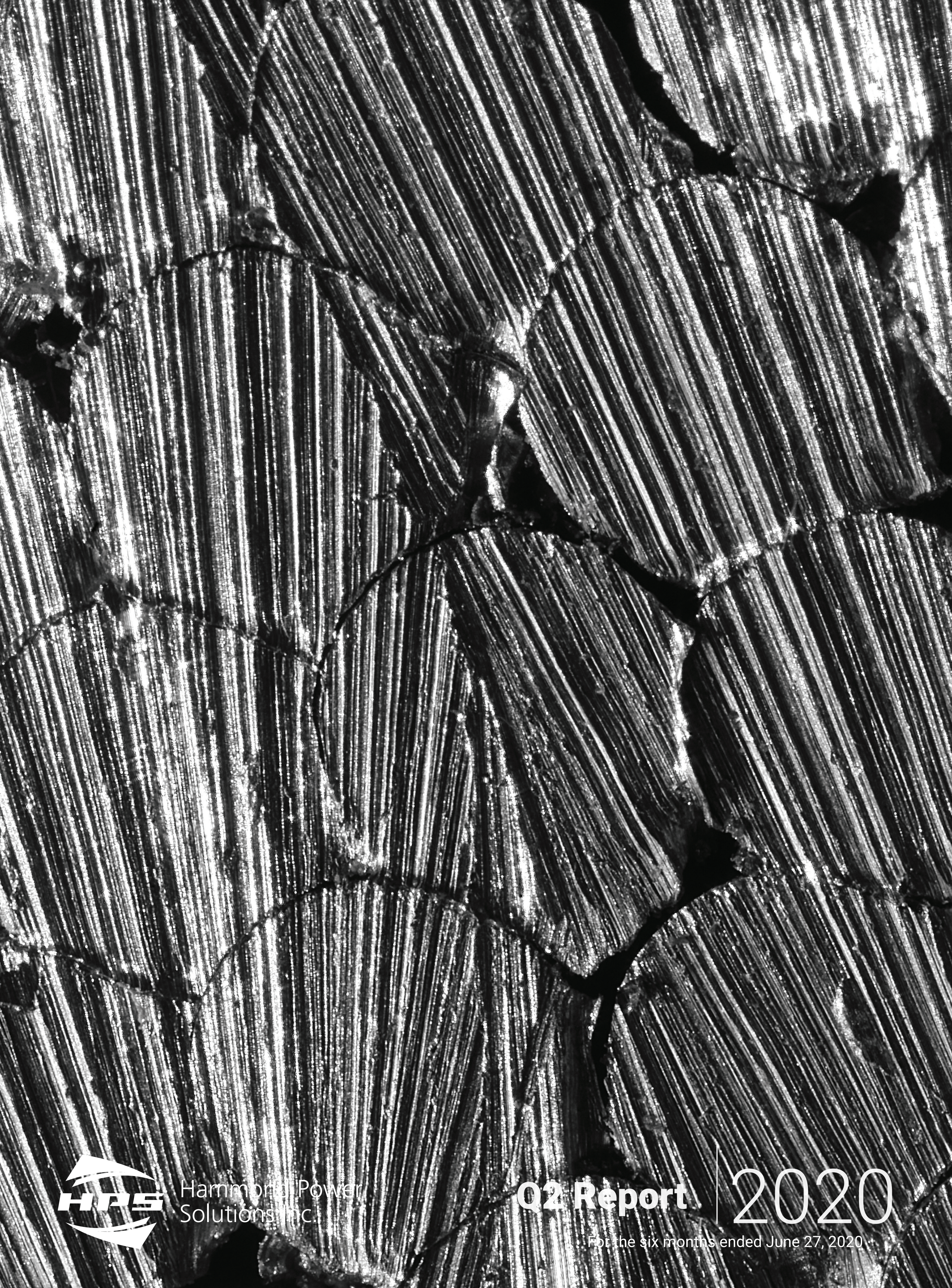

HPS

Hammond Power
Solutions Inc.

Q2 Report 2020

For the six months ended June 27, 2020

Our Vision

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

Our Mission

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

Our Values

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

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

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

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

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

Fellow shareholder,

Hammond Power Solutions Inc. ("HPS") along with the rest of the world continues to maneuver through one of the most challenging periods in history. These challenges and uncertainties created by COVID-19 have been unprecedented and we realize that this crisis is far from over. We are very proud of our performance as a Company during this fragile time and of the safeguards taken to protect the health of our employees as well as the health of our business.

Our highest priority has been and remains the well-being of our employees around the globe. We believe the strict health and safety precautions we implemented at the onset of the pandemic assisted in minimizing the number of employee cases throughout our 14 facilities and nearly 1,400 employees in Canada, the United States ("U.S."), Mexico and India. This has allowed HPS facilities to continue to operate in North America. In India however, the federal and state governments have mandated the closure of all businesses in most parts of the country for a period as long as three months. As waves of this virus continue to surge over parts of the globe, our priority will remain on protecting the health of our employees and their families.

As mentioned, this focus has allowed HPS to continue operating in its North American facilities where warehouses also remain open and continue to serve the needs of our distributors and customers. As anticipated, our Quarter 2, 2020 results were heavily impacted by the widespread economic shutdown across most of North America in April and May. Some parts of our business saw declines in activity of 30-50%, particularly in Canada where government measures were considerably more restrictive. On a year-to-date basis our total sales at the half-way point are down 7.3%.

The strength and resiliency of our business has contributed to our relative success during this pandemic. Our diversity in terms of geography, channels, markets and products has moderated the impact of certain devastated markets. Our dominance in the distributor channel along with the broad and deep inventories that we have maintained over the last months has assisted us with market share growth even as the economy has slowed. We have been able to take advantage of situations where a number of competitors have not been able to supply products as their U.S. and Mexican operations were closed due to COVID outbreaks.

The Company has been able to deliver higher than expected profitability through a combination of favourable product mix and cost reductions, as well as the ability to charge premium pricing on short lead time business. The Company also qualified for a wage subsidy provided by the Canadian federal government which provided support to companies with a significant downturn in their Canadian sales. This has been beneficial in allowing HPS to continue to serve the needs of our customers while supporting our employees and their families.

All considered, we are very pleased with our relative performance over the first half of 2020. We know that considerable uncertainty and volatility will continue into next year coupled with the added complications of the U.S. election as well as global geo-political trade tensions. Nonetheless, we believe that when this crisis has abated, HPS will emerge in a stronger market position. We will continue to focus on fiscal discipline and striking the right balance between short and long-term strategic investments that we believe will position us well for the future.

