NAV CANADA

MANAGEMENT'S DISCUSSION AND ANALYSIS

ON FORM 51-102F1

THREE MONTHS ENDED

NOVEMBER 30, 2016

January 11, 2017

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MANAGEMENT'S DISCUSSION AND ANALYSIS
Q1 FISCAL 2017
(in millions of dollars)

INTRODUCTION

This management's discussion and analysis (MD&A) relates to the unaudited interim consolidated financial condition, results of operations, comprehensive income and cash flows for the three months ended November 30, 2016 (Q1 fiscal 2017) of NAV CANADA and its subsidiaries (also referred to in this MD&A as we, our, us or the Company). It should be read in conjunction with our unaudited interim condensed consolidated financial statements for Q1 fiscal 2017 (Q1 fiscal 2017 financial statements), our audited annual consolidated financial statements and the accompanying notes for the year ended August 31, 2016 (fiscal 2016), our fiscal 2016 annual MD&A, as well as our 2016 Annual Information Form dated October 27, 2016 (fiscal 2016 AIF). Additional information about NAV CANADA, including our consolidated financial statements for Q1 fiscal 2017 and fiscal 2016, our fiscal 2016 annual MD&A, and our fiscal 2016 AIF are filed on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

Our financial statements are prepared in Canadian dollars (CDN) and in accordance with International Financial Reporting Standards (IFRS). Our Q1 fiscal 2017 financial statements have been prepared in accordance with International Accounting Standards (IAS) 34 *Interim Financial Reporting*. Our Audit & Finance Committee reviewed this MD&A and our Board of Directors (the Board) approved it before it was filed.

Caution Concerning Forward-Looking Information

This MD&A and, in particular, but without limitation, sections "RESULTS OF OPERATIONS – Financial Outlook" and "LIQUIDITY AND CAPITAL RESOURCES – Financial Instruments and Risk Management: Restructured and Other Investments in ABCP" of this MD&A, contain certain statements about NAV CANADA's future expectations. These statements are generally identified by words like "anticipate", "plan", "believe", "intend", "expect", "estimate", "approximate" and the like, as well as future or conditional verbs such as "will", "should", "would" and "could", or negative versions thereof. Because forward-looking statements involve future risks and uncertainties, actual results may be quite different from those expressed or implied in these statements. Examples include geopolitical unrest, terrorist attacks and the threat of terrorist attacks, war, epidemics or pandemics, natural disasters, weather patterns, environmental concerns, cyber security attacks, labour negotiations, arbitrations, workforce recruitment, training and retention, general aviation industry conditions, air traffic levels, the use of telecommunications and ground transportation as alternatives to air travel, capital market and economic conditions, the ability to collect customer service charges and reduce operating costs, the satisfaction of criteria for the remaining Aireon LLC (Aireon) investment tranche, the success of our investment in space-based aircraft surveillance through Aireon, credit losses on investments, changes in interest rates, changes in laws, tax changes, adverse regulatory developments or proceedings and lawsuits. Some of these risks and uncertainties are explained under "Risk Factors" in our fiscal 2016 AIF. The forward-looking statements contained in this MD&A represent our expectations as of January 11, 2017 and are subject to change after this date. Readers of this MD&A are cautioned not to place undue reliance on any forward-looking statement. We disclaim any intention or obligation to update or revise any forward-looking statements included in this document whether as a result of new information, future events or for any other reason, except as required by applicable securities legislation.

Our Business

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

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

Financial Strategy and Rate Regulation

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

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

In preparing our consolidated financial statements, the timing of recognition of certain revenue and expenses differs from what would otherwise be expected for companies that are not subject to regulatory statutes governing the level of charges. For example, we adjust our net income (loss) through transfers to or from the rate stabilization account, based on variations from the amounts that were used when establishing customer service charges. If our actual revenue exceeds actual expenses, the excess is reflected as a credit to the rate stabilization account and is returnable to customers through future customer service charges. Similarly, if actual revenue turns out to be less than actual expenses, the revenue shortfall is reflected as a debit to the rate stabilization account and is recoverable from customers through future customer service charges (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account"). In the process of determining future customer service charges, we take into account the balance of the rate stabilization account, adjusted "notionally" for the non-credit related portion of the fair value adjustments that have been provided on restructured and other investments in asset-backed commercial paper (ABCP).

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

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

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

(in millions of dollars)

Financial Highlights

Results of operations for the three months ended November 30, 2016

The Company recorded breakeven results in Q1 fiscal 2017 (Q1 fiscal 2016 - net loss of $2). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $12 (Q1 fiscal 2016 - net income of $16). The net loss was lower than planned as the Company has achieved positive financial performance compared to its approved budget, as reflected by the $17 of favourable variances from planned results shown below. This was primarily due to $15 higher revenue than planned.

	Three months ended November 30		
	2016	2015	Change
Revenue	$ 332	$ 342	$ (10)
Operating expenses	321	296	25
Other (income) and expenses	22	30	(8)
Income tax expense	1	-	1
Net income (loss), before rate stabilization and regulatory deferral account adjustments	(12)	16	(28)
Net movement in regulatory deferral accounts			
Rate stabilization adjustments:			
Favourable variances from planned results	(17)	(13)	(4)
Initial approved adjustment[(1)]	10	(8)	18
	(7)	(21)	14
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	30	11	19
Other employee benefits	(3)	(3)	-
Investment in preferred interests, net of tax	(9)	(6)	(3)
Realized hedging transactions	1	1	-
	19	3	16
	12	(18)	30
Net income (loss), after rate stabilization and regulatory deferral account adjustments	$ -	$ (2)	$ 2

(1) The Company approved a $38 transfer out of the rate stabilization account to be recorded in the year ending August 31, 2017 (fiscal 2017) (fiscal 2016 – $31 transfer in to the rate stabilization account), in order to achieve planned breakeven results of operations. The adjustment is being transferred evenly throughout the fiscal year. For the three months ended November 30, 2016, $10 has been transferred from the rate stabilization account (three months ended November 30, 2015 - $8 had been transferred to the rate stabilization account).

(in millions of dollars)

The Company is subject to legislation that regulates the level of its charges (see "INTRODUCTION – Financial Strategy and Rate Regulation"). The timing of the recognition of certain revenue and expenses recovered through charges is recorded through movements in regulatory deferral accounts. The net movement in regulatory deferral accounts for the three months ended November 30, 2016 was an income of $12 as compared to a loss of $18 over the same period in fiscal 2016. This change in regulatory deferrals of $30 as compared to the same period in fiscal 2016 is due to lower deferrals of favourable results through rate stabilization adjustments of $14 and a $16 net increase in regulatory deferral adjustments to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting.

