical personnel and management. If we were required to change a supplier in a short period of time, our business would be disrupted. In addition, we may be unsuccessful in identifying a new supplier capable of meeting and willing to meet our needs on terms that we would find acceptable. Consolidation involving suppliers could further reduce the number of alternatives available to us and increase the cost of parts, which would make our products less competitive and result in lower margins.

If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial information or prevent fraud, which could harm our operating results and cause investors to lose confidence in our reported financial information.

Effective internal controls are necessary for us to provide reliable and accurate financial information and effectively prevent fraud. We devote significant resources and time to comply with the internal control over financial reporting requirements of the Sarbanes-Oxley Act of 2002. In addition, Section 404 of the Sarbanes-Oxley Act of 2002 requires that we assess and our auditors attest to the design and operating effectiveness of our controls over financial reporting. Our compliance with the annual internal control report requirement for each fiscal year will depend on the effectiveness of our financial reporting as well as data systems and controls throughout our company and operating subsidiaries. Furthermore, we cannot be certain that these measures will ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future, especially in light of having acquired Navtel Communications and Brix Networks or the likely future acquisition of companies that are not in compliance with Section 404 of the Sarbanes-Oxley Act of 2002. As well, the complexity of our systems and controls may become more difficult to manage as we transform our operating structure and continue to reduce infrastructure costs. To effectively manage these changes, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. Any failure to implement required new or improved

controls, difficulties encountered in their implementation or operation, or difficulties in the assimilation of acquired businesses into our control system could harm our operating results or cause it to fail to meet our financial reporting obligations. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on our share price and our access to capital.

Table of Contents

Regulatory changes may cause us to incur increased costs.

Changes in the laws and regulations affecting public companies may increase our expenses as we may have to devote resources to respond to these new requirements. In particular, we incurred and may incur additional general administrative expenses to comply with Section 404 of the Sarbanes-Oxley Act, which requires management to report on internal controls over financial reporting. In addition, the process of moving from Canadian GAAP to IFRS, which will extend from fiscal 2009 to 2011, will require management's time and attention, and cause our general and administrative expenses to increase. Compliance with new rules could require the further commitment of significant financial resources and result in the diversion of management's time and attention from revenue-generating activities. Finally, the impact of these changes could make it more difficult for us to attract and retain qualified persons to serve on our Board of Directors or as executive officers, which could harm our business.

We require employees and management resources who are knowledgeable about the specialized nature of our business. If we are unable to attract and retain sufficient numbers of highly skilled technical, sales, marketing, senior management and other personnel, our operations and financial results will suffer.

Due to the specialized nature of our business, we are highly dependent on the continued service of and on the ability to attract qualified engineering, sales, marketing, senior management and other personnel. If we are unable to attract and retain such qualified personnel, it could have a material adverse effect on our business, results of operations and financial condition.

We must also provide significant training for our employee base due to the highly specialized nature of telecommunications test, measurement, and service assurance as well as life sciences and industrial technologies. Our current personnel may be inadequate and we may fail to assimilate and train new employees. Highly skilled employees with the education and training that we require – especially employees with significant experience and expertise, international business development, product management, sales, engineering and operation – may be difficult to find. Once trained, our employees may also be hired by our competitors or leave the organization.

Our insurance may not be sufficient to cover all potential liability. A successful claim exceeding our policy limits will reduce our cash position, increase our expenses and have a negative effect on our business, operating results and financial condition.

Our products are designed to help network service providers, cable operators and manufacturers of optical networks and components ensure network reliability. We also leverage our core telecom technologies for life sciences and industrial applications. The failure of our products to perform to client expectations could give rise to product liability and warranty claims. We carry insurance for product liability and take accounting reserves for warranty claims that we consider adequate in view of industry practice.

In addition, we may face other types of claims by third parties in relation to the conduct of our business; a successful claim against us for an amount exceeding our policy limits would force us to use our own resources to pay the claim, which could result in a reduction of our cash available for other uses, increase our expenses and have a negative effect on our business, results of operations and financial condition.

We may become involved in costly and time-consuming litigation that may substantially increase our costs and harm our business.

We may from time to time become involved in various lawsuits and legal proceedings. For example, we are a defendant in a putative securities class action filed in the United States District Court for the Southern District of New York involving approximately 300 other issuing companies. Litigation is subject to inherent uncertainties, and an

adverse result in these or other matters that may arise from time to time could have a material adverse effect on our business, results of operations or financial condition. Any litigation to which we are subject could require significant involvement of our senior management and may divert management attention from our business and operations.

Table of Contents

If we suffer loss to our factories or facilities, our operations could be seriously harmed.

Our factories and facilities are subject to catastrophic loss due to fire, vandalism, terrorism or other natural or man-made disasters. We do not have redundant multiple-site capacity and if any of our facilities or factories were to experience a catastrophic loss, it would disrupt our operations, delay production, shipments and revenue and result in large expenses, thereby harming our results of operation.

Unexpected declines in our research and development and other tax credits and grants may have an adverse effect on our business.

Our historical operating results reflect substantial benefits from programs sponsored by federal and provincial governments for the support of research and development activities, as well as in relation to other activities. For example, research and development tax credits and grants represented 17.2% of our gross research and development expenses for the year ended August 31, 2008.

If unexpected changes in the laws or government policies terminate or adversely modify the Canadian and Quebec government programs, under which we receive the majority of our research and development and other tax credits and grants, or if we unexpectedly become unable to participate in or take advantage of these programs, then our net research and development and other expenses will materially increase or we may decrease our research and development activities. In addition, to the extent that we have increased our research and development activities outside of Canada and Quebec, resulting from the hiring of additional personnel at our software development center in Pune, India and acquisition of Brix Networks, or potential future acquisitions, our increased R&D activities may not be eligible for these programs. If we were required to decrease our research and development activities, or were unable to benefit from other tax credits and grants, this could have a material adverse effect on our business, results of operations and financial condition.

Changes in our effective tax rate or adverse outcomes resulting from tax audits may have an adverse impact on our results.

As an international corporation, we are subject to taxation in the various jurisdictions in which we conduct business. Significant judgment is required in the determination of our worldwide provision for income taxes and this determination requires the interpretation and application of complex tax laws and regulations. Our effective tax rate may be adversely impacted by the level of earnings, by changes in the mix of earnings among companies and countries which may have different statutory tax rates, by the valuation of our deferred tax assets, and by changes in tax rules and regulations. We are also subject to income tax audits and transfer pricing audits in the respective jurisdictions in which we conduct business and we regularly assess the likelihood of adverse outcomes resulting from these audits to ascertain the adequacy of our provisions for income taxes and transfer pricing policies. There can be no assurance that the outcomes of these tax audits will not have an adverse impact on our result and financial condition.

Our current principal stockholder has effective control over our business.

As of November 3, 2008, Germain Lamonde, our Chairman of the Board, President and Chief Executive Officer, held 92.29% of the voting rights in our stock. By virtue of such stock ownership, Mr. Lamonde has effective control over all matters submitted to our stockholders, including the election of our Directors, and exercises significant control over our policies and affairs. Such concentration of voting power could have the effect of delaying, deterring or preventing a change in control or other business combinations that might otherwise be beneficial to our stockholders.

Table of Contents

If we complete major acquisitions of complementary businesses, products or technologies, we may need additional capital, and may not be able to raise additional capital on favorable terms or at all, which could limit our ability to grow and could increase our costs.

Our future liquidity and capital requirements are difficult to predict because they depend on numerous factors, including the success of our existing and new product offerings as well as competing technological and market developments. As a result, we may not be able to generate sufficient cash flows from our operations to meet additional working capital requirements, support additional capital expenditures or take advantage of acquisition opportunities. In fiscal 2008, the acquisitions of Navtel Communications ($11.3 million) and Brix Networks ($29.7 million), combined with $6.5 million in capital expenses, exceeded the $13.8 million provided by cash flows from operations. As at August 31, 2008, we held $87.5 million in cash and short-term investments.

We may need to raise additional capital in the future. Our ability to obtain additional financing will be subject to a number of factors, including market conditions, effects of the financial crisis, reduced access to credit facility and our operations performance. These factors may render the timing, amount, terms and conditions of additional financing unattractive for us. If we raise additional funds by selling equity securities, the relative ownership of our existing investors could be diluted or the new investors could obtain terms more favorable than previous investors. If we raise funds through debt financing, we could incur significant borrowing costs. If we are unable to raise additional funds when needed or at terms satisfactory to us, our ability to operate and grow our business could be impeded.

Our business and operations would suffer in the event of a failure of our information technology infrastructure.

We rely upon the capacity, efficiency and security of our information technology hardware and software infrastructures as well as our ability to expand and update these infrastructures in response to our evolving needs. Any failure to manage, expand or update our information technology infrastructures or any failure in the operation of this infrastructure could harm our business.

Our information systems are vulnerable to damages from computer viruses, natural disasters, unauthorized access and other similar disruptions. Any system failure, accident or security breach could result in disruptions to our operations. To the extent that any disruption or security breach results in a loss or damage to our data, or inappropriate disclosure of our confidential information, it could harm our business. In addition, these events may force us to devote more money and resources in order to protect ourselves against damages caused by these disruptions or security breaches in the future.

Table of Contents

Item 4. Information on the Company

A. History and Development of the Company

Our legal name and commercial name is EXFO Electro-Optical Engineering Inc. / EXFO Ingénierie électro-optique inc. Our head office is located at 400 Godin Avenue, Quebec, Quebec, Canada, G1M 2K2 and our main telephone number is (418) 683-0211. Our e-mail address is info@EXFO.com and our website is www.EXFO.com. Information on our website is not incorporated by reference in this annual report. Our agent for service in the United States is CT Corporation System, 111 Eighth Avenue, New York, New York 10011. Our Transfer Agent and Registrar is CIBC Mellon Trust Company, 2001 University Street, Suite 1600, Montreal, Quebec, Canada, H3A 2A6. This annual report contains trademarks and registered trademarks of us and other companies.

We were incorporated on September 18, 1985 pursuant to the Canada Business Corporations Act. Since that date, we have amended our articles on various occasions mainly to modify our legal and corporate names and our share capital.

On December 20, 2000, we acquired all of the shares of EXFO Burleigh Products Group Inc. (formerly Burleigh Instruments, Inc.) ("EXFO Burleigh"), Burleigh Instruments GmbH and Burleigh Instruments (U.K.) Ltd. for an aggregate purchase price of US$189.3 million, comprised of 6,488,816 of our subordinate voting shares and US$42.5 million in cash pursuant to the terms of an Agreement of Merger and Plan of Reorganization among us, EXFO Sub, Inc. and the selling shareholders, dated November 4, 2000, as amended on December 20, 2000. In April 2002, the name of Burleigh Instruments, Inc. was changed to EXFO Burleigh Products Group Inc. On November 12, 2002, Burleigh Instruments (UK) Ltd. was dissolved. EXFO Burleigh is a U.S. company that manufactures precision scientific instruments used in basic and applied research engineering and production test applications in a variety of fields.

On March 15, 2001, we acquired all of the shares of EXFO Photonic Solutions Inc. (formerly EFOS Inc.) ("EXFO Photonic"), a privately held company in Toronto, Canada, for a total consideration of US$110.1 million, of which US$25.1 million was paid in cash. We also issued 3,700,000 of our subordinate voting shares in connection with the acquisition. In September 2001, the name EFOS Inc. was changed to EXFO Photonic Solutions Inc.

EXFO Photonic, operating since 1984, is a supplier of precision light-based adhesive spot curing products as well as curing process control for the global optical component manufacturing market and other non-telecom markets. Its products deliver precise doses of the appropriate spectral light into photo-sensitive and heat-cured adhesives to significantly reduce bonding time and increase repeatability in optical component and other manufacturing activities. EXFO Photonic light-based curing technologies are supported by an extensive understanding of bonding and material sciences and by a broad intellectual property portfolio. EXFO Photonic, as of November 3, 2008, has 26 patents and 8 patents pending.

Also on March 16, 2001, our wholly owned subsidiary, Burleigh Automation Inc. ("Burleigh Automation"), acquired substantially all the assets of Vanguard Technical Solutions, Inc., a wholly owned subsidiary of DT Industries, Inc. for a purchase price of US$600,000 paid in cash. Vanguard, an automation equipment manufacturer in Tucson, Arizona, specialized in the design and manufacturing of ultra-precision assembly equipment for sensitive process and critical assembly challenges on the production floor. This acquisition, which complemented our acquisition of Burleigh, was planned to fit with our overall strategy at that time of providing customers with a comprehensive solution for the assembly, alignment and testing of optical components and subsystems. Since September 2001, Burleigh Automation has ceased operations and we have transferred all material intellectual property assets and most of the physical assets of Burleigh Automation to EXFO Burleigh.

In November 2001, we acquired all of the shares of Avantas Networks Corporation and simultaneously changed the name of that company to EXFO Protocol Inc. (“EXFO Protocol”). We paid a total consideration of US$69.4 million (or US$95.0 million for the equity minus US$25.6 million of cash in the hands of the acquired company) to acquire EXFO Protocol. Consideration paid consisted of 4,374,573 of our subordinate voting shares and US$9.8 million in cash, net of cash acquired. EXFO Protocol, a company based in Montreal, Canada operating since 1998 is a supplier of fiber-optic testing and optical network performance management equipment that supports a wide range of protocols and data transmission rates.

Table of Contents

During fiscal 2001, we were forced to align our cost structure to market conditions. On June 27, 2001, we announced the reduction of non-customer-related expenses, postponement of plans to build a new facility in the Quebec Metro High-Tech Park, termination of non-cure operations of Nortech, a subsidiary that specialized in manufacturing fiber-optic temperature sensors and reduction of our work force by 15%. Our plan to build a new facility has been cancelled since then.

During fiscal 2002, we were forced to re-align our cost structure to market conditions. First, on December 5, 2001, we announced the lowering of our operating expenses, a freeze in employee salaries, and the reduction of our workforce by 10%. Then, on May 15, 2002, we announced a further 20% reduction of our global workforce in an effort to lower our cost structure. In May 2002, we performed an assessment of the carrying value of goodwill and intangible assets recorded in conjunction with the three acquisitions made during the previous 18 months. Considering the ongoing unfavorable market conditions, we recorded a charge of US$222.2 million to write down a significant portion of goodwill and a charge of US$23.7 million to write down a significant portion of acquired core technology. Also, overall for fiscal 2002, we wrote off US$18.5 million in excess and obsolete inventories.

In August 2002, EXFO Burleigh received confirmation of the extension of its contract with the U.S. Air Force Research Laboratory into phase 2 of a project for the development by EXFO Burleigh of new high-precision actuator system. The contract for phase 2 provided for an additional funding of US$1.7 million and extended through the first quarter of 2005.

In October 2002, our newly created, wholly owned subsidiary, EXFO Gnubi Products Group Inc. (“EXFO Gnubi”), acquired substantially all the assets of gnubi communications L.P., including its technology, expertise, customer base, inventories and capital assets. Consideration paid consisted of US$1.9 million in cash and 1,479,290 of our subordinate voting shares. Furthermore, an additional cash amount of US$241,000, based on sales volumes, was paid in fiscal 2004 in accordance with earn out provisions. With the acquisition of these assets, EXFO Gnubi, based in Dallas, Texas, continues the operations of gnubi communications, L.P., as a supplier of multi-channel telecom and datacom testing solutions serving optical transport equipment manufacturers and research and development laboratories. At the time of the asset acquisition, 30 employees of gnubi communications, L.P. transferred to EXFO Gnubi.

During fiscal 2003, we were required to implement further restructuring measures as a result of depressed spending levels in the telecommunications industry and economic uncertainty. We reduced our workforce by 30%, rationalized our business activities and consolidated certain manufacturing operations. These measures incurred charges of US$4.1 million. The rationalization and consolidation initiatives involved the reorganization of our business into two new reportable market segments: Telecom Division and Photonics and Life Sciences Division and the exiting of the optical component manufacturing automation business. Our Telecom Division consists of the former Portable and Monitoring and telecom related Industrial and Scientific product lines. Our Photonics and Life Sciences Division includes previous non-telecom Industrial and Scientific product lines. Each division has been structured with its own sales, marketing, manufacturing, research and development and management teams.

In May 2003, we performed our annual impairment test on goodwill recorded in conjunction with the acquisitions of EXFO Burleigh, EXFO Photonic and EXFO Protocol and also reviewed the carrying value of intangible assets related to these acquisitions. As a result of this assessment, we concluded that the carrying value of goodwill related to EXFO Burleigh and the carrying value of intangible assets related to EXFO Burleigh and EXFO Photonic was impaired and we recorded a charge of US$4.5 million to write down goodwill and a pre-tax charge of US$2.9 million to write down acquired core technology. Of the total impairment loss of US$7.4 million, US$6.9 million is related to EXFO Burleigh for goodwill and acquired core technology and US$0.6 million is related to EXFO Photonic for acquired core technology.

In addition, in an effort to simplify our structure and stream-line our operations, the operations of EXFO Protocol were merged with those of the Corporation as of September 1, 2003 and effective December 1, 2003, the operations of EXFO Gnubi were merged with those of EXFO America Inc.

In fiscal 2004, EXFO also closed a public offering of 5.2 million subordinate voting shares to a syndicate of Canadian-based underwriters for net proceeds of US$29.2 million (CA$38.4 million).

Furthermore in fiscal 2004, we consolidated our protocol test operations (EXFO Protocol and EXFO Gnubi) in Montreal, Canada to improve efficiency and reduce costs.

Table of Contents

In March 2004, we renewed our collective bargaining agreement with unionized manufacturing employees in Quebec City, Canada. Such agreement will expire in February 2009.

During fiscal 2005, our Photonics and Life Sciences Division was renamed the Life Sciences and Industrial Division to better reflect its market focus.

During fiscal 2005, we completed the consolidation of our Life Sciences and Industrial Division in Toronto, Canada and we recorded US$482,000 in restructuring expenses. Altogether, we incurred US$2.5 million in restructuring and other charges since the fourth quarter of 2004 in conjunction with this consolidation process. Following this process all of the operating activities of EXFO Burleigh were transferred mainly in Toronto, Canada.

In January 2006, we acquired substantially all the assets of Consultronics Limited ("Consultronics"), a leading supplier of test equipment for copper-based broadband access networks. Consultronics is a privately held company based in Toronto, Canada with subsidiaries in the United Kingdom and Hungary. We acquired all of the subsidiaries' respective issued and outstanding shares. Consultronics specializes in x-Digital Subscriber Line (xDSL), Internet Protocol TV (IPTV) and Voice-over-Internet Protocol (VoIP) test solutions for the broadband access market. We paid consideration equal to approximately US$19.1 million, including debt assumption and other acquisition-related costs.

In November 2006, we incorporated EXFO Electro-Optical Engineering India Private Limited as our wholly-owned subsidiary to establish a software development center in Pune, India. In October 2007, we acquired substantially all of the assets of JamBuster Technologies Private Limited, for an immaterial consideration, a company duly incorporated in Pune, India which is engaged in the business of software development services.

In April 2007, we established a wholly-owned foreign entity in Shenzhen China, EXFO Telecom Equipment (Shenzhen) Co. Ltd. for manufacturing purposes. We started ramping up manufacturing in September 2007 at our Chinese facility.

On November 5, 2007, the Board of Directors approved a share repurchase program, by way of a normal course issuer bid on the open market of up to 9.9% of our public float (as defined by the Toronto Stock Exchange), or 2,869,585 shares at the prevailing market price. The period of the normal course issuer bid commenced on November 8, 2007, and ended on November 7, 2008. We repurchased a total of 1,859,835 shares. All shares repurchased under the bid were cancelled. We shall provide to any person or company, upon request to our Secretary, at 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2, phone number (418) 683-0913 ext. 3704 or fax number (418) 683-9839 a copy of the notice sent to the Toronto Stock Exchange (TSX) according to its normal course issuer bid.

In March 2008, we acquired all the issued and outstanding shares of Navtel Communications Inc. ("Navtel"), a leading provider of Internet Protocol Multimedia Subsystem (IMS) and Voice-over-Internet Protocol (VoIP) test solutions for Network Equipment Manufacturers (NEMs) and Network Service Provider (NSP) labs. Navtel is a privately held company based in Toronto, Canada with subsidiaries in the Province of Ontario, Canada, United States and Germany. We paid consideration equal to approximately US$11,477,000, or US$11,332,000 net of US$145,000 of cash acquired. The total consideration included acquisition-related costs of US$172,000.

In April 2008, we acquired all the issued and outstanding shares of Brix Networks Inc. ("Brix"), a global provider of open and extensible converged service assurance solutions. Brix is a privately held company based near Boston, USA with a subsidiary in the United Kingdom. We paid consideration equal to approximately US$29,696,000, or US$29,684,000 net of US$12,000 of cash acquired, plus a contingent cash consideration of up to a maximum of US$7,537,000, based upon the achievement of a bookings volume exceeding US$16,000,000 up to US$40,000,000 in the 12 months following this acquisition.

16

Table of Contents

On November 6, 2008 we announced the renewal of a share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of our public float (as defined by the Toronto Stock Exchange), or 2,738,518 subordinate voting shares at the prevailing market price. We expect to use cash, short-term investments or future cash flow from operations to fund the repurchase of shares. The normal course issuer bid will start on November 10, 2008, and end on November 9, 2009, or on an earlier date if we repurchase the maximum number of shares permitted under the bid. The program does not require that we repurchase any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled. We shall provide to any person or company, upon request to our Secretary, at 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2, phone number (418) 683-0913 ext. 3704 or fax number (418) 683-9839 a copy of the notice sent to the Toronto Stock Exchange (TSX) according to its normal course issuer bid.

On November 10, 2008 we announced a substantial issuer bid (the "Offer") to purchase for cancellation up to 8,823,529 shares for an aggregate purchase price not to exceed CA$30 million. The Offer is being made by way of a "modified Dutch Auction" pursuant to which shareholders may tender all or a portion of their shares (i) at a price not less than CA$3.40 per share and not more than CA$3.90 per share, in increments of CA$0.05 per share, or (ii) without specifying a purchase price, in which case their shares will be purchased at the purchase price determined in accordance with the Offer. The Offer will expire at 5 p.m. (Eastern time) on December 16, 2008, unless withdrawn, extended or varied by us. We expect to use cash, short-term investments or future cash flow from operations to fund the repurchase of shares. The Offer is not conditional upon any minimum number of shares being tendered, but it is subject to certain other conditions. A complete description of the terms and conditions of the Offer is contained in the Offer to Purchase and Issuer Bid Circular and related documents filed with the applicable securities regulatory authorities in Canada and the United States and mailed to holders of shares on or about November 10, 2008. We shall provide to any person or company, upon request to our Secretary, at 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2, phone number (418) 683-0913 ext. 3704 or fax number (418) 683-9839 a copy of such documentation sent to the Toronto Stock Exchange (TSX) according to its normal course issuer bid.

Upon the approval of the Offer, we suspended the normal course issuer bid that we had renewed on November 6, 2008 referred above, until 20 business days after the expiration of the Offer.

B. Business Overview

Company Overview

EXFO is a leading provider of testing, measuring and monitoring solutions for network service providers and equipment manufacturers in the global telecommunications industry. The Telecom Division, which represents more than 85% of our business, offers a wide range of innovative solutions extending across the full technology lifecycle from design to technology deployment and onto service assurance and covering all the layers of a network infrastructure to enable triple-play services and next-generation, converged IP networking. The Life Sciences and Industrial Division offers solutions in medical-device and opto-electronics assembly, fluorescence microscopy, UV printing ink curing and other life sciences sectors.

We were founded in 1985 in Quebec City, Canada. Our original products were focused on the needs of installers and operators of fiber-optic networks. Customers use these field-portable testing products for the installation, maintenance, monitoring and troubleshooting of optical networks. In 1996, we supplemented our product portfolio with an extensive line of high-end products that are mainly dedicated to research and development as well as manufacturing activities of optical component manufacturers and system vendors.

Over the past several years, we have enhanced our competitive position and breadth of products through the acquisition of companies that specialize in transport and data communications testing higherlayer protocol testing and emulation, copper/xDSL testing and network communications service assurance.

Table of Contents

In April 2008, we acquired all issued and outstanding shares of Brix Networks Inc. (renamed EXFO Service Assurance Inc.), for a cash consideration of US$29.7 million, plus a contingent cash consideration of up to a maximum of US$7.5 million, based on booking levels exceeding US$16 million up to US$40 million in the 12 months following the closing of the deal. Brix Networks, a privately held company located in the Boston (MA) area, offers VoIP and IPTV service assurance solutions across the three areas most affecting the success of a real-time service: signaling quality (signaling path performance), delivery quality (media transport performance) and content quality (overall quality of experience). Brix Networks' service assurance solutions are mainly designed for network service providers (NSPs) and large enterprises.

In March 2008, we acquired all issued and outstanding shares of Navtel Communications Inc., for a cash consideration of US$11.3 million. Navtel Communications, a privately held company in Toronto, Canada, is a leading provider of IMS and VoIP(based on SIP Protocol) test solutions for network equipment manufacturers (NEMs) and NSP labs. Navtel Communications specializes in testing next-generation IP networks that are increasingly combining wireline and wireless technologies. Subsequent to the acquisition, Navtel Communications was merged into the parent company.

In fiscal 2008, we opened our own telecom manufacturing facilities in Shenzhen, China. We now have two main manufacturing sites for our Telecom Division and one smaller plant for our Life Sciences and Industrial Division. Over time, low-volume, high-complexity telecom products will be manufactured in Quebec City, whereas high-volume, low-complexity telecom products will be manufactured in Shenzhen.

In fiscal 2008, we accelerated the deployment of a software development center in Pune, India, to supplement the research and development capabilities of our R&D labs in Boston, Toronto, Montreal and Quebec City. This will enable us to benefit from the wealth of IP expertise in India, to accelerate product development especially for our software-intensive protocol test solutions to take advantage of a lower cost structure.

In January 2006, we acquired substantially all the assets of Consultronics Limited, a leading supplier of test equipment for copper-based broadband access networks, for a total cash consideration of US$19.1 million. Above and beyond copper/xDSL test solutions, Consultronics had a rich product portfolio for testing next-generation technologies, such as IPTV and VoIP, which are critical for NSPs in their deployment of triple-play services (voice, data, video) over optical and copper links in access networks. This acquisition was a strategic initiative to position EXFO as a strong supplier of broadband access and triple-play testing because it complemented our market leadership in the optical FTTx test market.

In November 2001, we acquired Avantas Networks Corporation (renamed EXFO Protocol Inc. and which has since been merged with EXFO), a supplier of transport and datacom testing equipment for NSPs. This transaction enabled us to combine optical and protocol test modules inside a single field-portable test platform in order to help our customers increase revenues and reduce operating costs. In October 2002, our wholly-owned subsidiary, EXFO Gnubi, purchased substantially all the assets of gnubi communications, L.P., a supplier of multichannel telecom and datacom testing solutions for the system manufacturer market. These strategic acquisitions which were consolidated in Montreal, Canada, in fiscal 2004 enabled us to more than double our addressable market, as we expanded from optical testing to transport and datacom (Layers 1-3) testing applications, and to offer a more complete line of test solutions to our customers.

Previously, we had completed two acquisitions to bolster growth in the optical component manufacturing market. We acquired Burleigh Instruments, Inc. (renamed EXFO Burleigh Products Group Inc.) in December 2000 for its wavelength measurement instruments and nanopositioning alignment systems. We also added EFOS Inc. (renamed EXFO Photonic Solutions Inc.) in March 2001 for its precision light-based, adhesive spot-curing technology. We have since exited the optical component manufacturing automation business, and the remaining operations of EXFO

Burleigh have mostly been consolidated with those of EXFO Photonic Solutions in Toronto, Canada. These consolidated businesses now fall under our Life Sciences and Industrial Division.

Table of Contents

We launched 27 new products in fiscal 2008, including seven in the fourth quarter, compared to 20 in fiscal 2007. Key product introductions in fiscal 2008 included among others a multiservice, multimedium modular handheld platform for characterizing and troubleshooting access networks (AXS-200 SharpTESTER) along with related DSL, copper access, Ethernet and optical test modules; a compact multiservice transport test set that combines next-generation SONET/SDH and Ethernet testing inside a single module (FTB-8120NGE/FTB-8130NGE Power Blazer); 40/43 Gbit/s SONET/SDH field and lab oriented solutions (FTB-8140/IQS-8140 Transport Blazer) for high-speed optical networks; an all-in-one chromatic dispersion (CD) and polarization mode dispersion (PMD) analyzer (FTB-5700 Single-Ended Dispersion Analyzer) that requires only one technician to characterize a link from a single end; a triple-play test set (AXS-200/630 VDSL, ADSL2+ and IP Triple-Play Test Set) for the deployment and troubleshooting of ADSL2+/VDSL2 networks; and the advanced IQS-600 Integrated Qualification System, a next-generation, modular test platform for R&D and manufacturing applications. Following the year-end, we introduced an enhanced version of Navtel's InterWatch platform that simulates up to 256,000 unique IPv6 subscriber addresses per chassis, and new software features on the Transport Blazer test modules for characterizing 40G/43G SONET/SDH networks. Sales from products that have been on the market two years or less accounted for 34.6% for the fiscal year, while our published goal is 30%.

Overall for fiscal 2008, we increased sales 20.2% to $183.8 million from $152.9 million in 2007. Global sales for fiscal 2008 included $5.4 million from newly acquired Brix Networks and Navtel Communications since their acquisitions in the third quarter of 2008. GAAP net earnings reached $18.4 million, or $0.27 per diluted share, including $5.3 million for the recognition of previously unrecognized future income tax assets in the United States, $2.7 million for income tax recovery following the review of our tax strategy related to recently substantively enacted income tax rates in Canada, $1.5 million of income tax expense to account for the recently substantively enacted income tax rate on our future income tax assets in Canada, an extraordinary gain of $3.0 million related to the negative goodwill on the Navtel acquisition, as well as $3.0 million in after-tax amortization of intangible assets and $1.3 million in stock-based compensation costs. In 2007, GAAP net earnings reached $42.3 million, or $0.61 per diluted share, including $24.6 million in recognition of previously unrecognized future income taxes, $3.2 million in recognition of previously unrecognized research and development tax credits, $2.9 million in amortization of intangible assets, $1.1 million from a government grant recovery and $1.0 million in stock-based compensation costs.

In fiscal 2008, we faced a substantial and sudden increase in the value of the Canadian dollar versus the US dollar. The average value of the Canadian dollar increased 11.4% in fiscal 2008, compared to the same period last year. Given that most of our sales are denominated in US dollars but a significant portion of our expenses are denominated in Canadian dollars, our financial results were negatively affected.

On November 5, 2007, the Board of Directors approved a share repurchase program, by way of normal course issuer bid on the open market, up to 9.9% of our public float (as defined by the Toronto Stock Exchange), or 2.9 million of subordinate voting shares, at the prevailing market price. The period of the normal course issuer bid commenced on November 8, 2007 and ended on November 7, 2008. All shares repurchased under the bid were cancelled. We redeemed 1.9 million subordinate voting shares for a total consideration of $8.5 million under that program.

On November 6, 2008, we announced a renewal of our share repurchase program, by way of a normal course issuer bid on the open market, of up to 10% of our public float (as defined by the Toronto Stock Exchange), or 2,738,518 subordinate voting shares, at the prevailing market price. We expect to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The period of the normal course issuer bid starts on November 10, 2008, and will end on November 9, 2009, or on an earlier date if we repurchase the maximum number of shares permitted under the bid. The program does not require that we repurchase any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled.

19

Table of Contents

On November 10, 2008, we announced a substantial issuer bid (the "Offer") to purchase for cancellation up to 8.8 million subordinate voting shares for an aggregate purchase price not to exceed CA$30 million. The Offer is being made by way of a "modified Dutch Auction" pursuant to which shareholders may tender all or a portion of their shares (i) at a price not less than CA$3.40 per share and not more than CA$3.90 per share, in increments of CA$0.05 per share, or (ii) without specifying a purchase price, in which case their shares will be purchased at the purchase price determined in accordance with the Offer. The Offer will expire on December 16, 2008, unless withdrawn, extended or varied. We expect to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The Offer is not conditional upon any minimum number of shares being tendered, but it is subject to certain other conditions.