In closing, I would like recognize the incredible efforts of our employees as well as the amazing support of our suppliers, distributors and customers.

Thank you all!

WGH

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

Management's Discussion and Analysis

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

The following is Management’s Discussion and Analysis (“MD&A”) of the Company’s consolidated operating results for the six months ended June 27, 2020, and should be read in conjunction with the accompanying unaudited Condensed Interim Consolidated Financial Statements of the Company for the second quarter of fiscal 2020. This information is based on Management’s knowledge as at July 30, 2020. The Company assumes that the reader of this MD&A has access to and has read the audited Annual Consolidated Financial Statements and MD&A of the Company, contained in our 2019 Annual Report and accordingly, the purpose of this document is to provide a second quarter update to the information contained in the fiscal 2019 MD&A. All amounts are reported under International Financial Reporting Standards (“IFRS”). All amounts in this report are expressed in thousands of Canadian dollars unless otherwise noted. Additional information relating to the Company may be found on SEDAR’s website at www.sedar.com, or on the Company’s website at www.hammondpowersolutions.com.

Caution regarding forward-looking information

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

Additional GAAP and Non-GAAP measures

This document uses the terms "earnings from operations" which represents earnings before finance and other costs/(income) and income taxes. "EBITDA" is also used and is defined as earnings before interest, taxes, depreciation and amortization. "Adjusted EBITDA" from continuing operations represents EBITDA from continuing operations adjusted for foreign exchange gain or loss. Operating earnings, EBITDA and Adjusted EBITDA are some of the measures the Company uses to evaluate the operational profitability. The Company presents EBITDA to show its performance before interest, taxes and depreciation and amortization. Management believes that HPS shareholders and potential investors in HPS use additional GAAP and non-GAAP financial measures, such as operating earnings, EBITDA and Adjusted EBITDA in making investment decisions about the Company and to measure its operational results. A reconciliation of EBITDA and Adjusted EBITDA to net earnings for the quarters ending June 27, 2020 and June 29, 2019 is contained in the MD&A. Earnings from operations, EBITDA and Adjusted EBITDA should not be construed as a substitute for net earnings determined in accordance with IFRS.

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

Sales

Sales from continuing operations for the quarter-ended June 27, 2020 were $75,393, a decrease of $16,544 or 18.0% from Quarter 2, 2019 sales of $91,937. The sales decline was primarily impacted by the negative effect that the COVID-19 global pandemic had on many of our markets and our customers due to the delay of electrical projects and their suspension of operations due to lockdowns. Year-to-date 2020 sales from continuing operations decreased $12,814 or 7.3% to $163,813 compared to $176,627 in 2019.

Sales in the United States ("U.S.") decreased by $7,354 or 12.4%, finishing at $51,892 for Quarter 2, 2020 compared to $59,246 in Quarter 2, 2019. Year-to-date U.S. sales were $108,233 in 2020 and $113,440 in 2019, a decline of $5,207 or 4.6%. The decrease in the Quarter 2, 2020 sales is a result of declines in the North American Electrical Distributor ("NAED") channel, private branding, technical services, motor control, specialty and mining markets, partially offset by an increase in capital equipment.

Second quarter sales were favourably affected by a 3.7% stronger U.S. dollar ("USD") $1.00 USD = $1.39 Canadian dollar ("CAD") compared against $1.00 USD = $1.34 CAD in Quarter 2, 2019. Year-to-date sales were positively impacted by a 2.3% stronger U.S. dollar - $1.00 USD = $1.36 CAD compared against $1.00 USD = $1.33 CAD in 2019.

U.S. sales, when stated in U.S. dollars were $37,314 in Quarter 2, 2020, compared to Quarter 2, 2019 of $44,282, a decline of $6,968 or 15.7%. Year-to-date U.S. sales stated in U.S. dollars were $79,397 in 2020 compared to $85,027 in 2019, a decrease of $5,630 or 6.6%.

Canadian sales were $21,922 for the quarter, a decrease of $7,361 or 25.1% from Quarter 2, 2019 sales of $29,283. Year-to-date Canadian sales were $49,266 in 2020 compared to $55,524 in 2019, a decrease of $6,258 or 11.3%. Canadian sales experienced declines in a number of markets this quarter compared to the same quarter last year, specifically NAED, motor control, capital equipment and switchgear markets.

Indian sales for Quarter 2, 2020 finished at $1,579 versus $3,408 in Quarter 2, 2019, a decrease of $1,829 or 53.7% due to government imposed COVID-19 100% lockdown of the country during the quarter. Year-to-date Indian sales were $6,314 in 2020 compared to $7,663 in 2019, a decrease of $1,349 or 17.6%.

Quarter 2, 2020 sales from continuing operations stated by geographic segment were derived from U.S. sales of 68.8% (Quarter 2, 2019 – 64.4%) of total sales, Canadian sales of 29.1% (Quarter 2, 2019 – 31.9%), and Indian sales of 2.1% (Quarter 2, 2019 – 3.7%).

The impact of COVID-19 was evident in the Company's second quarter sales where declines were seen across many markets and customers. In Quarter 1, 2020 the Company had experienced market share growth through U.S. distributor channels due to the ability to produce both standard and custom transformers. In the first quarter of 2020, the Company experienced an increase in distribution transformer sales through the NAED channel – specifically used for new U.S. field hospitals that were being established as a result of the increased hospitalization demand caused by the impact of COVID-19.

While second quarter sales declined due to the impact of the global pandemic, the Company was steadfast in growing market share through its strong NAED and Original Equipment Manufacturer ("OEM") channels. This was achieved through the Company's broad product offerings, organic customer diversity, new customer business development and geographically diverse manufacturing capabilities. The Company's market share continues to be industry leading – distributor conversions, standard and custom transformers manufacturing capabilities and service commitment all allow the Company to be a leader in the electrical transformer market.

We are unwavering in our commitment to providing exceptional value to our customers through product breadth, competitive custom engineered designs, uncompromised quality, new product development and ease of doing business.

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

The Company prides itself on building our value proposition to our customers through consistent quality, innovative and competitive product design, industry expertise in custom engineered products and expanded product breadth. These factors coupled with a strong, effective distribution channel, multi-national manufacturing capabilities and global reach will continue to be an advantage for the Company and important to continued revenue growth. The Company's market diversification strategy is not single-market or industry dependent, resulting in a natural business hedge as some markets grow while others decline.