As shown below, cash increased by $105 during the three months ended November 30, 2016 and the Company experienced positive free cash flow of $24, which is a non-GAAP (Generally Accepted Accounting Principles) financial measure (see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended November 30, 2016" for additional information on non-GAAP financial measures and a discussion of cash flows).

	Three months ended November 30		
	2016	2015	Change
Cash flows from:			
Operations [1]	$ 56	$ 86	$ (30)
Investing [1]	48	(6)	54
Cash flows from operating and investing activities	104	80	24
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase in cash and cash equivalents	105	80	25
Cash and cash equivalents, beginning of period	119	230	(111)
Cash and cash equivalents, end of period	$ 224	$ 310	$ (86)
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations[1]	$ 56	$ 86	$ (30)
Capital expenditures[2]	(32)	(34)	2
Free cash flow	$ 24	$ 52	$ (28)

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended November 30, 2016" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q1 fiscal 2017 financial statements.

(in millions of dollars)

Financial position as at November 30, 2016

The following table outlines significant changes in our assets and liabilities between August 31, 2016 and November 30, 2016:

	November 30 2016	August 31 2016	Change
Assets			
Current assets			
Cash	$ 224	$ 119	$ 105
Accounts receivable and other	95	107	(12)
Investments	304	373	(69)
Other current assets	11	10	1
	634	609	25
Non-current assets			
Investment in preferred interests	301	291	10
Property, plant and equipment	664	664	-
Intangible assets	948	953	(5)
	1,913	1,908	5
Total assets	2,547	2,517	30
Regulatory deferral account debit balances	1,355	1,708	(353)
Total assets and regulatory deferral account debit balances	$ 3,902	$ 4,225	$ (323)
Liabilities			
Current liabilities			
Trade and other payables	$ 213	$ 202	$ 11
Current portion of long-term debt	125	25	100
Other current liabilities	5	6	(1)
	343	233	110
Non-current liabilities			
Long-term debt	1,594	1,694	(100)
Employee benefits	1,406	1,694	(288)
Other non-current liabilities	66	100	(34)
	3,066	3,488	(422)
Total liabilities	3,409	3,721	(312)
Equity			
Retained earnings	28	28	-
Regulatory deferral account credit balances	465	476	(11)
Total liabilities, equity and regulatory deferral account credit balances	$ 3,902	$ 4,225	$ (323)

For a discussion of the changes in cash flows from August 31, 2016, see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended November 30, 2016".

See "INTRODUCTION – Significant Financial Matters: Financing Activities" for discussion of the significant changes in investments and long-term debt during the three months ended November 30, 2016.

The change in non-current employee benefit liabilities are a result of the re-measurement gains of employee defined benefit plans recorded during the quarter. The change in other non-current liabilities is a result of positive fair value adjustments recorded on the Company's interest rate hedges. These changes along with the related changes in regulatory deferral account debit balances are discussed further in "RESULTS OF OPERATIONS – Other Comprehensive Income (Loss)".

The balance in retained earnings as at November 30, 2016 reflects the earnings up to that date. We plan our operations to essentially result in an annual financial breakeven position after expenses are met through customer service charges and other revenue sources, and after adjustments are made to the rate stabilization account. As a result, the balance in the retained earnings account at the end of each fiscal year has remained stable at $28. Any variation from this amount at the end of any interim period reflects seasonal or other planned fluctuations in revenue and expenses.

Significant Financial Matters

The following items have significant financial importance to the Company:

1. Rate Stabilization Account

As at November 30, 2016, the rate stabilization account (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account") had a credit balance of $176 and the "notional" balance of the rate stabilization account was a credit balance of $179, which is above its target of $101 for fiscal 2017 (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

The rate stabilization account improved by $7 during fiscal 2017. This improvement was due to $17 of favourable variances from planned results, arising mainly from higher than planned revenue, partially offset by the $10 initially approved adjustment to the rate stabilization account. Rate stabilization adjustments are described under "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account".

2. Air Traffic and Customer Service Charges[1]

During Q1 fiscal 2017, air traffic volumes increased by 5.5% year-over-year. The approved budget for the fiscal year had assumed growth of 1.1%. The Company's current forecast for air traffic growth for fiscal 2017 is 3.9%.

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

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

3. Pension Plans

The Company funds its registered pension plans based on the January 1, 2016 actuarial valuations, as discussed in our fiscal 2016 annual MD&A. We use an annual measurement date of August 31 for determining the accounting surplus or deficit and establishing pension costs for the coming fiscal year. The Company's pension plans had an accounting deficit of $1,415 as at the annual measurement date of August 31, 2016 and an accounting deficit of $1,138 as at November 30, 2016. The $277 decrease in the deficit position during Q1 fiscal 2017 is primarily due to net actuarial gains of $307 partially offset by actuarial accounting expense exceeding Company contributions by $30. The $307 of net actuarial gains are primarily due to a $414 actuarial gain from a 40 basis point increase in the discount rate partially offset by a return on plan assets $107 less than the expected return based on the discount rate.

Further information on the Company's pension plans is discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Cash Requirements: Pension Plans".

4. Investment in Space-Based Aircraft Surveillance through Aireon:

As discussed in note 4 to the Q1 fiscal 2017 financial statements, as at November 30, 2016, the Company has invested $120 U.S. ($161 CDN) (August 31, 2016 - $120 U.S. ($157 CDN)). The Company is represented by four out of the eleven directors on Aireon's board of directors. The Company's investment in Aireon is in preferred interests, which are redeemable or convertible to common equity.

As at November 30, 2016, the Company's total fully diluted common equity interest on a post conversion basis is 36.5% (August 31, 2016 – 36.5%).

Subsequent to November 30, 2016, the Company completed the fourth tranche investment of $15 U.S. ($16 CDN) on December 21, 2016, bringing its total investment to $135 U.S. ($181 CDN). The Company's total fully diluted common equity interest on a post conversion basis has increased to 38.1%.

5. Settlement of Collective Agreements

All eight of our collective agreements are in force with contract expiries ranging from March 2017 to February 2018. During fiscal 2016, seven collective agreements, representing approximately 89% of our unionized workforce, were ratified. These ratifications added a 2.5% salary increase for the additional one year extension of each collective agreement.

All of the Company's eight collective agreements include significant changes in the pension area as outlined in the fiscal 2016 annual MD&A.

6. Financing Activities

During the quarter, the Company received $73 of principal relating to the Master Asset Vehicle II (MAV II) notes as well as the remaining $7 principal balance of the restructured ABCP. The remaining balances of the MAV II notes are expected to be received in fiscal 2017.

Subsequent to November 30, 2016, on December 16, 2016, the Company redeemed $100 of the $350 Series MTN 2009-1 General Obligation Notes with proceeds from the MAV II notes and surplus cash.