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

Key Industry Trends

The basic fundamentals of the global telecom industry remain solid for the moment. However, it is still unknown what impact the financial crisis might have on the global economy and the telecom industry in particular, especially in the United States where a severe economic slowdown could potentially reduce investments and affect other parts of the world. Fundamental telecom business drivers are based on exponential growth in bandwidth demand, coupled with intense competition between telecom operators (telcos) and cable companies (cablecos). Both classes of companies are funding massive investments in converged, next-generation Internet protocol (IP) networks to capitalize on significant operational efficiencies and to attract/retain subscribers and increase revenues through improved service offerings.

Global Internet bandwidth demand is growing very rapidly, due to a myriad of applications like video, Web gaming, etc. TeleGeography Research estimated that bandwidth demand has grown at a compound annual growth rate (CAGR) of 54% from 2004 to 2008. This trend is likely to remain steady in the years to come with the upcoming deployments of IPTV (Internet protocol television), HD-IPTV (high-definition Internet protocol television) and increased online video streaming, since these applications, among others, will consume a colossal amount of additional bandwidth. As a result, telcos and cablecos are investing substantially in their access networks in order to provide differentiated, revenue-generating services to attract and retain consumers who are increasingly relying on broadband network services for their work, entertainment and everyday activities. From a telco perspective, it is likely that fiber-to-the-home (FTTH) will become the access network architecture of choice that will allow them to meet heightened bandwidth requirements and future-proof their access networks, as residential bandwidth requirements are growing from the 1 to 5 Mbit/s (megabits per second) of the past to the 30 to 100 Mbit/s required in the long-term. Hybrid architectures, combining copper and fiber (fiber-to-the-curb, or FTTC, and fiber-to-the-node, or FTTN), will continue expanding in the short term, since they are less-expensive methods to increase bandwidth and can be mass-deployed faster.

These investment decisions are applicable not only to green-field deployments and high-rise buildings, but also to larger-scale rollouts as long-term operating costs are less than FTTC and FTTN. The cost of deploying FTTH has been decreasing over the last few years as volume increased and deployment tools, like those we offer, are making the task increasingly simple and efficient. Networks are in the early stages of fiber deployments in access networks in both the Americas and around the world. In addition, Western Europe and China have become increasingly committed to deploying FTTH networks, given their high population density. Both Japan and South Korea have already adopted fiber to the home as a mainstream method of broadband residential service.

As bandwidth growth in access networks continues to increase it has begun placing a strain on metro rings and core networks. It is also driving the need for higher-speed technologies; for example, 43 Gbit/s (gigabits per

second) SONET/SDH is now increasingly deployed and becoming mainstream, while 100 Gbit/s Ethernet is in early field trials. The deployment of these solutions is expected to be significantly more economical if it alleviates the need for trenches need to be dug in order to deploy new fiber in metro or long-distance routes.

Table of Contents

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

These market dynamics positively affected telecom test, measurement and service assurance suppliers in fiscal 2008; however, deteriorating macro-economic conditions in the United States could instigate a slowdown in capital spending among customers, which would necessarily reduce demand for our test, measurement and service assurance solutions.

In terms of our Life Sciences and Industrial Division, key market trends for the niche markets that we serve include:

- Industrial UV Spot-Curing: The end-markets for precision assembled products manufactured with UV curing remains healthy, especially for the assembly of medical devices, despite weaker economic conditions. The market in Asia, dominated by high volume opto-electronics manufacturing, is increasingly adopting LED (light emitting diode) UV spot curing equipment.
- Life Sciences: The fluorescence microscopy market continues to increase steadily with the majority of the growth happening in live cell and quantitative imaging applications.
- Industrial UV Digital Print Ink Curing: The digital print markets that we target are exhibiting strong growth as printing press equipment continues to make the transition from analog to digital technology.

Three-Year Corporate Objectives

Our vision is to become a strong market leader in the global telecom test, measurement and service assurance industry offering market-driven solutions mainly for network service providers and increasingly covering the service and application layers of the network infrastructure to enable triple-play services and next-generation, converged IP networking.

We do not intend to become a one-stop shop for our customers, but rather continue to be a strong player in selected, high-growth and synergistic markets. We will follow this roadmap by offering best-in-class solutions that anticipate market needs, while focusing on the highest level of customer satisfaction.

To achieve our long-term vision, we plan to expand our leadership position in the portable Optical segment, while growing our Transport and Data communications testing (Protocol) business even faster to surpass the Optical segment in terms of sales. This plan is based first and foremost on organic growth, but it will be supported by strategic acquisitions of small to mid-size companies with best-in-class technologies in nascent, high-growth markets that are complementary to us. We also intend to improve our competitive position through strategic alliances and partnerships.

Following our practice of benchmarking performance, we have established three corporate performance objectives to measure the success of our three-year plan ending at the close of fiscal 2011. These long-term objectives are intended to replace the performance goals that the company provided on an annual basis. These new objectives reflect the clear direction management is taking towards long-term value creation.

21

Table of Contents

Objective	Three-Year Metric
Increase sales significantly faster than the industry growth rate	20% CAGR
Grow EBITDA* in dollars faster than sales	>20% CAGR
Continue raising gross margin	62%

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

The EXFO Solution

We offer an extensive range of test, measurement and service assurance solutions to the global telecommunications industry. Our success has been largely predicated on our core expertise in producing test equipment for optical telecommunications. We also leverage this expertise to develop products for life sciences and high-precision assembly applications. Our solution is based on the following key attributes:

Modular System Design. In 1996, we established an industry-first by launching the original modular optical test platform. This system design consists of a PC-based, MS Windows-driven platform that can accommodate several test modules performing various types of measurements. We have since developed additional compatible test platforms and extended our test module offering for both NSPs and system manufacturers based on the same modular design. Our modular product design provides the following advantages:

- unlike stand-alone units, new test modules can be rapidly developed to address changing industry requirements;
- as customers' testing requirements change, they can purchase additional modules that are compatible with their previously purchased platforms, thus protecting their initial investments;
- our standard graphical user interface reduces training costs because customers are familiar with previously acquired software products;
- the flexibility of our systems allows customers to develop customized and automated solutions for their specific test requirements;
- our test platforms are PC-based and MS Windows-driven, thus they can support third-party software solutions.

High Degree of Technological Innovation. We have established a strong reputation for technological innovation over the last 23 years. In fact, we believe this attribute represents a key differentiator for us within a competitive marketplace. Following are some of our industry firsts:

- the first PC-based modular test platform for field applications;
- the first all-in-one optical loss test set combining several instruments;
- the first portable polarization mode dispersion (PMD) analyzer;
- the first modular platform to combine optical and protocol test solutions;
- the first line of portable test instruments designed for FTTx testing; and
- the first fully integrated Ethernet-over-SONET test solution.

High-Quality Products. Product quality is an integral part of our solution. Our Quebec City, Canada, operations have maintained ISO 9001 certification since 1994 and they are now certified to the new 2000 edition of the standard. Our manufacturing plant in Shenzhen, China, which started operations in September 2007, is responsible for the production of high-volume, low-complexity telecom products. Quality-control responsibilities for products manufactured in China will remain in Quebec City until the Shenzhen facility obtains full ISO-9000 certification. All of our products meet required industry standards, and some of our products meet additional voluntary standards, such as those set by Telcordia, formerly Bellcore, IEC, IETF, ETSI and other industry-leading standards bodies. During

manufacturing, each product has a related quality-assurance plan, with rigorous checkpoints, to ensure product conformity. Various tasks in the quality assurance process include quality control, conformity testing, product documentation, product improvement, regulatory compliance, metrology and calibration.

Table of Contents

Our product designs comply with Directive 2002/96/EC, a legislation enacted by the European Union regarding the disposal of waste electrical and electronic equipment (WEEE), for all products exported to Europe. In regard to the Directive 2002/96/EC (RoHs), test and measurement manufacturers have been provided a limited exemption until 2012.

Products

Our test platforms, namely the AXS-200 SharpTESTER, FTB-200 Compact Platform, FTB-400 Universal Test System (UTS), and IQS-600 Intelligent Test System (ITS), are at the core of our product portfolio. The AXS-200 SharpTESTER, which was launched in September 2007, is a multi-service, multi-medium handheld test platform designed for characterizing and troubleshooting commercial and residential access networks. It can easily be configured for copper/DSL/triple-play, Ethernet or optical testing applications. The FTB-200 Compact Platform is a two-slot portable test unit optimized for multi-technology, multi-application characterization of metro and access networks. The FTB-400 field-testing platform provides network service providers with a simple, yet efficient way to perform multiple, advanced test operations for installation, maintenance and troubleshooting applications. Our IQS-600 ITS, which was launched in the second quarter of 2008, is designed for manufacturing and R&D applications. It tests optical as well as transport and data communications technologies increasingly based on IP. All platforms and related test modules are supported by integrated and highly intuitive graphical user interfaces (GUIs), enabling the user to easily store, handle and retrieve test results and measurement data. In addition, EXFO offers a number of handheld and benchtop test and measurement products, some of which are modular in nature.

Following the acquisition of Navtel Communications in March 2008, we offer the InterWatch platform series, a line of advanced hardware and software-based test systems that enable network equipment manufacturers and network service provider labs to fully test their complex digital telecommunications equipment and services more quickly and cost-effectively, while helping to ensure interoperability and reliability. These advanced software and hardware solutions assist customers in the design, integration, installation and acceptance testing of a broad range of Internet Protocol Multimedia Subsystem (IMS)/Next-Generation Network (NGN) telecommunications equipment and services by performing a variety of test functions:

- Design and feature verification;
- Interoperability testing;
- Load and stress testing; and
- Monitoring and analysis.

Following the acquisition of Brix Networks in April 2008, we also offer various Brix Solutions, a comprehensive service assurance and performance monitoring systems for advanced IP services such as IPTV, voice-over-IP, virtual private networks (VPNs), video on demand, and video conferencing. The Brix System, a family of integrated software and hardware components, proactively monitors quality by providing complete visibility across all IP services, throughout the lifecycle of the service, and across the entire network.

In the Brix Solutions, advanced performance management applications, running on a central-site software engine, called BrixWorx, analyze and display performance data collected from the measurement sources, Brix Verifiers, deployed throughout the network being monitored. Brix Verifiers execute protocol-specific tests to precisely calculate crucial availability and performance metrics through proactive testing, ongoing monitoring, and the collection of data directly from infrastructure devices.

BrixWorx provides all performance data analysis, configuration, and management for the distributed Brix System, while test suites offer broad and deep visibility into the performance of converged network services.

Furthermore, EXFO offers network monitoring systems and test probes used in third-party network monitoring solutions.

Table of Contents

The following table summarizes the principal types of test instruments for the telecommunications industry, typical applications and the formats in which we offer them:

Instrument Type	Typical Application	NSP Market				Manufacturer /R&D Market	
		FTB 400 Modules	FTB 200 Modules	AXS 200 Modules	Handhelds	IQS-600 Modules	Bench top Instruments
ADSL/ADSL2+ Service Verification Tool	Based on a DSL “golden modem”, these units are used to test the function, speed and quality of a DSL service at the subscriber premises.			X	X		
Broadband source	Used for testing wavelength-dependent behavior of fiber cables and dense wavelength division multiplexing (DWDM) optical components.					X	X
Chromatic dispersion analyzer	Measures increasing levels of chromatic dispersion in high-capacity optical networks. Chromatic dispersion is a physical phenomenon inherent to optical fiber and optical components that causes information bits to spread along a network. This degrades the quality of the transmission signal and, in turn, limits the transmission speed carried by optical networks.	X					
Clip-on coupling device	Clips to an optical fiber and allows non-invasive testing.				X		
Fibre Channel tester	Brings FC-0, FC-1 and FC-2 logical layer Fibre Channel testing to services delivered via transport protocols, such as dense wavelength division multiplexing (DWDM), SONET/SDH and dark fiber. It provides valuable timing information and buffer credit	X	X			X	

	estimation for Fibre Channel network deployment.						
Gigabit Ethernet tester	Measures data integrity for high-speed Internet protocol telecommunications in metro and edge networks.	X	X	X		X	
10 Gigabit Ethernet tester	Benchmarks and verifies high-speed 10 Gbit/s Ethernet network performance and service-level agreements.	X	X			X	
HDTV, SDTV and IPTV service test instrument	Used to test the quality and functionality of standard and high definition television signals that are delivered over higher-rate ADSL, ADSL2+ and VDSL2 transmission technologies.				X		
Laser spectrum analyzer	Performs high-resolution, spectral characterization of continuous CW laser sources						X
Telephone for traditional voice and VoIP service testing	Used by telephone line and DSL installers to test the proper functioning of both traditional and next-generation voice and data communication services.				X		
Live fiber detector	Clips on to a fiber and is used to detect the presence and direction of a signal without interrupting the traffic.				X		
Loss test set	Integrates a power meter and a light source to manually or automatically measure the loss of optical signal along a fiber.	X	X	X	X	X	X
Narrowly tunable laser	A laser that can be precisely tuned to simulate a DWDM light sources. Used primarily for testing optical amplifiers.					X	
		X				X	

Next-generation SONET/SDH analyzer	Full SONET/SDH protocol testing functionality, including support for generic framing procedure (GFP), virtual concatenation (VCAT), and link-capacity adjustment scheme (LCAS) next generation enhancements.						
Optical coupler	Used in test system to combine sources or signals. Also uses as splitters to monitor signals.				X		
Optical power meter	Measures the power of an optical signal. It is the basic tool for the verification of transmitters, amplifiers and optical transmission path integrity.	X	X		X	X	X
Optical power reference module	Provides a highly accurate and traceable measurement of power for the calibration or verification of other power measurement instruments.				X		

Table of Contents

Instrument Type	Typical Application	NSP Market			Manufacturer /R&D Market	
		FTB 400 Modules	FTB 200 Modules	AXS 200 Handhelds	IQS-600 Modules	Bench top Instruments
Optical return loss meter	Combines a laser and a power meter to measure the amount of potentially degrading back reflection.	X	X	X	X	
Optical spectrum analyzer	Produces a graphical representation of power versus wavelength for an optical signal. Useful for measuring the drift, power and signal-to-noise ratio for each wavelength in a DWDM system.	X				
Optical switch	Provides switching between fibers. Used to provide flexible and automated test setups such as the measurement of multiple fibers or components with multiple ports with one instrument.	X			X	
Optical time domain reflectometer (OTDR)	Like a radar, it measures the time of arrival of reflections of an optical signal to determine the distance to the breaks or points of excessive loss in a fiber network.	X	X	X		
Passive component analyzer	Characterizes passive wavelength-selective devices, such as multiplexers, demultiplexers and add/drop filters, with respect to absolute wavelength in order to guarantee their performance within dense wavelength division multiplexing (DWDM) systems.					X
Passive optical network (PON) power	Determines the power level of various signal types,			X		

meter	including continuous (e.g., TV signal at 1550 nm) and framed (e.g., ATM or Ethernet at 1490 nm or 1310 nm) within a passive optical network. Various baud rates are covered, ranging from 155 Mbit/s to 2.5 Gbit/s, for both synchronous and non-synchronous signals.					
Polarization-dependent loss meter	Measures the difference in loss of power for the different states of polarization.				X	
Polarization mode dispersion analyzer	Measures the dispersion of light that is caused by polarization. Generally used to determine the speed-distance limitation of fiber and cables.	X				
SONET/ SDH analyzer	Provides accurate bit-error rate and performance analysis of SONET/SDH overhead format that reflects the quality of a transmission system.	X	X		X	
Stable light source	Emitting diode or lasers used in connection with a power meter to measure signal loss.	X		X	X	X
Synchronization analyzer	Portable, stand-alone tester for network synchronization analysis and wander measurement in wireless and wireline transport networks.					X
Talk set	A device that attaches to an optical fiber and serves as a temporary voice link facilitating coordination of work among installation crews.	X		X		
Telephone wire analyzer	Used by telecommunications service providers that have networks that are comprised mostly or partially of			X		

	twisted-pair local loops to ensure that those loops are of sufficient quality to carry higher-frequency signals required for DSL.					
Variable optical attenuator	Used in network simulation setups to provide calibrated variable reduction of the strength of an optical signal.			X	X	X
Visual fault locator	A visible laser that can be connected to an optical fiber network to help locate breaks or points of excessive loss.	X	X	X		
Widely tunable laser	Can produce laser light across a broad range of wavelengths. Used to test DWDM components and value-added optical modules.				X	X

Table of Contents

Products for Network Service Providers

Test Equipment

We offer an extensive range of field-portable test, measurement and monitoring solutions that are mainly used by network service providers that can also be utilized by network equipment manufacturers. These products are available as handheld test instruments, portable platforms with related modules, and as rack-mount chassis with related modules. Our handheld instruments are durable, compact and easy to use. Our AXS-200 SharpTESTER platform, which is designed for entry-level field technicians in access networks, can easily be configured for copper/DSL/triple-play, Ethernet or optical testing applications. We released Ethernet/IP and ADSL2+ triple-play test modules for the AXS-200 SharpTESTER in fiscal 2008, while several others modules and applications will be introduced in upcoming months. Our FTB-200 Compact Platform, designed for the “super field technician”, holds up to two interchangeable modules that are fully compatible with the highly entrenched FTB-400 platform. Test technologies well-suited for the FTB-200 Compact Platform include a wide range of singlemode and multimode optical time-domain reflectometers (OTDRs), automated optical loss test sets (OLTSs), SONET/SDH analyzers from DS0 up to OC-192, as well as Gigabit Ethernet (GigE) and 10 Gigabit Ethernet testers. Our second-generation field-testing platform, the FTB-400 UTS, is available in four configurations: the two-slot model is ideal for OTDR, OLTS and Gigabit Ethernet applications; the four-slot model offers a high-speed bus, ideal for extensive datacom testing and dedicated OTDR, optical loss and Ethernet (up to 10 Gigabit) testing; the seven-slot model is used for dispersion characterization (PMD and CD), DWDM testing (OSA and MWM) and protocol (SONET/SDH/datacom) testing. Finally, the eight-slot model is a high-performance, multiple-protocol configuration that allows users to combine next-generation SONET/SDH functions with Ethernet, Fibre Channel and optical-layer testing capabilities. Our portable platforms are PC-centric, Windows-based, highly flexible and fully scalable. Their large robust touchscreens are very practical for field use.

Service Assurance Systems

We also offer a family of service assurance and performance monitoring solutions, collectively known as the Brix System, to network service provider labs and large enterprises. The following describes the software and hardware elements of the Brix System:

Centralized Management and Correlation -- BrixWorx

BrixWorx represents the core of the Brix System. BrixWorx provides network- and service-wide control, visibility, and analysis for the fully integrated Brix System. Using the BrixWorx Operations Center user interface, administrators remotely control each component of the system and can easily configure and modify all aspects of the geographically distributed network of Verifiers and third-party measurement sources, including: choosing the desired performance tests and configuring their parameters, threshold values, and schedules.

The BrixWorx unified correlation engine quickly turns data into actionable information through a visualization layer for service-level agreement (SLA) conformance, root-cause analysis, troubleshooting, usage patterns, and trending.

The highly scalable BrixWorx architecture easily accommodates hundreds of thousands of Brix Verifier test points and third-party measurement sources.

Visualisation and Business Intelligence -- BrixView

Seamlessly integrated with the BrixWorx correlation engine, BrixView enables the flexible presentation of performance and quality information to all decision makers. With interactive dashboard views, customizable reporting

packages, and individual content portals, BrixView delivers fast, simple access to information when it is needed and in the format it is needed for all levels of users across an organization.

BrixView produces visualization and reports of varying levels to allow a broad audience to take the appropriate actions. With the appropriate information, network operators spend less time working with static charts and spreadsheets, and business owners and executives have the information and insights they need to make intelligent decisions and drive business value for the organization.

Table of Contents

Testing Across the Entire Network -- Brix Verifiers

Installed at customer premise locations, the Brix Verifiers' various interfaces include Ethernet, ATM, and Euro/ISDN PRI. Similarly, Verifier test capacity scales from the modest requirements of an enterprise branch office running hundreds of tests to a network core running hundreds of thousands of tests.

In addition to Brix Verifiers, the Brix System also supports selected third-party measurement sources. Brix Verifiers are designed for long-term 24x7 deployments in the lights-out, production networks of service providers and enterprises. Once a Brix Verifier is deployed, administrators do not need to locally access it again.

End-to-End IP Service Assurance: BrixNGN

The network core is the heart of the service delivery network, and where successful providers' service assurance strategies start. To effectively guarantee end-to-end SLAs and meet customers' requirements, providers must implement a service assurance solution that provides visibility from the provider edge and to end-users, while allowing segmented views of service quality for problem isolation. By continually monitoring the performance and quality of real-time IP services, and not just the physical network devices, BrixNGN provides the most effective service assurance solution.

With BrixNGN, providers can continuously collect, correlate, analyze, and visualize critical quality of service (QoS) and quality of experience (QoE) data from the network core to the customer endpoint for capacity planning, verifying service turn-ups, and identifying, diagnosing, and quickly resolving network and service performance issues before customers are impacted—thereby guaranteeing quality.

The BrixNGN software module performs proactive monitoring of the network core, extended Ethernet and IP networks between partners and customers, and data services, including E-mail, web-based applications, file transfers, and more. BrixNGN enables early detection and quick resolution of service affecting issues.

Performance Monitoring for IP Video: BrixVision

The BrixVision product line is a family of IPTV service assurance products that measure the end-to-end quality of IP-based video services and validate performance of broadcast and on-demand channel quality. The BrixVision product line provides full service lifecycle performance monitoring for IP Video services such as broadcast TV, video on demand, gaming, and videoconferencing. BrixVision provides visibility into service performance using a combination of proactive testing and user transaction generation, passive monitoring, and the collection of performance metrics from service delivery or home network devices.

Voice over IP Testing and Monitoring: BrixCall

BrixCall provides comprehensive visibility into the performance of live VoIP traffic to ensure call quality from the network core to customer care. Deployed in conjunction with the Brix family of Verifiers, BrixCall is an integrated component of EXFO Service Assurance's live call monitoring solution and employs Brix Verifiers to monitor call signaling and media traffic throughout the network with the advanced BrixCall stream correlation and analysis engine. The solution delivers a single detailed Call Quality Report for each call monitored as well as visibility across all monitored calls.

In addition, the BrixCall dashboard presents critical information about the current state of the service, including all performance threshold violations, call disposition, average Mean Opinion Score (MOS), peak call volume and bandwidth utilization, answer seizure and network efficiency ratios, and call duration information.

BrixCall features the unique Brix Tri-Q Analysis, and graphically displays the impact of each of the elements that contribute to a user’s satisfaction with a call — signaling quality, delivery quality, and call quality.

Table of Contents

The following table summarizes the principal service assurance solutions we provide as well as their typical applications:

Service Assurance Solutions

Product Type	Product	Typical Application
Software Products	BrixWorx	Central site operations center
	BrixCall	Advanced analysis and correlation of VoIP calls
	BrixVision	Advanced analysis and correlation of live video sessions
	BrixNGN	Network core and MPLS analysis, correlation and reporting
Brix Verifier	Brix 100M Verifier	Customer premise end point monitoring
	Brix 1000 Verifier	Network edge and lower capacity monitoring
	Brix 2500 Verifier	Network core, at a higher capacity
	Brix 3500T Verifier	PSTN monitoring
	Brix 4100 Verifier family	In-network live voice or video monitoring

Products for Network Equipment/Component Manufacturers

Test Equipment

Our network equipment/component vendor solutions, mainly built around our IQS-600 ITS, are available as test modules or stand-alone benchtop instruments. The next-generation IQS-600 platform can efficiently run as many as 100 optical test modules using a single controller unit. The IQS-600 platform is equipped with the software and hardware technology to support single-button operation for automated testing. Its system-based approach – one box, several test modules – combined with an open architecture (PXI, Windows, LabVIEW™, etc.) and ease of programming, produces a highly flexible test environment.

The IQS-600 also provides backward compatibility with recent IQ-generation test modules, while delivering all the power and advantages of a next-generation platform. EXFO's wide selection of high-performance test modules includes high-speed power meters, light sources, WDM laser sources, tunable laser sources, variable attenuators, multi-wavelength meters, polarization-dependent loss (PDL) and optical return loss (ORL) meters, polarization controllers and optical switches.

As demonstrated by the release of our IQS-12001B Cable Assembly and Component Test System in fiscal 2007, our system/component vendor solutions also address testing issues that cannot be handled by standard test modules or stand-alone benchtop instruments. We have developed a number of integrated test systems and offer them as off-the-shelf solutions to suit a wide range of customer needs. In addition, we have created a software development kit for developers who prefer writing their own programs for our instruments. Following is a list of integrated test systems that we provide for characterizing optical components, subsystems and networks:

· CWDM/FTTH passive optical component test system	Used to automatically characterize all critical specifications, including spectral insertion loss, polarization-dependent loss and optical return loss of a CWDM passive component or a FTTH splitter with a high degree of accuracy, ease of use and speed.
· Cable assembly and component test system	Used to perform insertion loss and mandrel-free reflection measurements with the highest degree of

	accuracy and repeatability on short fiber assemblies (including multifiber patchcords, hybrids and fan-out patchcords) and components like PLC splitters and fiber arrays.
· DWDM passive component test system	Used to automatically characterize all critical specifications, including spectral insertion loss, polarization-dependent loss and optical return loss of a DWDM passive component with a high degree of accuracy, ease of use and speed.

Table of Contents

IMS/VoIP Test Systems

InterWatch Product Line

In addition, we offer a line of hardware modules and SolarisTM software-based telecommunications test products operating on a common hardware platform range. This product line consists of the InterWatch R14 system, originally introduced in 2005 and since extensively upgraded, and the M7 system, introduced in 2004. Our products simulate both network subscribers and network elements used in emerging IMS and NGN networks.

We maintain an extensive library of software modules that provide test support for a large number of industry standard protocols and variants thereon. Our emphasis is on testing complex, high-level and emerging protocols, including:

- IP Multimedia Subsystem (IMS);
- IP Telephony (Voice over IP or VoIP);
- Asynchronous Transfer Mode (ATM);
- Packetcable;
- ISUP.

Our extensive technical know-how and proprietary software development tools enable us to implement test support for new protocols and protocol variants rapidly in response to customer needs. With their extensive libraries of software protocol test modules, large selection of proprietary hardware physical interfaces and versatile range of hardware platforms, our products are easily configured to support a wide variety of digital testing functions, thereby reducing a customer's need for multiple test systems. In addition, the systems' multi-protocol, multi-user capabilities allow multiple complex testing operations to be performed simultaneously, helping our customers to accelerate their product development cycles.

Our InterWatch test systems consist of advanced proprietary software together with our proprietary hardware interface and co-processor cards. When acquiring a system, customers typically license one or more software modules and purchase hardware and ongoing software support. Customers may upgrade their systems by purchasing additional software protocol test modules and additional hardware interfaces to meet future testing needs. Prices for our systems vary widely depending upon the overall system configuration parameters, including the number and type of software protocol modules and the number of physical interfaces required by the customer.

Applications

The principal applications of our InterWatch test systems are:

Feature Verification. Our systems are used to perform feature verification by simulating one or more network devices and testing a wide variety of possible scenarios to establish if the device under test can handle all features specified by the protocol. Users are able to initiate multiple simultaneous calls across one or many links, create correct call scenarios, send messages out of sequence to verify error response mechanisms and verify a voice or data path.

Interoperability Testing. Our systems are used to simulate one or more network devices, emulating their actions and responses. By simulating various network devices, such as digital switches, wireless base stations, network access nodes and network databases, our products assist engineers with the cost-effective development of equipment that will be compatible with other devices in the networks within which they will be deployed. This helps ensure that network equipment will interoperate reliably, thereby reducing costly failures after installation.

Load and Stress Testing. Our systems are used to verify that a device under test can successfully handle its designed traffic capacity and that its performance will degrade gracefully, rather than fail completely, when stressed beyond its specifications. The scalable architectures of the systems significantly improve our ability to address our customers' growing need to generate and maintain high traffic volumes for load testing.

Table of Contents

Monitoring and Analysis. Our systems are used in development laboratories to monitor network links and store network activity information for future analysis, typically without affecting network traffic. By collecting and analyzing traffic, our systems help ensure that the links have been brought into service and that the devices connected by the links are functioning properly.

Products for life sciences and industrial applications

Over the years, we have developed and acquired a number of core technologies that we leverage in selected high-precision assembly and life sciences markets. For example, we offer several light-based curing solutions for optical component manufacturing applications and have adapted our approach for other industries, such as semiconductor, microelectronic, and medical device manufacturing, in order to maximize revenues. Our Omnicure® systems deliver precise doses of the appropriate spectral light onto photosensitive adhesives to significantly reduce bonding time and increase repeatability. These light-based curing systems, supported by patented optical feedback, thermal control and radiometry technology, produce a high-quality bonding solution. Our technology and application knowledge place us at the forefront of this market.

Another key product line is the X-Cite fluorescence illumination systems for microscope manufacturers. X-Cite systems deliver excellent image quality and at least 2000 hours of lamp life, which is over 60% longer than previous models and up to 10 times longer than conventional illumination systems.

X-Cite systems are self-contained illumination units separate from a microscope. A simple light guide attachment through custom-coupling optics ensures a uniformly illuminated field of view with no heat from the lamp being transferred to the microscope. Models range from the basic X-Cite 120XL for routine imaging applications to the full-featured X-Cite Exacte, designed to provide maximum illumination stability and control for the most advanced live cell research.

The following table summarizes the principal types of high-precision assembly and life science solutions we provide as well as their typical applications:

Light Sources and Accessories

Product Type	Product	Typical Application
UV Light Sources	Omnicure® S1000 Omnicure® S2000	Used to initiate photo chemical reactions in polymer-based materials for a variety of end use applications. Examples include adhesive curing for manufacturing of high value-added items such as medical devices, micro-electronic and opto-electronic components, displays, and data storage devices.
Fluorescent Light Sources	X-Cite® 120XL X-Cite® 120 PC X-Cite® exacte	Fluorescence light source that attaches directly to most microscopes currently sold by major microscopes manufacturers.
Optical Accessories		Optional custom delivery optics used with EXFO UV light sources to tailor the properties of light beams to end-user applications.
High Power Fiber Light Guide		Provides an equal distribution of light energy to multiple cure sites with 50% more throughput than standard fiber guides.

30

Table of Contents

Optical Instruments

Product Type	Product	Typical Application
Radiometer	R5000 R2000 X-Cite® Radiometer	Handheld, broadband optical radiometers used in conjunction with EXFO UV light sources to ensure process quality control at the end-user location.
Cure-Site Radiometer		Attachments for the R2000 and R5000 radiometers that enable optical measurements under customer specific configurations. Examples include the cure-ring radiometer, which measures the output power of light from an EXFO cure ring; ideal for applications that requires a uniform 360° exposure.

Precision Positioning Instruments

Product Type	Product Line	Typical Application
Micromanipulators	PCS-6000 Micromanipulators PCS-5000 Micromanipulators	Electrophysiology research such as patch clamp recording experiments on cells from the brain and central nervous system.
Microscope Platforms	Gibraltar Platform/Stage	Stable mechanical platforms that facilitate cellular research with micropositioning and microinjection systems.
Microinjection Systems	MIS-5000 Microinjection manipulator	Microinjection and nuclear transfer for genetics and reproductive sciences research.

Research and Development

We believe that our future success largely depends on our ability to maintain and enhance our core technologies and product functionality. To keep developing new products and enhancements, it is important that we retain and recruit highly skilled personnel. Our Telecom Division's research and development department is headed by a Vice-President of Research and Development, while our Life Sciences and Industrial Division has a Director of Research and Development.

In fiscal 2008, we accelerated our software development capabilities at our R&D center in India at a lower cost. We had initially acquired a small outsourcing company based in Pune, India.