Order bookings and backlog

Due to the onset of the COVID-19 pandemic in both North America and India the Company experienced decreased bookings of 18.5% as compared to Quarter 2, 2019.

Booking rates in the distributor channel decreased 19.4% versus Quarter 2, 2019. On a direct channel basis, bookings were lower than Quarter 2, 2019 by 17.0%. Despite the decline, the Company's market position is well anchored in both the U.S. and Canadian distribution markets as the Company continues to hold a strong market share position in our traditional markets through the distribution channel.

Further, as a result of the Quarter 2, 2020 pandemic impact on new order development, the overall year-to-date Company bookings have decreased 12.9% over the same period as last fiscal year. The distributor channel bookings decreased 10.8% and the direct channel bookings are lower by 16.3%.

The Company, does have a solid order backlog decreasing marginally by 2.9% over Quarter 2, 2019, even though bookings rates were lower as product shipments were delayed due to project delays and company closures as a result of the pandemic. Late quarter quotation activity was fairly active – a positive indicator of future sales. It is expected the combination of the Company's strategic sales initiatives, service, dominant distributor footprint and new product development will support our booking rates.

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

Gross margin

The company was successful at delivering an increase in its gross margin rate for Quarter 2, 2020, which was 28.4% compared to a Quarter 2, 2019 gross margin rate of 23.5%, a significant increase of 4.9% of sales. The year-to-date gross margin rate was 25.8% in 2020 versus 23.7% in 2019, an increase of 2.1%. The margin rate improvement is attributed to a combination of a number of factors: sales mix, market selling price realization, lower raw material commodity costs and receipt of the Canadian Emergency Wage Subsidy ("CEWS") benefit in Quarter 2, 2020. The CEWS program provides an employee wage subsidy for our Canadian entities for periods where there was a significant decline in Canadian trade sales due to the impact of COVID-19. During the quarter the wage subsidy received for production labour was $2,527 or 3.4% of sales. The company did incur extraordinary operating expenses of $1,074 or 1.4% of sales relating to wages paid for suspended operational employee wages, non-productive wage support for "at risk" employees, employee transportation, increased cleaning, sanitation and personal protective equipment expenses for the safety of its employees. Excluding the wage subsidy, the Company still delivered an increase in gross margin rate of 1.5% during the quarter.

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

The demand for our product exists but sales volumes will be determined primarily by which industries and customers are continuing to operate and in what capacity. As sales decrease, the lower manufacturing throughput will have a dilutive impact on margin rates. The Company will still realize growth in some markets and experience a decline in others underscoring the volatility of markets and sales demand. We are steadfast in our implementation of initiatives to manage the negative volatility impact, and our distributor footprint in North America and its Indian market presence, cost reduction and containment, product and market breadth and multi-national manufacturing capabilities will support the business.

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

Selling and distribution expense

Total selling and distribution expenses were $9,351 in Quarter 2, 2020 or 12.4% of sales versus $10,848 in Quarter 2, 2019 or 11.8% of sales, a decrease of $1,497 but an increase of 0.6% of sales. Year-to-date selling and distribution expenses were $20,491 or 12.5% of sales in 2020 compared to $20,846 or 11.8% in 2019, a decrease of $355 but an increase of 0.7% of sales. The increase in the percentage of sales is due to the reduced sales for Quarter 2, 2020. The company did incur lower variable selling costs for commissions and freight expenses due to the lower sales volumes in the quarter.

The year-over-year increase in selling and distribution expenses is a result of higher variable freight and commission expenses in the first quarter and the start-up and operational expenses related to a new distribution centre in Reno, Nevada. Expenses were partially reduced by the CEWS wage support subsidy of $386 or 0.5% of sales.

General and administrative expense

General and administrative expenses for Quarter 2, 2020 was $5,560 or 7.4% of sales, compared to Quarter 2, 2019 expenses of $6,044 or 6.6% of sales, a decrease of $484 but an increase of 0.8% of sales. Additional provisions for doubtful accounts receivable, were offset by the CEWS wage subsidy in the amount of $822 or 1.1% of sales in the quarter.

Year-to-date general and administrative expenses were $12,261 or 7.5% of sales in 2020, compared to $11,821 or 6.7% of sales in 2019, an increase of $440 or 0.8% of sales. The increases in the percentage of sales is due to the lower sales value for Quarter 2, 2020. The year-to-date increase in these expenses can be attributed to continuing costs related to our European business and property holdings in Italy, compensation costs and additional provisions for doubtful accounts receivable, which are partially offset by the CEWS government wage subsidy.

Earnings from continuing operations

Quarter 2, 2020 earnings from operations were $6,514, an increase of $1,783 or 37.7% from $4,731 for the same quarter last year. The year-to-date earnings from operations were $9,547 in 2020 compared to $9,210 in 2019, an increase of $337 or 3.7%. The improvement in the quarter is mainly a result of the increase in gross margin dollars, an increase gross margin rate from price realization, government wage subsidy support and foreign exchange gains – partially offset by increased operating expenses related to the pandemic.

DOLLARS IN THOUSANDS UNLESS OTHERWISE STATED

Year-to-date earnings from operations increased due to the increase in gross margin dollars and lift from the gross margin rate, government wage subsidy support and foreign exchange gains in the current year compared to losses in 2019.

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

	Quarter 2, 2020	Quarter 2, 2019	YTD 2020	YTD 2019
Net earnings from continuing operations	$ 4,420	$ 3,352	$ 6,568	$ 5,860
Add:				
Income tax expense	1,838	1,399	2,821	2,806
Interest expense	315	409	711	641
Foreign exchange (gain) loss	(103)	44	(479)	69
Share of loss (income) of investment in joint venture	11	(506)	(140)	(225)
Other	33	33	66	59
Earnings from operations	$ 6,514	$ 4,731	$ 9,547	$ 9,210

Net finance and other costs

Interest expense for Quarter 2, 2020 was $315, a decrease of $94 or 23.0% compared to the Quarter 2, 2019 expense of $409. Year-to-date interest cost was $711, an increase of $70 or 10.9% when compared to the 2019 year-to-date expense of $641. A portion of the change in Quarter 2, $82 in the current year and $77 in the prior year, was due to the accounting standard adoption of IFRS 16 for leases which allocates part of lease costs to interest expense. The year-to-date interest expense related to leases was $179 in 2020 and $155 in 2019. The remainder of the change in the interest expense is a result of lower operating debt levels during the quarter. The year-to-date increase is due to slightly higher operating debt levels in the first quarter of the year and working capital requirements. Interest expense includes all bank fees.