(in millions of dollars)

RESULTS OF OPERATIONS

Revenue

The following table provides a breakdown of our revenue by category. Our fiscal 2016 AIF and the notes to our fiscal 2016 annual consolidated financial statements provide more information about the different categories of our customer service charges.

	Three months ended November 30			
	2016	2015	Change	%
Enroute	$ 167	$ 176	$ (9)	(5%)
Terminal	116	116	-	- %
Daily / annual / quarterly	21	20	1	5%
North Atlantic and international communication	11	12	(1)	(8%)
Total customer service charges	315	324	(9)	(3%)
Other	17	18	(1)	(6%)
	$ 332	$ 342	$ (10)	(3%)

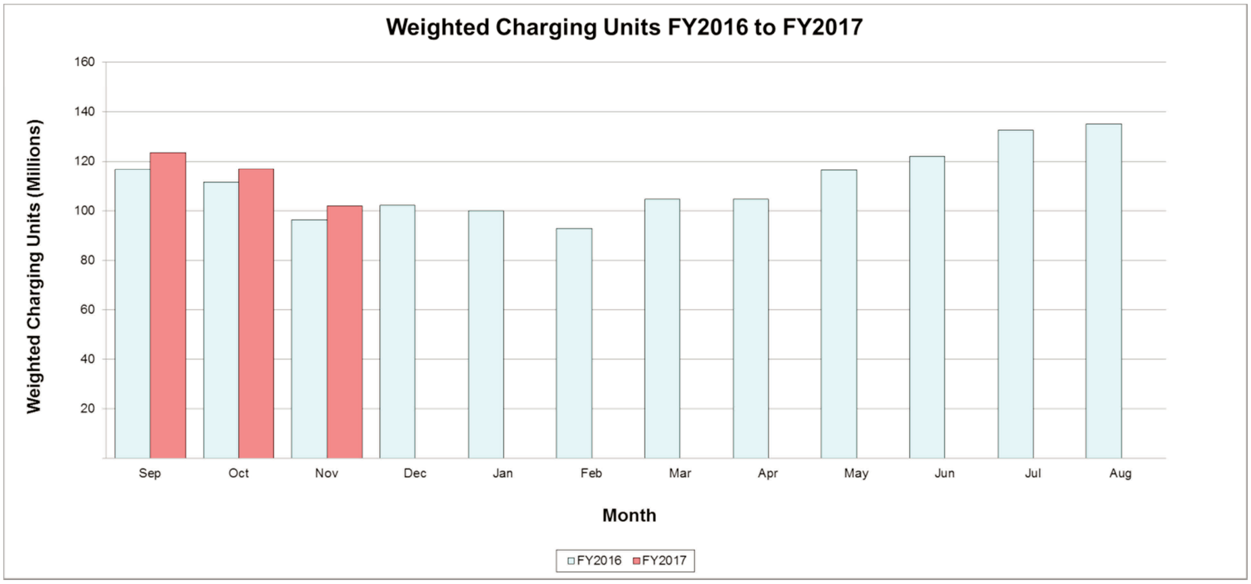
Other revenue consists of service and development contracts, conference centre services at our facility in Cornwall (Ontario), the sale of civil aeronautical publications and other miscellaneous revenue.

Revenue for Q1 fiscal 2017 was $332 compared to $342 for Q1 fiscal 2016. The $10 decrease is primarily due to a $9 decrease in customer service charge revenue arising from lower revised service charges (7.6% on average) that became effective September 1, 2016, partially offset by a 5.5% growth in air traffic volumes during Q1 fiscal 2017.

Air Traffic

Air traffic increased by 5.5% in Q1 fiscal 2017 when compared to Q1 fiscal 2016. This increase is illustrated in the following chart showing air traffic by month since September 2015.

The chart illustrates the seasonal variations in traffic. The chart shows traffic in "weighted charging units", which reflect the number of flights, aircraft size and distance flown.



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

(in millions of dollars)

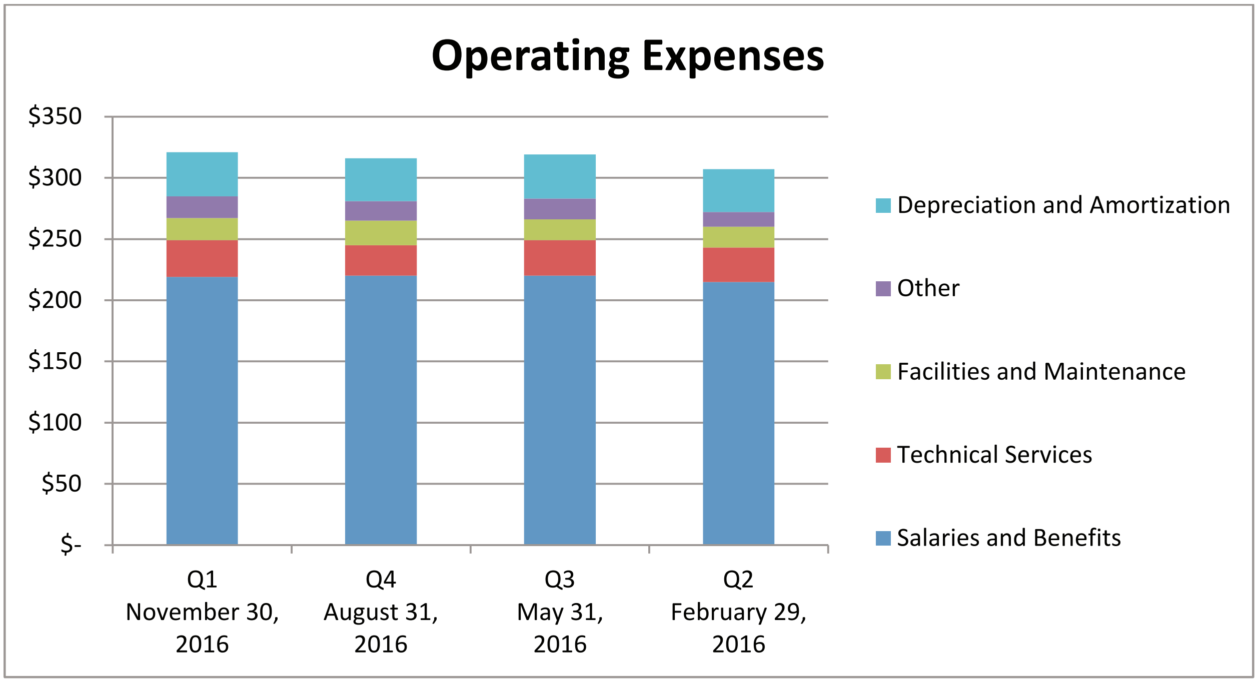
Operating Expenses

	Three months ended November 30			
	2016	2015	Change	%
Salaries and benefits	$ 219	$ 203	$ 16	8%
Technical services	30	30	-	- %
Facilities and maintenance	18	16	2	13%
Depreciation and amortization	36	35	1	3%
Other	18	12	6	50%
	$ 321	$ 296	$ 25	8%

Salaries and benefits expense in Q1 fiscal 2017 increased by $16 compared to Q1 fiscal 2016 primarily due to increased compensation levels and pension current service costs.