As of November 3, 2008, our research and development departments included 359 full-time engineers, scientists and technicians, of who 62 hold post-graduate degrees. Gross research and development expenditures in fiscal 2008 reached $32.5 million, compared to $25.2 million in 2007 and $19.5 million in 2006. We launched 27 new products in fiscal 2008 compared to 20 in 2007 and 18 in 2006. Approximately 35% of sales in fiscal 2008 originated from products that have been on the market two years or less compared to 34% in 2007 and 37% in 2006.

Through market-oriented product portfolio review processes at our telecom sites in Quebec City, Canada, Montreal, Canada, Concord, Canada, Chelmsford, USA, and Pune, India, we ensure that our investments in research and development are aligned with our market opportunities and customers' needs. This process enables us to maximize our returns on R&D investments by focusing our resources on prioritized projects. Quarterly product portfolio review meetings enable us to select a realistic, balanced mix of new products and allocate the necessary resources for their development. All our projects, including those already underway, are reviewed, given a priority rating and allocated budgets and resources. Our existing projects can be stopped or substantially redefined if there have been significant changes in market conditions, or if the project development schedule or budget have significantly changed.

31

Table of Contents

To manage our research projects once they are underway, we use a structured management process known as the stage-gate approach. The stage-gate approach is based on a systematic review of a project's progress at various stages of its life cycle. The following are the key review stages of the stage-gate approach:

- market study and research feasibility;
- product definition;
- development feasibility;
- development;
- qualification; and
- transfer to production.

At each stage, we review our project risks, costs and estimated completion time. We compare our design to anticipated market needs and ensure that our new product development is synchronized with other internal departments and external industry events. Adherence to these inter-related portfolio review and stage-gate processes enabled us to be named winners of the Outstanding Corporate Innovator Award in 2000 by the U.S.-based Product Development and Management Association.

We also maintain research and development programs for our life sciences and industrial activities in Toronto, Canada. The product development process is managed using a similar stage-gate process, and projects are reviewed and approved through a quarterly portfolio review. The future success of our life sciences and industrial operations largely depends on our ability to maintain and enhance our core technology in light-based curing, fluorescence illumination systems and piezoelectric positioning.

Strong R&D capabilities at our Life Sciences and Industrial Division site in Toronto, Canada have made it possible to bring a number of successful new products to market quickly and retain customer intimacy. In the process, it has enhanced our ability to customize products for special applications and to develop original equipment manufacturing (OEM) products under partnerships and exclusive contracts. Outside consultants are often used for added support in areas like software development, mechanical design and rapid prototyping.

Customers

Our global and diversified telecom customer base relies on our test, measurement and service assurance solutions to enable optical networks to perform impeccably during their complete life cycles: research, development, manufacturing, installation, maintenance and monitoring. We also have selected customers in high-precision assembly and life science sectors that require our solutions to render them more efficient in their respective fields. Our telecom customers include network service providers, cable television companies, public utilities, private network operators, third-party installers, equipment rental companies, large enterprises, network equipment manufacturers, component vendors and laboratory researchers. Our life science and industrial customers consist of major manufacturers of medical devices, microelectronics, optical displays, electronic storage systems, photonic components and microscopes, as well as universities, medical schools, governments, and private and industrial research laboratories. In fiscal 2008, our top customer accounted for 7.4% of our sales and our top three customers represented 13.1% of our sales. In comparison, in 2007 our top customer accounted for 14.7% of sales and our top three customers represented 19.6%, while in 2006, our top customer accounted for 13.8% of sales and our top three customers represented 19.4%.

With regard to geographic distribution, sales to customers in the Americas (US, Canada and Central & South America) represented 56% of our sales in fiscal 2008, while sales to customers in EMEA (Europe, Middle East and Africa) and Asia-Pacific accounted for 28% and 16% of sales, respectively. In comparison, the Americas, EMEA and Asia-Pacific accounted for 59%, 27% and 14% of sales, respectively, in 2007, and 60%, 25% and 15%, respectively, in 2006.

32

Table of Contents

Sales

We sell our telecom test, measurement and service assurance solutions through direct and indirect sales channels in the Americas (US, Canada, Central & South America) and around the world.

In the Americas, we use a hybrid model, combining key account management with direct and indirect sales coverage. We typically use key account managers to serve large customers that generate high sales volumes or might potentially represent high sales volumes in the future. These key account managers are supplemented by regional sales managers, sales engineers, sales representatives and distributors in US as well as Central and South American metropolitan areas, and regional sales managers in Canada.

We opt for a direct sales approach when selling higher-end, highly technical products to sophisticated buyers. Sales of low- to medium-level complexity products to less stringent technical buyers are usually done through a manufacturer representative organization supported by regional sales managers. Our main sales offices and service centers in the Americas are located in Plano, Texas, Quebec City, Canada, and Concord, Canada. They are supplemented by a regional presence in cities across the US, Central and South America, as well as Canada.

On the international front, we have sales personnel covering strategic areas such as EMEA (Europe, Middle-East and Africa) and APAC (Asia-Pacific region). Our sales network in EMEA is supported by a main office and service center in Southampton, UK, which maintains our head of European sales operations and also provides repair and calibration services for our EMEA customers. We also have additional sales offices in multiple countries across EMEA to serve and support our various customers and distributors.

As for APAC, our main sales offices for South East Asia is located in Singapore, while our main sales representative offices for mainland China are located in Shenzhen and Beijing, which also acts as a service center to better serve our customer base in that geographic area. In addition, we have other sales offices in strategic locations around the world to support our network of distributors and various customers.

We rely on a network of more than 90 distributors worldwide to work with us in supporting mostly our international sales and to participate in a large number of our international events. We believe that the local presence and cultural attributes of our distributors allow us to better serve our global markets.

Our direct telecom sales team consists of a Vice-President of Sales for the Americas and a Vice-President of International Sales. They are supported by nine regional sales directors that are leading a widely distributed team of more than 112 people acting as key account managers, regional sales managers, sales engineers and application engineers. Our sales people are located throughout major metropolitan areas around the world. This group of sales professionals has on average more than 14 years of experience in the fields of telecommunications, fiber optics, or test and measurement. We also have an in-house Customer Service Group to meet the needs of existing and new customers. This group is responsible for providing quotations to customers, supporting our sales force, managing demonstration units, order management, technical support and training as well as calibration and repair services.

Following the acquisitions of Navtel Communications and Brix Networks (renamed EXFO Service Assurance Inc.) in the third quarter of fiscal 2008, sales responsibilities within our Telecom Division were modified. Navtel Communications' sales team was fully integrated within the Telecom Division, while EXFO Service Assurance's sales force remained stand-alone as its systems are more complex than traditional test equipment and require longer sales cycles. EXFO Service Assurance, with its main sales office located in Chelmsford, MA, USA, consists of regionally based account executives and sales engineers that target carriers, service providers and cable MSOs. Regional sales offices are located in Southampton, England, Singapore and Beijing, China.

EXFO Service Assurance sells its solutions mainly through direct channels in the Americas (US, Canada, Central and South America) and around the world. In the EMEA and Asia/Pac regions, its sales teams work with resellers that have a strong local presence.

Table of Contents

The main office for our Life Sciences and Industrial Division is located in Toronto, Canada. We use mixed sales channels to serve various markets supported by this division, depending on product line and geography. Optical light sources and related accessories used for industrial applications are sold in North America through a network of more than 10 manufacturer representatives and, internationally, through a network of more than 20 distributors. The X-Cite 120 and Exacte Fluorescence Illumination Systems are sold through value-added reseller agreements with major microscope companies and system integrators in North America and Europe. Positioning products are sold directly to customers in North America, which includes the United States and Canada, and internationally through a network of technical distributors. To gain additional access to the positioning life science research market in the United States and Canada, distributor agreements are in place with major microscope manufacturers, which include Leica, Nikon, Olympus and Zeiss. These companies often combine the sale of their microscopes with our product.

Product Management, Marketing/Communications and Customer Support

Product Management

Our telecom Product Management Group consists of one Vice-President responsible for our Optical, Protocol, Copper Access, and Systems product lines – as well as directors and product managers who have various degrees in engineering, science and business administration. Directors and product managers, under the direction of the Vice-President, are responsible for all aspects of our telecom marketing program including product strategy, new product introductions, definition of new features and functions, pricing, product launches and advertising campaigns. We follow up our marketing initiatives by attending industry trade shows. Furthermore, we have a customer relationship management (CRM) system to compile market and customer information including forecasts, opportunities, leads and competitive data. We use this information to make strategic business decisions. Finally, strategic marketing specialists analyze our markets of interests, compile competitive information and identify macro-trends in our sector.

Following the acquisitions of Navtel Communications and Brix Networks in the third quarter of fiscal 2008, product management responsibilities have remained within their respective groups. Under the direction of a Vice-President/General Manager for each group, directors and product managers are responsible for product strategy, new product introductions, definition of new features and functions, pricing, product launches and advertising campaigns.

Our Life Sciences and Industrial Group consists of a Director – responsible for both life sciences and precision assembly sectors – as well as product managers who have various degrees in engineering, science and business administration. Product managers, under the direction of the Director, are responsible for all aspects of their business line marketing programs including product strategy, new product introductions, definition of new features and functions, pricing, product launches and advertising campaigns.

The Telecom Division product management group and the Life Sciences and Industrial Division product management group include 34 and 4 employees, respectively.

Marketing/Communications

The Telecom Division’s Marketing-Communications team, which consists mainly of project managers, marketing writers, translators and graphic artists, supports our Product Management Group by producing marketing and corporate documentation. Literature includes specification sheets, application notes, product catalogues, advertising copy and an electronic corporate newsletter. This Marketing-Communications team is also responsible for all sales tools required by our worldwide sales force and for updating the marketing contents of our Website. This team falls under the responsibility of the Vice-President, Telecom Product Management and Marketing.

34

Table of Contents

The Life Sciences & Industrial Division's Marketing-Communications team shares a variety of marketing initiatives. This group is assisted by product managers, who provide the technical data and collaborative support required to produce product specification sheets, catalogues, application notes and multimedia marketing tools. This Marketing-Communications team is responsible for all advertising material, Website updates, events planning (including trade shows) and direct promotional marketing such as mass mailings and telemarketing. This team also provides the sales tools required by the Life Sciences and Industrial Division's worldwide sales channels, including maintaining our elite partner program. This team falls under the responsibility of the Director of Marketing for the Life Sciences and Industrial Division.

Customer Support

Customer support is deemed a corporate mandate at EXFO. As such, our Customer Support Group handles requests from customers worldwide. We aim to anticipate our customers' needs, offering Inside Sales, Technical Support and After-Sales Service. EXFO Customer Service Department offers customer support in French, English, Chinese, German, Spanish, Portuguese, Italian, Russian and Japanese.

Our employees in the Inside Sales Team are mainly responsible for guiding customers in purchasing the correct equipment for their respective applications, issuing quotations and promoting our Flexcare extended warranty service and support program. In order to provide customers with one central point of contact, our service representatives work with the customer from purchasing equipment to helping them service the equipment, if necessary.

Within our Technical Support team, we have agents who provide troubleshooting support to our customers as well as trainers and installers who offer on-site servicing for more complex equipment.

To offer superior after-sales service worldwide, we have service centers in North America, Europe and Asia. These support centers provide technical support, order processing, inside sales, calibration and repairs for our customers.

To ensure that we exceed customer satisfaction and continue to improve our service, we measure our performance by sending surveys and logging customer feedbacks.

Manufacturing

Our telecom manufacturing operations consist mainly of material planning, procurement, sub-assembly, final assembly and test, software loading, calibration, quality assurance, shipping, billing and customs management. As of November 3, 2008, we had 310 employees involved in our telecom manufacturing operations. Most of our telecom manufacturing activities, which occupy a total of approximately 115,000 square feet, are spread among four buildings: two in Quebec City, Canada, one in Shenzhen, China, and one in Chelmsford, MA, USA.

These manufacturing operations include the following responsibilities:

- Production. From production planning to product shipment, our production department is responsible for manufacturing high-quality products on time. Factories are organized in work cells; each cell consists of specialized technicians and equipment and has full responsibility over a product family. Technicians are cross-trained and versatile enough, so that they can carry out specific functions in more than one cell. This allows shorter lead times by alleviating bottlenecks.

- Product Engineering and Quality. This department, which supports our production cells, acts like a gatekeeper to ensure the quality of our products and the effectiveness of our manufacturing processes. It is responsible for the transfer of products from research and development to manufacturing, product improvement, documentation,

metrology, and the quality assurance and regulatory compliance process. Quality assurance represents a key element in our manufacturing operations. Quality is assured through product testing at numerous stages in the manufacturing process to ensure that our products meet stringent industry requirements and our customers' performance requirements.

Table of Contents

- Supply-Chain Management. This department is responsible for sales forecasting, raw material procurement, material-cost reduction and vendor performance management. Our products consist of optical, electronic and mechanical parts, which are purchased from suppliers around the world. Approximately one-third of our parts are manufactured to our specifications. Materials represent the biggest portion of our cost of goods. Our performance is tightly linked to vendor performance, requiring greater emphasis on this critical aspect of our business.

Our Life Sciences and Industrial Division's manufacturing operations occupy 8,000 square feet in Toronto, Canada. This group manufactures light sources and related accessories, fluorescence illumination systems and precise positioning equipment for the life sciences and high-precision assembly markets. Operations consist of manufacturing, procurement, warehousing, quality control and document control managed by various elements of the ISO 9001 certified quality system. Recognizing the importance of reduced time-to-market for our solutions, we have focused efforts on designing products with an emphasis on standardization, modularity, as well as ease of fabrication and assembly. Following are key manufacturing responsibilities in Toronto, Canada:

Manufacturing – consists primarily of assembly and test capabilities in which all major manufacturing elements are subcontracted to various key suppliers. These components are integrated into assemblies and tested in order to ensure all operating specifications have been met for each product manufactured. Cross-training of assembly technicians for each product group ensures scalability of manufacturing to meet customer demand. In addition, this group is responsible for capacity and production planning, which are necessary on an on-going basis to ensure that adequate resources are available to meet forecasted and actual demand.

Supply Chain Management – is responsible for the planning of materials required by manufacturing and developing key-supplier relationships to ensure materials have been manufactured to our specifications. This group's main focus is to work with our worldwide supplier base to find effective manufacturing and logistic solutions in order reduce costs and cycle time. Paramount to this process is an effective communication system that provides timely feedback to our suppliers and forms an important element of our supplier evaluation system.

Manufacturing Engineering and Quality Assurance – is responsible for product integrity throughout the manufacturing cycle. From the release of new products, through our new product introduction process, and configuration management to manage engineering change, we ensure consistent manufacturing processes throughout the product life cycle. In conjunction with the above process, quality is maintained by performing quality tests at incoming receiving and final product verification. The responsibility for product quality is shared by all team members throughout the company and does not reside solely with the quality group.

Competition

The telecommunications test, measurement and monitoring industry is highly competitive and subject to rapid change as a result of technological developments and market conditions. We compete with many different companies, depending on product family and geographical market. We believe that the main competitive factors in the industry include the following:

- product performance and reliability;
- price;
- level of technological innovation;
- product lead times;
- breadth of product offerings;
- ease of use;
- brand-name recognition;
- customer service and technical support;

- strength of sales and distribution relationships; and
- financial stability.

Table of Contents

Generally, competitors fall into two categories. The first category consists of global test and measurement vendors, who complement their broad range of products with telecom test, measurement and service assurance equipment. These companies include Agilent Technologies, Inc., Anritsu Corporation, Danaher Corporation (Tektronix), JDS Uniphase Corporation, Spirent plc, and Yokogawa.

The second category refers to niche companies in the telecom test, measurement and service assurance industry. These companies typically have limited product lines and in some cases may be geographically limited in their customer base. Such companies include Digital Lightwave Inc., Empirix, Inc., IneoQuest Technologies, Inc., IXIA, Sunrise Telecom Inc., and VeEX Inc.

Competition for our life sciences and industrial solutions is quite varied, depending upon product line. Competitors that sell light-based curing products include Dymax, Henkle-Loctite in North America and Europe as well as Hamamatsu, Ushio and Matsushita (Panasonic) in Asia. With regard to our X-Cite 120 Fluorescence Illumination System, main competitors consist of microscope manufacturers who have developed lamp housings for low-wattage mercury burners in-house. Finally, our motion control Life Science instruments, which are designed for various life science applications, compete against products from companies such as Sutter Instruments and Narishige.

Regulatory Environment

In most countries where our products are sold, our products must comply with the regulations of one or more governmental entities. These regulations often are complex and vary from country to country. Depending upon the country and the relevant product, the applicable regulations may require product testing, approval, registration, marking and unique design restrictions. Accordingly, we have appointed a team of engineers who are responsible for ensuring that our products comply with all applicable regulations.

In the United States, our products must comply with the regulations of several agencies of the U.S. federal government, including the Federal Communications Commission (FCC), the Food and Drug Administration (FDA) and the Occupational Safety and Health Administration (OSHA). Under the FCC's regulations, our products must comply with certain electro magnetic compatibility (EMC) requirements to insure they do not generate and are immune from electrical noise which could possibly cause undesirable operation, as well as affect other surrounding devices. Depending upon the product, compliance with these rules may necessitate applying for and obtaining an FCC equipment authorization prior to importing into the United States, or marketing, any units of the relevant product. Additionally, some of our products must comply with the FDA's non-medical performance standards and related rules concerning light-emitting products, such as lasers. The FDA's regulations are intended to promote safety by limiting human exposure to harmful non-iodizing radiation. Similarly, our products must comply with safety standards adopted by OSHA. Furthermore, for our Life Science and Industrial Division, certain U.S. states require mandatory product registration and reporting of Mercury-added products being imported. This registration is controlled by the Interstate Mercury Education and Reduction Clearinghouse (IMERC).

Similar regulations apply in other countries. For example, in Canada our products must comply with the applicable standards adopted by the Standards Council of Canada (SCC). These include product safety standards developed by the Canadian Standards association as well as EMC requirements adopted by Industry Canada. Countries in the European Union require product compliance as dictated by an applicable directive, often referred to as CE marking. This includes testing to ensure compliance with harmonized European Norm (EN) standards for both product safety and EMC requirements.

In Europe, with the implementation of the WEEE directives for recycling of electronic products in selected European Countries (2002-96-CE), we have appointed a task force committee consisting of our management and employees, distributors and other partners as the case may be, to ensure full compliance with regulations and oversee the

management, logistics, recycling rate, disposal services and activities related to recycling of electronic equipment and products within the member states.

Additionally, to address the issue of environmental compliance, the European Union has mandated the Restriction of the Use of Certain Hazardous Substances or "RoHS" Directive, which applies to all products included within the scope of WEEE directive with the exception of Categories 8 (Medical devices) and 9 (Monitoring and control instruments). Mandatory product compliance includes the ban of certain substances within specified concentrations, unless formally exempted by the directive. To ensure compliance to this directive, a formal restricted substances control (RSC) program was implemented for our products included within the scope of WEEE. This program ensures the design, procurement and manufacturing of affected products prevents the inclusion of the banned substances as specified by the RoHS directive.

Table of Contents

Other significant types of regulations not described in this annual report also may apply, depending upon the relevant product and country of destination.

Intellectual Property

Our success and ability to compete are dependent in part on our ability to develop and protect our proprietary technology. We file U.S. and international applications to protect technology, inventions and improvements important to the development of our business. We also rely on a combination of copyright, trademark, trade secret rights, licensing and confidentiality agreements.

As of August 31, 2008, we held 41 actively maintained granted patents from the U.S. (including one “design” patent), seven from Canada, four from Germany (including one “Utility Model”), four from the United Kingdom, three from France, and two from China. In addition, we have 20 US patent applications in process, eleven Canadian patent applications in process, three European applications in process, three applications in China, two direct national entry in Germany (not via the European application) and one in Russia, these applications being either direct national or regional submissions or submissions as applications under the Patent Cooperation Treaty. The expiration dates of our issued patents range from October 3, 2008 to January 13, 2026.

We consider eight of our inventions for which patents have either been granted or are pending to be material. These inventions are:

- a method and apparatus for “non-intrusive” live-fiber detection and monitoring. This invention permits a fiber “clip-on” device to be attached to a cabled fiber, essentially guaranteeing that the induced bending loss to a live-traffic link will never exceed 1 dB. This is a key invention for our LFD-250, LFD-300, and TG-300 product;

- the measurement of attenuation of optical fibers using bidirectional transmission of information via the fiber, which forms the basis of our FOT-930 and FTB-3920 products;

- a method and apparatus for characterizing optical power levels in three-wavelength, bidirectional fiber-to-the-home systems. This invention describes how the optical power can be measured at the two-downstream and one upstream wavelengths used to connect a residence or business customer, while maintaining the signal continuity necessary to keep the home-based Optical Network Terminal operating. This invention underlies the two-port version of our PPM-350B PON Power Meter;

- an optical spectrum analyzer using optical fibers as input and output “slits”. This invention forms the basis of our FTB-5240, FTB-5240B and IQ-5250 products;

- a light-curing system with closed-loop control and work-piece recording which is at the heart of the spot-curing systems manufactured by EXFO Photonic Solutions;

- a special optical design used in some of the X-Cite adaptors to prevent structure in the beam from reducing the uniformity of illumination at the microscope objective plane, which is a key patent for our X-Cite fluorescent illumination system;

- a method and apparatus to determine the theoretical and practical data rates for a cable under test. This invention forms the basis of the EXFO CableSHARK product, describing how two test devices, communicating with each other via the cable under test, can predict the performance of a pair of ADSL (Asymmetric Digital Subscriber Line) modems, and in case of problems, analyze the cause of the modems failing to synchronize;

- a method and system for hardware time stamping packetized data to provide sub-microsecond accuracy in test measurements, which is embedded in the Brix100M, Brix1000, and Brix2500 Series Verifiers.

Confidentiality and proprietary information agreements with our senior management, employees and others generally stipulate that all confidential information developed or made known to these individuals by us during the course of their relationship is to be kept confidential and not disclosed to third parties, except in specific circumstances. The agreements also generally provide that all intellectual property developed by the individual in the course of rendering services to us belongs exclusively to us. These efforts afford only limited protection.

Table of Contents

C. Organizational Structure

As of November 3, 2008, the following chart presents our corporate structure, the jurisdiction of incorporation of our subsidiaries and the percentage of shares that we hold in those subsidiaries.

Table of Contents

D. Property, Plant and Equipment

Our head offices and facilities are located in Quebec City, Province of Quebec, Canada where we occupy two buildings. These buildings house our executive and administrative offices, research and development facilities and production facilities. We also have facilities in Montreal, Province of Quebec, Canada (formerly EXFO Protocol), in Concord, Ontario, Canada (formerly Consultronics Limited), in Markham, Ontario, Canada (formerly Navtel Communications Inc.), in Mississauga, Ontario, Canada (EXFO Photonic), in Chelmsford, Massachusetts, United States (EXFO Service Assurance Inc.), in Eastleigh, Hampshire, United Kingdom (EXFO Europe), in Shenzhen, China (EXFO Telecom Equipment (Shenzhen) Co. Ltd.) and in Pune, India (EXFO India). EXFO Burleigh's facilities located in Victor, New York, were sold on August 31, 2006.

In addition, we maintain sales offices and/or have regional sales managers located in China, Czech Republic, France, Germany, Great Britain, Mexico, Singapore, Spain, United Arab Emirates and the United States.

In September 2002, we obtained ownership of one of the buildings housing production facilities in Quebec City that was previously leased from a company controlled by EXFO's president and chief executive officer. In September 2003, due to down-sizing efforts, we were able to move all of our Quebec City activities into two buildings, rather that three. Though we no longer occupy the facilities at 465 Godin Avenue in Quebec City, we remain bounded by the lease until November 30, 2006. However, on September 1, 2004, we were released from our obligations under the lease with a final payment of $194,000 (CA$250,000).

The following table sets forth information with respect to the main facilities that we occupy as of November 3, 2008.

Location	Use of Space	Square Footage	Type of Interest
436 Nolin Street Quebec (Quebec) G1M 1E7	Partially occupied for manufacturing of telecom products	44,164 (1)	Owned
400 Godin Avenue Quebec (Quebec) G1M 2K2	Fully occupied for research and development, manufacturing, management and administration	128,800 (2)	Owned
2260 Argentia Road Mississauga (Ontario) L5N 6H7	Partially occupied for research and development, manufacturing of life science and industrial products, management and administration	25,328 (3)	Leased
2650 Marie-Curie St-Laurent (Quebec) H4S 2C3	Fully occupied for research and development, management and administration	26,000	Leased
160 Drumlin Circle Concord (Ontario) L4K 3E5	Partially occupied for research and development, product management and administration	23,500 (4)	Owned
55 Renfrew Drive, Suite 100 Markham (Ontario) L3R 8H3	Unoccupied, lease expired on April 30, 2009	26,690	Leased

285 Mill Road Chelmsford, MA 01824 United States	Partially occupied for research and development, manufacturing, management and administration	23,052 (5)	Leased

Table of Contents

Location	Use of Space	Square Footage	Type of Interest
Omega Enterprise Park Electron Way, Chandlers Ford, Eastleigh, Hampshire S053 4SE United Kingdom	Fully occupied for European customer service, sales management and administration	10,000	Leased
Hua Chuang Da Industrial Park Bldg D, 2/F, Hangcheng Blvd, Gushu, Xixiang Shenzhen 518126 China	Partially occupied for manufacturing of telecom products	40,000 (6)	Leased
113/1, Lane 4A Koregaon Park Pune 411001 India	Fully occupied for research and development	5,986	Leased
Office No 701, Building 1 The Cerebrum IT Park Wadgaon Sheri, Pune 411014 India	Fully occupied for research and development	16,840	Leased

(1) Approximately 5% of these premises are not occupied.
(2) Including the warehouse space. Premises without the warehouse are approximately 115,000 square feet.
(3) 9,792 square feet have been subleased to a third party. The total square footage leased is 36,000.
(4) Approximately 1/3 of these premises are not occupied.
(5) 7,950 square feet have been subleased to a third party. The total square footage leased is 31,002.
(6) Approximately 35% of these premises are occupied.

Item 4A. Unresolved Staff Comments

Not applicable.

Table of Contents

Item 5. Operating and Financial Review and Prospects

This discussion and analysis contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition. Words such as may, will, expect, believe, anticipate, intend, could, estimate, continue, or the negative or comparable terminology are intended to identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events and circumstances are considered forward-looking statements. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including consolidation in the global telecommunications test, measurement and monitoring industry; capital spending levels in the telecommunications, life sciences and high-precision assembly sectors; concentration of sales; fluctuating exchange rates and our ability to execute in these uncertain conditions; the effects of the additional actions we have taken in response to such economic uncertainty (including our ability to quickly adapt cost structures with anticipated levels of business, ability to manage inventory levels with market demand); market acceptance of our new products and other upcoming products; limited visibility with regards to customer orders and the timing of such orders; our ability to successfully integrate our acquired and to-be-acquired businesses; our ability to successfully expand international operations; the retention of key technical and management personnel; and future economic, competitive, financial and market conditions, including any slow-down or recession in the global economy. Assumptions relating to the foregoing involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. Other risk factors that may affect our future performance and operations are detailed in our Annual Report, on Form 20-F, and our other filings with the U.S. Securities and Exchange Commission and the Canadian securities commissions. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure you that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document.

The following discussion and analysis of the consolidated financial condition and results of operations of EXFO Electro-Optical Engineering Inc. for the fiscal years ended August 31, 2006, 2007 and 2008, should be read in conjunction with our consolidated financial statements and the related notes included elsewhere in this Annual Report. Our consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada, or Canadian GAAP. Significant differences in measurement and disclosure from generally accepted accounting principles in the United States, or U.S. GAAP, are set out in note 19 to our consolidated financial statements. Our measurement currency is the Canadian dollar although we report our financial statements in US dollars.

The following discussion and analysis of financial condition and results of operations is dated November 3, 2008, except as indicated herein.

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

INDUSTRY OVERVIEW

The basic fundamentals of the global telecom industry remain solid for the moment. However, it is still unknown what impacts the current financial crisis might have on the global economy particularly in the United States, where a severe economic slowdown could potentially reduce investments and affect other parts of the world. The main fundamental telecom drivers are based upon exponential growth in bandwidth demand, as well as on the intense competition

between telecom operators (telcos) and cable companies (cablecos), who are pushing massive investments in Internet protocol (IP) converged next-generation networks to capitalize on significant operational efficiencies and service revenues.

Table of Contents

Global Internet bandwidth demand is growing very rapidly, due to a wide range of applications like video, webgaming, etc. TeleGeography Research has estimated its compound annual growth rate (CAGR) at 54% from 2004 to 2008. This trend is likely to remain steady in the years to come, with the upcoming deployments of Internet protocol television (IPTV), high-definition Internet protocol television (HD-IPTV) and increased online video streaming, since these applications, among others, will consume a colossal amount of additional bandwidth. As a result, telcos and cablecos are investing substantially in their access networks in order to provide differentiated, revenue-generating services to attract and retain consumers, who are increasingly relying on broadband network services for their work, entertainment and everyday activities. From a telco perspective, it is now clear that fiber-to-the-home (FTTH) will become the access network architecture of choice, which will allow them to meet heightened bandwidth requirements and future-proof their access networks, as residential bandwidth requirements are growing from the 1 to 5 Mbit/s (megabits per second) of the past to the 30 to 100 Mbit/s required in the long-term to assure multiple HD-IPTV channels, online gaming, high-speed content-rich Internet, VoIP (voice-over-Internet protocol) telephony and a myriad of other IP-based applications. Hybrid architectures, combining copper and fiber (fiber-to-the-curb, or FTTC, and fiber-to-the-node, or FTTN), will also keep expanding in the short term, since they are less-expensive methods to increase bandwidth and can be mass-deployed faster.

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

As bandwidth growth in access networks continues to increase, it has begun placing a strain on metro rings and core networks. It is also driving the need for higher-speed technologies; for example, 43 Gbit/s (gigabits per second) SONET/SDH is now seeing early deployments and becoming mainstream, while the upcoming 100 Gbit/s Ethernet is in early field trials. The deployment of these solutions is expected to be significantly more economical, especially if trenches need to be dug in order to deploy new fiber in metro or long-distance routes.

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

These market dynamics positively affected telecom test and monitoring suppliers in fiscal 2008; however, deteriorating macro-economic conditions in the United States could instigate a slowdown in capital spending among customers, which would necessarily reduce demand for our test and monitoring solutions.

COMPANY OVERVIEW

EXFO is a leading provider of test and monitoring solutions for network service providers and equipment manufacturers in the global telecommunications industry. The Telecom Division, which represents more than 85% of our business, offers a wide range of innovative solutions extending across the full technology lifecycle from design to technology deployment and onto service assurance and covering all the layers of a network infrastructure to enable triple-play services and next-generation, converged IP networking. The Life Sciences and Industrial Division offers solutions in medical-device and opto-electronics assembly, fluorescence microscopy and other life sciences sectors.

Table of Contents

We were founded in 1985 in Quebec City, Canada. Our original products were focused on the needs of installers and operators of fiber-optic networks. Customers use these field-portable testing products for the installation, maintenance, monitoring and troubleshooting of optical networks. In 1996, we supplemented our product portfolio with an extensive line of high-end products that are mainly dedicated to research and development as well as manufacturing activities of optical component manufacturers and system vendors.

Over the past several years, we have enhanced our competitive position through acquisitions of protocol, copper/xDSL and service assurance test businesses.

In April 2008, we acquired all issued and outstanding shares of Brix Networks Inc. (renamed EXFO Service Assurance Inc.), for a cash consideration of $29.7 million, plus a contingent cash consideration of up to a maximum of $7.5 million, based on booking levels exceeding $16 million up to $40 million in the 12 months following the closing of the deal. Brix Networks, a privately held company located in the Boston (MA) area, offers VoIP and IPTV service assurance solutions across the three areas most affecting the success of a real-time service: signaling quality (signaling path performance), delivery quality (media transport performance) and content quality (overall quality of experience). Brix Networks' service assurance solutions are mainly designed for network service providers (NSPs) and large enterprises.