The foreign exchange gain in Quarter 2, 2020 was $103, an increase of $147 compared to the loss of $44 in Quarter 2, 2019. The year-to-date foreign exchange gain for 2020 was $479, compared to a loss of $69 for the same period last year. This gain relates primarily to the transactional exchange pertaining to the Company's U.S. dollar trade accounts payable in Canada. The earnings impact of the foreign exchange gains and losses are related to the increased volatility in the exchange rates during the past year.

As at June 27, 2020, the Company had outstanding foreign exchange contracts in place for 17,400 Euros ("EUR") and $11,000 USD – all of which are implemented as an economic hedge against translation gains and losses on inter-company loans as well as $50,000 USD to economically hedge the U.S. dollar denominated accounts payable in Canadian HPS operations.

Corefficient de R.L. de C.V. ("Corefficient") realized a small loss of $11 for Quarter 2, 2020 compared to Income of $506 for Quarter 2, 2019, a decline of $517. Year-to-date Corefficient has generated income of $140 in 2020 compared to income of $225 in 2019, a decline of $85. While Quarter 1 showed an improvement in the joint venture performance as a result of elevated sales, higher manufacturing throughput, lower material costs and increased selling prices, Quarter 2 has been impacted by increased costs related to COVID-19 management as well as a decline in volume.

Income taxes

Quarter 2, 2020 income tax expense was $1,838 as compared to $1,399 in Quarter 2, 2019, an increase of $439 or 31.4%. Year-to-date income tax expense was comparable at $2,821 in 2020 and $2,806 in 2019.

The consolidated effective tax rate for both Quarter 2, 2020 and 2019 was 29.4%. The year-to-date effective tax rate for the first six months of 2020 was 30.0% compared to 32.4% for the same period in 2019, a decrease of 2.4%. The changes in the effective tax rates are greatly impacted by changes in the earnings mix of the Company and the share of the loss of investment in joint venture. The Company income is generated from different tax jurisdictions and is subject to different tax rates and regulations.

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

Net earnings from continuing operations

Net earnings from continuing operations for Quarter 2, 2020 finished at $4,420 compared to net earnings of $3,352 in Quarter 2, 2019, an improvement of $1,068 or 31.9%. Year-to-date net earnings from continuing operations were $6,568 in 2020 compared to $5,860 in 2019, an increase of $708 or 12.1%. The increase in the earnings from continuing operations is a result of the increase in gross margin dollar contribution, government wage subsidy support and foreign exchange gains in the current year compared to losses in 2019.

Discontinued operations

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

Earnings per share from continuing operations

The basic earnings per share from continuing operations was $0.38 for Quarter 2, 2020, versus $0.29 in Quarter 2, 2019, an improvement of $0.09 or 31%. The year-to-date basic earnings per share from continuing operations was $0.56 in 2020 and $0.50 in 2019, an increase of $0.06 or 12%.

EBITDA

EBITDA for Quarter 2, 2020 was $8,447 versus $7,111 in Quarter 2, 2019, an increase of $1,336 or 18.8%. Year-to-date EBITDA was $14,125 in 2020 and $13,222 in 2019, an increase of $903 or 6.8%.

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

	Quarter 2, 2020	Quarter 2, 2019	**YTD 2020**	YTD2019
Net earnings from continuing operations	$ 4,420	$ 3,352	$ 6,568	$ 5,860
Add:				
Interest expense	315	409	711	641
Income tax expense	1,838	1,399	2,821	2,806
Depreciation and amortization	1,874	1,951	4,025	3,915
EBITDA from continuing operations	$ 8,447	$ 7,111	$ 14,125	$ 13,222
(Subtract) Add:				
Foreign exchange (gain) loss	(103)	44	(479)	69
Adjusted EBITDA from continuing operations	$ 8,344	$ 7,155	$ 13,646	$ 13,291

DOLLARS IN THOUSANDS UNLESS OTHERWISE STATED

Summary of Quarterly Financial Information (Unaudited)

Fiscal 2020 Quarters	Quarter 1, 2020	Quarter 2, 2020	YTD Total
Sales	$ 88,420	$ 75,393	$ 163,813
Net earnings	$ 2,148	$ 4,420	$ 6,568
Net earnings per share – basic	$ 0.18	$ 0.38	$ 0.56
Net earnings per share – diluted	$ 0.18	$ 0.38	$ 0.56
Average U.S. to Canadian exchange rate	$ 1.3388	$ 1.3907	$ 1.3647

Fiscal 2019 Quarters	Quarter 1, 2019	Quarter 2, 2019	Quarter 3, 2019	Quarter 4, 2019	Total
Sales	$ 84,690	$ 91,937	$ 91,502	$ 90,653	$ 358,782
Net earnings from continuing operations	$ 2,508	$ 3,352	$ 3,595	$ 3,851	$ 13,306
Net earnings per share from continuing operations – basic	$ 0.21	$ 0.29	$ 0.31	$ 0.32	$ 1.13
Net earnings per share from continuing operations – diluted	$ 0.21	$ 0.29	$ 0.31	$ 0.32	$ 1.13
Average U.S. to Canadian exchange rate	$ 1.3301	$ 1.3379	$ 1.3198	$ 1.320	$ 1.327

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

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

Fluctuations in exchange rates resulted in a gain in foreign exchange in the first half of 2020 of $479 compared to a loss of $69 in 2019.

Selling and distribution expenses have decreased in the quarter due to lower variable freight and commission expenses attributed to the decreased sales and receipt of the CEWS reimbursement. General and administrative expense increase can be attributed to continuing costs related to our European business and property holdings in Italy, increased compensation costs, additional provisions for doubtful accounts receivable, which is partially offset by CEWS reimbursement.

Corefficient, our joint venture that manufactures transformer cores, had a slight loss for the quarter of $11 in 2020 and income of $506 in 2019. Year-to-date the joint venture generated income of $140 for 2020 compared $225 in 2019. While Quarter 1 showed an improvement in the joint venture performance as a result of elevated sales, higher manufacturing throughput, lower material costs and increased selling prices, Quarter 2 has been impacted by increased costs related to COVID-19 management as well as a decline in volume.