Technical services, facilities and maintenance and depreciation and amortization expenses were comparable to Q1 fiscal 2016.

In fiscal 2016, the Company received a refund of commodity taxes previously paid which was included in other operating expenses. In Q1 fiscal 2017, there is no refund offsetting expenses, and therefore other operating expenses are higher by $6 compared to Q1 fiscal 2016.



(in millions of dollars)

Other (Income) and Expenses

	Three months ended November 30		
	2016	2015	Change
Finance income			
Interest income	$ (1)	$ (1)	$ -
Net change in fair value of financial assets at FVTPL[1]			
MAV II, ABCP and other investments	(12)	1	13
Investment in preferred interests	(3)	(3)	-
	(15)	(2)	13
	(16)	(3)	13
Net interest costs relating to employee benefits	14	11	(3)
Other finance costs			
Interest expense	21	25	4
Redemption premium	10	-	(10)
	31	25	(6)
Other gains	(7)	(3)	4
	$ 22	$ 30	$ 8

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

The net change in fair value of financial assets at FVTPL increased by $13 compared to Q1 fiscal 2016. Positive fair value adjustments on MAV II, ABCP and other investments of $12 were recorded in Q1 fiscal 2017 compared to negative fair value adjustments of $1 in Q1 fiscal 2016.

The $3 increase in net interest costs relating to employee benefits in Q1 fiscal 2017 is primarily due to lower pension interest income than in Q1 fiscal 2016.

The $6 increase in other finance costs in Q1 fiscal 2017 is primarily due to the redemption premium of $10 related to the early redemption of $100 of the Series $350 MTN 2009-1 General Obligation Notes, partially offset by $4 lower interest costs on long-term debt due to lower debt levels in Q1 fiscal 2017 compared to Q1 fiscal 2016.

Other gains increased by $4 in Q1 fiscal 2017 compared to Q1 fiscal 2016 mainly due to higher unrealized foreign exchange gains on the investment in Aireon due to the fluctuation of the Canadian dollar against the U.S. dollar.

(in millions of dollars)

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

The net movement in regulatory deferral accounts related to net income (loss) represents the regulatory accounting adjustments, including the rate stabilization mechanism, to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting. The Company's regulatory approach has not changed from that disclosed in the fiscal 2016 annual MD&A.

	Three months ended November 30		
	2016	2015	Change
Rate stabilization account	$ (7)	$ (21)	$ 14
Other regulatory deferral accounts			
Employee benefit pension contributions	30	11	19
Other employee benefits	(3)	(3)	-
Investment in preferred interests, net of tax	(9)	(6)	(3)
Realized hedging transactions	1	1	-
	$ 12	$ (18)	$ 30

The movements in the rate stabilization account are detailed in the table below.

The net movement in the employee benefit pension contributions regulatory deferral account for Q1 fiscal 2017 increased by $19 compared to Q1 fiscal 2016. Regulatory adjustments to adjust the total pension benefit expense to the level of pension contributions to be recovered through rate setting were $30 in Q1 fiscal 2017 compared to $11 in Q1 fiscal 2016.

The net movement of other employee benefits regulatory deferral accounts in Q1 fiscal 2017 are comparable to the net movement in Q1 fiscal 2016.

The $3 increase in the investment in preferred interests regulatory deferral account in Q1 fiscal 2017 was primarily due to the regulatory deferral of higher unrealized foreign exchange gains recorded due to the fluctuation of the Canadian dollar against the U.S. dollar.

The realized hedging transactions regulatory deferral account is comparable to Q1 fiscal 2016.

(in millions of dollars)

Movements in Rate Stabilization Account

Our rate stabilization mechanism and accounting are described at the beginning of this MD&A and in notes 1 and 9 of our fiscal 2016 annual consolidated financial statements. The table below shows the movements in the rate stabilization account.

	Three months ended November 30		
	2016	2015	Change
Credit balance on the statement of financial position, beginning of period	$ 169	$ 81	$ 88
Variances from planned results:			
Revenue higher than planned	15	3	12
Operating expenses lower than planned	1	19	(18)
Other (income) and expenses lower than planned	2	5	(3)
Net movement in other regulatory deferral accounts	(1)	(14)	13
Total variances from planned results	17	13	4
Initial approved adjustment	(10)	8	(18)
Net movement in rate stabilization account recorded in net income (loss)	7	21	(14)
Credit balance on the statement of financial position, end of period	$ 176	$ 102	$ 74

The $7 improvement in the rate stabilization account during the three months ended November 30, 2016 is primarily due to:

- revenue that was $15 higher than planned due to an increase in customer service charge revenue arising from higher air traffic;
- other (income) and expense that was $2 higher than planned as a result of positive fair value adjustments of $12, partially offset by the redemption premium of $10;

partially offset by:

- the planned adjustment of $10, representing one quarter of the anticipated net loss at the time the fiscal 2017 budget was approved.

(in millions of dollars)

Other Comprehensive Income (Loss)

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

	Three months ended November 30		
	2016	2015	Change
Items that will not be reclassified to income or (loss):			
Re-measurements of employee defined benefit plans	$ 318	$ 117	$ 201
Net movement in regulatory deferral accounts	(318)	(117)	(201)
	-	-	-
Items that will be reclassified to income or (loss):			
Changes in fair value of cash flow hedges	36	(11)	47
Net movement in regulatory deferral accounts	(36)	11	(47)
	-	-	-
Total other comprehensive income (loss)	$ -	$ -	$ -

Re-measurement gains of employee defined benefit plans in Q1 fiscal 2017 of $318 are a result of actuarial gains of $425, primarily due to a 40 basis point increase in the discount rates, partially offset by a return on plan assets $107 less than the expected return based on the discount rate. In Q1 fiscal 2016, the re-measurement gains of $117 were mainly due actuarial gains of $103, primarily due to a 10 basis point increase in the discount rate, and a return on plan assets $11 greater than the expected return based on the discount rate.

During Q1 fiscal 2017, positive fair value adjustments of $36 were recorded on the Company's interest rate hedges related to the re-financing of debt instruments that will mature in the fiscal year ending August 31, 2019 (fiscal 2019). In Q1 fiscal 2016, negative fair value adjustments of $11 were recorded on interest rate hedges related to the refinancing of debt maturing in fiscal 2016 and fiscal 2019.