In March 2008, we acquired all issued and outstanding shares of Navtel Communications Inc., for a cash consideration of $11.3 million. Navtel Communications, a privately held company in Toronto, Canada, is a leading provider of Internet protocol multimedia subsystem (IMS) and VoIP test solutions for network equipment manufacturers (NEMs) and NSP labs. Navtel Communications specializes in testing next-generation IP networks that are increasingly combining wireline and wireless technologies. Subsequent to the acquisition, Navtel Communications was merged into the parent company.

In fiscal 2008, we opened our own telecom manufacturing facilities in Shenzhen, China. We now have two main manufacturing sites for our Telecom Division and one plant for our Life Sciences Division. Over time, low-volume, high-complexity telecom products will be manufactured in Quebec City, whereas high-volume, low-complexity telecom products will be manufactured in Shenzhen.

In fiscal 2008, we accelerated the deployment of a software development center in Pune, India, to supplement the research and development capabilities of our labs in Boston, Toronto, Montreal and Quebec City. This will enable us to benefit from the wealth of IP expertise in India, to accelerate product development especially for our software-intensive protocol test solutions to take advantage of a lower cost structure.

In January 2006, we acquired substantially all the assets of Consultronics Limited, (now merged with the parent company) a leading supplier of test equipment for copper-based broadband access networks, for a total cash consideration of $19.1 million. Above and beyond copper/xDSL test solutions, Consultronics had a rich product portfolio for testing next-generation technologies, such as IPTV and VoIP, which are critical for NSPs in their deployment of triple-play services (voice, data, video) over optical and copper links in access networks. This acquisition was a strategic initiative to position EXFO as a genuine one-stop shop for broadband access and triple-play testing, since it complemented our market leadership in the optical FTTx test market.

In November 2001, we acquired Avantas Networks Corporation (renamed EXFO Protocol Inc. and now merged with the parent company), a supplier of protocol-testing and optical-network performance management equipment for NSPs. This transaction enabled us to combine optical and protocol test modules inside a single field-portable test platform in order to help our customers increase revenues and reduce operating costs. In October 2002, our wholly-owned subsidiary, EXFO Gnubi, purchased substantially all the assets of gnubi communications, L.P., a supplier of multichannel telecom and datacom testing solutions for the system manufacturer market. These strategic

acquisitions which were consolidated in Montreal, Canada, in fiscal 2004 enabled us to more than double our addressable market, as we expanded from optical testing to protocol testing applications, and to offer a more complete line of test solutions to our customers.

Table of Contents

Previously, we had completed two acquisitions to bolster growth in the optical component manufacturing market. We acquired Burleigh Instruments, Inc. (renamed EXFO Burleigh Products Group Inc.) in December 2000 for its wavelength measurement instruments and nanopositioning alignment systems. We also added EFOS Inc. (renamed EXFO Photonic Solutions Inc.) in March 2001 for its precision light-based, adhesive spot-curing technology. We have since exited the optical component manufacturing automation business, and the remaining operations of EXFO Burleigh have mostly been consolidated with those of EXFO Photonic Solutions in Toronto, Canada.

We launched 27 new products in fiscal 2008, including seven in the fourth quarter, compared to 20 in fiscal 2007. Key product introductions in fiscal 2008 included among others a multiservice, multimedium modular handheld platform for characterizing and troubleshooting access networks (AXS-200 SharpTESTER) with related copper access, protocol and optical test modules; a compact multiservice transport test set that combines next-generation SONET/SDH and Ethernet testing inside a single module (FTB-8120NGE/FTB-8130NGE Power Blazer); a 40/43 Gbit/s SONET/SDH field-test solution (FTB-8140 Transport Blazer) for high-speed optical networks; an all-in-one chromatic dispersion (CD) and polarization mode dispersion (PMD) analyzer (FTB-5700 Single-Ended Dispersion Analyzer) that requires only one technician to characterize a link from a single end; a triple-play test set (AXS-200/630 VDSL, ADSL2+ and IP Triple-Play Test Set) for the deployment and troubleshooting of ADSL2+/VDSL2 networks; and the advanced IQS-600 Integrated Qualification System, a next-generation, modular test platform for R&D and manufacturing applications. Following the year-end, we introduced an enhanced version of Navtel's InterWatch platform that simulates up to 256,000 unique IPv6 subscriber addresses per chassis, and new software features on the Transport Blazer test modules for characterizing 40G/43G SONET/SDH networks. Sales from products that have been on the market two years or less accounted for 34.6% for the fiscal year, while our published goal is 30%.

Overall for fiscal 2008, we increased sales 20.2% to $183.8 million from $152.9 million in 2007. Global sales for fiscal 2008 included $5.4 million from newly acquired Brix Networks and Navtel Communications since their acquisitions in the third quarter of 2008. GAAP net earnings reached $18.4 million, or $0.27 per diluted share, including $5.3 million for the recognition of previously unrecognized future income tax assets in the United States, $2.7 million for income tax recovery following the review of our tax strategy related to recently substantively enacted income tax rates in Canada, $1.5 million of income tax expense to account for the recently substantively enacted income tax rate on our future income tax assets in Canada, an extraordinary gain of $3.0 million related to the negative goodwill on the Navtel acquisition, as well as $3.0 million in after-tax amortization of intangible assets and $1.3 million in stock-based compensation costs. In 2007, GAAP net earnings reached $42.3 million, or $0.61 per diluted share, including $24.6 million in recognition of previously unrecognized future income taxes, $3.2 million in recognition of previously unrecognized research and development tax credits, $2.9 million in amortization of intangible assets, $1.1 million from a government grant recovery and $1.0 million in stock-based compensation costs.

In fiscal 2008, we faced a substantial and sudden increase in the value of the Canadian dollar versus the US dollar. The average value of the Canadian dollar increased 11.4% in fiscal 2008, compared to the same period last year. Given that most of our sales are denominated in US dollars but a significant portion of our expenses are denominated in Canadian dollars, our financial results were negatively affected.

On November 5, 2007, the Board of Directors approved a share repurchase program, by way of normal course issuer bid on the open market, up to 9.9% of our public float (as defined by the Toronto Stock Exchange), or 2.9 million of subordinate voting shares, at the prevailing market price. The period of the normal course issuer bid commenced on November 8, 2007, and ended on November 7, 2008. All shares repurchased under the bid were cancelled. We redeemed 1.9 million subordinate voting shares for a total consideration of $8.5 million under that program.

Table of Contents

On November 6, 2008, the Board of Directors approved a renewal of our share repurchase program, by way of a normal course issuer bid on the open market, of up to 10% of our public float (as defined by the Toronto Stock Exchange), or 2.7 million subordinate voting shares, at the prevailing market price. We expect to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The period of the normal course issuer bid starts on November 10, 2008, and will end on November 9, 2009, or on an earlier date if we repurchase the maximum number of shares permitted under the bid. The program does not require that we repurchase any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled.

On November 10, 2008, the Board of Directors approved a substantial issuer bid (the "Offer") to purchase for cancellation up to 8.8 million subordinate voting shares for an aggregate purchase price not to exceed CA$30 million. The Offer is being made by way of a "modified Dutch Auction" pursuant to which shareholders may tender all or a portion of their shares (i) at a price not less than CA$3.40 per share and not more than CA$3.90 per share, in increments of CA$0.05 per share, or (ii) without specifying a purchase price, in which case their shares will be purchased at the purchase price determined in accordance with the Offer. The Offer will expire on December 16, 2008, unless withdrawn, extended or varied. We expect to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The Offer is not conditional upon any minimum number of shares being tendered, but it is subject to certain other conditions.

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

Sales

We sell our products to a diversified customer base in approximately 95 countries through our direct sales force and channel partners like sales representatives and distributors. Most of our sales are denominated in US dollars and Euros.

In fiscal 2008, no customer accounted for more than 10% of our global sales, with our top customer representing 7.4% of our global sales. In fiscal 2006 and 2007, our top customer accounted for 13.8% and 14.7% of global sales, respectively. The significant sales concentration with this Tier-1 carrier in fiscal 2006 and 2007 was largely due to our leadership position in the FTTx test market and the fact that we benefited from aggressive FTTH rollouts from this customer. This sales concentration significantly decreased in fiscal 2008. However, we do not believe that we have lost market share with this particular customer in fiscal 2008 as the sales level with this customer may fluctuate year-over-year, based on the amount of budget available, the allocation of such budget and the timing and scope of projects. It should also be noted that over the last three years, we significantly increased our business with several other accounts around the globe. Although we maintained our leadership position with this customer, we reduced our customer concentration to a lower level with this customer while increasing our penetration with other accounts.

We believe that we have varied product lines, a diversified customer base, and a market for our products that is spread across geographical areas, which we believe helps protect us against concentration of sales and credit risk.

Cost of Sales

Cost of sales includes raw materials, salaries and related expenses for direct and indirect manufacturing personnel (net of government grants) as well as overhead costs. Excess, obsolete and scrapped materials are also included in cost of sales. However, cost of sales is exclusive of amortization, which is shown separately in the statements of earnings.

Operating Expenses

We classify our operating expenses into three main categories: selling and administrative expenses, research and development expenses and amortization expenses.

Table of Contents

Selling and administrative expenses consist primarily of salaries and related expenses for personnel, sales commissions, travel expenses, marketing programs, professional services, information systems, human resources and other corporate expenses.

Gross research and development expenses consist primarily of salaries and related expenses for engineers and other technical personnel, material component costs as well as fees paid to third-party consultants. We are eligible to receive research and development tax credits and government grants on research and development activities carried out in Canada. All related research and development tax credits and government grants are recorded as a reduction of gross research and development expenses.

OUR STRATEGY, KEY PERFORMANCE INDICATORS AND CAPABILITY TO DELIVER RESULTS

Strategic Objectives for Fiscal 2008

In our fiscal 2007 Annual Report, we established three strategic objectives for fiscal 2008. We planned to increase sales through market-share gains, maximize profitability and focus on innovation. The following section reviews our strategic objectives for fiscal 2008 and the results achieved for each of these objectives.

Increase sales through market-share gains

We increased our annual sales 20.2% to $183.8 million in fiscal 2008, while our corporate metric for the fiscal year was 20%. In fiscal 2008, our Telecom Division generated a sales growth of 24.0% year-over-year, including 97.4% growth for our protocol test business. It should be noted that Brix Networks and Navtel Communications, which were acquired in the third quarter of 2008, contributed $5.4 million to our protocol test sales in 2008. We also expanded our international presence in Europe, Middle-East and Africa (26.3% sales growth year-over-year) and in the Asia-Pacific region (40.1% sales growth year-over-year). On the other hand, sales from our copper access test business (3.9% decrease year-over-year), optical test business (12.7% growth year-over-year) as well as in the Americas region (12.8% growth year-over-year) fell short of our plans. With regard to the modest growth in our optical test business and Americas region, it is largely attributable to reduced spending by our top customer in fiscal 2008, compared to 2007. We do not believe that we lost market share with this customer, but this Tier-1 network service provider reduced its capital expenditures in fiscal 2008. The decline in our copper access business is mainly due to the fact that we integrated Consultronics' products into a new modular platform (AXS-200 SharpTESTER) in fiscal 2008, and we anticipate returning to a growth mode in 2009.

Maximize profitability

We generated GAAP earnings from operations of 6.5% in fiscal 2008, while our published metric was 8%. Our GAAP earnings from operations in fiscal 2008 included the negative contribution from newly acquired Brix Networks and Navtel Communications, which was not initially forecasted in our corporate metric. Excluding the negative contribution from these acquisitions, our earnings from operations would have been above 8%.

Focus on innovation

Sales from new products (on the market two years or less) accounted for 34.6% of total sales in 2008, compared to our stated goal of 30%.

Three-year Strategic Objectives

Our goal is to become a strong market leader in the global telecom test and service assurance industry offering market-driven solutions mainly to NSPs and increasingly covering the service and application layers on a network infrastructure to enable triple-play services and next-generation, converged IP networking.

Table of Contents

To achieve our long-term vision, we plan to expand our leadership position in the portable optical segment, while growing our protocol business even faster to surpass optical in terms of sales. This plan is based first and foremost on organic growth, but it will be supported by strategic acquisitions of small to mid-size companies with best-of-class technologies in nascent, high-growth markets complementary to EXFO's. We also intend to improve our competitive position through strategic alliances and partnerships.

Following our practice of benchmarking performance, we have established three corporate performance objectives to gauge the success of our overall plan over the next three years:

- Increase sales significantly faster than the industry growth rate (20% CAGR)
- Grow EBITDA* in dollars faster than sales (>20% CAGR)
- Continue raising gross margin (62%)

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

These three-year objectives will guide our actions in upcoming years as we are committed to maximizing shareholder value. They are meant to replace the performance goals that we have been providing on an annual basis. Hopefully, this new information will draw attention to our long-term potential and offer investors a more complete picture of our investment proposition.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management's discussion and analysis of financial conditions and results of operations is based on our consolidated financial statements included elsewhere in this Annual Report. As previously mentioned, they have been prepared in accordance with Canadian GAAP. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting years. On an ongoing basis, we evaluate these estimates and assumptions, including those related to the fair value of financial instruments, the allowance for doubtful accounts receivable, the amount of tax credits recoverable, the provision for excess and obsolete inventories, the useful lives of capital assets, the valuation of long-lived assets, the valuation allowance of future income tax assets, the amount of certain accrued liabilities and deferred revenue as well as stock-based compensation costs. We base our estimates and assumptions on historical experience and on other factors that we believe to be reasonable under the circumstances, the result of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

The following summarizes our critical accounting policies as well as other policies that require the most significant judgment and estimates in the preparation of our consolidated financial statements.

Revenue recognition. For products in which software is incidental, we recognize revenue when persuasive evidence of an arrangement exists, the product has been delivered, the price is fixed or determinable and collection of the resulting receivable is reasonably assured. In addition, provisions are made for estimated returns, warranties and support obligations.

For products in which software is not incidental, revenues are separated into two categories: product and post-contract customer support (PCS) revenues, based upon vendor-specific objective evidence of fair value. Product revenues for these sales are recognized as described above. PCS revenues are deferred and recognized ratably over the years of the

support arrangement. PCS revenues are recognized at the time the product is delivered when provided substantially within one year of delivery, the costs of providing this support are insignificant (and accrued at the time of delivery) and no (or infrequent) software upgrades or enhancements are provided.

Table of Contents

Maintenance contracts generally include the right to unspecified upgrades and enhancements on a when-and-if available basis and ongoing customer support. Revenue from these contracts is recognized ratably over the terms of the maintenance contracts on a straight-line basis.

Revenue for extended warranties is recognized on a straight-line basis over the warranty period.

For all sales, we use a binding purchase order as evidence that a sales arrangement exists.

Delivery generally occurs when the product is handed over to a transporter for shipment.

At the time of the transaction, we assess whether the price associated with our revenue transaction is fixed or determinable, and whether or not collection is reasonably assured. We assess whether the price is fixed or determinable based on the payment terms associated with the transaction. We assess collection based on a number of factors, including past transaction history and the creditworthiness of the customer. Generally, collateral or other security is not requested from customers.

Most sales arrangements do not generally include acceptance clauses. However, if a sales arrangement does include an acceptance provision, acceptance occurs upon the earliest of the receipt of a written customer acceptance or the expiration of the acceptance period. For these sales arrangements, the sale is recognized when acceptance occurs.

Allowance for doubtful accounts. We estimate collectibility of accounts receivable on an ongoing basis by reviewing balances outstanding over a certain period of time. We determine our allowance for doubtful accounts receivable based on our historical accounts receivable collection experience and on the information that we have about the status of our accounts receivable balances. If the financial conditions of our customers deteriorate, resulting in an impairment of their ability to make required payments, additional allowance may be required, which could adversely affect our future results.

Reserve for excess and obsolete inventories. We state our inventories at the lower of cost, determined on an average cost basis, and replacement cost or net realizable value, and we provide reserves for excess and obsolete inventories. We determine our reserves for excess and obsolete inventories based on the quantities we have on hand versus expected needs for these inventories, so as to support future sales of our products. It is possible that additional inventory reserves may occur if future sales are less than our forecasts or if there is a significant shift in product mix compared to our forecasts, which could adversely affect our future results.

Research and development tax credits and government grants. We record research and development tax credits and government grants based on our interpretation of tax laws and grant programs, especially regarding related eligible projects and expenses, and when there is reasonable assurance that we have complied and will continue to comply with all conditions and laws. Also, our judgment and estimates are based on historical experience. It is possible, however, that the tax authorities or the sponsors of the grant programs have a different interpretation of laws and application of conditions related to the programs or that we do not comply with all conditions related to grants in the future, which could adversely affect our future results. Furthermore, a significant part of our research and development tax credits are refundable against income taxes payable, causing their ultimate realization to be dependent upon the generation of taxable income. If we obtain information that causes our forecast of future taxable income to change or if actual taxable income differs from our forecast, we may have to revise the carrying value of these tax credits, which would affect our results in the period in which the change was made.

Impairment of long-lived assets and goodwill. We assess impairment of long-lived assets when events or circumstances indicate that costs may not be recoverable. Impairment exists when the carrying value of an asset, or a group of assets, is greater than the pre-tax undiscounted future cash flows expected to be provided by the asset or the

group of assets. The amount of impairment loss, if any, is the excess of the carrying value over the fair value. We assess fair value of long-lived assets based on discounted future cash flows.

Table of Contents

We assess impairment of goodwill on an annual basis, or more frequently, if events or circumstances indicate that it might be impaired. Recoverability of goodwill is determined at the reporting-unit level using a two-step approach. First, the carrying value of a reporting unit is compared to its fair value, which is determined based on a combination of discounted future cash flows and a market approach. If the carrying value of a reporting unit exceeds its fair value, the second step is performed. In this step, the amount of impairment loss, if any, represents the excess of the carrying value of goodwill over its fair value and the loss is charged to earnings in the period in which it is incurred. For the purposes of this impairment test, the fair value of goodwill is estimated in the same way as goodwill is determined in business combinations; that is, the excess of the fair value of a reporting unit over the estimated fair value of its net identifiable assets.

Future income taxes. We account for income taxes using the liability method of tax allocation. Under this method, future income tax assets and liabilities are determined based on deductible or taxable temporary differences between financial statement values and tax values of assets and liabilities as well as the carryforward of unused tax losses and deductions, using substantively enacted income tax rates for the years in which the assets are expected to be realized or the liabilities to be settled. In assessing the recoverability of our future income tax assets, we consider whether it is more likely than not that some or all of the future income tax assets will not be realized. The ultimate realization of our future income tax assets is dependent upon the generation of sufficient future taxable income during the periods in which those assets are expected to be realized.

Stock-based compensation costs. We account for all forms of employee stock-based compensation using the fair value-based method. This method requires that we make estimates about the expected volatility of our shares, the expected life of the awards and the forfeiture rate.

Adopted in fiscal 2008

On September 1, 2007, we adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1530, “Comprehensive Income”, Section 3251, “Equity”, Section 3855, “Financial Instruments – Recognition and Measurement”, and Section 3865, “Hedges”. Sections 3251 and 3865 have been adopted prospectively, while Section 3855 has been applied retroactively, without restatement of prior years’ financial statements and Section 1530 has been applied retroactively with restatement of prior years’ financial statements.

Following the adoption of Section 3855, we classified our financial instruments as follows:

Cash

Cash is classified as a financial asset held for trading and is carried at fair value in the balance sheet, and any changes in its fair value are reflected in the statements of earnings.

Short-term investments

We elected to classify our short-term investments as available-for-sale securities; therefore, they are carried at fair value in the balance sheet, and any changes in their fair value are reflected in comprehensive income. Upon the disposal or maturity of these assets, accumulated changes in their fair value are reclassified in the statements of earnings. Also, upon the adoption of this new standard, unrealized losses on short-term investments as of August 31, 2007, in the amount of $55,000 (previously recorded in the statements of earnings), have been reclassified from the opening balance of retained earnings to the opening balance of accumulated other comprehensive income for the year ended August 31, 2008.

Interest income on short-term investments is recorded in interest income in the statements of earnings and in cash flows from operating activities in the statements of cash flows.

Accounts receivable

Accounts receivable are classified as loans and receivable. After their initial measurement at fair value, they are carried at amortized cost, which generally corresponds to nominal amount due to their short-term maturity.

Table of Contents

Accounts payable and accrued liabilities

Accounts payable and accrued liabilities are classified as other financial liabilities. They are initially measured at their fair value. Subsequent measurements are at amortized cost, using the effective interest rate method. For us, that value corresponds to nominal amount as a result of their short-term maturity.

Forward exchange contracts

Our forward exchange contracts, which qualify for hedge accounting, are used to hedge anticipated US-dollar-denominated sales and the related accounts receivable. They are recorded at fair value in the balance sheet with changes in their fair value being reported in comprehensive income. Upon the recognition of related hedged sales, accumulated changes in fair value are reclassified in the statements of earnings. Unrecognized gains on forward exchange contracts as of August 31, 2007, in the amount of $1.9 million, net of future income taxes of $916,000, have been reflected as an adjustment to the opening balance of accumulated other comprehensive income for the year ended August 31, 2008.

Cumulative foreign currency translation adjustment

The cumulative foreign currency translation adjustment, which is solely the result of the translation of our consolidated financial statements in US dollars (our reporting currency), has been reclassified to be presented as a component of accumulated other comprehensive income for all years presented.

Transition

We elected to use September 1, 2002, as the transition date for embedded derivatives.

Other than the adjustments described above for the short-term investments and the forward exchange contracts, the recognition, derecognition and measurement methods used to prepare the consolidated financial statements have not changed from the methods of periods prior to the effective date of the new standards. Consequently, there were no further adjustments to record on transition.

Section 1506, “Accounting Changes”

On September 1, 2007, we adopted Section 1506, “Accounting Changes”. This section establishes criteria for changes in accounting policies, accounting treatment and disclosures regarding changes in accounting policies, estimates and corrections of errors. In particular, this section allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information. Furthermore, this section requires disclosure of when an entity has not applied a new source of GAAP that has been issued but is not yet effective. The adoption of this section had no effects on our consolidated financial statements for the year ended August 31, 2008.

To be adopted after fiscal 2008

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

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

disclosures and simplify the disclosures about concentrations of risk, credit risk, liquidity risk and price risk currently found in Section 3861.

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

Table of Contents

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

Sections 1535, 3862 and 3863 apply to fiscal years beginning on or after October 1, 2007. We will adopt these new standards on September 1, 2008, and are currently assessing the disclosure effects these new standards will have on our consolidated financial statements.

In June 2007, the CICA issued Section 3031, "Inventories". This standard requires the measurement of inventories at the lower of cost and net realizable value and includes guidance on the determination of cost, including allocation of overheads and other costs to inventory. The standard also requires the consistent use of either first-in, first-out (FIFO) or weighted average cost formula to measure the cost of inventories and requires the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. The new standard applies to fiscal years beginning on or after January 1, 2008. We will adopt this new standard on September 1, 2008, and its adoption will have no significant effect on our consolidated financial statements.

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

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

Table of Contents

RESULTS OF OPERATIONS

The following table sets forth certain Canadian GAAP consolidated financial statements data in thousands of US dollars, except per share data, and as a percentage of sales for the years indicated:

Consolidated statements of earnings data:	2008	2007	2006	2008	2007	2006
Sales	$ 183,790	$ 152,934	$ 128,253	100.0%	100.0%	100.0%
Cost of sales (1)	75,624	65,136	57,275	41.1	42.6	44.7
Gross margin	108,166	87,798	70,978	58.9	57.4	55.3
Operating expenses						
Selling and administrative	61,153	49,580	40,298	33.3	32.4	31.4
Net research and development (2)	26,867	16,668	15,404	14.6	10.9	12.0
Amortization of property, plant and equipment	4,292	2,983	3,523	2.4	1.9	2.7
Amortization of intangible assets	3,871	2,864	4,394	2.1	1.9	3.4
Impairment of long-lived assets	–	–	604	–	–	0.5
Government grants	–	(1,079)	(1,307)	–	(0.7)	(1.0)
Total operating expenses	96,183	71,016	62,916	52.4	46.4	49.0
Earnings from operations	11,983	16,782	8,062	6.5	11.0	6.3
Interest income	4,639	4,717	3,253	2.5	3.0	2.5
Foreign exchange gain (loss)	442	(49)	(595)	0.3	–	(0.5)
Earnings before income taxes and extraordinary gain	17,064	21,450	10,720	9.3	14.0	8.3
Income taxes						
Current	(7,094)	3,741	2,585	(3.9)	2.4	2.0
Future	14,094	–	–	7.7	–	–
Recognition of previously unrecognized future income tax assets	(5,324)	(24,566)	–	(2.9)	(16.0)	–
	1,676	(20,825)	2,585	0.9	(13.6)	2.0
Earnings before extraordinary gain	15,388	42,275	8,135	8.4	27.6	6.3
Extraordinary gain	3,036	–	–	1.6	–	–
Net earnings for the period	$ 18,424	$ 42,275	$ 8,135	10.0%	27.6%	6.3%
Basic and diluted earnings before extraordinary gain per share	$ 0.22	$ 0.61	$ 0.12			
Basic and diluted net earnings per share	$ 0.27	$ 0.61	$ 0.12			
Segment information						
Sales:						
Telecom Division	$ 160,981	$ 129,839	$ 107,376	87.6%	84.9%	83.7%
Life Sciences and Industrial Division	22,809	23,095	20,877	12.4	15.1	16.3
	$ 183,790	$ 152,934	$ 128,253	100.0%	100.0%	100.0%

Earnings from operations:						
Telecom Division	$ 9,524	$ 13,132	$ 6,679	5.2%	8.6%	5.2%
Life Sciences and Industrial Division	2,459	3,650	1,383	1.3	2.4	1.1
	$ 11,983	$ 16,782	$ 8,062	6.5%	11.0%	6.3%
Research and development data:						
Gross research and development	$ 32,454	$ 25,201	$ 19,488	17.7%	16.5%	15.2%
Net research and development (2)	$ 26,867	$ 16,668	$ 15,404	14.6%	10.9%	12.0%
Consolidated balance sheets data:						
Total assets	$ 293,066	$ 279,138	$ 219,159			

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

(2) Net research and development expenses for the year ended August 31, 2007 include recognition of previously unrecognized research and development tax credits of $3,162, or 2.1% of sales.

Table of Contents

SALES

Fiscal 2008 vs. 2007

In fiscal 2008, our global sales increased 20.2% to $183.8 million from $152.9 million for the same period last year, with an 88%–12% split in favor of our Telecom Division (85%–15% in 2007).

Telecom Division

In fiscal 2008, sales of our Telecom Division increased 24.0% to $161.0 million from $129.8 million in 2007.

In fiscal 2008, we posted sales growth due to the market acceptance of our next-generation IP test solutions and continued market-share gains in optical test solutions; due to revenue from newly acquired Brix Networks and Navtel Communications; and due to continued spending in access networks fuelled by the competitive dynamic between telephone and cable companies.

In fiscal 2008, sales of our optical test solutions increased 12.7% to $115.1 million, from $102.1 million in 2007. In addition, in fiscal 2008, we posted record-high sales and bookings of protocol test solutions, including next-generation IP test solutions and product lines of newly acquired Brix Networks and Navtel Communications. Protocol test solutions represented our fastest-growing product line with a year-over-year sales increase of 97.4% (organic growth of 65.6% excluding sales of $5.4 million from our new acquisitions of fiscal year 2008) as they reached $33.7 million in 2008, compared to $17.1 million in 2007. Also, they represented more than 20% of our telecom sales in 2008 (more than 10% in 2007). With these two acquisitions as well as the recent launches of significant strategic protocol test solutions—namely, a compact multiservice transport test set that combines next-generation SONET/SDH and Ethernet testing inside a single module (FTB-8120NGE/FTB-8130NGE Power Blazer), a 40/43 Gbit/s SONET/SDH field-test solution for high-speed optical networks (FTB-8140 Transport Blazer) as well as the advanced IQS-600 Integrated Qualification System, a highly scalable modular test platform for R&D and manufacturing applications—we have a much more comprehensive offering in this market segment, which provides us with a significant competitive advantage; we believe this should help us further increase our market share and sales in the upcoming quarters.

However, in fiscal 2008, we posted a year-over-year sales decrease of 3.9% ($7.4 million in fiscal 2008, compared to $7.7 million in 2007) for our copper-access test solutions given that our highly competitive new product offering is only just starting to establish itself on the market and that large-scale IPTV deployments have been delayed, which affected our sales in fiscal 2008 to some extent. During fiscal 2008, we launched new added-value products that integrate Consultronics (copper-access) core knowledge and intellectual property, such as the new AXS-200 SharpTESTER. Also in 2008, we launched a new test module housed inside the AXS-200 SharpTESTER platform, which differentiates our access network offering from those of other vendors. The AXS-200/630 Triple-Play Test Set, which leverages the benefits of Broadcom's customer premises equipment (CPE) multimode VDSL2 chipset, enables the installation and troubleshooting of ADSL2+ and VDSL2 access networks with the highest level of interoperability. These new, innovative products have yet to contribute to our sales for this market segment. A large portion of our sales of copper-access products in fiscal 2007 were made to a Tier-1 carrier in the United States. In fiscal 2008, sales of copper-access test solutions made to this customer significantly decreased compared to 2007, which means that we were able to diversify our customer base year-over-year.

It should be noted however that in fiscal 2007, we benefited from aggressive FTTH rollouts from our top customer, and sales to this customer represented 17.3% ($22.5 million) of our telecom sales in fiscal 2007, compared to 8.4% ($13.6 million) this year. Excluding sales to this customer, our telecom sales would have increased 37.3% in fiscal 2008, compared to 2007; we believe this shows that we have properly diversified our customer base

year-over-year.

In fiscal 2008, foreign exchange gains on our forward exchange contracts, which are included in our telecom sales, amounted to $4.2 million, compared to $1.3 million in 2007. In fiscal 2008, the average value of the Canadian dollar increased 11.4% versus the US dollar compared to 2007, which contributed to the increase in the foreign exchange gains on our forward exchange contracts year-over-year.

Table of Contents

Life Sciences and Industrial Division

In fiscal 2008, sales of our Life Sciences and Industrial Division decreased 1.2% year-over-year at $22.8 million from $23.1 million in 2007.

A significant portion of sales of that division are conducted through original equipment manufacturer (OEM) agreements. Consequently, we are dependent, to some extent, on the buying pattern of our customers. In particular, one of our major OEM customers significantly reduced its purchases of our products following the launch of its own solution that competes against our products. Excluding sales to this customer, sales of this division would have increased 3.5% year-over-year.

Net Bookings

Overall, for the two divisions, net accepted orders increased 17.8% year-over-year to a record-high $184.6 million in fiscal 2008 from $156.7 million in 2007, for a book-to-bill ratio of 1.00 (excluding the backlog of Brix Networks and Navtel Communications) in fiscal 2008. Our 17.8% increase in net accepted orders in fiscal 2008, compared to the same period last year, is mainly due to the increased demand for our next-generation IP and optical test solutions, and the contribution of Brix Networks and Navtel Communications since their acquisitions.

Fiscal 2007 vs. 2006

In fiscal 2007, our global sales increased 19.2% to $152.9 million from $128.3 million in 2006, with an 85%–15% split in favor of our Telecom Division (84%–16% in 2006).

Telecom Division

In fiscal 2007, sales of our Telecom Division increased 20.9% to $129.8 million from $107.4 million in 2006.

In fiscal 2007, we posted organic sales growth due to market-share gains in optical testing and next-generation IP test solutions and due to continued spending in access networks fueled by the competitive dynamic between telephone and cable companies. In fiscal 2007, sales of our optical test solutions increased 19.9% to $102.1 million ($85.2 million in 2006), and we earned our fourth consecutive Growth Strategy Leadership Award from Frost & Sullivan for largest market-share gains in optical testing. Also, during fiscal 2007, protocol test solutions were our fastest-growing product line with a sales increase of 48.2% year-over-year as they reached $17.1 million, compared to $11.5 million in 2006. These products represented more than 10% of our Telecom sales in 2007.