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

Capital resources and liquidity

Net cash generated by operating activities for Quarter 2, 2020 was $7,229 versus $507 in Quarter 2, 2019, an improvement of $6,722. This change has been generated by a decrease in cash used for working capital during the Quarter. Year-to-date net cash generated by operating activities was $1,191 compared $2,823 in 2019, a decrease of $1,632. The year-to-date decrease is a result of higher earnings, offset by a rise in cash utilized for working capital, particularly in Quarter 1 2020.

During the quarter, non-cash working capital used cash of $1,451 compared to $6,317 for the same quarter last year, a decrease of $4,866. The year-to-date change in non-cash working capital was a usage of cash of $11,298 in 2020 compared to $10,431 in 2019, an increase of usage of $867. The year-to-date working capital changes are primarily related to a decrease in accounts payable.

Cash used in investing activities decreased by $29 from $1,562 in the first six months of 2019 to $1,533 in the same period of 2020. Capital expenditures were $177 in Quarter 2, 2020 compared to $621 for Quarter 2, 2019, a decrease of $444. Year-to-date capital expenditures were $1,530 in the current year compared to $1,561 in 2019. The Company continues to invest in the areas of manufacturing processes and capabilities, information technology and new product development.

Total cash used in financing activities for Quarter 2, 2020 was $9,987 as compared to $5,600 in Quarter 2, 2019, an increase of $4,387. The source of this change was higher repayment of operating debt in Quarter 2, 2020. Year-to-date financing activities used cash of $10,459 compared to $6,711 in the first six months of 2019.

Bank operating lines of credit have decreased from prior year levels finishing Quarter 2, 2020 at $26,177 compared to $29,235 at the end of Quarter 2, 2019, a decrease of $3,058. The bank operating lines of credit have decreased $6,520 since the year-end balance of $32,697 and decreased $8,040 since the Quarter 1, 2020 balance of $34,217.

The Company's overall operating debt balance net of cash was $12,906 in Quarter 2, 2020 compared to $18,582 in Quarter 2, 2019, a decrease in debt position of $5,676 primarily reflective of increased profitability and receipt of CEWS payments.

All bank covenants continue to be met as at June 27, 2020.

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

Contractual obligations

	2020	2021	2022	2023	2024	Total
Accounts payable and accrued liabilities	$ 39,502	–	–	–	–	$ 39,502
Capital expenditure purchase commitments	3,253	–	–	–	–	3,253
Bank operating lines	–	26,177	–	–	–	26,177
Lease liabilities	2,229	2,111	2,217	1,730	1,389	9,676
Total	$ 44,984	$ 28,288	$ 2,217	$ 1,730	$ 1,389	$ 78,608

Regular quarterly dividend declaration

During Quarter 2, 2020 the Board of Directors of HPS declared a quarterly cash dividend of eight and a half cents ($0.085) per Class A Subordinate Voting Share of HPS and a quarterly cash dividend of eight and a half cents ($0.085) per Class B Common Share of HPS payable on June 18, 2020 to shareholders of record at the close of business on June 11, 2020. The ex-dividend date was June 16, 2020. The Company has paid a cash dividend of seventeen cents ($0.17) per Class A Subordinate Voting Share and seventeen cents ($0.17) per Class B Common Share year-to-date.

Controls and procedures

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

During Quarter 2, 2020 there were no material changes identified in HPS' internal controls over financial reporting that had materially affected, or was reasonably likely to materially affect HPS' internal control over financial reporting. HPS does carry out ongoing improvements to its internal controls over financial reporting but nothing considered at a material level.

Risks and uncertainties

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

Coronavirus (COVID-19) – Business Disruption

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

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

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

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

Other Business Risks

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

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

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

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

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

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

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

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

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

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

Worldwide HPS is subject to, and required to comply with, multiple income and other taxes, regulations and is exposed to uncertain tax liabilities risk.

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

We face the potential harms of natural disasters, acts of war, terrorism, international conflicts or other disruptions to our operations.

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

The U.S. political uncertainty and potential for changes in the business environment can lead to legislative changes that could impact business.

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

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

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

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

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

The business practice of extending credit to customers can lead to a risk of uncollectability.
A substantial portion of the Company's accounts receivable are with customers in manufacturing sectors and are subject to credit risks normal to those industries. The Company's expansion into emerging markets increases credit risk which is partially mitigated by progress payments. Approvals are based on trade information, payment history, credit rating and financial analysis. Although the Company has historically incurred very low bad debt expense, the current economic environment conditions elevate this exposure.

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

Off-balance sheet arrangements

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

Transactions with related parties

The Company had no transactions with related parties in 2019, other than transactions disclosed in Note 12 in the Condensed Notes to the Condensed Consolidated Interim Financial Statements contained in our Quarter 2, 2020 Report.

Proposed transactions

The Company continues to evaluate strategic business development initiatives and has no firm transactions as at June 27, 2020.

Financial instruments

As at June 27, 2020, the Company had outstanding foreign exchange contracts in place for 17,400 EUR and $11,000 USD – all of which are implemented as a hedge against translation gains and losses on inter-company loans as well as $50,000 USD to hedge the U.S. dollar denominated accounts payable in Canadian operations of HPS.

Critical accounting estimates

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

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

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

Outstanding share data

Details of the Company's outstanding share data:

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

Adopted accounting pronouncements

Definition of a Business (Amendments to IFRS 3)

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

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

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

Strategic direction and outlook

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

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

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

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

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

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

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

The implementation of the ERP system has allowed HPS to enhance the availability and quality of information accessible to support operational performance, supplement strategic decision making, improve customer service and audit and control. The ERP system implementation was completed in our Indian facility in Quarter 2, 2019 and an implementation project began in Quarter 3, 2019 for the Company's remaining operation that will be converted to our ERP platform. It is expected to be fully implemented in late 2020 or early 2021. The consolidation to the ERP platform is an important step towards providing one global, integrated, consistent source of information and data.

HPS continues to focus on customer service and growth – expanding existing relationships as well as exploring new opportunities. Past regulatory requirements to comply with the U.S. Department of Energy and the upcoming Canadian efficiency standard changes (NRCan) has created opportunities for HPS to deliver energy efficient, regulatory compliant transformers fulfilling the needs of our customers. These regulation changes have resulted in new product development and manufacturing techniques.

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

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

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

The combination of our resilience, decades of experience, commitment, engineering expertise, solid supplier relationships and a broad and unique business perspective gained through our diverse products, customers and markets are all key success factors critical to our success. Our strategic vision and operational initiatives have supported our leadership, operational strength and financial stability.