(in millions of dollars)

Amounts Considered for Rate Setting Purposes

As discussed under "INTRODUCTION – Financial Strategy and Rate Regulation", when establishing customer service charges the Board considers the Company's current and future financial requirements as well as the current and anticipated balance in the rate stabilization account, adjusted notionally for the non-credit related portion of the fair value variance from face value on investments, as compared to its target balance.

The table below shows the "notional" credit balance of the rate stabilization account as compared to its target balance.

	November 30 2016	August 31 2016	Change
Rate stabilization account credit balance	$ 176	$ 169	$ 7
Fair value variances on ABCP investments[1]	-	11	(11)
Face value variance on MAV II Class A-2 notes when purchased in fiscal 2011	3	3	-
Credit loss provisions on ABCP investments	-	-	-
Net non-credit related fair value variances from face value	3	14	(11)
"Notional" balance of the rate stabilization account[1]	179	183	(4)
Target balance of the rate stabilization account[2]	(101)	(100)	(1)
Amount to be returned over time through rate setting	$ 78	$ 83	$ (5)

As at August 31, 2016, the amount to be returned over time through rate setting was $83. There has been a decrease in the amount to be returned over time through rate setting to $78 during fiscal 2017.

(1) The fair value variance from face value on restructured ABCP investments held by the Company as at November 30, 2016 of $3 is comprised of the realized fair value variance on MAV II Class A-2 notes when purchased in the year ended August 31, 2011 (fiscal 2011). The Company currently estimates that the full fair value variance from face value of $3 will be recovered over time, as the fair value of these investments should ultimately reflect the face value of the notes less credit losses, which are currently estimated at $nil. Accordingly, $3 has been added to the rate stabilization account credit balance to arrive at the "notional" balance.

(2) The long-term target credit balance of the rate stabilization account is 7.5% of total planned annual expenses net of other (income) and expenses, excluding non-recurring items, on an ongoing basis. For fiscal 2017, the target balance was $101.

(in millions of dollars)

Financial Outlook[2]

Presented below are the Company's current projected annual consolidated results before rate stabilization for fiscal 2017 compared to fiscal 2016 results.

	Fiscal 2017	Fiscal 2016	Change	%
Before rate stabilization				
Revenue	$ 1,333	$ 1,393	$ (60)	(4%)
Operating expenses and other (income) and expenses, including other regulatory adjustments	1,347	1,305	42	3%
Net income (loss) before rate stabilization adjustments	$ (14)	$ 88	$ (102)	

Revenue

Total revenue for fiscal 2017 is expected to decrease by approximately 4.3% or $60 from $1,393 in fiscal 2016, primarily due to the lower revised service charges (7.6% on average) that became effective September 1, 2016, partially offset by forecasted air traffic growth of 3.9%.

In our fiscal 2016 annual MD&A, we had disclosed anticipated revenue of $1,329 for fiscal 2017. The $4 increase in forecasted revenue is primarily due to an increase in air traffic, which grew by 5.5% during Q1 fiscal 2017 compared to the forecast of 5.0%.

Operating Expenses and Other (Income) and Expenses

Operating expenses and other (income) and expenses before rate stabilization for fiscal 2017 are expected to be $1,347. This is an increase of $42 compared to fiscal 2016 due to:

- higher compensation levels, including increased overtime;
- increased pension current service costs and net interest costs related to employee benefits;
- increased operational requirements in the areas of technical services and facilities and systems maintenance;
- increased other operating expenses, as refunds of $7 relating to commodity taxes paid in prior years were received in fiscal 2016 with no equivalent amount forecasted for fiscal 2017; and
- the effects of inflation;

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

partially offset by:

- lower expected regulatory pension expense, due to lower expected pension contributions on which the regulatory pension expense is based; and
- higher forecasted positive fair value adjustments on investments.

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

In our fiscal 2016 annual MD&A, we had disclosed anticipated operating expenses and other (income) and expenses, before rate stabilization of $1,343 for fiscal 2017. The $4 increase is primarily due to higher forecasted pension current service costs and other (income) and expenses, partially offset by a decrease in operating expenses and the change in the net movement in regulatory deferral accounts.

Cash Flows

Given the expected net cash flows from operations and cash flows from investing and financing activities in fiscal 2017, the Company's cash position is currently expected to decrease to $117 as at August 31, 2017 from $119 as at August 31, 2016. This cash outlook is based on anticipated annual cash inflows from operating and investing activities of $140 and $84 respectively, offset by cash outflows from financing activities of $226 for the repayment of long-term debt (based on the assumption that it will be economically attractive to redeem outstanding debt). Investing activities in fiscal 2017 are forecast to include cash inflows of $292 from proceeds from the maturity of ABCP investments, partially offset by cash outflows for projected capital expenditures of $167, additional investment in preferred interests of Aireon of $36 and an income tax payment of $5. As discussed below, the Company has adequate existing sources of financing to cover all of its anticipated cash flow requirements.

In our fiscal 2016 annual MD&A, we had disclosed an anticipated cash position of $112 by the end of fiscal 2017. The $5 increase in our cash position at the end of fiscal 2017 is primarily due to an increase in cash inflows from operations as a result of a decrease in forecasted interest payments.

Rate Stabilization Account

As noted above, the Company has implemented revisions to its customer service charges, effective September 1, 2016. In addition to revising our base rates in order to ensure they are aligned with costs, we have also implemented a temporary one-year reduction in base rates, representing on average a 3.7% reduction from fiscal 2016 base rates. The purpose of the one-year temporary rate reduction is to return to customers the estimated amount by which the notional balance of the rate stabilization account exceeded its target balance at August 31, 2016 (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

The Company currently anticipates that the rate stabilization account will have a credit balance of $155 at the end of fiscal 2017, resulting from estimated revenue of $1,333, after considering the revisions to base rates and the temporary rate reduction, and total operating expenses and other (income) and expense (including other regulatory adjustments) of $1,347 (before rate stabilization). It is anticipated that the "notional" balance of the rate stabilization account will also be $155 at the end of fiscal 2017, as we are expecting that our ABCP investments will have matured by year-end. The target balance of the rate stabilization account in fiscal 2017 is $101.

In our fiscal 2016 annual MD&A, we had forecast an anticipated rate stabilization account credit balance of $155 at the end of fiscal 2017. The changes in the forecast discussed above have not resulted in a change in the expected balance of the rate stabilization account at the end of fiscal 2017.

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

Earnings and Cash Flow Coverage

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

For the twelve months ended November 30, 2016, the Company achieved net income of $2. Our interest cost was $99. Consolidated earnings (after rate stabilization) before interest were $101, which is 1.02 times our interest requirement for the fiscal year and just above our one-to-one target. Depreciation and amortization expense for this period was $142. Our cash flow coverage was 2.45 times our interest requirement for this period.