In addition, during fiscal 2007, sales of our copper-access test solutions increased 15.5% to $7.7 million, compared to $6.7 million in 2006. It should be noted however that Consultronics (acquired in January 2006) contributed to our sales during the whole period compared to about seven months in 2006, which contributed to the increase in our sales year-over-year. This business unit did not perform as well as expected in 2007, as large-scale IPTV deployments were delayed. A large portion of our sales of copper-access products in fiscal 2007 were made to a Tier-1 carrier in the United States.

During fiscal 2007, we faced increased pricing pressure, especially in the Asia-Pacific region, which prevented us from further increasing our sales year-over-year.

Life Sciences and Industrial Division

In fiscal 2007, sales of our Life Sciences and Industrial Division increased 10.6% to $23.1 million from $20.9 million in 2006. The increase in sales in fiscal 2007, compared to 2006, is mainly due to increased sales activities in the curing market as well as market-share gains in the fluorescence illumination market, following our efforts to expand international markets, mainly Europe and Asia.

Table of Contents

Geographic distribution

Fiscal 2008 vs. 2007

In fiscal 2008, sales to the Americas, Europe, Middle-East and Africa (EMEA) and Asia-Pacific (APAC) accounted for 56%, 28% and 16% of global sales, respectively, compared to 59%, 27% and 14%, respectively in 2007.

In fiscal 2008, we reported sales increases (in dollars) in every geographic area. In fact, sales to the Americas, EMEA and APAC increased (in dollars) 12.8%, 26.3% and 40.1%, respectively, which resulted in a larger percentage of sales coming from international markets.

In the Americas, the increase in sales in fiscal 2008, compared to the same period last year, comes from every region; we posted a sales growth of 47.8%, 7.9% and 16.7% in Canada, United States and Latin America, respectively. In the United States, despite the decrease in sales to our top customer year-over-year, we were able to increase our sales in this region. Additionally, Brix Networks and Navtel Communications contributed to the increase in sales in the United States and in Canada year-over-year as most of their sales are made in these two countries. As mentioned above, during fiscal 2007, we benefited from aggressive FTTH rollouts from our top customer, and sales to this customer represented 14.7% ($22.5 million) of our global sales in fiscal 2007, compared to 7.4% ($13.6 million) this year. We believe that we did not lose market share with this particular customer in fiscal 2008; in fact, we believe we have expanded market share as we successfully got additional product-line approvals to partially offset the decline in optical business. Excluding sales to this customer, sales to the United States would have increased 28.7% in dollars year-over-year; this shows that, overall, we have diversified our customer base year-over-year in this region. Finally, sales to Latin America fluctuate depending on the timing and scope of our customers' projects.

The increase in sales in the EMEA market, in dollars, in fiscal 2008, compared to 2007, is a result of our continued strategy to aggressively develop this market in the past several years, to consistently invest in sales resources, and to develop stronger support and service operations in this region. In addition, many Tier-1 carriers in EMEA are migrating their traditional circuit-switched core networks to higher-speed, dense wavelength-division multiplexing (DWDM) and next-generation packet-based architectures, which is creating a market demand for our protocol test solutions as well as our DWDM, ROADM and fiber characterization test kits. Furthermore, we are leveraging our FTTx leadership gained in the United States to provide consultancy with many of the early adopters in this field in EMEA.

In the APAC market, we are seeing the continued return on investment of some specific optical, protocol as well as life sciences and industrial products developed and targeted for this important market. This increasingly competitive range, coupled with our steadily expanding market presence, is responsible for the higher sales in this region in fiscal 2008, compared to 2007.

Fiscal 2007 vs. 2006

In fiscal 2007, sales to the Americas, Europe, Middle-East and Africa (EMEA) and Asia-Pacific (APAC) accounted for 59%, 27% and 14% of global sales, respectively, compared to 60%, 25% and 15%, respectively in 2006.

In fiscal 2007, we reported sales increases in dollars in every geographic area. In fact, sales to the Americas, EMEA and APAC increased (in dollars) 18.7%, 27.5% and 7.8% year-over-year, respectively.

In the Americas, the increase in sales in dollars in fiscal 2007, compared to the same period last year, comes from the United States and Canada, where we witnessed an increase in sales of our optical and protocol test solutions. In the United States, we continue leveraging our dominant FTTx market position to increase our sales. In addition, sales to

our top customer, who is located in the United States, increased in dollars in fiscal 2007, compared to 2006. Sales to this customer represented $22.5 million, or 14.7% of global sales in 2007, compared to $17.7 million, or 13.8% of our global sales in 2006, representing an increase of 27.0% year-over-year. In Latin America, we reported a slight decrease in sales in fiscal 2007 compared to 2006.

Table of Contents

The significant increase in sales in the EMEA market, in dollars, in fiscal 2007, compared to 2006, is apparent in the results for all our product lines, following our efforts to aggressively develop this market in the past several years, and our continued investment to increase our sales presence as well as our initiatives to develop stronger support and service operations in this region. Many Tier-1 carriers in EMEA are migrating their traditional circuit-switched core networks to higher-speed, DWDM and next-generation packet-based architectures, which is creating a market demand for our protocol test solutions and fiber characterization test kits. In addition, we are leveraging our FTTx leadership gained in the United States to provide consultancy with many of the early adopters in this field in EMEA.

In the APAC market, we started to see the impact of the introduction of some specific optical, protocol and life sciences and industrial products as we steadily increase our market presence in this growth region; this explains the increase in sales in this region in fiscal 2007, compared to the corresponding period last year. However, although we reported sales growth year-over-year in this region, we are facing significant competitive pricing pressure, which prevented us from reaching expected sales growth. In addition, a significant portion of our sales to this market are made through tenders, which vary in number and importance year-over-year.

Through our two divisions, we sell our products to a broad range of customers, including network service providers, network equipment manufacturers, wireless operators, cable TV operators, optical system and component manufacturers, as well as customers in the life sciences and high-precision assembly sectors. In fiscal 2008, no customer accounted for more than 10% of our global sales, and our top three customers accounted for 13.1% of our global sales. In fiscal 2007, our top customer accounted for 14.7% ($22.5 million) of our global sales, and our top three customers accounted for 19.6% of our global sales.

GROSS MARGIN

Gross margin amounted to 58.9%, 57.4% and 55.3% of sales in fiscal 2008, 2007 and 2006, respectively.

Fiscal 2008 vs. 2007

Fiscal 2008 marked the sixth consecutive year that the company raised its gross margin as it reached its highest level since fiscal 2001. The increase in our gross margin in fiscal 2008, compared to 2007, can be explained by the following factors. First, in fiscal 2008, our gross margin was positively affected by the significant increase in sales of our protocol test solutions year-over-year, including those of Brix Networks and Navtel Communications, as these products have better margins than our other test solutions. In addition, the significant increase in global sales, year-over-year, resulted in an increase in manufacturing activities, allowing us to better absorb our fixed manufacturing costs. Furthermore, we were able to reduce our cost of goods sold by better leveraging our supplier base and by developing innovative new products with cost-effective design. Also, our cost of goods was positively affected by lower costs for raw material due to the significant increase in the value of the Canadian dollar, compared to the US dollar in previous quarters, as most of these costs are incurred in US dollars.

However, the shift in sales between the Americas in favor of APAC had a negative impact on our gross margin year-over-year. In fact, sales to APAC tend to have lower margins than sales to the Americas since we are facing higher pricing pressure in the APAC region. In addition, we are facing continued aggressive pricing pressure worldwide. Furthermore, in fiscal 2008, a stronger Canadian dollar, compared to the US dollar year-over-year, prevented us from further improving our gross margin as most of our overhead costs and a portion of our raw material purchases are denominated in Canadian dollars. Finally, the startup of our own manufacturing activities in China, over the last few months, resulted in additional expenses, which reduced our gross margin in fiscal 2008, compared to 2007.

On an ongoing basis and when technically possible, we adjust the design of our products to reuse excess inventory; over the past few years, we experienced higher sales than expected on some product lines and consumed such excess inventory. Consequently, we were able to reuse excess inventories that were written off in previous years. Excess inventory reuse accounted for approximately $1.2 million, or 0.7% of sales in fiscal 2008, compared to approximately $1.7 million, or 1.1% of sales in 2007 and approximately $1.2 million, or 0.9% of sales in 2006.

Table of Contents

Fiscal 2007 vs. 2006

Despite the increased strength of the Canadian dollar, compared to the US dollar in fiscal 2007 versus 2006, and the intense competitive pressure on selling prices that we faced in 2007, we were able to significantly increase our gross margin (2.1%) year-over-year.

This increase in our gross margin in fiscal 2007, compared to 2006, can be explained by several factors. First, the increase in sales year-over-year resulted in an increase in manufacturing activities, allowing us to better absorb our fixed manufacturing costs. In addition, sales of our protocol test solutions increased in dollars and as a percentage of sales year-over-year; this had a positive impact on our gross margin, as these products are more software-intensive and tend to have better gross margins than our optical test solutions. Furthermore, we were able to reduce our cost of goods sold by better leveraging our supplier base and by developing innovative new products with cost-effective design. Finally, our initiative to outsource the manufacturing of some product lines to China in fiscal 2007 helped us to improve our gross margin year-over-year.

However, we are facing continued aggressive pricing pressure worldwide, which negatively affected the gross margin in fiscal 2007. In addition, in 2007, a stronger Canadian dollar, compared to the US dollar year-over-year, prevented us from further improving our gross margin, as some cost of sales items are denominated in Canadian dollars. Furthermore, the transfer, in fiscal 2007, of our protocol and copper access manufacturing operations from Montreal and Concord to our Quebec City plant resulted in one-time charges, which negatively affected our gross margin during that period. Finally, the setup of our own manufacturing activities in China late in fiscal 2007 resulted in additional one-time costs in 2007, thus reducing the gross margin of that year.

Outlook for Fiscal 2009

Considering our expectations of sales growth in fiscal 2009, our expectations of increase in sales of protocol products and the full contribution of Brix Networks and Navtel Communications (which historically have generated higher margins than our own product lines), the cost-effective design of our products, our manufacturing activities in China and our tight control on operating costs, while no assurance can be given, we expect our gross margin to improve in the next few years. However, our gross margin may fluctuate quarter-over-quarter as our sales may fluctuate. Furthermore, our gross margin can be negatively affected by increased competitive pricing pressure, customer concentration and/or consolidation, increased obsolescence costs, shifts in customer and product mix, under-absorption of fixed manufacturing costs, challenges encountered in the ramp-up of our manufacturing facilities in China and increases in product offerings by other suppliers in our industry. Finally, any increase in the strength of the Canadian dollar, compared to the US dollar, would have a negative impact on our gross margin in fiscal 2009 and beyond.

SELLING AND ADMINISTRATIVE

Selling and administrative expenses were $61.2 million, $49.6 million and $40.3 million for fiscal 2008, 2007 and 2006, respectively. As a percentage of sales, selling and administrative expenses amounted to 33.3%, 32.4% and 31.4% for fiscal 2008, 2007 and 2006, respectively.

In fiscal 2008, we continued intensifying our sales and marketing activities to develop our markets and leverage our significant research and development investments; this resulted in higher sales and marketing expenditures (including number of employees and expenses to support the launch of several new products and to increase brand-name recognition), compared to 2007.

Also, Brix Networks and Navtel Communications contributed about four months and five months, respectively, in fiscal 2008, which caused our selling and administrative expenses to increase compared to 2007.

The substantial increase in the average value of the Canadian dollar compared to the US dollar also had a significant negative impact ou our selling and administrative expenses since more than half of these expenses are denominated in Canadian dollars and since these expenses increased year-over-year as our sales grew.

Fiscal 2008 vs. 2007

In fiscal 2008, we continued intensifying our sales and marketing activities to develop our markets and leverage our significant research and development investments; this resulted in higher sales and marketing expenditures (including number of employees and expenses to support the launch of several new products and to increase brand-name recognition), compared to 2007.

Also, Brix Networks and Navtel Communications contributed about four months and five months, respectively, in fiscal 2008, which caused our selling and administrative expenses to increase compared to 2007.

The substantial increase in the average value of the Canadian dollar compared to the US dollar also had a significant negative impact ou our selling and administrative expenses since more than half of these expenses are denominated in Canadian dollars and since these expenses increased year-over-year as our sales grew.

Table of Contents

In addition, the setup in 2008 of manufacturing facilities in China and a software development center in India contributed to an increase in our administrative expenses year-over-year.

Finally, in fiscal 2008, we discontinued certain product lines, which led to the layoff of some of our sales and marketing personnel, resulting in severance expenses during that year.

However, in fiscal 2007, we had large orders sold directly to international customers, for which we still had to pay commissions to distributors instead of selling through our distributors at a discounted price; this did not occur at the same extent in 2008, resulting in higher selling expenses for 2007, compared to 2008.

In fiscal 2008, and despite an increase in sales, our selling and administrative expenses increased in percentage of sales compared to 2007. The significant increase in the average value of the Canadian dollar compared to the US dollar year-over-year, the setup of our manufacturing facilities in China and R&D center in India, as well as the impacts of the acquisitions of Brix Networks and Navtel Communications—whose selling expenses tend to be higher as their products deliver better margins compared to the rest of our product lines—contributed to the increase in these expenses as a percentage of sales.

Fiscal 2007 vs. 2006

In fiscal 2007, we intensified our sales and marketing activities to develop our markets and leverage the significant research and development investments of the prior years; this resulted in higher sales and marketing expenditures (including the number of employees), compared to 2006.

In addition, our overall commission expenses increased in fiscal 2007, compared to the corresponding period last year, due to the increase in sales year-over-year and the shift in customer mix. In fact, in fiscal 2007, we had large orders sold directly to international customers for which we still had to pay commissions to distributors instead of selling through our distributors at a discounted price, which increased our selling expenses year-over-year, but had, to some extent, a positive impact on our gross margin.

Furthermore, Consultronics, acquired in January 2006, contributed to our selling and administrative expenses throughout the entire period, compared to about seven months in 2006, thus increasing these expenses year-over-year.

Also, a stronger Canadian dollar on average for the period, compared to the US dollar during fiscal 2007 versus 2006, caused our selling and administrative expenses to increase year-over-year, as more than half of these expenses are denominated in Canadian dollars.

In addition, late in fiscal 2007, the setup of manufacturing facilities in China and a software development center in India contributed to an increase in our administrative expenses year-over-year.

Finally, in fiscal 2007, and despite an increase in sales, our selling and administrative expenses increased in percentage of sales compared to the corresponding period last year. Larger commissions on international sales as well as our efforts to develop international markets and operations contributed to the increase in these expenses as a percentage of sales.

Outlook for Fiscal 2009

For fiscal 2009, considering the significant impacts of the acquisitions of Brix Networks and Navtel Communications on our selling and administrative expenses—whose selling expenses tend to be higher, as their products deliver better margins compared to the rest of our product lines—we expect our selling and administrative expenses to increase in

dollars and range between 32% and 34%. In particular, in fiscal 2009, we expect our commission expenses to increase as sales volume increases. Furthermore, considering our goal of becoming the leading player in the telecom test, measurement and monitoring space, we plan to continue intensifying our sales and marketing efforts, both domestic and international, which will also cause our expenses to rise. Finally, any increase in the strength of the Canadian dollar would also cause our selling and administrative expenses to increase, as more than half of these expenses are incurred in Canadian dollars.

Table of Contents

RESEARCH AND DEVELOPMENT

Gross research and development expenses

Gross research and development expenses totaled $32.5 million, $25.2 million and $19.5 million for fiscal 2008, 2007 and 2006, respectively. As a percentage of sales, gross research and development expenses amounted to 17.7%, 16.5% and 15.2% for fiscal 2008, 2007 and 2006, respectively, while net research and development expenses accounted for 14.6%, 10.9% and 12.0% of sales for these respective periods. Net research and development expenses for fiscal 2007 included the recognition of non-refundable research and development tax credits in the amount of $3.2 million that were written off in fiscal 2003 following the downturn in the telecommunications industry; this represented 2.1% of sales.

Fiscal 2008 vs. 2007

In fiscal 2008, the significant increase in the average value of the Canadian dollar, compared to the US dollar year-over-year, had a significant and negative effect on our gross research and development expenses as a significant portion of these expenses are denominated in Canadian dollars and also because these expenses increased year-over-year. In addition, we intensified our research and development activities, including additional employees, which resulted in more gross research and development expenses in both divisions in fiscal 2008, compared to 2007. Furthermore, Brix Networks and Navtel Communications contributed about four months and five months, respectively, in fiscal 2008, which caused our gross research and development expenses to increase compared to 2007. It should be noted that Brix Networks and Navtel Communications tend to incur a higher percentage of sales for research and development expenses compared to our other product lines as their products are more software-intensive; but they deliver higher margins than most of our other product lines. Also, we established a research and development center focused on software development in Pune, India, which resulted in increased expenses year-over-year. Finally, in fiscal 2008, we closed down our R&D operations in Budapest, Hungary, and certain R&D projects, which resulted in severance expenses during that year and caused our fiscal 2008 expenses to increase year-over-year.

The increase in our gross research and development expenses as a percentage of sales year-over-year is mainly due to the negative effect of the increased value of the Canadian dollar versus the US dollar year-over-year, the impact of the acquisitions of Brix Networks and Navtel Communications as well as the severance expenses incurred in fiscal 2008.

Fiscal 2007 vs. 2006

In fiscal 2007, we intensified our research and development activities in both divisions, which resulted in higher gross research and development expenses, including additional employees, compared to 2006. In addition, in fiscal 2007, we subcontracted a larger portion of our research and development projects in Canada and India, compared to the corresponding period last year, which resulted in an increase in our gross research and development expenses year-over-year.

Furthermore, Consultronics contributed to our research and development expenses during the whole period this year, compared to about seven months in 2006, thus increasing these expenses year-over-year. Finally, in fiscal 2007, the increased strength of the Canadian dollar, on average, compared to the US dollar year-over-year, contributed to the increase in our gross research and development expenses, as most of these are denominated in Canadian dollars.

The above-mentioned factors explain the increase of our gross research and development expenses as a percentage of sales in fiscal 2007, compared to 2006.

Tax credits

In fiscal 2008, tax credits from the Canadian federal and provincial governments for research and development activities were $5.6 million, $8.5 million and $4.1 million for fiscal 2008, 2007 and 2006, respectively. As a percentage of gross research and development expenses, tax credits and grants reached 17.2%, 33.9% and 21.0% for fiscal 2008, 2007 and 2006, respectively.

Table of Contents

Fiscal 2008 vs. 2007

In fiscal 2007, and as explained below, tax credits included $3.2 million, or 12.5% of gross research and development expenses, for the recognition of non-refundable research and development tax credits that were written off in fiscal 2003 following the downturn in the telecommunications industry. Excluding this one-time revenue, tax credits would have increased $216,000 in fiscal 2008, compared to 2007.

This increase in the dollar amount of our tax credits in fiscal 2008, compared to 2007, is due to the increased strength of the Canadian dollar, compared to the US dollar year-over-year, since these credits are solely earned on research and development expenses incurred in Canada. However, the decrease in research and development tax credits as a percentage of gross research and development expenses is mainly due to the fact that since the beginning of fiscal 2008, the portion of gross research and development incurred in Canada, where we are entitled to tax credits, was lower than in fiscal 2007 following the establishment of our new software development center in India as well as the acquisition of Brix Networks, which is located in the United States. Our research and development activities conducted outside Canada are not entitled to tax credits.

Fiscal 2007 vs. 2006

During fiscal 2003, following the downturn in the telecommunications industry and after being in a cumulative loss position, we wrote off deferred non-refundable research and development tax credits of our parent company because it was more likely than not that these assets would not be realized.

In fiscal 2007, after reviewing both available positive and negative evidence, and because we were in a cumulative profit position in the parent company at the Canadian federal level, and also because we expect to generate sufficient taxable income in future years, we concluded that is was more likely than not that deferred non-refundable income tax credits of our parent company would be realized. Consequently, in fiscal 2007, we recorded previously unrecognized non-refundable research and development tax credits in the amount of $3.2 million, or 12.5% of gross research and development expenses. These non-refundable tax credits of $3.2 million recognized in fiscal 2007 can be carried forward against future years' Canadian federal income taxes payable and expire between 2011 and 2014.

In addition to this one-time tax credit, our tax credits increased in dollars in fiscal 2007, compared to 2006, for several reasons. First, the increase in gross research and development expenses in Canada in 2007, compared to 2006, resulted in more expenses being eligible for tax credits as we were entitled to similar grant programs and tax credits year-over-year. In addition, the increased strength of the Canadian dollar, compared to the US dollar year-over-year, resulted in higher tax credits since these credits are solely earned on research and development expenses incurred in Canada.

Also, due to the one-time recognition of non-refundable tax credits from prior years, our tax credits significantly increased as a percentage of gross research and development expenses. Had prior years' credits not been recognized, our tax credits would have been flat year-over-year as a percentage of gross research and development expenses, as we incurred most of our expenses in Canada and were entitled to the same grant programs and tax credits.

Outlook for Fiscal 2009

For fiscal 2009, we expect that our research and development expenses will increase in dollars, and range between 14% and 16% of sales, given our focus on innovation, the addition of Brix Networks and Navtel Communications, whose products are software-intensive, the addition of software features in our products, our desire to gain market share and our goal to exceed customer needs and expectations. Also, we are increasingly taking advantage of talent pools around the world with the establishment of a research and development center focused on software development

in Pune, India. Finally, any increase in the strength of the Canadian dollar in the upcoming quarters would cause our net research and development expenses to increase, as most of these are incurred in Canadian dollars.

Table of Contents

AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

In fiscal 2008, amortization of property, plant and equipment was $4.3 million, compared to $3.0 million in 2007 and $3.5 million in 2006.

Fiscal 2008 vs. 2007

The recent startup of our own manufacturing and research and development facilities in China and India, the upgrade of our IT systems, and the impact of the acquisition of Brix Networks and Navtel Communications, which contributed about four months and five months in fiscal 2008, respectively, resulted in an increase in our amortization expenses in fiscal 2008 compared to last year. In addition, the increase in the average value of the Canadian dollar versus the US dollar in fiscal 2008, compared to 2007, contributed to the increase in our amortization expenses year-over-year as most of these expenses are denominated in Canadian dollars.

Fiscal 2007 vs. 2006

The decrease in amortization expenses in fiscal 2007, compared to 2006, despite the increase in the strength of the Canadian dollar, compared to the US dollar, as well as the acquisition of Consultronics in January 2006, is mainly due to the fact that some of our property, plant and equipment became fully amortized in 2007 and 2006.

Outlook for Fiscal 2009

For fiscal 2009, we expect the amortization of property, plant and equipment to increase in dollars due to the upgrade of our IT systems in fiscal 2008, the full impact of the acquisitions of Brix Networks and Navtel Communications, and, more importantly, the expansion of our own manufacturing and research and development facilities in China and India. Also, any increase in the strength of the Canadian dollar in the upcoming quarters would cause our amortization of property, plant and equipment to increase, as most of these are denominated in Canadian dollars.

AMORTIZATION OF INTANGIBLE ASSETS

In conjunction with the business combinations we completed over the past several years, we recorded intangible assets, primarily consisting of core technology. These intangible assets resulted in amortization expenses of $3.9 million, $2.9 million and $4.4 million for fiscal 2008, 2007 and 2006, respectively.

Fiscal 2008 vs. 2007

The increase in amortization expenses in fiscal 2008, compared to 2007, is mainly due to the acquisition of Brix Networks core technology, acquired in the third quarter of 2008 and the increased strength of the Canadian dollar compared to the US dollar.

Fiscal 2007 vs. 2006

The decrease in amortization expenses in fiscal 2007, compared to 2006, despite the increased strength of the Canadian dollar compared to the US dollar, and the acquisition of Consultronics in January 2006 is mainly due to the fact that some of our core technologies became fully amortized during fiscal 2005 and 2006; namely, those related to the acquisition of EXFO Burleigh, EXFO Photonics Solutions and EXFO Protocol.

Outlook for Fiscal 2009

For fiscal 2009, we expect the amortization of intangible assets to increase because we will have the full impact of the acquisition of Brix Networks.

Table of Contents

IMPAIRMENT OF LONG-LIVED ASSETS

Fiscal 2006

In June 2006, we entered into an agreement to sell one of our buildings (located in Rochester, NY) along with some equipment, and we recorded an impairment charge of $604,000 in the third quarter of fiscal 2006. The impairment charge represented the excess of the carrying value of these assets over the expected net selling price of $1.2 million. The sale of these assets was finalized in the fourth quarter of 2006 for the expected net selling price. These assets were related to the Life Sciences and Industrial Division.

GOVERNMENT GRANTS

During 1998, we entered into an agreement with the Quebec Minister of Industry, Commerce, Science and Technology ("The Minister"). Pursuant to this agreement, the Minister agreed to contribute, in the form of grants, up to CA$2.2 million over the period from January 1, 1998, through December 31, 2002, payable based on the number of full-time jobs created during that period.

The above grants were subject to the condition that jobs created pursuant to the agreement be maintained for a period of at least five years from the date of creation. Since the beginning of the program, we deferred CA$1.5 million (US$1.3 million) in the balance sheet until we received the final approval by the sponsor of the program related to jobs created. In fiscal 2006, the sponsor of the program granted us with its final approval and we recorded CA$1.5 million (US$1.3 million) in the earnings from operations in the statement of earnings of fiscal 2006.

Furthermore, until December 31, 2006, companies operating in the Quebec City area were eligible for a refundable credit granted by the Quebec provincial government. This credit was earned based on the increase of eligible production and marketing salaries incurred in the Quebec City area at a rate of 40%. From the total amount we claimed under this program, a sum of CA$1.1 million (US$1.1 million) was deferred in the balance sheet until we received the final approval of eligible salaries by the sponsor of the program. In fiscal 2007, the sponsor of the program granted us its final approval, and we recorded CA$1.1 million (US$1.1 million) in the earnings from operations in the statement of earnings of fiscal 2007.

As at August, 31, 2007 and 2008, we were not part of any significant grant programs.

INTEREST INCOME

Our interest income mainly resulted from our short-term investments, less interests and bank charges. Interest income amounted to $4.6 million, $4.7 million and $3.3 million for fiscal 2008, 2007 and 2006, respectively.

Fiscal 2008 vs. 2007

The slight decrease in interest income in fiscal 2008, compared to 2007, is mainly due to the decrease of our cash and short-term investments following the cash payment of $41.0 million for the acquisitions of Brix Networks and Navtel Communications, the redemption of share capital for $8.1 million in accordance with our share buy-back program as well as the general reduction in interest rates year-over-year. However, the significant increase in the average value of the Canadian dollar, compared to the US dollar year-over-year, contributed to the increase in our interest income in fiscal 2008, compared to 2007, as it is denominated in Canadian dollars. In addition, in fiscal 2008, we received interest of $241,000 by the Canadian tax authorities following the recovery during that period of prior years' income

tax receivable.

Fiscal 2007 vs. 2006

The increase in our interest income in fiscal 2007, compared to 2006, is mainly due to the increase in interest rates year-over-year. Also, our average cash position increased in fiscal 2007 due to cash flows from operating activities, which contributed to the further increase in interest revenue year-over-year.

Table of Contents

Outlook for Fiscal 2009

Assuming no acquisitions paid in cash are made in fiscal 2009 and relative stability in interest rates, we expect our interest income to decrease in 2009 as our average cash position is expected to be lower in fiscal 2009, considering the impact of our share repurchase programs and the cash used in fiscal 2008, namely for the consideration paid for the acquisitions of Brix Networks and Navtel Communications, the redemption of share capital and the additions of capital assets. This should be slightly mitigated by cash flows from operating activities in 2009.

FOREIGN EXCHANGE GAIN (LOSS)

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

Our foreign exchange gain amounted to $442,000 in fiscal 2008, compared to foreign exchange losses of $49,000 and $595,000 for 2007 and 2006, respectively.

In fiscal 2008, we witnessed instability in the value of the Canadian dollar as it fluctuated compared to the US dollar, which overall, resulted in a foreign exchange gain of $442,000. The average exchange rate was CA$1.0071 = US$1.00 in fiscal 2008, compared to a year-end exchange rate of CA$1.0564 = US$1.00 as at August 31, 2007, and CA$1.0626 = US$1.00 as at August 31, 2008.

In fiscal 2007, we also witnessed instability in the value of the Canadian dollar as it fluctuated compared to the US dollar, which overall, resulted in a small foreign exchange loss of $49,000. The average exchange rate was CA$1.1215 = US$1.00 in fiscal 2007, compared to a year-end exchange rate of CA$1.1066 = US$1.00 as at August 31, 2006, and CA$1.0564 = US$1.00 as at August 31, 2007.

It should be noted that foreign exchange rate fluctuations also flow through P&L line items as a significant portion of our operating items are denominated in Canadian dollars and we report our results in US dollars. Consequently, the significant increase in the average value of the Canadian dollar in fiscal 2008, compared to 2007, resulted in a significant and negative impact on our financial results. This was amplified by the fact that our operating activities incurred in Canadian dollars increased year-over-year. In fact, the average value of the Canadian dollar in fiscal 2008 was CA$1.0071 = US$1.00 versus CA$1.1215 = US$1.00 in 2007, representing an increase of 11.4% in the average value of the Canadian dollar year-over-year. In fiscal 2007, the average value of the Canadian dollar was CA$1.1215 = US$1.00 versus CA$1.1481 = US$1.00 in 2006, representing an increase of 2.4% in the average value of the Canadian dollar year-over-year.

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

INCOME TAXES

We recorded an income tax expense of $1.7 million in fiscal 2008, compared to an income tax recovery of $20.8 million in 2007, and an income tax expense of $2.6 million in 2006.

Fiscal 2006

Since fiscal 2003, we have maintained a full valuation allowance against our consolidated future income tax assets. In fiscal 2006, we recorded an income tax expense of $2.6 million. Most of this expense represented income taxes payable at the Canadian federal level, which were reduced by research and development tax credits that were recorded against gross research and development expenses in the statement of earnings of that year.

Table of Contents

Fiscal 2007

During fiscal 2007, after reviewing both available positive and negative evidence, and because we were in a cumulative profit position in the parent company (Canadian federal and provinces levels) and in one of our subsidiaries, located in the United States, and also because we expected to generate sufficient taxable income in future years, we concluded that it was more likely than not that future income tax assets and deferred non-refundable research and development tax credits of the parent company and a portion of our future income tax assets in the United States would be realizable. Consequently, we reversed a portion of our valuation allowance against future income tax assets in the amount of $24.6 million. From this amount, $16.2 million was related to the Canadian federal level, $3.2 million was related to the Canadian provincial levels and $5.2 million was related to the United States level. Future income tax assets recognized in 2007 were recorded in the income tax provision in the statement of earnings for that year.

However, in the United States (federal level), based on available positive and negative evidence as at August 31, 2007, as well as the level and the nature of cumulative and expected profits, we maintained a valuation allowance of $7.6 million on a portion of our future income tax assets in this tax jurisdiction because it was more likely than not that these assets would not be recovered. These future income tax assets consisted of operating losses carried forward.

In other tax jurisdictions where we have future income tax assets, we were still in a cumulative loss position as at August 31, 2007, and available negative evidence outweighed positive evidence. Consequently, for these tax jurisdictions, we maintained a full valuation allowance against our future income tax assets. As at August 31, 2007, the valuation allowance recorded for these tax jurisdictions amounted to $4.9 million and mainly related to deferred operating losses.

Except for the reversal of the valuation allowance in fiscal 2007, most of the income tax expenses recorded in fiscal 2007 represent income taxes payable at the Canadian federal level, which are reduced by research and development tax credits that are recorded against gross research and development expenses in the statements of earnings.

Fiscal 2008

During fiscal 2008, reductions to the Canadian federal statutory tax rate were substantively enacted. Therefore, Canadian federal future income tax assets decreased by $1.5 million and generated a future income tax expense in the same amount during the year.

In addition, during fiscal 2008, taking into account these new Canadian federal substantively enacted tax rates, we reviewed our tax strategy for the future use of our Canadian federal operating losses, research and development expenses, certain timing differences and research and development tax credits to minimize income taxes payable on future years' taxable income. Consequently, we amended our prior year's income tax returns to generate a net operating loss to be carried back to prior years, which reinstated previously used research and development tax credits. This resulted in an increase of $2.7 million in both our tax-related assets in the balance sheet and future income tax recovery in the statement of earnings for the year ended August 31, 2008.