HPS is committed to buffering and battling the impact the pandemic will have on our financial performance. The Company will maintain its liquidity and Balance Sheet strength.

Selected Annual and Quarterly Information

(tabular amounts in thousands of dollars)

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

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

	2018		2019				2020	
Quarterly Information	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Sales	81,553	86,714	84,690	91,937	91,502	90,653	88,420	75,393
Earnings from operations	3,219	4,780	4,479	4,731	5,471	5,862	3,033	6,514
EBITDA	3,879	8,221	6,111	7,111	7,302	7,651	5,678	8,447
Net earnings (loss)	1,391	(14,833)	2,508	3,352	3,595	2,152	2,148	4,420
Total assets	200,954	205,527	206,554	205,059	206,586	214,953	212,929	197,895
Non-current liabilities	3,291	2,528	10,914	10,558	9,947	11,271	9,729	9,039
Total liabilities	83,253	96,793	99,939	99,640	96,870	105,186	97,156	81,375
Total shareholders' equity attributable to equity holders of the Company	117,701	108,734	106,615	105,419	109,716	109,767	115,773	116,520
Operating debt, net of cash	(20,502)	(17,056)	(16,588)	(18,582)	(22,678)	(9,326)	(18,356)	(12,906)
Cash provided by (used in) operations	2,468	4,941	2,316	507	(1,460)	16,447	(6,038)	7,229
Basic earnings (loss) per share	0.12	(1.27)	0.20	0.25	0.27	0.27	0.18	0.38
Diluted earnings (loss) per share	0.12	(1.27)	0.20	0.25	0.27	0.27	0.18	0.38
Dividends declared and paid	704	706	822	821	821	823	998	999
Average exchange rate (USD$=CAD$)	1.307	1.319	1.330	1.338	1.320	1.320	1.339	1.390
Book value per share	10.02	9.26	9.09	8.99	9.33	9.36	9.86	9.92

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

Consolidated Statements of Financial Position

(unaudited) (tabular amounts in thousands of dollars)

	As at June 27, 2020	As at December 31, 2019
Assets		
Current assets		
Cash	$ 13,271	$ 23,371
Accounts receivable	62,710	64,004
Inventories	48,772	50,926
Income taxes receivable	1,278	1,626
Prepaid expenses and other assets	1,916	2,657
Total current assets	$ 127,947	$ 142,584
Non-current assets		
Long-term lease receivable	3,257	3,180
Property, plant and equipment (note 4 and 7)	30,100	32,468
Investment in properties	3,854	3,709
Investment in joint venture (note 5)	14,277	13,428
Deferred tax assets	1,440	1,944
Intangible assets (note 6)	5,761	6,331
Goodwill	11,259	11,309
Total non-current assets	69,948	72,369
Total assets	$ 197,895	$ 214,953
Liabilities		
Current liabilities		
Bank operating lines of credit	$ 26,177	$ 32,697
Accounts payable and accrued liabilities	41,706	56,216
Income tax liabilities	1,350	1,055
Provisions	874	1,710
Current portion of lease liabilities (note 7)	2,229	2,237
Total current liabilities	$ 72,336	$ 93,915
Non-current liabilities		
Provisions	239	285
Deferred tax liabilities	1,353	1,819
Long-term portion of lease liabilities (note 7)	7,447	9,167
Total non-current liabilities	9,039	11,271
Total liabilities	$ 81,375	$ 105,186
Shareholders' Equity		
Share capital	14,491	14,491
Contributed surplus	2,498	2,498
Accumulated other comprehensive income (note 9)	9,621	7,439
Retained earnings	89,910	85,339
Total shareholders' equity	$ 116,520	$ 109,767
Total liabilities and shareholders' equity	$ 197,895	$ 214,953

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Operations

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

	Quarter Ending		Six Months Ending	
	June 27, 2020	June 29, 2019	**June 27, 2020**	June 29, 2019
Sales (note 10)	$ 75,393	$ 91,937	$ 163,813	$ 176,627
Cost of sales (note 11)	53,968	70,314	121,514	134,750
Gross margin	21,425	21,623	42,299	41,877
Selling and distributio (note 11)	9,351	10,848	20,491	20,846
General and administrative (note 11)	5,560	6,044	12,261	11,821
Earnings from operations	6,514	4,731	9,547	9,210
Finance and other costs (income):				
Interest expense	315	409	711	641
Foreign exchange (gain) loss	(103)	44	(479)	69
Share of loss (income) of investment in joint venture (note 5)	11	(506)	(140)	(225)
Other	33	33	66	59
Net finance and other costs (income)	256	(20)	158	544
Earnings before income taxes	6,258	4,751	9,389	8,666
Income tax expense	1,838	1,399	2,821	2,806
Net earnings from continuing operations	$ 4,420	$ 3,352	$ 6,568	$ 5,860
Loss from discontinued operations, net of tax	–	(394)	–	(587)
Net earnings	$ 4,420	$ 2,958	$ 6,568	$ 5,273
Earnings per share				
Basic earnings per share	$ 0.38	$ 0.25	$ 0.56	$ 0.45
Diluted earnings per share	$ 0.38	$ 0.25	$ 0.56	$ 0.45
Basic earnings per share from continuing operations	$ 0.38	$ 0.29	$ 0.56	$ 0.50
Diluted earnings per share from continuing operations	$ 0.38	$ 0.29	$ 0.56	$ 0.50

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Comprehensive Income

(unaudited) (tabular amounts in thousands of dollars)

	Quarter Ending		Six Months Ending	
	June 27, 2020	June 29, 2019	**June 27, 2020**	June 29, 2019
Net earnings	$ 4,420	$ 2,958	$ 6,568	$ 5,273
Other comprehensive income (loss)				
Foreign currency translation differences for foreign operations (note 9)	(2,674)	(3,220)	2,182	(4,223)
Total comprehensive income (loss) for the period	$ 1,746	$ (262)	$ 8,750	$ 1,050

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Changes in Equity

(unaudited) For the six months ended June 27, 2020

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2020	$ 14,491	$ 2,498	$ 7,439	$ 85,339	$ 109,767
Total comprehensive income for the year					
Net earnings	–	–	–	6,568	6,568
Other comprehensive income					
Foreign currency translation differences related to joint venture (note 5)	–	–	709	–	709
Foreign currency translation differences (note 9)	–	–	1,473	–	1,473
Total other comprehensive loss	–	–	2,182	–	2,182
Total comprehensive income for the year	–	–	2,182	6,568	8,750
Transactions with owners, recorded directly in equity					
Dividends to equity holders (note 8)	–	–	–	(1,997)	(1,997)
Total transactions with shareholders	–	–	–	(1,997)	(1,997)
Balance at June 27, 2020	$ 14,491	$ 2,498	$ 9,621	$ 89,910	$ 116,520