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

We maintain a debt service reserve fund and an operations and maintenance reserve fund under our Master Trust Indenture and we are subject to liquidity covenants under our General Obligation Indenture, designed to cover 12 months interest on borrowings and 25% of our annual operating and maintenance expenses. As at November 30, 2016, we were in full compliance with our debt indentures, including the Master Trust Indenture's requirements regarding the reserve funds, the flow of funds and with the rate covenants, as well as the liquidity and other provisions of the General Obligation Indenture.

Related Party Transactions

The Company's related parties include its key management personnel, subsidiaries, joint venture and registered pension plans for its employees. The transactions with these related parties are not materially different from what was reported in the fiscal 2016 annual MD&A.

(in millions of dollars)

SUMMARY OF QUARTERLY RESULTS

Quarterly Financial Information (unaudited)

	Three months ended			
	Q1 November 30 2016	Q4 August 31 2016	Q3 May 31 2016	Q2 February 29 2016
Revenue	$ 332	$ 405	$ 337	$ 309
Operating expenses	321	316	319	307
Other (income) and expenses	22	27	34	25
	(11)	62	(16)	(23)
Income tax expense	1	1	-	1
Net income (loss) before net movement in regulatory deferral accounts	(12)	61	(16)	(24)
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	(7)	(32)	(16)	(19)
Other regulatory deferral account adjustments	19	20	24	4
	12	(12)	8	(15)
Net income (loss) after net movement in regulatory deferral accounts	$ -	$ 49	$ (8)	$ (39)

	Three months ended			
	Q1 November 30 2015	Q4 August 31 2015	Q3 May 31 2015	Q2 February 28 2015
Revenue	$ 342	$ 384	$ 329	$ 296
Operating expenses	296	305	304	300
Other (income) and expenses	30	24	37	17
	16	55	(12)	(21)
Income tax expense	-	1	-	1
Net income (loss) before net movement in regulatory deferral accounts	16	54	(12)	(22)
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	(21)	2	-	-
Other regulatory deferral account adjustments	3	(14)	4	(11)
	(18)	(12)	4	(11)
Net income (loss) after net movement in regulatory deferral accounts	$ (2)	$ 42	$ (8)	$ (33)

Discussion of Quarterly Results

The quarterly variations in revenue mainly reflect seasonal fluctuations. Typically, revenue is highest in our fourth quarter (June to August) as a result of increased air traffic in the summer months. The second quarter (December to February) typically has the lowest air traffic volumes. Air traffic for Q1 fiscal 2017 was 5.5% higher on average than in Q1 fiscal 2016. Effective September 1, 2016, the Company implemented revisions to its service charges resulting in reductions on average of 7.6%.

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

Other (income) and expenses fluctuate primarily due to:

- fair value adjustments on investments and derivative instruments which change based on market factors and changes in expectations of credit losses; and
- changes in foreign exchange (gains) or losses as a result of the strengthening or weakening of the Canadian dollar compared to foreign currencies in which the Company transacts, mainly the U.S. dollar.

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

- changes in the rate stabilization account based on variances from planned results and the initial approved adjustment;
- changes in employee benefit pension contributions;
- changes in other employee benefits, including LTD funding requirements;
- changes in the investment in preferred interests of Aireon, net of tax; and
- changes in realized hedging transactions.

LIQUIDITY AND CAPITAL RESOURCES

Our fiscal 2016 annual MD&A explains how we manage our cash and capital resources. There have been no changes in that approach for the three months ended November 30, 2016. The following sections discuss changes in our cash and capital resources since August 31, 2016.

As at November 30, 2016, we had $224 of cash and committed credit facilities of $1,190, of which $446 was available for unrestricted use (see "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

(in millions of dollars)

Cash flows for the three months ended November 30, 2016

	Three months ended November 30		
	2016	2015	Change
Cash flows from:			
Operations	$ 56	$ 86	$ (30)
Investing	48	(6)	54
Cash flows from operating and investing activities	104	80	24
Effect of foreign exchange on cash and cash equivalents	1	-	1
Increase in cash and cash equivalents	105	80	25
Cash and cash equivalents, beginning of period	119	230	(111)
Cash and cash equivalents, end of period	$ 224	$ 310	$ (86)
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations	$ 56	$ 86	$ (30)
Capital expenditures [(1)]	(32)	(34)	2
Free cash flow	$ 24	$ 52	$ (28)

(1) See the statement of cash flows in our Q1 fiscal 2017 financial statements.

As shown above, cash increased by $105 for the three months ended November 30, 2016 and the Company experienced positive free cash flow of $24, which is a non-GAAP financial measure. Non-GAAP financial measures do not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers. The Company defines free cash flow as cash generated from operations, less capital expenditures and investments in Aireon and other subsidiaries. Management places importance on this indicator as it assists in measuring the impact of its investment program on the Company's financial resources.

Cash flows from operations for the three months ended November 30, 2016 decreased by $30 from the three months ended November 30, 2015, primarily due to higher payments to employees and suppliers of $28 and lower receipts from customers of $10, partially offset by lower special pension payments of $7.

Cash flows from investing activities for the three months ended November 30, 2016 were inflows of $48 compared to outflows of $6 in the three months ended November 30, 2015. During Q1 fiscal 2017, we invested $31 in capital projects (cash outflows of $32) compared to $35 in Q1 fiscal 2016 (cash outflows of $34). In addition, we received $80 of proceeds from MAV II notes and restructured ABCP compared to $2 received in the three months ended November 30, 2015.

For the three months ended November 30, 2015, our cash balance increased by $80. This was primarily due to cash inflows from operations of $86 and the receipt of recoverable input tax payments of $26 on termination of the cross border transaction, partially offset by capital expenditures of $34.

(in millions of dollars)

Liquidity and Financing Strategy

Our liquidity and financing strategy remains unchanged from that disclosed in our fiscal 2016 annual MD&A.

Subsequent to November 30, 2016, the Company redeemed $100 of the $350 Series MTN 2009-1 General Obligation Notes with proceeds from the MAV II notes and surplus cash.

We are exposed to re-financing risk with respect to our bond and note maturities, including the $25 annual amortizing payment due on the Series 97-2 amortizing revenue bonds. We mitigate this risk by maintaining committed credit facilities in an amount sufficient to meet our refinancing needs in the event of temporary capital market disruptions or lack of access to the market for any reason. The Company also has a Base Shelf Prospectus in place that is valid until December 6, 2017.