Finally, during fiscal 2008, considering the expected positive impacts the acquisitions of Navtel Communications and Brix Networks will have on future years' taxable income at the United States federal level and because actual taxable income in the United States is greater than initially expected, we concluded that it was more likely than not that all future income tax assets of our existing consolidated US group would be recovered. Consequently, we reversed our valuation allowance against future income tax assets in the amount of $7.6 million. The portions of the valuation allowance that were reversed, and that were attributable to the effects of the Navtel Communications and Brix

Networks acquisitions—in the amount of $652,000 and $1.6 million, respectively—were included in the purchase price allocation of the related acquired businesses. The remainder of the reversal, in the amount of $5.3 million, has been recorded in income taxes in the statement of earnings for the year ended August 31, 2008.

Table of Contents

As at August 31, 2008, our net future income tax assets amounted to $24.7 million, and our non-refundable research and development tax credits amounted to $20.7 million. In order to realize these future income tax assets and non-refundable research and development tax credits, we need to generate approximately $174 million in pretax earnings at the Canadian federal level, approximately $33 million at the Canadian provincial levels, and approximately $37 million at the United States federal level.

Based on the existing and expected levels of pretax earnings in these tax jurisdictions, we believe that we should be able to recover our income tax assets at the Canadian federal level, at the Canadian provincial levels, and at the United States federal level over the next seven years, four years and nine years, respectively.

Valuation allowance

As at August 31, 2008, we were still in a cumulative loss position in certain of our subsidiaries and negative evidence outweighed positive evidence. For these subsidiaries, we maintained a full valuation allowance against our future income tax assets. As at August 31, 2008, the valuation allowance for these subsidiaries amounted to $15.5 million and mainly related to operating losses and research and development expenses carried forward. Of the global valuation allowance of $15.5 million, $8.2 million related to Brix Networks. In the event that we reverse a portion of or all the valuation allowance, the amount of such reversal would reduce the amount of goodwill recognized for this acquisition.

Please refer to note 15 of our consolidated financial statements included elsewhere in this Annual Report for more details on income taxes and a full reconciliation of the income tax provision.

EXTRAORDINARY GAIN

In conjunction with the acquisition of Navtel Communications, we recorded negative goodwill in the amount of $3.0 million. This negative goodwill has been recorded as an extraordinary gain in the statement of earnings for fiscal 2008.

LIQUIDITY AND CAPITAL RESOURCES

Cash Requirements and Capital Resources

As at August 31, 2008, cash and short-term investments totalled $87.5 million, while our working capital was at $144.6 million. Our cash and short-term investments decreased $42.2 million in fiscal 2008, compared to 2007, mainly due to the cash payments of $41.0 million, $6.5 million and $8.1 million for the acquisitions of Brix Networks and Navtel Communications, the purchases of capital assets and the redemption of share capital, respectively. On the other hand, operating activities generated cash flows of $13.8 million. We also recorded an unrealized foreign exchange gain on our cash and short-term investments of $0.4 million. This unrealized foreign exchange gain resulted from the translation, in US dollars, of our Canadian-dollar-denominated cash and short-term investments and was included in the accumulated other comprehensive income in the balance sheet.

Our short-term investments consist of commercial paper issued by ten (seven as at August 31, 2007) high-credit quality corporations and trusts; therefore, we consider the risk of non-performance of these financial instruments to be limited. None of these debt instruments are expected to be affected by a liquidity risk; and none of them represents asset-backed commercial paper. For the purposes of managing our cash position, we have established a cash management policy, which we follow and monitor on a regular basis. These short-term investments will be used for

working capital and other general corporate purposes, including other potential acquisitions and our share repurchase programs.

Table of Contents

We believe that our cash balances and short-term investments will be sufficient to meet our liquidity and capital requirements for the foreseeable future, including the cash contingent consideration payable for the acquisition of Brix Networks and the effect of our share repurchase programs. In addition to these assets, we have unused available lines of credit totaling $10.5 million for working capital and other general corporate purposes and unused lines of credit of $18.5 million for foreign currency exposure related to forward exchange contracts. However, possible operating losses and/or possible investments in or acquisitions of complementary businesses, products or technologies may require additional financing. There can be no assurance that additional debt or equity financing will be available when required or, if available, that it can be secured on satisfactory terms. Our lines of credit bear interest at prime rate.

As at August 31, 2008, our commitments under operating leases amounted to $3.6 million in 2009, $3.1 million in 2010, $1.5 million in 2011, $629,000 in 2012 and $57,000 in 2013 and after, for total commitments of $8.9 million.

Sources and Uses of Cash

We finance our operations and meet our capital expenditure requirements mainly through cash flows from operating activities, the use of our cash and short-term investments as well as the issuance of subordinate voting shares.

Operating Activities

Cash flows provided by operating activities were $13.8 million in fiscal 2008, compared to $14.4 million in 2007 and $12.3 million in 2006.

Fiscal 2008 vs. 2007

Cash flows provided by operating activities in fiscal 2008 were attributable to the net earnings after items not affecting cash of $34.7 million, offset in part by the negative net change in non-cash operating items of $20.9 million. The negative net change in non-cash operating items was mainly due to the negative effect on cash of the increase of $4.3 million of our accounts receivable, the negative effect on cash of the increase of $12.8 million of our income tax and tax credits recoverable, the negative effect on cash of the increase of $2.2 million of our inventories as well as the negative effect on cash of the decrease of $1.4 million of our accounts payable and accrued liabilities. The increase of our accounts receivable is directly attributable to the increase in sales year-over-year. The increase in our income taxes and tax credits is mainly due to the increase in our tax credits recoverable that were earned during the year but not yet recovered as well as the effect of the change in our tax strategy, explained elsewhere in this document. This increase was mostly offset by the positive effect on cash of the decrease of our future income tax assets (in items not affecting cash), which also resulted from the change in the tax strategy. The increase in our inventories resulted from expected increased sales activities for the next quarters. The decrease in our accounts payable and accrued liabilities is due to the timing of certain purchases and payments.

Fiscal 2007 vs. 2006

Cash flows provided by operating activities in fiscal 2007 were attributable to the net earnings after items not affecting cash of $24.6 million, less the negative net change in non-cash operating items of $10.2 million. Our accounts receivable, our income taxes and tax credits recoverable as well as our inventories increased in fiscal 2007, resulting in negative effects on cash flows of $5.5 million, $3.4 million and $5.5 million, respectively. However, our accounts payable and accrued liabilities increased during fiscal 2007, resulting in a positive effect on cash flows of $4.1 million. The increase in sales year-over-year explains the increase in accounts receivable. Also, one-time recognition of prior years' non-refundable tax credits of $3.2 million explains most of the increase in our income taxes and tax credits recoverable year-over-year. Furthermore, increased sales activities in fiscal 2007 resulted in higher inventory levels in 2007 in order to sustain these additional sales activities. However, increased levels of activities in

fiscal 2007, compared to 2006, resulted in an increase in our accounts payable and accrued liabilities year-over-year.

Table of Contents

Investing Activities

Cash flows used by investing activities amounted to $4.2 million in fiscal 2008, compared to $16.1 million in 2007 and $13.2 million in 2006.

Fiscal 2008 vs. 2007

In fiscal 2008, we disposed (net of acquisitions) of $43.3 million worth of short-term investments to pay for the cash consideration of $41.0 million for the two business combinations closed during the year. Also, we paid $6.5 million for the purchase of capital assets.

Fiscal 2007 vs. 2006

In fiscal 2007, we acquired (net of sales) $13.6 million worth of short-term investments and paid $5.6 million for the purchase of capital assets. On the other hand, in fiscal 2007, we received net proceeds of $3.1 million from the disposal of capital assets.

Financing activities

Cash flows used by financing activities amounted to $8.0 million in fiscal 2008, compared to cash flows provided of $330,000 in 2007 and of $142,000 in 2006.

Fiscal 2008 vs. 2007

In fiscal 2008, we redeemed share capital for a cash consideration of $8.1 million. However, during that year, exercise of stock options generated $61,000 ($557,000 and $802,000 in fiscal 2006 and 2007, respectively).

FORWARD EXCHANGE CONTRACTS

We utilize forward exchange contracts to manage our foreign currency exposure. Our policy is not to utilize those derivative financial instruments for trading or speculative purposes.

Our forward exchange contracts, which are used to hedge anticipated US-dollar-denominated sales, qualify for hedge accounting; therefore, foreign exchange translation gains and losses on these contracts are recognized as an adjustment of the revenues when the corresponding sales are recorded.

As at August 31, 2008, we held forward exchange contracts to sell US dollars at various forward rates, which are summarized as follows:

Expiry dates	Contractual amounts	Weighted average contractual forward rates
September 2008 to August 2009	$36,600,000	1.0686
September 2009 to August 2010	$17,400,000	1.0535
	$2,400,000	1.0619

September 2010 to August 2011

As at August 31, 2008, the fair value of our forward exchange contracts, which represents the amount we would receive or pay to settle the contracts based on the forward exchange rate at year end, represented net gains of $62,000 ($3.4 million as at August 31, 2007).

Table of Contents

CONTINGENCY

On November 27, 2001, a class-action suit was filed in the United States District Court for the Southern District of New York against EXFO, four of the underwriters of our Initial Public Offering and some of our executive officers pursuant to the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder and Sections 11, 12 and 16 of the Securities Act of 1933. This class action alleges that EXFO's registration statement and prospectus filed with the Securities and Exchange Commission on June 29, 2000, contained material misrepresentations and/or omissions resulting from (i) the underwriters allegedly soliciting and receiving additional, excessive and undisclosed commissions from certain investors in exchange for which they allocated material portions of the shares issued in connection with EXFO's Initial Public Offering; and (ii) the underwriters allegedly entering into agreements with customers whereby shares issued in connection with EXFO's Initial Public Offering would be allocated to those customers in exchange for which customers agreed to purchase additional amounts of shares in the after-market at predetermined prices.

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

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

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

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

69

Table of Contents

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

Due to the inherent uncertainties of litigation, it is not possible to predict the final outcome of the case, nor to determine the amount of any possible losses. We will continue to defend our position in this litigation that the claims against EXFO, and our officers, are without merit. Accordingly, no provision for this case has been made in the consolidated financial statements as at August 31, 2008.

SHARE CAPITAL AND STOCK-BASED COMPENSATION PLANS

Share Capital

As at November 3, 2008, EXFO had 36,643,000 multiple voting shares outstanding, entitling to ten votes each and 30,606,791 subordinate voting shares outstanding. The multiple voting shares and the subordinate voting shares are unlimited as to number and without par value. In fiscal 2008, we redeemed 1,682,921 subordinated voting shares for a total consideration of $8.1 million based on our share buy-back program.

Long-Term Incentive Plan and Deferred Share Unit Plan

The aggregate number of subordinate voting shares covered by stock options, restricted share units (RSUs) and deferred share units (DSUs) granted under the Long-Term Incentive Plan and the Deferred Share Unit Plan was 2,748,457 as at August 31, 2008. The maximum number of subordinate voting shares issuable under these two plans cannot exceed 6,306,153 shares. The following tables summarize information about stock options, RSUs and DSUs granted to the members of the Board of Directors and to Management and Corporate Officers of the company and its subsidiaries as at August 31, 2008:

Stock Options	Number	% of issued and outstanding	Weighted average exercise price
Chairman of the Board, President and CEO (one individual)	179,642	10%	$9.05
Board of Directors (five individuals)	194,375	11%	$6.23
Management and Corporate Officers (eight individuals)	212,139	11%	$14.49
	586,156	32%	$10.08

Restricted Share Units (RSUs)	Number	% of issued and outstanding
Chairman of the Board, President and CEO (one individual)	85,460	10%
Management and Corporate Officers (ten individuals)	238,069	28%
	323,529	38%

Table of Contents

Deferred Share Units (DSUs)	Number	% of issued and outstanding
Board of Directors (four individuals)	79,185	100%

OFF-BALANCE SHEET ARRANGEMENTS

As at August 31, 2008, our off-balance sheet arrangements consisted of letters of guarantee and forward exchange contracts. As at August 31, 2008, our letters of guarantee amounted to $5.7 million; these letters of guarantee expire at various dates through fiscal 2010. From this amount, we had $1.5 million worth of letters of guarantee for our own selling and purchase requirements, which were reserved from one of our lines of credit. The remainder in the amount of $4.2 million was used to secure our line of credit in Chinese currency. This line of credit was unused as at August 31, 2008. These letters of guarantee were secured by short-term investments. Our forward exchange contracts are described above.

VARIABLE INTEREST ENTITY

As of August 31, 2008, we did not have interests in any variable interest entities.

Table of Contents

Item 6. Directors, Senior Management and Employees

A. Directors and Senior Management

The following table sets forth information about our executive officers, senior managers and Directors as of November 3, 2008.

Name and Municipality of Residence	Positions with EXFO
PIERRE-PAUL ALLARD Pleasanton, California	Independent Director
JON BRADLEY Worminghall, United Kingdom	Vice-President, Telecom Sales - International
STEPHEN BULL Quebec City, Quebec	Vice-President, Research and Development, Telecom Division
NORMAND DUROCHER St-Sauveur, Quebec	Vice-President, Human Resources
ALLAN FIRHOJ Georgestown, Ontario	Vice-President and General Manager, Life Sciences and Industrial Division
ROBERT FITTS Minesing, Ontario	Vice-President, Corporate Development
ÉTIENNE GAGNON Quebec City, Quebec	Vice-President, Telecom Product Management and Marketing
LUC GAGNON St-Augustin-de-Desmaures, Quebec	Vice-President, Telecom Manufacturing Operations and Customer Service
VIVIAN HUDSON Beaconsfield, Quebec	Vice-President and General Manager, EXFO Service Assurance Business Unit
GERMAIN LAMONDE St-Augustin-de-Desmaures, Quebec	Chairman of the Board, President and Chief Executive Officer
PIERRE MARCOUILLER Magog, Quebec	Independent Director
GUY MARIER Lakefield Gore, Quebec	Independent Lead Director
PIERRE PLAMONDON Quebec City, Quebec	Vice-President, Finance and Chief Financial Officer
BENOIT RINGUETTE Boischatel, Quebec	General Counsel and Corporate Secretary
JOSEPH SUTHERLAND Apsley, Ontario	Vice-President and General Manager, Navtel Product Group
DAVID A. THOMPSON Newton, North Carolina	Independent Director
ANDRÉ TREMBLAY Outremont, Quebec	Independent Director
DANA YEARIAN Lake Forest, Illinois	Vice-President, Telecom Sales - Americas

The address of each of our executive officers, senior managers and Directors is c/o EXFO Electro-Optical Engineering Inc., 400 Godin Avenue, Quebec, Quebec, Canada. The following is a brief biography of each of our executive officers, senior managers and Directors.

72

Table of Contents

Pierre-Paul Allard was appointed a member of EXFO's Board of Directors in September 2008 and has been a board member of many other technology companies in Canada and in the US. Today, he is also an active philanthropist for l'Institut de Cardiologie de Québec. Mr. Allard is presently Area Vice-President, Sales for Cisco Systems Inc., where he has held several management positions over the years. Currently, he is responsible for sales and field operations of Cisco's Global Enterprise Client segment, focusing on new market opportunities, accelerated revenue growth and increased customer satisfaction. Prior to joining Cisco, Mr. Allard worked for IBM Canada for 12 years. In 2002, Mr. Allard co-chaired the Canadian e-Business Initiative, a private-public partnership aiming to measure the role e-Business plays in increasing productivity levels, job creation and competitive position. In 1998, he was the laureate of the Arista-Sunlife Award, for Top Young Entrepreneur in Large Enterprise, by the Montreal Chamber of Commerce. In 2003, he received the Queen's Golden Jubilee Medal, which highlights significant contributions to Canada. In the same year, he was also awarded the prestigious Trudeau Medal from the University of Ottawa, School of Management. Pierre-Paul Allard holds a bachelor's and masters' degree in Business Administration from the University of Ottawa, School of Management, in Canada.

Jon Bradley was appointed Vice-President, Telecom Sales - International for EXFO in March 2007. He is responsible for managing telecom sales, both direct and indirect, and for the execution of sales strategies in the international arena. He manages an accomplished and diverse sales and distribution team. As a member of the Strategy and Management Committees, he also develops corporate strategy for EXFO. Prior to his appointment as Vice-President, International Telecom Sales, Dr. Bradley held the position of Sales Director for the Europe, Middle East and Africa (EMEA) territory from 2003 to 2007, and Regional Sales Manager from 1999 to 2003. Before joining EXFO in 1999, Dr. Bradley was employed as Sales and Marketing Director by Queensgate Instruments (UK) from 1997 to 1999 and as Sales Engineer by Lambda Photometrics (UK) from September 1993 to September 1997. Dr. Bradley holds an honors degree in chemistry, as well as a Ph.D. in Raman spectroscopy from the University of Durham in the United Kingdom.

Stephen Bull was appointed our Vice-President, Research and Development, Telecom Division in December 1999. He joined us in July 1995 and held the positions of Assistant Director-Engineering from September 1997 to December 1999 and Group Leader (Engineering Management) from July 1995 to September 1997. From June 1990 to March 1995, Mr. Bull held the position of General Manager and Managing Director for Space Research Corporation, a military engineering company in Belgium. Mr. Bull holds a bachelor's degree in Electrical Engineering from Laval University in Quebec City, Canada.

Normand Durocher was appointed Vice-President of Human Resources in April 2004. In addition to managing our human resources team, his main responsibility is to develop and implement a human resources plan that supports EXFO's business strategy. Mr. Durocher began his career in labor relations in the Cable division of Nortel and then took on several key roles at Nortel Networks and Nordx/CDT, all relating to human resources and operations. Since then, Normand Durocher has accumulated more than 25 years' experience in operations and human resources management within the telecommunications industry. Prior to joining EXFO, Mr. Durocher ran his own human resources consulting business. Normand Durocher holds a Bachelor of Science from the University de Montreal and also completed the Advanced Human Resources program at Dalhousie University in Halifax, Nova Scotia, Canada.

Allan Firhoj was appointed Vice-President and General Manager, Life Sciences and Industrial Division in July 2003. Prior to that, he held the position of General Manager of EXFO Photonic Solutions Inc. since November 2001. He is responsible for the overall strategic direction and management of the Life Sciences and Industrial Division. Mr. Firhoj joined EFOS Inc. in 1996, where he was responsible for Sales, Marketing and Business Development of the Dental Curing-Products Division. Following the sale of this division to Dentsply International in 1997, he was appointed Director of Marketing and Business Development. Mr. Firhoj continued in this capacity until being appointed to the position of General Manager of EXFO Photonic Solutions Inc. Prior to joining us, Mr. Firhoj spent six years with The Horn Group, a plastics business involved in medical devices/instrumentation and office communication equipment.

He successively held the positions of ISO 9000 Implementation Manager, Technical Sales Manager as well as Marketing and Business Development Manager. In this latter role, he successfully contributed to increasing sales in their medical market by an annual average of 60% during a three-year period. Mr. Firhoj holds a bachelor's degree in Political Science from Bishop's University in Lennoxville, Quebec.

Table of Contents

Robert Fitts was nominated Vice-President, Corporate Development in May 2007. His main role is to seek out new business opportunities (such as strategic alliances, OEM agreements and acquisitions), which will allow the company to enhance its competitive position in the telecom test and measurement market. Prior to this appointment, Mr. Fitts acted as Vice-President, Product Management - Copper Access Products, since our acquisition of Consultronics in January 2006. Before taking on this position, Mr. Fitts was Executive Vice-President at Consultronics, where he began his career more than 20 years earlier. He therefore has extensive experience in the telecommunications testing industry and, more specifically, has been an active participant in the field of local-loop testing, DSL, IPTV and VoIP. Robert Fitts attended the University of Guelph in Ontario, Canada, and has a degree in electrical engineering (computer option) technology from Fleming College, near Toronto, Canada. Mr. Fitts is also a graduate of the executive program given by Queens University School of Business, located in Kingston, Ontario.

Étienne Gagnon was appointed Vice-President, Telecom Product Management and Marketing in May 2003 and, in May 2007, he took on the responsibility of all our telecom business units – Optical; Transport and Datacom; and Access. As such, he is responsible for EXFO's general marketing direction on both the product level and communications level. Mr. Étienne Gagnon is not related to Mr. Luc Gagnon. For nearly three years, before returning to EXFO in early 2003, Mr. Gagnon was Vice-President of Sales and Marketing at TeraXion, an optical component manufacturer based in Quebec City. Mr. Gagnon began his career as a design engineer for Bombardier/Canadair, where he worked on the Canadian Regional Jet project between 1990 and 1993. Later, he held the position of Business Development Manager for France Telecom in Hungary. In 1994, he joined EXFO's European office as a Regional Sales Manager, and in 1996, he was brought back to Quebec City to head the OSP marketing group. Mr. Gagnon then went on to become the director of our Outside Plant division in 1998, and remained in that function until he joined TeraXion in 2000. Etienne Gagnon holds a bachelor's degree in mechanical engineering from the University of Montreal's School of Engineering, and a master's degree in European business from the Ecole nationale supérieure des télécommunications in France.

Luc Gagnon was appointed Vice-President, Telecom Manufacturing Operations in May 2003 and, in May 2007, he also took on the vice-presidency of the Customer Services department. Mr. Luc Gagnon is not related to Mr. Étienne Gagnon. He is responsible for ensuring the smooth operation of all manufacturing activities, which include production, purchasing, product engineering, quality assurance, planning, manufacturing engineering, product configuration, transportation and customs, as well as material resources. In addition, he maintains an ongoing and efficient relation between the manufacturing process and the end customer. Prior to his nomination in 2003, Mr. Gagnon held the position of Production Director since 2000. Before joining EXFO, he had similar roles in several other high-technology companies. He worked for Mendes from 1999 to 2000, for C-MAC from 1997 to 1999, for STERIS from 1993 to 1997 and for MITEL from 1991 to 1993. Luc Gagnon holds a bachelor's degree in electrical engineering and master's degree in engineering, both from the Université de Sherbrooke, in Canada.

Vivian Hudson was nominated Vice-President and General Manager for EXFO's Service Assurance business unit in September 2008. Prior to joining EXFO, Ms. Hudson held various general management positions at Nortel, including those of General Manager for the Systems Integration unit for the Microsoft-Nortel Innovative Communications Alliance; the GSM business in France; and the High-Capacity Optical Networks group. Ms. Hudson first began at Nortel in 1990 and worked through the ranks, namely in European Marketing (based in the UK and in France), Optical Product Management, Wireless Operations, as well as Optical and Wireless General Management. Prior to this, she held positions at Bell Canada as a business/services planner, at Canadian Pacific as a telecommunications networking end user, and at DMR as a telecommunications consultant. A recognized global high-tech business leader, Ms. Hudson has also pursued sustainable development activities in the telecommunications area and serves on several boards. Namely, she is a governor of Carleton University's Board of Governors and sits on the board of Shad International. She also holds the ICD.D designation from the Institute of Corporate Directors of Canada. Vivian Hudson holds a Bachelor of Science from Université Laval in Quebec City, and a Master of Business Administration from McGill University in Montreal.

74

Table of Contents

Germain Lamonde, a company founder, has been Chairman of the Board, President and CEO of EXFO since its inception in his apartment in 1985. Mr. Lamonde, who is responsible for the overall management and strategic direction of EXFO and its subsidiaries and divisions, has grown the company from the ground up into global leader in the telecommunications test and measurement industry. Mr. Lamonde has served on the boards of several organizations such as the Canadian Institute for Photonic Innovations, the Pole QCA Economic Development Corporation and the National Optics Institute of Canada to name a few. Germain Lamonde holds a bachelor's degree in physics engineering from the University of Montreal's School of Engineering (École Polytechnique), a master's degree in optics from Laval University, and is also a graduate of the Ivey Executive Program offered by the University of Western Ontario.

Pierre Marcouiller has served as our Director since May 2000. Mr. Marcouiller is Chairman of the Board and CEO of Camoplast Inc., an industrial manufacturer specializing in rubber tracks, molded composites, thermoplastic components and off-road tracked vehicles. Prior to joining Camoplast, Mr. Marcouiller was President and General Manager of Venmar Ventilation Inc. (1988-1996), where he was the controlling shareholder from 1991 to 1996. Mr. Marcouiller is also a Director of Canam Group Inc., an industrial company specialized in the design and fabrication of construction products and solutions in the commercial, industrial, institutional, residential, and bridge and highway infrastructures markets. Mr. Marcouiller also holds directorships in other privately held companies. Pierre Marcouiller holds a bachelor's degree in business administration from the Université du Québec à Trois-Rivières and an MBA from the Université de Sherbrooke.

Guy Marier has served as our Director since January 2004. Formerly President of Bell Québec (1999 to 2003), Guy Marier completed his successful 33-year career at Bell as Executive Vice-President of the Project Management Office, before retiring at the end of 2003. From 1988 to 1990, Mr. Marier headed Bell Canada International's investments and projects in Saudi Arabia and, for the three following years, served as President of Télébec. He then returned to the parent company to hold various senior management positions. Guy Marier holds a Bachelor of Arts from the University of Montreal and a Bachelor of Business Administration from the Université du Québec à Montréal.

Pierre Plamondon has been our Vice-President, Finance and Chief Financial Officer since January 1996. Prior to joining us, Mr. Plamondon served as Senior Manager for Price Waterhouse, now PricewaterhouseCoopers LLP, from September 1981 to December 1995 in Canada and France. Pierre Plamondon holds a bachelor's degree in business administration and a license in accounting, both from Laval University in Quebec City, Canada. Mr. Plamondon has been a member of the Canadian Institute of Chartered Accountants since 1983 and a member of the Board of Directors of SOVAR Inc. (Société de valorisation des applications de la recherche de l'Université Laval) since December 2000.

Benoit Ringuette has been our in-house Legal Counsel and Corporate Secretary since April 2004. Prior to joining EXFO, Mr. Ringuette practiced mainly in commercial, corporate and securities law from 1998 to 2003 as an associate in the law firms of O'Brien, Flynn Rivard in Quebec City and Desjardins Ducharme Stein Monast in Quebec City. Mr. Ringuette has been a member of the Quebec Bar since 1998. Mr. Ringuette holds a bachelor's degree in Civil Law and a master's degree in Business Administration (MBA) from Laval University in Quebec City, Canada.

Joseph Sutherland was appointed Vice-President and General Manager of Navtel Product Group in March 2008, following EXFO's acquisition of Navtel Communications Inc., an Ontario-based, communications software company. Mr. Sutherland was President of Navtel Communications Inc. from 2005 to 2008, and from 1976 to 1998. In this role, he was responsible for growing the company from inception to over $40 million in revenue with several hundred employees. During his tenure at Navtel, Mr. Sutherland raised significant venture capital, conducted several acquisitions and successfully divested Navtel to a large European public company. After divesture, he continued on as Divisional President of GN Nettest and was part of the executive management team, participating in numerous acquisition and strategy development activities until his retirement in 1998. Prior to resuming his functions as President of Navtel in 2005, Mr. Sutherland served on several boards. Namely, from 1998 until his successful exit in

2004, he was Chairman of the Board of Toogood Financial Systems, a financial software company based in Richmond Hill, Ontario Mr. Sutherland completed an Executive Management Program in Marketing and Sales Management at the University of British Columbia in Canada.

Table of Contents

David A. Thompson has served as our Director since June 2000. Dr. David A. Thompson is currently Vice-President and Director of Hardware & Equipment Technology at Corning Cable Systems, where he has held this position since January 2006. Prior to this, he was Vice President and Director of Hardware & Equipment Technology Strategy for Corning Cable Systems from January 2002 to December 2005. Dr. Thompson first joined Corning Incorporated in 1976 as a Senior Chemist in glass research. He then took on several technology Directorships and strategic planning roles for Corning's Component and Photonics Technologies Division between 1988 and 1998; and in 1999, he was appointed technical leader for the creation of the new Samsung-Corning Micro-Optics joint venture. His last position at Corning prior to transferring to Corning Cable Systems in January 2002 was Division Vice-President for the Strategic Planning & Innovation Effectiveness in Research, Development and Engineering. David A. Thompson holds a Bachelor of Science in chemistry from Ohio State University and a doctorate in inorganic chemistry from the University of Michigan.

André Tremblay has served as our Director since June 2000. Mr. Tremblay is a Founder and Managing Partner of Trio Capital Inc, a private equity fund management company. He has more than 20 years experience in the telecommunications industry, having been actively involved in the conception, financing and management of several companies. As a special advisor to the President of Telesystem Ltd., and as President of Telesystem Enterprises Ltd. from 1992 to 1998, he managed a portfolio of telecommunication companies. For almost 10 years, he served as President and Chief Executive Officer of Microcell Telecommunications, a wireless network and service provider, which he led from its inception on through the different phases of its evolution. During that time, he has also provided early-stage financing, along with strategic advice and direction, for start-up technology firms. In 2005, he was appointed by Canada's Industry Minister as member of the Telecommunications Policy Review Panel to make recommendations on how to modernize Canada's telecommunication policies and regulatory framework. Mr. Tremblay holds bachelor's degrees in management and in accounting from Laval University, a master's degree in taxation from Université de Sherbrooke, and is also a graduate of Harvard Business School's Advanced Management Program.

Dana Yearian was appointed our Vice President, Telecom Sales - Americas in March 2007. Prior to this appointment, Mr. Yearian held the position of Vice-President, Telecom Sales – North America. He is responsible for managing telecom sales, both direct and indirect, and the execution of sales strategies across North, Central and South America. Mr. Yearian oversees all sales-related functions for the EXFO sales organization throughout this territory, including sales operations, global account management and partner programs. As a member of the Strategy and Management committees, he also helps develop corporate strategy. Prior to joining EXFO, Mr. Yearian held senior executive sales positions at Spirent Communications Service Assurance Division and Acterna Corp. Mr. Yearian also held various executive positions; namely, at Toshiba America, Silicon Sensors (Advanced Photonix, Inc.), and Impell Corporation (ABB Ltd.). Mr. Yearian holds a bachelor's degree in electrical engineering from the Illinois Institute of Technology in Chicago and has completed MBA course work at DePaul University, also in Chicago, Illinois, USA.

Term of Executive Officers

Executive officers are appointed annually by the Board of Directors and serve until their successors are appointed and qualified or until earlier resignation or removal.

Table of Contents

B. Compensation

Director Compensation

In the financial year ended August 31, 2008, each director who was not an employee of the Corporation or any of its subsidiaries received the level of compensation set forth in the table below as annual compensation payable in a combination of cash and Deferred Share Units ("DSUs") as chosen by the Director pursuant to the Deferred Share Unit Plan.

Annual Retainer for Directors (1)	CA$50,000 (2)	US$49,648 (3)
Annual Retainer for Lead Director	CA$5,000	US$4,965 (3)
Annual Retainer for Committee Chairman	CA$5,000	US$4,965 (3)
Annual Retainer for Committee Members	CA$3,000	US$2,979 (3)
Fees for all Meetings Attended per day in Person	CA$1,000	US$993 (3)
Fees for all Meetings Attended per day by Telephone	CA$500	US$496 (3)

(1) All the Directors elected to receive 50% of their Annual Retainer in form of Deferred Share Units except Mr. André Tremblay who elected to receive 100% of his Annual Retainer in form of Deferred Share Units.

(2) The Annual Retainer for Mr. David A. Thompson is US$50,000 (CA$50,355). The Annual Retainer for Mr. Pierre-Paul Allard will also be in US$.

(3) The compensation information has been converted from Canadian dollars to U.S. dollars based upon an average foreign exchange rate of CA$1.0071 = US$1.00 for the financial year ending August 31, 2008.