*AOCI – Acculated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Changes in Equity

(unaudited) For the six months ended June 29, 2019

(tabular amounts in thousands of dollars)	SHARE CAPITAL	CONTRIBUTED SURPLUS	AOCI*	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
Balance as at January 1, 2019	$ 14,217	$ 2,559	$ 12,740	$ 79,218	$ 108,734
Impact of application of new accounting standard	–	–	–	(2,603)	(2,603)
Adjusted balances as of January 1, 2019	14,217	2,559	12,740	76,615	106,131
Total comprehensive income for the year					
Net earnings	–	–	–	5,273	5,273
Other comprehensive loss					
Foreign currency translation differences related to joint venture (note 5)	–	–	(620)	–	(620)
Foreign currency translation differences (note 9)	–	–	(3,603)	–	(3,603)
Total other comprehensive loss	–	–	(4,223)	–	(4,223)
Total comprehensive (loss) income for the year	–	–	(4,223)	5,273	1,050
Transactions with owners, recorded directly in equity					
Repurchase of shares	(45)	(8)	–	(161)	(214)
Stock options exercised	111	(16)	–	–	95
Dividends to equity holders (note 8)	–	–	–	(1,643)	(1,643)
Total transactions with owners	66	(24)	–	(1,804)	(1,762)
Balance at June 29, 2019	$ 14,283	$ 2,535	$ 8,517	$ 80,084	$ 105,419

*AOCI – Acculated other comprehensive income

See accompanying notes to condensed consolidated interim financial statements

Consolidated Statements of Cash Flows

(unaudited) (tabular amounts in thousands of dollars)	Six Months Ending June 27, 2020	Six Months Ending June 29, 2019
Cash flows from operating activities		
Net earnings	$ 6,568	$ 5,273
Adjustments for:		
Share of income of investment in joint venture	(140)	(225)
Amortization of property, plant and equipment	3,691	3,554
Amortization of intangible assets	334	361
Provisions	(130)	(547)
Interest expense	711	641
Income tax expense	2,821	2,806
Change in unrealized gain on derivatives included in accounts payable and accrued liabilities	812	4,083
	14,667	15,946
Change in non-cash working capital (note 13)	(11,298)	(10,431)
Cash generated in operating activities	3,369	5,515
Income tax paid	(2,178)	(2,692)
Net cash generated by operating activities	1,191	2,823
Cash flows from investing activities		
Acquisition of property, plant and equipment (note 4)	(1,530)	(1,561)
Acquisition of intangible assets (note 6)	(3)	(1)
Cash used in investing activities	(1,533)	(1,562)
Cash flows from financing activities		
Repayments of borrowings	(6,520)	(3,366)
Receipt of lease receivable payments	92	92
Issue of common shares	–	95
Share repurchase	–	(214)
Payment of lease liabilities (note 7)	(1,323)	(1,034)
Cash dividends paid (note 8)	(1,997)	(1,643)
Interest paid	(711)	(641)
Cash used in financing activities	(10,459)	(6,711)
Foreign exchange on cash held in a foreign currency	701	558
Decrease in cash	(10,100)	(4,892)
Cash and cash equivalents at beginning of period	23,371	15,545
Cash and cash equivalents at end of period	$ 13,271	$ 10,653

See accompanying notes to condensed consolidated interim financial statements

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

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

1. Reporting entity

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

The Condensed Consolidated Interim Financial Statements of the Company as at and for the second quarter ended June 27, 2020 comprise the Company and its subsidiaries (together referred to as the "Group" and individually as "Group entities"). The Group primarily is involved in the design and manufacture of custom electrical magnetics, cast resin, custom liquid filled distribution and power transformers and standard electrical transformers, serving the electrical and electronic industries. The Group has manufacturing plants in Canada, the United States ("U.S."), Mexico and India. The Company also holds a 55% economic interest in a joint venture located in Mexico called Correfficient de R.L. de C.V. ("Corefficient").

2. Basis of preparation

(a) Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with requirements of IAS 34, Interim Financial Reporting and do not include all of the information required for full annual financial statements. These condensed consolidated interim financial statements were approved by the Board of Directors on July 30, 2020.

(b) Use of estimates and judgments

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

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

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

3. Summary of significant accounting policies:

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

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

Changes to accounting policies

Definition of a Business (Amendments to IFRS 3)

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

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

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

4. Property, plant and equipment

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

	June 27, 2020	December 31, 2019
Property, plant and equipment owned	$ 22,532	$ 23,415
Right-of-use assets (note 7)	7,568	9,053
	$ 30,100	$ 32,468

The Group had acquisitions of fixed assets for the six months ended June 27, 2020 in the amount of $1,530,000 of machinery and equipment (2019 – $1,561,000).

5. Joint venture

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

	June 27, 2020	December 31, 2019
Cost of investment in joint venture	$ 20,032	$ 20,032
Cumulative share of loss in investment in joint venture, net of tax	(3,255)	(3,395)
Foreign currency translation differences related to the joint venture	(2,500)	(3,209)
	$ 14,277	$ 13,428

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

Selected financial information relating to Corefficient is as follows:

	June 27, 2020	December 31, 2019
Cash	$ 2,847	$ 4,341
Trade and other receivables	10,078	11,286
Inventories	2,523	3,047
Other current assets	86	118
Total current assets	$ 15,534	$ 18,792
Non-current assets	18,820	19,697
Total assets	$ 34,354	$ 38,489
Current liabilities	$ 7,427	$ 12,744
Non-current liabilities	1,243	1,603
Total liabilities	$ 8,670	$ 14,347

	Six Months Ending	
	June 27, 2020	June 29 2019
Revenue	$ 29,440	$ 25,669
Income for the period	255	410

The income for the six months ended June 27, 2020 includes depreciation and amortization expense of $1,616,000 (2019 – $1,187,000), interest expense of $30,000 (2019 – interest income of $17,000) and an income tax expense of $5,000 (2019 – $102,000) related to Corefficient.

6. Intangible assets and goodwill

The Group had acquisitions of intangible assets for the six months ended June 27, 2020 in the amount of $3,000 (2019 – $1,000), for the addition of software. None of the intangible assets have been developed internally.