The Company has a revolving credit facility with a syndicate of Canadian financial institutions and separate letter of credit facilities for pension funding purposes. As at November 30, 2016, the credit facilities are utilized as follows:

Credit facilities:		
Credit facility with a syndicate of Canadian financial institutions [(1)]	$	675
Letter of credit facilities for pension funding purposes [(2)]		515
Total available credit facilities		1,190
Less: Outstanding letters of credit [(2)]		474
Undrawn committed borrowing capacity		716
Less: Operations and maintenance reserve fund allocation [(3)]		270
Credit facilities available for unrestricted use	$	446

(1) The Company's credit facility with a syndicate of Canadian financial institutions in the amount of $675 is comprised of two equal tranches maturing on September 12, 2019 and September 12, 2021. The credit facility agreement provides for loans at varying rates of interest based on certain benchmark interest rates, specifically the Canadian prime rate and the Canadian bankers' acceptance rate, and on the Company's credit rating at the time of drawdown. A utilization fee is also payable on borrowings in excess of 25% of the available facility. The Company is required to pay commitment fees, which are dependent on the Company's credit rating. The Company is in compliance with the credit facility covenants as at November 30, 2016.

(2) The letter of credit facilities for pension funding purposes are comprised of four facilities with Canadian financial institutions totalling $515, which will mature on December 31, 2017, unless extended. The Company intends to seek extensions of the maturity dates. Of the $474 in letters of credit shown above as outstanding as at November 30, 2016, $463 was drawn for pension solvency funding purposes.

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

(in millions of dollars)

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

	November 30 2016	August 31 2016
LONG-TERM DEBT:		
Bonds and notes payable		
Under the Master Trust Indenture	$ 525	$ 525
Under the General Obligation Indenture	1,200	1,200
	1,725	1,725
Adjusted for deferred financing costs and discounts	(6)	(6)
Total bonds and notes payable	1,719	1,719
Less: current portion	(125)	(25)
Total non-current loans and borrowings	$ 1,594	$ 1,694
LIQUIDITY (excludes MAV II, restructured ABCP and other notes shown below):		
Cash	$ 224	$ 119
Debt service reserve fund	94	94
	$ 318	$ 213
Undrawn committed borrowing capacity (1)	$ 716	$ 716
MAV II, RESTRUCTURED ABCP AND OTHER NOTES:		
Face value (2)	$ 213	$ 293
Fair value variance from face value	(3)	(14)
	$ 210	$ 279

(1) $446 of this borrowing capacity is available as described in the previous table.

(2) See also "LIQUIDITY AND CAPITAL RESOURCES – Financial Instruments and Risk Management: Financial Risk Management" (specifically "Liquidity Risk").

Credit Ratings

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

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

Our credit ratings remain unchanged from those described in our fiscal 2016 annual MD&A.

(in millions of dollars)

Cash Requirements

The following information about our contractual obligations and other commitments summarizes certain of our liquidity and capital resource requirements.

Pension Plans

Required pension contributions to the Company's pension plans are determined by annual actuarial valuations for funding purposes performed as at January 1 (see below under "Pension Contributions (Going Concern and Solvency)"). Our latest actuarial valuations (for funding purposes) as at January 1, 2016 were completed and filed with the Office of the Superintendent of Financial Institutions Canada in June 2016. Going concern pension contributions have not changed significantly from that reported in the Company's fiscal 2016 annual MD&A.

Pension Plans' Accounting Deficit: The Company's pension plans had an accounting deficit of $1,415 as at the annual measurement date of August 31, 2016 and an accounting deficit of $1,138 as at November 30, 2016. The $277 decrease in the deficit position during fiscal 2017 is primarily due to net actuarial gains of $307 partially offset by actuarial accounting expense exceeding Company contributions by $30. The $307 of net actuarial gains are primarily due to a $414 actuarial gain from a 40 basis point increase in the discount rate, partially offset by a return on plan assets $107 less than the expected return based on the discount rate.

Regulatory Recovery of Pension Costs: As described in our fiscal 2016 annual MD&A, the Company uses a regulatory approach for pension costs to determine the net impact charged to net income (loss). The objective of this approach is to expense the cost of the Company's cash contributions to the pension plans.

The recovery of pension benefit costs (charged to the statement of operations) was as follows:

	Three months ended November 30	
	2016	2015
Pension benefit costs (Per IAS 19 *Employee Benefits*)		
Current service costs	$ 44	$ 36
Net interest costs related to employee benefits	12	9
Net movement in regulatory deferral account related to pensions		
Regulatory decrease	(30)	(11)
Recovery of pension benefit costs	$ 26	$ 34

Pension Contributions (Going Concern and Solvency): The actuarial valuations for funding purposes of the pension plans performed as at January 1, 2016 reported a going concern deficit of $76 (January 1, 2015 – a deficit of $268).

(in millions of dollars)

The regulations governing the funding of federally regulated pension plans include a solvency test, which assumes the plans are terminated as at the valuation date. The actuarial valuations performed as at January 1, 2016 reported a statutory solvency deficiency of $306 (January 1, 2015 – a statutory solvency deficiency of $556).

The Company is currently meeting its pension solvency funding requirements with letters of credit. Pension funding regulations came into effect in April 2011 permitting solvency special payments to be replaced by letters of credit, provided the total value of the letters of credit does not exceed 15% of the pension plan's assets. As of November 30, 2016, the Company has put in place letters of credit totaling $463 (representing 9% of registered pension plan assets as at November 30, 2016) to meet its cumulative pension solvency funding requirements to the end of calendar year 2016. For the annual period beginning July 1, 2016, letters of credit are based on the January 1, 2016 actuarial valuations.

The amount of required Company contributions and additional letters of credit for future years will be dependent on the investment experience of plan assets, the discount rates and other assumptions that will be used in future actuarial valuations to determine plan liabilities, as well as any changes in pension plan design or funding requirements that may be enacted.

Contractual Obligations

A breakdown of contractual obligations for the next five fiscal years and thereafter is presented in the following table.

	Remaining payments – for years ending August 31						
	Total	2017	2018	2019	2020	2021	Thereafter
Derivative liabilities	$ 19	$ -	$ -	$ 19	$ -	$ -	$ -
Long-term debt (including current portion) (1), (2)	1,725	125	375	275	25	275	650
Interest payments (2)	680	68	77	69	53	46	367
Capital commitments (3)	121	38	28	11	12	6	26
Operating leases	42	6	8	7	6	6	9
Investment in preferred interests in Aireon (4)	36	16	20	-	-	-	-
Total contractual obligations	$ 2,623	$ 253	$ 508	$ 381	$ 96	$ 333	$ 1,052

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

(1) Payments represent principal of $1,725. The Company intends to refinance principal maturities at their maturity dates. The Company may choose to repay a portion of these maturities with available cash, and/or may increase the size of a re-financing to generate additional liquidity or for other purposes, and/or may choose to redeem, in whole or in part, an issue in advance of its scheduled maturity date. Subsequent to November 30, 2016, the Company reduced its long-term debt with the redemption of $100 of the $350 Series MTN 2009-1 General Obligation Notes, which were repaid with proceeds from the MAV II notes and surplus cash.