In the financial year ended August 31, 2008 and as of November 3, 2008, the Directors who were not employees received the following compensation in the form indicated:

Name	Annual Compensation Paid in Cash (US$) (1)	Annual Compensation Paid in DSUs (#) (2)	Estimated Value of DSUs at the time of grant (US$) (3)	Total Attendance Fees Paid in Cash (US$) (1)
Pierre-Paul Allard	–	–	–	–
Pierre Marcouiller (4)	30,781	5,174	24,824	5,461
Guy Marier (5)	35,746	5,174	24,824	8,440
Dr. David A. Thompson (6)	29,217	5,228	25,000	6,951
André Tremblay (7)	7,944	10,349	49,648	7,944
Michael Unger (8)	28,655	3,760	18,618	6,454

(1) The compensation information has been converted from Canadian dollars to U.S. dollars based upon an average foreign exchange rate of CA$1.0071 = US$1.00 for the financial year ending August 31, 2008 except for Mr. David A. Thompson who is paid in U.S. dollar for the portion of his annual retainer for Director. The Annual Compensation includes, as the case may be, the retainer for Director, Lead Director, Committee Members and Committee Chairman.

(2) Indicates the number of Subordinate Voting Shares granted under the Deferred Share Unit Plan. A DSU is converted in a Subordinate Voting Share when a Director ceases to be a member of the Board.

(3) The estimated value at the time of grant of a DSU is determined based on the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars, as required. The value at vesting of a DSU is equivalent to the market value of a Subordinate Voting Share when a DSU is converted to such Subordinate Voting Share.

(4) Member of the Audit Committee and the Human Resources Committee.

(5) Member of the Audit Committee and the Human Resources Committee, Lead Director and Chairman of the Human Resources Committee per interim in replacement of Mr. Unger and starting October 2008, he was confirmed as Chairman.

(6) Member of the Human Resources Committee and the Audit Committee since April 2008.

(7) Member of the Human Resources Committee and Chairman of the Audit Committee.

(8) Member of the Audit Committee and Chairman of the Human Resources Committee until his resignation that was effective on June 26, 2008.

Table of Contents

Executive Compensation

The table below shows compensation information during the three most recently completed financial years for Mr. Germain Lamonde, the Chairman of the Board, President and Chief Executive Officer of the Corporation, Mr. Pierre Plamondon, the Vice-President Finance and Chief Financial Officer and the three other most highly compensated executive officers of the Corporation and its subsidiaries who were serving the Corporation at the end of the financial year, (collectively, the "Named Executive Officers"). This information includes the U.S. dollar value of base salaries, bonus awards and Long-Term Incentive Plan grants, the number of options or Restricted Share Units granted, and other compensation, if any, whether paid or deferred.

Name and Principal Position	Financial Years	Salary (1) ($)	Bonus (2) ($)	Other Annual Compensation ($) (3)	Securities Under Options (4) (#)	Restricted Share Units (5) (#)	All Other Compensation ($)
Germain Lamonde, President and Chief Executive Officer	2008	347,533 (US) 350,000 (CA)	198,848 (US) 200,260 (CA)	-	-	29,910	-
	2007	294,334 (US) 330,096 (CA)	131,145 (US) 147,080 (CA)	-	-	25,347	-
	2006	271,753 (US) 312,000 (CA)	147,558 (US) 169,412 (CA)	-	11,218	21,477	-
Pierre Plamondon, Vice-President Finance and Chief Financial Officer	2008	201,569 (US) 203,000 (CA)	71,047 (US) 71,551 (CA)	-	-	9,637	5,240 (US) (6) 5,278 (CA)
	2007	173,862 (US) 194,986 (CA)	56,906 (US) 63,820 (CA)	-	-	12,930	4,836 (US) (6) 5,423 (CA)
	2006	165,691 (US) 190,230 (CA)	60,167 (US) 69,078 (CA)	-	3,653	6,994	4,283 (US) (6) 4,918 (CA)
Dana Yearian, Vice-President, Telecom Sales - Americas	2008	289,219 (US) 291,272 (CA)	4,826 (US) 4,861 (CA)	-	-	7,225	7,401 (US) (6) 7,453 (CA)
	2007	250,592 (US) 281,039 (CA)	8,326 (US) 9,338 (CA)	-	-	6,645	566 (US) (6) 634 (CA)
	2006	7,851 (US) (7) 9,014 (CA)	- -	-	-	5,000	236 (US) (6) 270 (CA)
Jon Bradley, Vice-President, Telecom Sales - International	2008	296,960 (US) 299,069 (CA) 149,276 (£)(8)	34,940 (US) 35,188 (CA) 17,563 (£)(8)	-	-	6,122	-
	2007	226,991 (US) 254,571 (CA) 116,011 (£)(8)	19,470 (US) 21,836 (CA) 9,951 (£)(8)	-	-	-	-
	2006	194,908 (US) 223,774 (CA) 108,778 (£)(8)	12,684 (US) 14,563 (CA) 7,079 (£)(8)	-	-	2,500	-
Stephen Bull, Vice-President. Research and Development, Telecom Division	2008	173,369 (US) 174,600 (CA)	49,835 (US) 50,189 (CA)	-	-	7,340	4,235 (US) (6) 4,265 (CA)
	2007	141,891 (US) 159,131 (CA)	35,399 (US) 39,700 (CA)	-	-	15,905	3,657 (US) (6) 4,102 (CA)
	2006	133,917 (US) 153,750 (CA)	33,144 (US) 38,053 (CA)	-	1,803	4,602	3,330 (US) (6) 3,823 (CA)

(1) The compensation information for Canadian residents has been converted from Canadian dollars to U.S. dollars based upon an average foreign exchange rate of CA$1.0071 = US$1.00 for the financial year ending August 31, 2008, CA$1.1215 = US$1.00 for the financial year ending August 31, 2007 and CA$1.1481 = US$1.00 for the financial year ending August 31, 2006. The currency conversions cause these reported salaries to fluctuate from year-to-year because of the fluctuation in exchange rate.

(2) A portion of the bonus amounts is paid in cash in the year for which they are awarded and the balance is paid in cash in the year following the financial year for which they are awarded.

(3) Indicates only an aggregate amount if such amount is equivalent or greater than $50,000 and 10% of the total of the annual salary and bonus of the Named Executive Officer for the financial year ended August 31, 2008.

(4) Indicates the number of Subordinate Voting Shares underlying the options granted under the Long-Term Incentive Plan during the financial year indicated.

Table of Contents

(5) Indicates the number of Restricted Share Units granted under the Long-Term Incentive Plan during the financial year indicated.
(6) Indicates the amount contributed by the Corporation during the financial year indicated to the Deferred Profit Sharing Plan or 401K Plan, as applicable, for the benefit of the Named Executive Officer. Mr. Lamonde is not eligible to participate in the Deferred Profit Sharing Plan and Mr. Bradley did not participate.
(7) This amount represents the salary paid to Mr. Yearian from August 14, 2006 until August 31, 2006 which is based on an annual salary amounted to US$173,424 (CA$199,109) for the financial year ended August 31, 2006.
(8) The compensation information for UK resident has been converted from British Pound to U.S. dollars based upon an average foreign exchange rate of £1.9893 = US$1.00 for the financial year ended August 31, 2008, £1.9566 = US$1.00 for the financial year ended August 31, 2007 and £1.7918 = US$1.00 for the financial year ended August 31, 2006. For the conversion from U.S. dollars to Canadian dollars, please refer to note 1 above. The currency conversions cause these reported salaries to fluctuate from year-to-year because of the fluctuation in exchange rate.

Employment Agreements

We have an employment agreement with Mr. Germain Lamonde. The agreement is for an indeterminate period and the compensation is reviewed annually. In the event of the termination of Mr. Lamonde's employment without cause, Mr. Lamonde will be entitled to severance payments (in no case exceeding 24 months of remuneration) and the immediate vesting of all stock options and RSUs. In addition, in the event that Mr. Lamonde's employment is terminated following a merger or an acquisition by a third party of substantially all of the Corporation's assets or of the majority of its share capital, he will be entitled to severance payments (in no case exceeding 24 months remuneration plus health benefits) and to the immediate vesting of all stock options and RSUs. If Mr. Lamonde voluntarily resigns, he will be entitled to immediate vesting of all stock options and RSUs.

We have an employment agreement with Mr. Pierre Plamondon, our Vice-President, Finance and Chief Financial Officer. The agreement is for an indeterminate period and the compensation is reviewed annually. In the event of termination of Mr. Plamondon's employment without cause, Mr. Plamondon will be entitled to severance payments (in no case exceeding 12 months of the current base salary). In addition, in the event Mr. Plamondon's employment is terminated following a merger or an acquisition by a third party of substantially all of the Corporation's assets or of the majority of its share capital, he will be entitled to severance payments (in no case exceeding 18 months remuneration plus health benefits) and to the immediate vesting of all stock options and RSUs.

We have an employment agreement with Mr. Dana Yearian, our Vice-President, Telecom Sales - Americas. The agreement is for an indeterminate period and the compensation is reviewed annually. In the event of termination of Mr. Yearian's employment without cause, Mr. Yearian will be entitled to severance payments (in no case exceeding 12 months of the current base salary). In addition, in the event Mr. Yearian's employment is terminated following a merger or an acquisition by a third party of substantially all of the our assets or of the majority of our share capital, he will be entitled to severance payments (in no case exceeding 18 months remuneration plus health benefits) and to the immediate vesting of all stock options and RSUs.

We have an employment agreement with Mr. Jon Bradley, our Vice-President, Telecom Sales - International. The agreement is for an indeterminate period and the compensation is reviewed annually. In the event of termination of Mr. Bradley's employment without cause, Mr. Bradley will be entitled to severance payments (in no case exceeding 12 months of the current base salary). In addition, in the event Mr. Bradley's employment is terminated following a merger or an acquisition by a third party of substantially all of the our assets or of the majority of our share capital, he will be entitled to severance payments (in no case exceeding 18 months remuneration plus health benefits) and to the immediate vesting of all stock options and RSUs.

We have an employment agreement with Mr. Stephen Bull, the Corporation's Vice-President, Research and Development, Telecom Division. The agreement is for an indeterminate period and the compensation is reviewed annually. In the event of termination of Mr. Bull's employment without cause, Mr. Bull will be entitled to severance payments (in no case exceeding 12 months of the current base salary). In addition, in the event Mr. Bull's employment is terminated following a merger or an acquisition by a third party of substantially all of the Corporation's assets or of the majority of its share capital, he will be entitled to severance payments (in no case exceeding 18 months remuneration plus health benefits) and to the immediate vesting of all stock options and RSUs.

Table of Contents

Key Elements and Policies for Compensation of Executive Officers

Our executive compensation plans are designed to attract, retain and motivate key executives who directly impact our long-term success and the creation of shareholder value. In determining executive compensation, the Committee considers the following four principles:

- Performance-based: Executive compensation levels reflect both corporation and individual results based on specific quantitative and qualitative objectives established at the start of each financial year in keeping with our long-term strategic objectives.

- Aligned with shareholder interests: A significant proportion of incentive compensation for executives is composed of equity awards to ensure that executives are aligned with the principles of sustained long-term shareholder value growth.

- Market competitive: Compensation of executives is designed to be externally competitive when compared against executives of comparable peer companies, and in consideration of our results relative to the results of peers.

- Individually equitable: Compensation levels are also designed to reflect individual factors such as scope of responsibility, experience, and performance against individual measures.

The key elements of our 2008 executive compensation program were Base salary, the Short Term Incentive Plan, and stock-based incentive compensation delivered through the Long Term Incentive Plan. To determine appropriate compensation levels for each pay component, the Committee considered all elements of the executive compensation program. The Committee did not assign specific weightings to any key element of our 2008 executive compensation program.

Base Salaries

In establishing the base salaries of senior officers, including the President and Chief Executive Officer, we take into consideration responsibilities, job descriptions and salaries paid by other similar Canadian organizations for positions similar in magnitude, scope and complexity. The Committee's objective is to align executive compensation levels with the median compensation offered within a reference group of comparable companies that are similar in size to the Corporation, with a particular focus on those within the high-technology/telecommunications and manufacturing-durable goods industries. The Committee reviews the base salary of each senior officer on an annual basis and recommends that our Board approve appropriate adjustments, if required, within the salary range in order to maintain a competitive position within the market place.

Short-Term Incentive Compensation

The short-term incentive plan ("STIP") provides senior executives with the opportunity to earn annual bonuses based on our financial performance and the achievement of strategic corporate and business unit objectives established on a yearly basis.

Target payout levels for Named Executive Officers eligible for incentive bonuses in the year ended August 31, 2008 were established to be in line with the objective of the Committee to align compensation with the median compensation offered in the reference group. The minimum, target and maximum payouts to senior officers under the STIP (expressed as a percentage of their base salary) for the financial year ending August 31, 2008 were as follows:

Our President and Chief Executive Officer, Mr. Germain Lamonde, has a short term incentive target of 55% of his annual base salary. That bonus is based on the achievement of financial, strategic and individual objectives as shown in the following table.

Our Chief Financial Officer, Mr. Pierre Plamondon, has a short term incentive target of 35% of his annual base salary. That bonus is based on the achievement of financial, strategic and individual objectives as shown in the following table.

Table of Contents

Our Vice-President, Research and Development, Telecom Division, Mr. Stephen Bull, has a short term incentive target of 30% of his annual base salary. That bonus is based on the achievement of financial, strategic and individual objectives as shown in the following table.

Measure (1)	Weighting Mr. Lamonde, Mr. Plamondon and Mr. Bull
Sales	35%
Earnings	15%
Gross margin	25%
Customer satisfaction (quality and on time delivery)	25%
Growth metrics	10%
Personal objectives (multiplier)	0% - 125%

(1) Sales, Earnings, Gross margin and Customer satisfaction measures are established to provide a metric from 0% to 150% and such a metric is multiplied by the personal objectives measure. This result is then multiplied by the short term incentive target % of the individual annual base salary.

Our Vice-President, Telecom Sales - International, Mr. Jon Bradley, and Vice-President, Telecom Sales - Americas, Mr. Dana Yearian, do not participate in the short term incentive plan that is available to the company's other senior executives. Instead, Mr. Bradley and Mr. Yearian participate in the company's sales incentive plan (SIP). Under the SIP, Mr. Bradley and Mr. Yearian have target incentives of 40% of their annual base salaries. The SIP is based 40% on the achievement of revenue targets (billings), 40% on margin targets and 20% on management objectives.

Long-Term Incentive Compensation

Long-Term Incentive Plan

We have a Long-Term Incentive Plan for our Directors, executive officers, employees and consultants and those of our subsidiaries as determined by our Board of Directors, to attract and retain competent Directors, executive officers, employees and consultants motivated to work toward ensuring our success and to encourage them to acquire our shares. A copy of the Long-Term Incentive Plan has been filed as exhibit 4.35 to our fiscal year 2005 annual report.

The principal component of the long-term incentive compensation that we offer is made up of the Long-Term Incentive Plan for directors, officers, employees and consultants of us and our subsidiaries.

Introduced in May 2000, amended in October 2004 and effective in January 2005, the Long-Term Incentive Plan is designed to provide directors, officers, employees and consultants with an incentive to create value and accordingly ensures that their interests are aligned with those of our shareholders. The LTIP is subject to Human Resources Committee review to ensure maintenance of its market competitiveness. Our Board has full and complete authority to interpret the Plan and to establish the rules and regulations applying to it and to make all other determinations it deems necessary or useful for the administration of the Plan, provided that such interpretations, rules, regulations and determinations are consistent with the rules of all stock exchanges on which our securities are then traded and with all relevant securities legislation.

The Long-Term Incentive Plan provides for the issuance of options to purchase Subordinate Voting Shares and the issuance of Restricted Share Units ("RSUs") redeemable for actual Subordinate Voting Shares or the equivalent in cash to directors, officers, employees and consultants. Our Board of Directors, upon recommendation of the Human

Resources Committee, designates the recipients of options or RSUs and determines the number of Subordinate Voting Shares covered by each option or RSU, the dates of vesting, the expiry date and any other conditions relating to these options or RSUs, in each case in accordance with the applicable legislation of the securities regulatory authorities. During the financial year ended August 31, 2008, target awards for eligible officers under the LTIP were established to be in line with the objective of the Committee to align compensation with the median compensation offered in the reference group. A portion of the target RSU awards are fixed, in order to encourage executive retention over the longer term, and the balance are made at, above, or below target levels based on merit, as determined by each executive's individual performance over the previous year.

Table of Contents

The exercise price of the options is determined by our Board of Directors at the time of granting the options, subject to compliance with the rules of all stock exchanges on which the Subordinate Voting Shares are listed and with all relevant securities legislation. In any event, the price at which the Subordinate Voting Shares may be purchased may not be lower than the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars. Any option issued is non-transferable. At the end of our financial year ended August 31, 2008, there were a total of 1,821,481 options granted and outstanding pursuant to the Long-Term Incentive Plan having a weighted average exercise price of US$13.83 (CA$20.66).

The fair value at the time of grant of a RSU is equal to the market value of Subordinate Voting Shares at the time RSUs are granted. At the end of financial year ended August 31, 2008, there were a total of 847,791 RSUs granted and outstanding pursuant to the Long-Term Incentive Plan having a weighted average fair value at the time of grant of US$5.62 (CA$6.05) per RSU.

The maximum number of Subordinate Voting Shares that are issuable under the Plan shall not exceed 6,306,153 Subordinate Voting Shares, which represents 9.4% of our issued and outstanding voting shares as of November 3, 2008. The maximum number of Subordinate Voting Shares that may be granted to any one individual shall not exceed 5% of the number of outstanding Subordinate Voting Shares.

Some options granted to Directors and employees vest on the first anniversary date of their grant. Some options granted in the financial year ended August 31, 2004 and 2005 vest at a rate of 12.5% six (6) months after the date of grant, 12.5% twelve (12) months after the date of grant and 25% annually thereafter commencing on the second anniversary date of the grant in October 2005. Otherwise all options vest a rate of 25% annually commencing on the first anniversary date of the grant. All options may be exercised in whole or in part once vested. All of the options that are granted under the Plan must be exercised within a maximum period of ten (10) years following the date of their grant or they will be forfeited.

All RSUs first vesting cannot be earlier than the third anniversary date of their grant. Some RSUs granted in the financial year ended August 31, 2008, vest at a rate of 1/2 annually commencing on the third anniversary date of the grants in October 2007, January 2008, April 2008 and July 2008. Some RSUs granted in the financial year ended August 31, 2007, vest at a rate of 1/2 annually commencing on the third anniversary date of the grants in September 2006, January 2007 and July 2007 and others at a rate of 1/3 annually on the third, fourth and fifth anniversary dates of the grants in September 2006, October 2006 and January 2007. Some RSUs granted in the financial year ended August 31, 2006 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in February 2006 and in June 2006 and others at a rate of 1/3 annually commencing on the third anniversary date of the grant in August 2006. Some RSUs granted in the financial year ended August 31, 2005 vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in February 2005 and others at a rate of 55%, 35% and 10%, on the third, fourth and fifth anniversary dates of the grant in January 2005. Some RSUs granted during the last four financial years vest on the fifth anniversary date of each grant respectively in October 2007, October 2006, December 2005 and in January 2005. However, these RSUs are subject to early vesting on the third and fourth anniversary dates of the grant on the attainment of performance objectives, namely related to long term growth of revenue and profitability, as determined by the Board of Directors of the Corporation. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant. If such vesting date falls into any black-out period or any other restrictive period during which the RSU holder is not entitled to trade the Corporation's Subordinate Voting Shares, then the units shall vest on the first trading day the RSU holder is entitled to trade after such black-out period or restrictive period.

Any option granted pursuant to the Long-Term Incentive Plan will lapse (i) immediately upon the termination of the relationship with us or one of our subsidiaries for a good and sufficient cause for employees or officers or at the date on which an employee or an officer resigns or leaves his employment with us or one of our subsidiaries (or within 30 days if the holder's employment is terminated for reasons not related to cause); and (ii) 30 days after a Director ceases to be a member of our Board of Directors or one of our subsidiaries. In the event of retirement or disability, any option held by an employee lapses 30 days after the date of any such disability or retirement. In the event of death, any option held by the optionee lapses 6 months after the date of death.

Table of Contents

Any RSU granted pursuant to the Long-Term Incentive Plan will lapse (i) immediately, where vesting of a unit is subject to the attainment of performance objectives, if such performance objectives have not been attained (or postponed at a further vesting date as determined by our Board of Directors.); (ii) immediately, whether or not subject to attainment of performance objectives, upon the termination of the relationship with us or one of our subsidiaries for a good and sufficient cause for employees or officers or at the date on which an employee or an officer resigns or leaves his employment with us or one of our subsidiaries.

Any RSU granted pursuant to the Long-Term Incentive Plan will vest immediately, to a certain proportion as determined by the Plan, upon the termination of the relationship of an employee or officer with us or one of our subsidiaries (i) for reasons not related to cause; (ii) because of death or permanent disability and (iii) retirement.

The following table summarizes information about stock options granted to the members of our Board of Directors, and to Management and Corporate Officers of us and our subsidiaries as at August 31, 2008:

	Number of Options	% of Issued and Outstanding Options	Weighted Average Exercise Price ($US/Security)
President and CEO (one individual)	179,642	9.86%	9.05
Board of Directors (five individuals)	194,375	10.67%	6.23
Management and Corporate Officers (eight individuals)	212,139	11.65%	14.49

The following table summarizes information about RSUs granted to the members of our Board of Directors and to Management and Corporate Officers of us and our subsidiaries as at August 31, 2008:

	Number of RSUs	% of Issued and Outstanding RSUs	Weighted Average Fair Value at the Time of Grant $US/RSU
President and CEO (one individual)	85,460	10.08%	5.66
Board of Directors (five individuals)	-	-	-
Management and Corporate Officers (ten individuals)	238,069	28.08%	5.62

Option Grants in Last Financial Year

There were no options to purchase the Corporation’s Subordinate Voting Shares granted during the financial year ended August 31, 2008. At the end of the financial year ended August 31, 2008, there were a total of 1,821 481 Subordinate Voting Shares covered by options granted and outstanding pursuant to the Long-Term Incentive Plan having a weighted average exercise price of US$13.83 (CA$20.66). See “Report on Executive Compensation by the Human Resources Committee - Long-Term Incentive Compensation” for a description of the Long-Term Incentive Plan.

Aggregated Option Exercises in Last Financial Year and Financial Year End Option Values

The following table summarizes, for each of the Named Executive Officers, the number of stock options, if any, exercised during the financial year ended August 31, 2008, the aggregate value realized upon exercise and the total number of unexercised options, if any, held at August 31, 2008. Value realized upon exercise is the difference between the market value of the underlying Subordinate Voting Shares on the exercise date and the exercise or base price of the option. The value of unexercised in-the-money options at financial year-end is the difference between its

exercise or base price and the market value of the underlying Subordinate Voting Shares on August 29, 2008, which was US$4.20 (CA$4.47) per share. These values, unlike the amounts set forth in the column “Aggregate Value Realized,” have not been, and may never be, realized. The underlying options have not been, and may never be exercised, and actual gains, if any, on exercise will depend on the value of the Subordinate Voting Shares on the date of exercise. There can be no assurance that these values will be realized. Unexercisable options are those that have been held for less than the time required for vesting.

Table of Contents

Name	Securities Acquired on Exercise (#)	Aggregate Value Realized (US$) (1) (4)	Unexercised Options at August 31, 2008 Exercisable (#)	Unexercisable (#)	Value of Unexercised "In-the-Money" Options at August 31, 2008 (2) (3) (4) Exercisable (US$)	Unexercisable (US$)
Germain Lamonde	-	-	169,549	10,093	92,654	-
Pierre Plamondon	-	-	77,804	3,172	37,061	-
Dana Yearian	-	-	-	-	-	-
Jon Bradley	-	-	25,500	1,000	-	-
Stephen Bull	-	-	25,328	2,100	-	-

(1) The aggregate value realized is equivalent to the difference between the market value of the securities underlying the options at exercise and the exercise price of the options. This value, as the case maybe, has been converted from Canadian dollars to U.S. Dollars based upon the average foreign exchange rate on the day of the exercise.
(2) "In-the-money" options are options for which the market value of the underlying securities is higher than the price at which such securities may be bought from the Corporation.
(3) The value of unexercisable "in-the-money" options is calculated using the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and on the NASDAQ National Market on August 29, 2008 using the noon buying rate of the Federal Reserve Bank of New York to convert the NASDAQ National Market closing price to Canadian dollars, as required, less the exercise price of "in-the-money" options.
(4) This value has been converted from Canadian to US dollars based upon the foreign exchange rate on August 29, 2008 of 1.0631.

Compensation of Chief Executive Officer

In establishing Mr. Lamonde's compensation for the year ending August 31, 2008, the Corporation relied on a study completed by an independent consulting firm (Mercer Human Resource Consulting). Such study indicated average salaries and bonuses, median salaries and bonuses and maximum salaries and bonuses paid to chief executive officers by Canadian and American computer hardware and software companies as well as by a specific group of companies active in the fiber optics industry identified by the Corporation that it considers to be the best available comparisons. It was decided that Mr. Lamonde's compensation should reflect the median of Canadian computer hardware and software companies and of the specific group of companies in fiber optics identified by the Corporation. In the financial year ended August 31, 2008, Mr. Lamonde's compensation was adjusted accordingly.

In the financial year ended August 31, 2008, the bonus portion of Mr. Lamonde's compensation was tied to the financial and strategic objectives of the Corporation based on the following factors:

Measure (1)	Weighting ALL
Sales	35%
Earnings	15%
Gross margin	25%
Customer satisfaction (quality and on time delivery)	25%
Growth metrics	10%
Personal objectives (multiplier)	0% - 125%

(1) Sales, Earnings, Gross margin and Customer satisfaction measures are established to provide a metric from 0% to 150% and such a metric is multiplied by the personal objectives measure. This result is then multiplied by the short term incentive target % of the individual annual base salary.

Mr. Lamonde's bonus is payable in the same proportion at which the Corporation attains such objectives. When the objectives are exceeded, the bonus is higher; when objectives are not met, the bonus is lower.

Table of Contents

Deferred Share Unit Plan

Introduced in October 2004 and effective as of January 2005, the Deferred Share Unit Plan is designed to align more closely the interests of its non-employee Directors with those of our shareholders. A copy of the Deferred Share Unit Plan has been filed as exhibit 4.36 to our fiscal year 2005 annual report.

Under the Deferred Share Unit Plan, non-employee Directors shall receive up to 100 % of their retainer fees in the form of Deferred Share Units ("DSUs"), each of which has a fair value at the time of grant equal to the market value of a Subordinate Voting Share at the time DSUs are credited to the Directors. The value of a DSU, when converted to Subordinate Voting Shares, is equivalent to the market value of a Subordinate Voting Share at the time the conversion takes place. DSUs attract dividends in the form of additional DSUs at the same rate as dividends on Subordinate Voting Share. When a Director ceases to be a member of our Board of Directors, the DSUs are either converted and paid in Subordinate Voting Shares purchased on the open market or issued by us. Such Subordinate Voting Shares issued by us will be issued from the same pool of Subordinate Voting Shares reserved for issuance pursuant to the Long-Term Incentive Plan, which is 9.4% of the total issued and outstanding voting shares.

The following table summarizes information about DSUs granted to the non-employee members of our Board of Directors as at November 3, 2008:

	Number of DSUs	% of Issued and Outstanding DSUs	Weighted Average Estimated Value at the Time of Grant $US/DSU
Board of Directors (five individuals)	79,185	100%	5.26

The following table summarizes information about DSUs converted and paid in Subordinate Voting Shares when a director ceased to be a member of the Board as at November 3, 2008:

Name	Number of DSUs converted	Aggregate Value Realized (US$) (1)
Michael Unger	20,695	88,894

(1) The aggregate value realized is equivalent to the market value of the securities underlying the DSUs at conversion. This value, as the case maybe, has been converted from Canadian dollars to U.S. dollars based upon the average foreign exchange rate on the day of conversion.

Deferred Share Unit Grants in Last Financial Year

The aggregate number of Deferred Share Units ("DSUs") credited to non-employee directors during the financial year ended August 31, 2008 and as of November 3, 2008 was 35,162. The estimated value at the time of grant of a DSU is determined based on the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars, as required. The value at vesting of a DSU is equivalent to the market value of a Subordinate Voting Share when a DSU is converted to such Subordinate Voting Share. As of November 3, 2008, there were a total of 79,185 DSUs credited to directors pursuant to the Deferred Share Unit Plan having an estimated value at the time of grant of US$416,640 (CA$461,587).

DSUs attract dividends in the form of additional DSUs at the same rate as dividends on Subordinate Voting Shares. The DSUs are converted and paid in Subordinate Voting Shares at the time a director ceases to be a member of our Board.

Therefore, the value at vesting of a DSU, when converted to Subordinate Voting Shares, is equivalent to the market value of a Subordinate Voting Share at the time the conversion takes place. The table below shows information regarding DSU grants made under the Deferred Share Unit Plan during the financial year ended August 31, 2008 and as of November 3, 2008.

Table of Contents

During the financial year ended August 31, 2008 and as of November 3, 2008, the following DSUs were granted to the directors:

DSUs #	Weighted Average Estimated Value at the Time of Grant US$/DSU	Vesting
35,162	5.14	At the time director cease to be a member of the Board of the Corporation

Restricted Share Unit Grants in Last Financial Year

The aggregate number of Restricted Share Units (RSUs) granted during the financial year ended August 31, 2008 was 469,847 having a weighted average fair value at the time of grant of US$5.46 (CA$5.43) per RSU. The fair value at the time of grant of a RSU is equal to the market value of Subordinate Voting Shares at the time RSUs are granted. At the end of the financial year ended August 31, 2008, there were a total of 847,791 RSUs granted and outstanding pursuant to the Long-Term Incentive Plan having a weighted average fair value at the time of grant of US$5.62 (CA$6.05) per RSU. All RSUs first vesting cannot be earlier than the third anniversary date of their grant. Some RSUs granted in the financial year ended August 31, 2008, vest at a rate of 1/2 annually commencing on the third anniversary date of the grants in October 2007, January 2008, April 2008 and July 2008. Some RSUs granted in the financial year ended August 31, 2007, vest at a rate of 1/2 annually commencing on the third anniversary date of the grants in September 2006, January 2007 and July 2007 and others at a rate of 1/3 annually on the third, fourth and fifth anniversary dates of the grants in September 2006, October 2006 and January 2007. Some RSUs granted in the financial year ended August 31, 2006, vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in February 2006 and in June 2006 and others at a rate of 1/3 annually on the third, fourth and fifth anniversary dates of the grant in August 2006. Some RSUs granted in the financial year ended August 31, 2005 vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in February 2005 and others at a rate of 55%, 35% and 10%, on the third, fourth and fifth anniversary dates of the grant in January 2005. Some RSUs granted during the last four financial years vest on the fifth anniversary date of each grant respectively in October 2007, October 2006, December 2005 and in January 2005. However, these RSUs are subject to early vesting on the third and fourth anniversary dates of the grant on the attainment of performance objectives, namely related to long term growth of revenue and profitability, as determined by the Board of Directors of the Corporation. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

The RSUs are redeemed for actual Subordinate Voting Shares or the equivalent in cash at the discretion of the Board of Directors of the Corporation on the vesting dates established by the Board of Directors of the Corporation at the time of grant in its sole discretion.

Therefore, the value at vesting of a RSU, when converted to Subordinate Voting Shares, is equivalent to the market value of a Subordinate Voting Share at the time the conversion takes place. The table below shows information regarding RSU grants made under the Long-Term Incentive Plan during the financial year ended August 31, 2008. See “Report on Executive Compensation by the Human Resources Committee – Long-Term Incentive Compensation – Long-Term Incentive Plan” for a description of the Long-Term Incentive Plan.

Table of Contents

During the financial year ended August 31, 2008, the following RSUs were granted:

RSUs #	Fair Value at the Time of Grant US$/RSU	Vesting (1)
29,000	6.28	50% on the third and fourth anniversary dates of the grant in October 2007 (2)
86,167	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (3)
76,200	4.16	50% on the third and fourth anniversary dates of the grant in January 2008 (4)
21,600	6.09	50% on the third and fourth anniversary dates of the grant in April 2008 (5)
185,570	5.82	50% on the third and fourth anniversary dates of the grant in April 2008 (6)
71,310	4.39	50% on the third and fourth anniversary dates of the grant in July 2008 (7)

(1) All RSUs first vesting cannot be earlier than the third anniversary date of their grant.