7. Lease assets and liabilities

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

	Buildings	Vehicles	Office Equipment	Total
Balance at January 1, 2020	$ 8,503	$ 523	$ 27	$ 9,053
Additions	–	143	–	143
Depreciation	(995)	(157)	(12)	(1,164)
Effect of movements in exchange rates	(475)	11	–	(464)
Balance at June 27, 2020	$ 7,033	$ 520	$ 15	$ 7,568

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

Maturity analysis – contractual undiscounted cash flows		**June 27, 2020**		December 31, 2019
Less than one year	$	2,683	$	2,602
One to five years		8,657		9,318
More than five years		409		696
Total undiscounted lease liabilities	$	11,749	$	12,616
Less: effect of discounting	$	(2,073)	$	(1,212)
Lease liabilities included in the statement of financial position	$	9,676	$	11,404
Current	$	2,229	$	2,237
Non-current	$	7,447	$	9,167

	Six Months Ending			
Amounts recognized in statement of operations		**June 27, 2020**		June 29 2019
Interest on lease liabilities	$	179	$	155

	Six Months Ending			
Amounts recognized in statement of cash flows		**June 27, 2020**		June 29, 2019
Payment of lease liabilities	$	1,323	$	1,034

8. Share capital

(a) Dividends

The following dividends were declared and paid by the Company:

	Six Months Ending			
		June 27, 2020		June 29, 2019
17 cents per Class A subordinate voting shares (2019: 14 cents)	$	1,525	$	1,255
17 cents per Class B common shares (2019: 14 cents)		472		388
	$	1,997	$	1,643

(b) Deferred Share Units

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

The movement in DSUs for the six months ended June 27, 2020 is as follows:

	Number of DSUs	Closing Share Price	
Balance at January 1, 2020	121,571	$	7.68
DSUs Issued	19,472		7.17
DSUs exercised	(14,788)		6.24
Balance at June 27, 2020	126,255	$	6.42

A recovery of $31,000 (2019 – expense of $305,000) for the six months ended June 27, 2020 was recorded in general and administrative expenses. The liability of $811,000 (December 31, 2019 – $699,000) related to these DSUs is included in accounts payable and accrued liabilities.

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

9. Accumulated other comprehensive income

Changes to the accumulated other comprehensive income ("AOCI") balance include foreign currency translation differences relating to the net assets of foreign operations which have been determined to have functional currencies under IFRS that are their respective domestic currencies. Total other comprehensive income for the six months ended June 27, 2020 was $2,182,000 (2019 – loss of $4,223,000), of which $1,473,000 (2019 – $3,603,000) relates to the translation of wholly-owned subsidiaries, resulting in an ending balance of accumulated other comprehensive income of $9,621,000 (June 29, 2019 – $8,517,000).

10. Sales

	Three Months Ending		Six Months Ending	
	June 27, 2020	**June 29, 2019**	**June 27, 2020**	June 29, 2019
Canada	$ 21,922	$ 29,283	$ 49,266	$ 55,524
United States and Mexico	51,892	59,246	108,233	113,440
India	1,579	3,408	6,314	7,663
	75,393	91,937	163,813	176,627
Italy – discontinued operations	–	–	–	281
	$ 75,393	$ 91,937	$ 163,813	$ 176,908

As at June 27, 2020, the Company has deferred revenue of $16,000 (December 31, 2019 – $197,000).

11. Government Subsidy

The Government of Canada implemented the Canadian Emergency Wage Subsidy program (CEWS) that provided a subsidy of 75% of eligible remuneration, paid by an eligible entity that experienced significant revenue declines due to the COVID-19 global pandemic. During Quarter 2, 2020 the Company qualified for a subsidy payment. The subsidy amounts have been recorded as a reduction in expenses as follows: cost of sales $2,527, selling and distribution $386 and general and administrative expenses $822 for a total of $3,735.

12. Related party transactions

Arathorn Investments Inc. beneficially owns 2,778,300 (2019 – 2,778,300) Class B common shares of the Company, representing 100% of the issued and outstanding Class B common shares of the Company and 1,063,152 (2019 – 1,061,202) Class A subordinate voting shares of the Company, representing approximately 11.9% (2019 – 11.9%) of the issued and outstanding Class A subordinate voting shares of the Company and as a result controls the Company. William G. Hammond, Chief Executive Officer and Chairman of the Company, owns all of the issued and outstanding shares of Arathorn Investments Inc. Total dividends paid during the quarter, directly and indirectly to William G. Hammond were $326,523 (Quarter 2 2019– $269,000).

Six months ended June 27, 2020 and June 29, 2019 (amounts in thousands of dollars except share and per share amounts)

13. Change in operating working capital

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

	Six Months Ending	
	June 27, 2020	June 29, 2020
Accounts receivable	$ 1,294	$ 2,055
Inventories	2,154	(4,296)
Prepaid expenses	753	338
Accounts payable and accrued liabilities	(15,322)	(3,655)
Provisions	(752)	(2,208)
Foreign exchange	575	(2,665)
	$ (11,298)	$ (10,431)

HPS Offices, Manufacturing Facilities and Warehouse Locations

Canada
Hammond Power Solutions Inc.

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

15 Industrial Road
Walkerton, Ontario N0G 2V0

10 Tawse Place
Guelph, Ontario N1H 6H9

Delta Transformers Inc.

795 Industriel Boul.
Granby, Quebec J2G 9A1

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

India
Hammond Power Solutions Private Limited

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

Italy
Hammond Power Solutions S.p.A.

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

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

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

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

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

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

United States
Hammond Power Solutions, Inc.

1100 Lake Street
Baraboo, Wisconsin 53913

17715 Susana Road
Compton, California 90224

6550 Longley Lane, Suite 135
Reno, Nevada 89511

Corporate Officers and Directors

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

Chris R. Huether
Corporate Secretary and
Chief Financial Officer

Donald H. MacAdam *+
Director

Grant C. Robinson *+
Director

David J. FitzGibbon *+
Director

Dahra Granovsky *+
Director

Fred M. Jaques *+
Director

Anne Marie Turnbull *+
Director

David M. Wood *+
Director

* Corporate Governance Committee
\+ Audit and Compensation Committee

Stock Exchange Listing

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

Registrar and Transfer Agent

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

Auditors

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

Legal Representation

Cassels, Brock and Blackwell LLP
40 King Street West, Suite 2100,
Toronto, Ontario M5H 3C2

Banking Institution

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

Investor Relations

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

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

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

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