(in millions of dollars)

(2) Further details on interest rates and maturity dates on long-term debt are provided in note 21 to our fiscal 2016 annual consolidated financial statements.

(3) The Company has firm commitments for the acquisition of property, plant and equipment and intangible assets amounting to $121 as at November 30, 2016 (August 31, 2016 - $118).

(4) Payments represent contractual obligations to invest in preferred interests of Aireon, subject to conditions pursuant to the agreements the Company entered into in November 2012 which set out the terms of its participation in Aireon, as amended (the November 2012 agreements). Amounts are presented in CDN translated using the hedged rate for each tranche investment. In March 2016, the November 2012 agreements were amended to reflect the extension of the fourth tranche investment milestone deadline to fiscal 2017. Subsequent to November 30, 2016, the Company completed its fourth tranche investment of $15 U.S. ($16 CDN) on December 21, 2016.

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

The Company's contributions to its pension plans are discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Cash Requirements: Pension Plans".

Capital Management

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

	November 30 2016	August 31 2016
Bonds and notes payable	$ 1,719	$ 1,719
Equity:		
Retained earnings	28	28
Regulatory deferral accounts:		
Debit balances	(1,355)	(1,708)
Credit balances	465	476
Employee benefits:		
LTD liability	1	1
Liability for funded pension benefits	1,066	1,346
Liability for accumulating sick leave	21	21
Total capital	$ 1,945	$ 1,883

Management's approach and objectives when managing capital remain unchanged from those described in our fiscal 2016 annual MD&A.

(in millions of dollars)

Financial Instruments and Risk Management

Restructured and Other Investments in ABCP[3]

(See also "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

The Company holds the following investments in MAV II and other investments (that were not subject to the restructuring by the Pan Canadian Investors Committee) as at November 30, 2016:

	Face value	Fair value variances	Fair value
MAV II notes			
Class A-1	$ 118	$ (1)	$ 117
Class A-2	94	(1)	93
	212	(2)	210
Other notes	1	(1)	-
Total	$ 213	$ (3)	$ 210

The restructured notes are designated as FVTPL. Changes in fair value are recorded in income as they arise. As shown in the table above, the fair value of these notes is $210 as at November 30, 2016, which is $3 below the face value of the notes. The Company's fair value methodologies are discussed in note 9 to our Q1 fiscal 2017 financial statements. The Company has used a discounted cash flow approach to determine the fair value of these investments, incorporating available information regarding market conditions as at the measurement date, November 30, 2016. The estimates arrived at by the Company are subject to measurement uncertainty and are dependent on market conditions as at the measurement date.

The future value of our investments in MAV II and other notes cannot be predicted with any degree of certainty. The asset provider counterparties to these transactions have the right to require that additional collateral be posted under these transactions if certain triggers are breached. If the collateral requirements are not met, the asset providers may unwind the trades and liquidate collateral to cover their losses. This would likely lead to the loss of a significant portion or all of our MAV II notes with a face value as at November 30, 2016 of $212. The likelihood of this occurring has been made more remote by certain features of the restructuring, including the provision of a margin funding facility, the adoption of more remote spread/loss triggers, the pooling of trades, and the retention of cash and traditional assets as collateral. In addition, a significant number of the high risk assets originally held within MAV II have now matured without incurring losses. As at November 30, 2016, the remaining unexpired index referenced in the spread/loss triggers was at 3% of its trigger level.

There is no assurance that the fair value of the Company's investments in MAV II and other notes will not decline or that significant deterioration in financial markets will not cause losses on the individual collateralized debt obligations or margin calls in excess of MAV II's ability to meet them, resulting in significant credit losses. The estimated fair value of the Company's investments, including the expected credit losses, may change in subsequent periods. Any such changes could be material and would be reflected in the statement of operations as they occur.

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

Reserve Funds and Financial Instruments

Under the Master Trust Indenture, we maintain a debt service reserve fund and an operations and maintenance reserve fund. We are also required to meet certain minimum liquidity levels under the General Obligation Indenture. The requirements of the debt service reserve fund and the operations and maintenance reserve fund remain unchanged from that described in our fiscal 2016 annual MD&A.

Financial Risk Management

The Company is exposed to several risks as a result of holding financial instruments, including interest rate risk, foreign exchange risk, price risk, credit risk and liquidity risk. The Company's exposure to financial risks and how the Company manages each of those risks are described in the Company's fiscal 2016 annual MD&A. There were no significant changes to those risks or to the Company's management of exposure to those risks during the three months ended November 30, 2016, except as noted below.

Foreign Exchange Risk: The Company designates certain of its forward contracts as cash flow hedging instruments to hedge the Company's exposure to the impact of exchange rate fluctuations. As at November 30, 2016, the Company has purchased $15 U.S. ($16 CDN) and entered into a forward contract to purchase an additional $15 U.S. ($20 CDN) to hedge the Canadian dollar cost related to its outstanding commitments to acquire additional preferred interests in Aireon.

Legal Proceedings

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

CHANGES IN ACCOUNTING POLICIES

The Company's Q1 fiscal 2017 financial statements were prepared in accordance with IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board (IASB). Significant accounting policies used in the Q1 fiscal 2017 financial statements are disclosed in note 3 of the Company's fiscal 2016 annual consolidated financial statements, except for the application of new standards, amendments and interpretations effective September 1, 2016. The accounting policies have been applied consistently to all periods presented, unless otherwise indicated.

In December 2014, the IASB issued Disclosure Initiative (Amendments to IAS 1 *Presentation of Financial Statements*). These amendments improve the existing presentation and disclosure requirements and encourage entities to apply professional judgment regarding disclosure and presentation in their financial statements. These amendments were adopted effective September 1, 2016. The adoption of these amendments resulted in no change to the Q1 fiscal 2017 financial statements. Immaterial disclosures are expected to be removed from the Company's annual consolidated financial statements.

Future Accounting Pronouncements

The IASB has issued a number of standards and amendments that are not yet effective. The Company continues to analyze these standards and amendments to determine the extent of their impact on its consolidated financial statements. At this time, the Company does not expect to adopt any of these standards or amendments before their effective dates.

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

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

The Company's critical accounting estimates and judgments applied in the preparation of the Company's Q1 fiscal 2017 financial statements are consistent with those applied and disclosed in our fiscal 2016 annual consolidated financial statements and as described in the fiscal 2016 annual MD&A.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes to the Company's internal control over financial reporting (ICFR) during the three months ended November 30, 2016 that have materially affected or are reasonably likely to materially affect the Company's ICFR.