(2) Those RSUs granted in the financial year ended August 31, 2008 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in October 2007.

(3) Those RSUs granted in the financial year ended August 31, 2008 vest on the fifth anniversary date of the grant in October 2007 but are subject to early vesting on the third and fourth anniversary dates of the grant on the attainment of performance objectives, namely related to long term growth of revenue and profitability, as determined by the Board of Directors of the Corporation. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

(4) Those RSUs granted in the financial year ended August 31, 2008 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in January 2008.

(5) Those RSUs granted in the financial year ended August 31, 2008 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in April 2008.

(6) Those RSUs granted in the financial year ended August 31, 2008 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in April 2008.

(7) Those RSUs granted in the financial year ended August 31, 2008 vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in July 2008.

During the financial year ended August 31, 2008, the following RSUs were granted to the following Named Executive Officers:

Name	RSUs #	Percentage of Net Total of RSUs Granted to Employees in Financial Year	Fair Value at the Time of Grant	Vesting (1)

		(%)	US$/RSU	
Germain Lamonde	29,910	6.37	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (2)
Pierre Plamondon	9,637	2.05	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (2)
Dana Yearian	7,225	1.54	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (2)

Table of Contents

Name	RSUs #	Percentage of Net Total of RSUs Granted to Employees in Financial Year (%)	Fair Value at the Time of Grant US$/RSU	Vesting (1)
Jon Bradley	6,122	1.30	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (2)
Stephen Bull	7,340	1.56	6.28	100% on the fifth anniversary date of the grant in October 2007 subject to early vesting up to 1/3 on the third anniversary date of the grant and up to 50% of the remaining units on the fourth anniversary date of the grant if the performance objectives are fully attained (2)

(1) All RSUs first vesting cannot be earlier than the third anniversary date of their grant.

(2) Those RSUs granted in the financial year ended August 31, 2008 vest on the fifth anniversary date of the grant in October 2007 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives, namely related to long term growth of revenue and profitability, as determined by the Board of Directors of the Corporation. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

Aggregated RSUs vested in Last Financial Year and Financial Year-End RSU Values

The following table summarizes, for each of the Named Executive Officers, the number of RSUs, if any, vested during the financial year ended August 31, 2008, the aggregate value realized upon vesting and the total number of unvested RSUs, if any, held at August 31, 2008. Value realized upon vesting is the market value of the Subordinate Voting Shares on the vesting date. The value of unvested RSUs at financial year-end is the market value of the Subordinate Voting Shares on August 29, 2008, which was US$4.20 per share. These values, unlike the amounts set forth in the column "Aggregate Value Realized", have not been and may never be realized. The actual gains on vesting will depend on the value of the Subordinate Voting Shares on the date of vesting. There can be no assurance that these values will be realized.

Name	Securities Acquired on Vesting (#)	Aggregate Value Realized (US$) (1)	Unvested RSUs at August 31, 2008 (#)	Value of Unvested RSUs at August 31, 2008 (US$) (2) (3)
Germain Lamonde	4,363	18,805	85,460	358,932
Pierre Plamondon	17,809	76,757	45,679	191,852
Dana Yearian	-	-	18,870	79,254

Jon Bradley	667	3,663	9,955	41,811
Stephen Bull	17,373	95,402	43,092	180,986

(1) The aggregate value realized is equivalent to the market value of the securities underlying the RSUs at vesting. This value, as the case maybe, has been converted from Canadian dollars to U.S. dollars based upon the average foreign exchange rate on the day of vesting.

(2) The value of RSUs is calculated using the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and on the NASDAQ National Market on August 29, 2008 using the noon buying rate of the Federal Reserve Bank of New York to convert the NASDAQ National Market closing price to Canadian dollars, as required.

(3) The actual gains on vesting will depend on the value of the Subordinate Voting Shares on the date of vesting. There can be no assurance that these values will be realized.

Table of Contents

Number of Subordinate Voting Shares reserved for future issuance

During the financial year ended August 31, 2008, 35,162 Deferred Share Units and 469,847 Restricted Share Units were granted to directors, officers and employees. Such awards were issued from the same pool of Subordinate Voting Shares reserved for issuance pursuant to the Long-Term Incentive Plan of which the maximum number of Subordinate Voting Shares issuable shall not exceed 6,306,153 Subordinate Voting Shares, which represents 9.4% of the Corporation's issued and outstanding voting shares as of November 3, 2008. As of November 3, 2008, the number of Subordinate Voting Shares reserved for future issuance is 2,440,302.

Stock Appreciation Rights Plan

On August 4, 2001, the Corporation established a Stock Appreciation Rights Plan ("SAR Plan") for the benefit of certain employees residing in countries where the granting of options under the Long-Term Incentive Plan is not feasible in the opinion of the Corporation. The Board has full and complete authority to interpret the SAR Plan and to establish the rules and regulations applying to it and to make all other determinations it deems necessary or useful for the administration of the SAR Plan.

Under the SAR Plan, eligible employees are entitled to receive a cash amount equivalent to the difference between the market price of the Subordinate Voting Shares on the date of exercise and the exercise price determined on the date of grant. No Subordinate Voting Shares are issuable under the SAR Plan.

The Board of Directors has delegated to Management the task of designating the recipients of stock appreciation rights, the date of vesting, the expiry date and other conditions. Under the terms of the SAR Plan, the exercise price of the stock appreciation rights may not be lower than the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and on the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars. Stock appreciation rights are non-transferable.

The stock appreciation rights vest over a four-year period, with 25% vesting annually commencing on the first anniversary date of the date of grant. However, since October 2007, some stock appreciation rights vest at a rate of 50% annually commencing on the third anniversary date of the grants in October 2007 and October 2008. Once vested, stock appreciation rights may be exercised between the second and the fifteenth business day following each release of the Corporation's quarterly financial results. All of the stock appreciation rights that are granted under the SAR Plan may be exercised within a maximum period of 10 years following the date of their grant. Any stock appreciation rights granted under the SAR Plan will lapse immediately upon the termination of the relationship with the Corporation or one of its subsidiaries for a good and sufficient cause or at the date on which an employee resigns or leaves his employment with the Corporation or one of its subsidiaries (or within 30 days if the holder is dismissed without cause). In the event of retirement or disability, any stock appreciation right held by an employee lapses 30 days after the date of any such disability or retirement. In the event of death, any stock appreciation right lapses 6 months after the date of death.

As of November 3, 2008, there were 40,374 SAR's outstanding.

Deferred Profit Sharing Plan

We maintain a plan for certain eligible Canadian resident employees, under which the Corporation may elect to contribute an amount equal to 2% of an employee's gross salary, provided that the employee has contributed at least 2% of his gross salary to a tax-deferred registered retirement savings plan. Cash contributions to this plan and expenses for the years ended August 31, 2006, 2007 and 2008, amounted to US$316,000, US$419,000 and

US$531,000, respectively.

Table of Contents

401(k) Plan

We maintain a 401(k) plan for eligible United States resident employees of our subsidiaries. Employees become eligible to participate in the 401(k) plan on the first day of the month following the completion of three months of continuous service. Employees may elect to defer their current compensation up to the lesser of 1% of eligible compensation or the statutorily prescribed annual limit and have the deferral contributed to the 401(k) plan. The 401(k) plan permits, but does not require us to make additional matching contributions to the 401(k) plan on behalf of the eligible participants, subject to a maximum of 50% of the first 6% of the participant's current compensation subject to certain legislated maximum contribution limits. In the years ended August 31, 2006, 2007 and 2008, we made an aggregate of US$126,000, US$166,000 and US$216,000 respectively, in matching contributions to the 401(k) plan. Contributions by employees or by us to the 401(k) plan and income earned on plan contributions are generally not taxable to the employees until withdrawn and contributions by us are generally deductible by us when made. At the direction of each participant, the trustees of the 401(k) plan invest the assets of the 401(k) plan in selected investment options. As of August 31, 2008, we made an aggregate of US$1,742,000 in matching contributions to the 401(k) plan.

Indemnification of Directors and Executive Officers and Limitation of Liability

Our by-laws require us, subject to the limitations provided by law, to indemnify our present or former Directors and officers or any persons who act or acted at our request as Directors or officers of a body corporate for all costs, losses, charges and expenses that arose or may arise by reason of their status as Directors or officers of us or such body corporate. A policy of Directors' and officers' liability insurance is maintained by us, which insures our Directors and officers and those of our subsidiaries against liability incurred by, arising from or against them for certain of their acts, errors or omissions. Accordingly, we maintain insurance protection against liability incurred by our officers and Directors as well as those of our subsidiaries in the performance of their duties. The entire premium, amounting to US$165,000 from September 30, 2008 to September 30, 2009, is paid by us. The aggregate limit of liability in respect of any and all claims is US$10 million per year. The policy provides for the indemnification of Directors and officers in the case of claims for which we have not indemnified or are not permitted by law to indemnify them, and for the reimbursement of us, subject to a deductible of US$250,000.

C. Board Practices

Board of Directors

Our Directors are elected at the annual meeting of shareholders for one-year terms and serve until their successors are elected or appointed, unless they resign or are removed earlier. Our articles of incorporation provide for a Board of Directors of a minimum of three (3) and a maximum of twelve (12) Directors. Our Board of Directors presently consists of six Directors. Under the Canada Business Corporations Act, twenty-five percent of the Directors and of the members of any committee of the Board of Directors must be resident Canadians. We have no arrangements with any of our Directors providing for the payment of benefits upon their termination of service as Director except for the vesting of their respective Deferred Share Units as detailed above.

The following table and notes set out the name of each of the individuals who served as a director of the Corporation during the last year term, all other positions and offices with the Corporation and its subsidiaries now held by each such individual, if any, the principal occupation or employment of each such individual, their respective period of service as a director.

Name and Position or Office with the Corporation	Principal Occupation or Employment	Residence	Director Since	Number of Subordinate	Number of Multiple Voting

				Voting Shares	Shares
Pierre-Paul Allard (1) Independent Director	Area Vice-President, Sales Cisco Systems Inc.	Pleasanton, California, USA	September 2008 (2)	-	-
Germain Lamonde Chairman of the Board, President and Chief Executive Officer	Chairman of the Board, President and Chief Executive Officer, EXFO Electro-Optical Engineering Inc.	St-Augustin-de-Desmaures, Quebec, Canada	September 1985	4,363	36,643,000 (3)

Table of Contents

Name and Position or Office with the Corporation	Principal Occupation or Employment	Residence	Director Since	Number of Subordinate Voting Shares	Number of Multiple Voting Shares
Pierre Marcouiller (4) (5) Independent Director	Chairman of the Board and Chief Executive Officer, Camoplast Inc. (6)	Magog, Quebec, Canada	May 2000	5,000	-
Guy Marier (4) (7) Independent Lead Director	Executive Consultant	Lakefield Gore, Quebec, Canada	January 2004	1,000	-
Dr. David A. Thompson, Ph.D.(5) (8) Independent Director	Vice-President & Director, Hardware & Equipment Technology, Corning Cable Systems (9)	Newton, North Carolina, USA	June 2000	2,100	-
André Tremblay (5) (10) Independent Director	Founder and Managing Partner, Trio Capital Inc., a private equity fund	Outremont, Quebec, Canada	May 2000	6,650 (11)	-

(1) Mr. Pierre-Paul Allard is presently Area Vice-President, Sales for Cisco Systems Inc. In this role, Mr. Allard is responsible for sales and field operations of Cisco's Global Enterprise Client Segment. From January 2003 to January 2007, Mr. Allard was Vice-President of Worldwide Enterprise Marketing where his primary responsibility was to develop Cisco's global enterprise market. Cisco Systems Inc. is a leading network equipment manufacturer in the global telecommunications industry.

(2) Named pursuant to a Board resolution in accordance with the Corporation's by-laws.

(3) Mr. Lamonde exercises control over this number of Multiple Voting Shares through G. Lamonde Investissements Financiers inc., a company controlled by Mr. Lamonde and through Fiducie Germain Lamonde, a family trust for the benefit of Mr. Lamonde's family.

(4) Member of the Audit Committee.

(5) Member of the Human Resources Committee.

(6) Camoplast Inc. designs, develops and manufactures specialized components, sub-systems and assemblies for the world leading original equipment manufacturers (OEMs) of both on- and off-road vehicles in a variety of markets including automotive, agricultural, construction and industrial, defense and powersports.

(7) Chairman of the Human Resources Committee since October 2008.

(8) Member of the Audit Committee since April 2008.

(9) Corning Incorporated is a diversified technology company that concentrates its efforts on high-impact growth opportunities. Corning combines its expertise in specialty glass, ceramic materials, polymers and the manipulation of the properties of light, with strong process and manufacturing capabilities to develop, engineer and

commercialize significant innovative products for the telecommunications, flat panel display, environmental, semiconductor, and life sciences industries.

(10) Chairman of the Audit Committee.

(11) Mr. Tremblay exercises control over this number of Subordinate Voting Shares through 9104-5559 Quebec inc., a company controlled by Mr. Tremblay.

Since September 1, 2007 until November 3, 2008, the Board met a total of fourteen (14) times. Attendance at all meetings was satisfactory, except Mr. Pierre Marcouiller who was absent four (4) times, Mr. David A. Thompson who was absent two (2) times and Mr. Pierre-Paul Allard, Mr. André Tremblay and Mr. Michael Unger who were absent one time.

Committees of the Board of Directors

Our Board of Directors has established an audit committee, a human resources committee and a disclosure committee.

Table of Contents

Our audit committee will recommend a firm to be appointed as independent auditors to audit financial statements and to perform services related to the audit, review the scope and results of the audit with the independent auditors, review with management and the independent auditors our annual operating results and consider the adequacy of the internal accounting procedures and the effect of the procedures relating to the auditors' independence. Further to changes to NASDAQ corporate governance rules and Securities and Exchange rules flowing from the adoption of the Sarbanes-Oxley Act, our audit committee charter is being revised every financial year to ensure that we comply with all new requirements. Accordingly, in March 2005, the Board updated and adopted an Audit Committee Charter. A copy of this Audit Committee Charter has been filed as Exhibit 11.6 to our fiscal year 2005 annual report and is also readily available from EXFO's website at www.EXFO.com. The audit committee revised such Charter in October 2008 but no amendment was required. The audit committee is composed of four independent Directors: André Tremblay, Guy Marier, Pierre Marcouiller and Mr. David A. Thompson since April 2008 in replacement of Mr. Unger. The chairperson of the audit committee is André Tremblay.

During the fiscal year ended August 31, 2008, the Audit Committee met a total of four (4) times and attendance was satisfactory at all meetings, except Mr. Pierre Marcouiller who was absent two (2) times and Mr. Michael Unger who were absent one time.

Our human resources committee will evaluate, review and supervise our procedures with regards to human resources and will assess the performance of our executive officers and the chief executive officer. This committee will also review annually the remuneration of the Directors and will recommend to the Board of Directors general remuneration policies regarding salaries, bonuses and other forms of remuneration for our Directors, executive officers and employees as a whole. Finally, the human resources committee will review our organizational structure annually and the development and maintenance of a succession plan. Accordingly, in March 2005, the Board updated and adopted a Human Resources Committee Charter which integrates the Compensation Committee Charter and the Nominating and Governance Committee Charter. A copy of this Human Resources Committee Charter has been filed as Exhibit 11.7 to our fiscal year 2005 annual report and is also readily available from EXFO's website at www.EXFO.com. The human resources committee is composed of four independent Directors: Pierre Marcouiller, Guy Marier, David A. Thompson and André Tremblay. Mr. Michael Unger was also a member of the Human Resources Committee until his resignation effective in June 2008. The chairperson of the Human Resources Committee is Mr. Guy Marier.

During the fiscal year ended August 31, 2008, the Human Resources committee met a total of four (4) times and attendance was satisfactory at all meetings, except Mr. Pierre Marcouiller who was absent two (2) times and Mr. David A. Thompson, Mr. André Tremblay and Mr. Michael Unger who were absent one time.

The disclosure committee is responsible for overseeing our disclosure practices. This committee consists of the chief executive officer, the chief financial officer, the manager of investor relations, the manager of financial reporting and accounting as well as our legal counsel and corporate secretary.

In addition, in order to deal with issues arising from our implication in the IPO class action suit, in October 2002, our Board of Directors appointed a litigation committee composed of four of our independent Directors.

Furthermore, our independent Directors hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance. The independent Directors hold as many meeting, as needed, annually and any Director may request such meeting at any time. Since September 1, 2007 and prior to November 3, 2008, four (4) meetings of independent Directors without management occurred.

D. Employees

We have fostered a corporate culture where growth and change are strongly encouraged. In fact, employees are constantly evolving with the rapid pace of technology to meet new challenges and realities. We believe that we possess a good cross-section of experience and youth to handle these inevitable changes in the industry.

Table of Contents

As of November 3, 2008, we had a total of 1,174 employees, up from a total of 1,046 on November 1, 2007. We have 888 employees in Canada, primarily based in Quebec, and 286 employees based outside of Canada. 419 are involved in research and development, 372 in manufacturing, 198 in sales and marketing, 98 in general administrative positions and 87 in communications and customer support. We have agreements with almost all of our employees covering confidentiality and non-competition. Only manufacturing employees based in Quebec City plants are represented by a collective bargaining agreement, which expires in 2009. We have never experienced a work stoppage. We believe that relations with our employees and bargaining unit are good.

E. Share Ownership

The following table presents information regarding the ownership of Subordinate Voting Shares, Exercisable "in-the-money" and "out-the-money" options and the beneficial ownership of our share capital as of November 3, 2008 by our Chief Executive Officer, Chief Financial Officer, our Directors, our three other most highly compensated executive officers, our other executive officers as a group, all of our Directors and executive officers as a group.

Each multiple voting share is convertible at the option of the holder into one subordinate voting share. Holders of our subordinate voting shares are entitled to one (1) vote per share and holders of our multiple voting shares are entitled to ten (10) votes per share.

			Currently Exercisable Options Owned as of November 3, 2008				Total Subordinate Voting Shares Beneficially Owned (3)				Total Percentage of Voting Power
	Subordinate Voting Shares Owned		In-the-money (1)		Out-the-money (2)				Multiple Voting Shares Beneficially Owned (3)		
Name	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Percent
Germain Lamonde	4,363	*	50,000	2.75%	119,549	6.57%	173,912	*	36,643,000 (4)	100	92,33
Pierre Plamondon	52,336 (5)	*	20,000	1.10%	59,150	3.25%	131,486	*	–	–	*
Pierre-Paul Allard	–	*	–	*	–	*	–	*	–	–	*
Pierre Marcouiller	5,000	*	12,500	*	36,382	2.00%	53,882	*	–	–	*
Guy Marier	1,000	*	–	*	12,500	*	13,500	*	–	–	*
David A. Thompson	2,100	*	12,500	*	30,234	1.66%	44,834	*	–	–	*
André Tremblay	6,650 (6)	*	12,500	*	32,191	1.77%	51,341	*	–	–	*
Dana Yearian	–	*	–	*	–	*	–	*	–	–	*
Jon Bradley	–	*	–	*	25,500	1.40%	25,500	*	–	–	*
Stephen Bull	30,389	*	–	*	26,226	1.44%	56,615	*	–	–	*
Other executive officers as a group	18,866	*	15,000	*	57,372	3.15%	91,238	*	–	–	*
All of our Directors and executive	120,704	*	122,500	6.73%	399,104	21.94%	642,308	2.06%	36,643,000	100	92.45

officers as a group

* Less than 1%.

(1) "In-the-money" options are options for which the market value of the underlying securities is higher than the price at which such securities may be bought from the Corporation. As of November 3, 2008 the market value of a Subordinate Voting Share was US$2.80.

(2) "Out-the-money" options are options for which the market value of the underlying securities is lower than the price of which such securities may be bought from the Corporation.

(3) Beneficial ownership is determined in accordance with the rules of the SEC and generally includes voting or investment power with respect to securities. Options that are currently exercisable (including options that have an exercise price above the market price) are deemed to be outstanding and to be beneficially owned by the person holding such options for the purpose of computing the percentage ownership of such person, but are not treated as outstanding for the purpose of computing the percentage ownership of any other person. Accordingly, DSUs and RSUs are not included.

(4) The number of shares held by Germain Lamonde includes 1,900,000 multiple voting shares held of record by Fiducie Germain Lamonde and 34,743,000 multiple voting shares held of record by G. Lamonde Investissements Financiers inc.

(5) The number of shares held by Pierre Plamondon includes 6,874 subordinate voting shares held of record by Fiducie Pierre Plamondon.

(6) The number of subordinate voting shares held of record by André Tremblay is held by 9104-5559 Québec Inc, a company controlled by Mr. Tremblay.

Table of Contents

The following table presents information regarding stock options held as of November 3, 2008 by our Chief Executive Officer, Chief Financial Officer, our Directors, our three other most highly compensated executive officers and our other executive officers as a group.

Name	Securities Under Options Granted (1) (#)	Exercise Price (2) (US$/Security)	Expiration Date
Germain Lamonde	25,402	$26.00	June 29, 2010
	5,080	$22.25	January 10, 2011
	70,000	$9.13	October 10, 2011
	50,000	$1.58	September 25, 2012
	17,942	$4.51	February 1, 2015
	11,218	$4.76	December 6, 2015
Pierre Plamondon	8,700	$26.00	June 29, 2010
	10,000	$45.94	September 13, 2010
	5,000	$34.07	October 11, 2010
	9,240	$22.25	January 10, 2011
	19,000	$9.13	October 10, 2011
	20,000	$1.58	September 25, 2012
	5,383	$5.13	October 26, 2014
	3,653	$4.76	December 6, 2015
Pierre-Paul Allard	–	–	–
Pierre Marcouiller	2,000	$26.00	June 29, 2010
	400	$22.25	January 10, 2011
	17,966	$9.13	October 10, 2011
	1,037	$12.69	December 1, 2011
	2,479	$5.65	March 1, 2012
	12,500	$1.58	September 25, 2012
	12,500	$3.51	October 27, 2013
Guy Marier	12,500	$4.65	March 24, 2014
David A. Thompson	2,000	$26.00	June 29, 2010
	400	$22.25	January 10, 2011
	15,334	$9.13	October 10, 2011
	12,500	$1.58	September 25, 2012
	12,500	$3.51	October 27, 2013
André Tremblay	2,000	$26.00	June 29, 2010
	400	$22.25	January 10, 2011
	17,291	$9.13	October 10, 2011
	12,500	$1.58	September 25, 2012
	12,500	$3.51	October 27, 2013
Dana Yearian	–	–	–
Jon Bradley	5,000	$45.94	September 13, 2010
	5,000	$22.25	January 10, 2011
	1,000	$12.22	January 3, 2012
	1,500	$3.19	January 7, 2013
	10,000	$3.50	December 17, 2013
	4,000	$4.51	February 1, 2015
Stephen Bull	900	$26.00	June 29, 2010
	5,000	$45.94	September 13, 2010

2,930	$22.25	January 10, 2011
15,000	$9.13	October 10, 2011
1,795	$5.13	October 26, 2014
1,803	$4.76	December 6, 2015

Table of Contents

Name	Securities Under Options Granted (1) (#)	Exercise Price (2) (US$/Security)	Expiration Date
Other Executive Officers as a group	3,000	$45.94	September 13, 2010
	4,000	$34.07	October 11, 2010
	3,250	$22.25	January 10, 2011
	10,000	$23.40	March 15, 2011
	18,000	$9.13	October 10, 2011
	15,000	$1.58	September 25, 2012
	5,000	$3.19	January 7, 2013
	9,259	$5.13	October 26, 2014
	2,000	$4.51	February 1, 2015
	7,726	$4.76	December 6, 2015

(1) Underlying securities: subordinate voting shares

(2) The exercise price of options granted is determined based on the highest of the closing prices of the subordinate voting shares on the Toronto Stock Exchange and the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars, as required.

The following table presents information regarding Deferred Share Units and Restricted Share Units held by our Chief Executive Officer, our Chief Financial Officer, our Directors, our three other most highly compensated executive officers, our other executive officers as a group, all of our Directors and executive officers as a group, as of November 3, 2008.

	DSUs			RSUs		
Name	Number	Percentage	Estimated Average Value at the time of grant US$/DSU (1)	Number	Percentage	Fair Value at the time of grant US$/RSU (2)
Germain Lamonde	–	–	–	8,726 (3)	0.72%	4.69
	–	–	–	21,477 (4)	1.76%	4.76
	–	–	–	25,347 (5)	2.08%	6.02
	–	–	–	29,910 (6)	2.46%	6.28
	–	–	–	65,254 (7)	5.36%	2.36
Pierre Plamondon	–	–	–	2,618 (3)	0.21%	4.69
	–	–	–	13,500 (8)	1.11%	4.69
	–	–	–	6,994 (4)	0.57%	4.76
	–	–	–	8,430 (5)	0.69%	6.02
	–	–	–	4,500 (9)	0.37%	6.02
	–	–	–	9,637 (6)	0.79%	6.28
	–	–	–	20,644 (7)	1.70%	2.36
	–	–	–	20,339 (10)	1.67%	2.36
Pierre-Paul Allard		–	–	–	–	–
Pierre Marcouiller	17,109 (11)	21.6%	5.26	–	–	–

Guy Marier	17,109 (11)	21.6%	5.26	–	–	–
David A. Thompson	19,097 (11)	24.1%	5.26	–	–	–
André Tremblay	25,870 (11)	32.7%	5.26	–	–	–
Dana Yearian	–	–	–	5,000 (12)	0.41%	5.16
	–	–	–	6,645 (5)	0.55%	6.02
	–	–	–	7,225 (6)	0.59%	6.28
	–	–	–	23,072 (7)	1.89%	2.36
	–	–	–	25,424 (10)	2.09%	2.36
Jon Bradley	–	–	–	1,333 (13)	0.11%	4.51
	–	–	–	2,500 (14)	0.21%	5.59
	–	–	–	6,122 (6)	0.50%	6.28
	–	–	–	16,826 (7)	1.38%	2.36
	–	–	–	25,416 (10)	2.09%	2.36
Stephen Bull	–	–	–	1,745 (3)	0.14%	4.69
	–	–	–	13,500 (8)	1.11%	4.69
	–	–	–	4,602 (4)	0.38%	4.76
	–	–	–	5,905 (5)	0.48%	6.02
	–	–	–	10,000 (9)	0.82%	6.02
	–	–	–	7,340 (6)	0.60%	6.28
	–	–	–	17,756 (7)	1.46%	2.36
	–	–	–	13,559 (10)	1.11%	2.36

Table of Contents

	DSUs			RSUs		
Name	Number	Percentage	Estimated Average Value at the time of grant US$/DSU (1)	Number	Percentage	Fair Value at the time of grant US$/RSU (2)
Other executive officers as a group	–	–	–	5,899 (3)	0.48%	4.69
	–	–	–	14,175 (8)	1.16%	4.69
	–	–	–	16,708 (4)	1.37%	4.76
	–	–	–	3,250 (14)	0.27%	5.59
	–	–	–	25,475 (5)	2.09%	6.02
	–	–	–	10,500 (9)	0.86%	6.02
	–	–	–	15,033 (15)	1.23%	6.42
	–	–	–	1,750 (16)	0.14%	6.42
	–	–	–	25,933 (6)	2.13%	6.28
	–	–	–	1,750 (17)	0.14%	4.16
	–	–	–	73,133 (7)	6.00%	2.36
	–	–	–	50,846 (10)	4.17%	2.36
All of the directors and executive officers as a group	–	–	–	18,988 (3)	1.56%	4.69
	–	–	–	41,175 (8)	3.38%	4.69
	–	–	–	1,333 (13)	0.11%	4.51
	–	–	–	49,781 (4)	4.09%	4.76
	–	–	–	5,750 (14)	0.47%	5.59
	–	–	–	5,000 (12)	0.41%	5.16
	–	–	–	71,802 (5)	5.90%	6.02
	–	–	–	25,000 (9)	2.05%	6.02
	–	–	–	15,033 (15)	1.23%	6.42
	–	–	–	1,750 (16)	0.14%	6.42
	–	–	–	86,167 (6)	7.08%	6.28
	–	–	–	1,750 (17)	0.14%	4.16
	–	–	–	216,685 (7)	17.79%	2.36
	–	–	–	135,584 (10)	11.13%	2.36
	79,185	100%	5.26	675,798	55.49%	5.62

(1) The estimated average value at the time of grant of a DSU is the average of the estimated value at the time of grant of a DSU which is determined based on the highest of the closing prices of the Subordinate Voting Shares on the Toronto Stock Exchange and the NASDAQ National Market on the last trading day preceding the grant date, using the noon buying rate of the Federal Reserve Bank of New York on the grant date to convert the NASDAQ National Market closing price to Canadian dollars, as required. The value at vesting of a DSU is equivalent to the market value of a Subordinate Voting Share when a DSU is converted to such Subordinate Voting Share.

(2) The fair value at the time of grant of a RSU is equal to the market value of Subordinate Voting Shares at the time RSUs are granted.

(3) Those RSUs will vest on the fifth anniversary date of the grant in January 2005 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

(4)

Those RSUs will vest on the fifth anniversary date of the grant in December 2005 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

(5) Those RSUs will vest on the fifth anniversary date of the grant in October 2006 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

(6) Those RSUs will vest on the fifth anniversary date of the grant in October 2007 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

(7) Those RSUs will vest on the fifth anniversary date of the grant in October 2008 but are subject to early vesting on the third and fourth anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the first early vesting is up to 1/3 of the units on the third anniversary date of the grant and the second early vesting is up to 50% of the remaining units on the fourth anniversary date of the grant.

Table of Contents

(8) Those RSUs will vest at a rate of 55%, 35% and 10%, on the third, fourth and fifth anniversary dates of the grant in January 2005.
(9) Those RSUs will vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in October 2006.
(10) Those RSUs will vest on the fifth anniversary date of the grant in October 2008 but are subject to early vesting on the third anniversary date of the grant on the attainment of performance objectives as determined by the Board of Directors. Accordingly, subject to the attainment of performance objectives, the early vesting is up to 100% of the units on the third anniversary date of the grant.
(11) Those DSUs will vest at the time Director ceases to be a member of the Board of the Corporation.
(12) Those RSUs will vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in August 2006.
(13) Those RSUs will vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in February 2005.
(14) Those RSUs will vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in February 2006.
(15) Those RSUs will vest at a rate of 1/3 annually commencing on the third anniversary date of the grant in January 2007.
(16) Those RSUs will vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in January 2007.
(17) Those RSUs will vest at a rate of 1/2 annually commencing on the third anniversary date of the grant in January 2008.

Escrowed Securities

The following table presents information regarding the number of securities of each class of the Corporation held, to our knowledge as of November 3, 2008, in escrow and the percentage outstanding securities of that class.

Designation of Class	Number of Securities held in escrow	Percentage of Class
Subordinate Voting Shares	nil	nil
Multiple Voting Shares	nil	nil

Table of Contents

Item 7. Major Shareholder and Related Party Transaction

A. Major Shareholders

The following table presents information regarding the beneficial ownership of our share capital as of November 3, 2008 by persons or groups of affiliated persons known by us to own more than 5% of our voting shares.

	Multiple Voting Shares Beneficially Owned (1)		Subordinate Voting Shares Beneficially Owned (1)		Total Percentage of Voting Power
Name	Number	Percent	Number	Percent	Percent
Germain Lamonde (2)	36,643,000	100%	173,912	0.57%	92.29%
Fiducie Germain Lamonde (3)	1,900,000	5%	Nil	Nil	4.79%
G. Lamonde Investissements Financiers inc. (4)	34,743,000	95%	Nil	Nil	87.51%
Connor, Clark & Lunn Investment Mgmt. Ltd.	Nil	Nil	1,693,900	5.53%	*

*Less than 1%

(1) Beneficial ownership is determined in accordance with the rules of the SEC and generally includes voting or investment power with respect to securities. Options that are currently exercisable (including options that have an exercise price above the market price) are deemed to be outstanding and to be beneficially owned by the person holding such options for the purpose of computing the percentage ownership of such person, but are not treated as outstanding for the purpose of computing the percentage ownership of any other person.

(2)