

Speaking notes for

Paul M. Tellier
President and Chief Executive Officer
Bombardier Inc.

Board of Trade of Metropolitan Montréal

For a Canadian aerospace policy

February 17, 2004
The Fairmont Queen Elizabeth Hotel
Montréal

Check against delivery

Distinguished guests,
Ladies and gentlemen,
Dear friends,

I would like to thank the Chamber of Commerce's directors and in particular, its dynamic president Benoît Labonté, for this invitation.

Today, I would like to talk to you about a key concern for Canada: the future of the Canadian aerospace industry.

It seems to me that, indeed, this is fundamental. Its future is a major issue in Canada's scientific, industrial and economic policy.

The refocusing of Bombardier

I would like to begin by pointing out that Bombardier is on the edge of completing its refocusing effort. As you know, ladies and gentlemen, Bombardier has changed a great deal in the past year.

It is now a company that concentrates on two sectors of activity. It is the world leader in the production of rail transportation equipment and it is the world's third-largest aircraft manufacturer.

This refocusing effort, which entailed painful decisions, was not easy for anyone. I would like to pay tribute to Laurent Beaudoin and to the Bombardier family for their constant support throughout this process.

With their characteristic spirit of entrepreneurship, creativity and innovation, Laurent Beaudoin and the Bombardier family will now contribute to the success of the recreational products business that we had to part with.

The refocusing of our operations will now enable us to cohesively focus all of our efforts on the solutions required by the vastly altered environments in the international aerospace and rail transportation equipment industries.

Bombardier intends to maintain its current leadership position in both of these industries.

That said, I would like to outline a few factors influencing their evolution.

Evolution of the rail transportation equipment market

Let us start with rail transportation equipment. As you know, rail passenger transportation is a central component of Europe's economy, and it was through our conquering of those markets that we established our international leadership position.

However, this industry is now undergoing fundamental changes due to pressure from factors such as deregulation, the emergence of private sector players and a transformation of policies and practices in the European Union.

To begin with, the consolidation of the industry has not eliminated excess production capacity. Bombardier is no exception. If we fail to act, our European plants will continue to operate at less than 50% capacity. In short, too many manufacturing facilities and a surplus workforce: important challenges, particularly in view of European employment regulations.

Secondly, the lack of product standardization prevents economies of scale. The fact that every customer has a specific product increases engineering hours and leads to increased production costs. We must, in short, tighten our cost structure.

We must act swiftly in Europe on all fronts, within a very sensitive political environment in which governments are customers and market regulators alike.

We are striving to act as quickly as possible, in consultation with our workplace partners and by rigorously following procedures in each jurisdiction.

Bombardier and the impact of September 11

In the aerospace arena, we must face, jointly and in solidarity with the global aerospace industry, the effects of September 11, the general fragility of the industry and the scarcity of sales financing sources.

To start with, September 11 and its consequences had a dire effect on commercial aviation. Airlines have been forced to adopt equipment that is better suited to the requirements of regional transportation between urban centres of different densities.

This situation should have worked to Bombardier's advantage, given that we revolutionized regional transportation with the creation of the regional jet. I might point out, in passing, that we delivered the thousandth such aircraft from our Dorval assembly plants in December.

Furthermore, we held a leadership position in the business aviation sector.

We have designed and put 14 new aircraft on the market in 14 years in these two fields—more than Boeing and Airbus combined.

A market anomaly

Following September 11, paradoxically, air carriers had little access to the financial resources they would normally need for acquiring new equipment to meet their regional transportation needs. A market anomaly resulted: our product is in high demand, but access to financing is very limited.

Under these circumstances, I am particularly proud that Bombardier—and only Bombardier—was successful this year in delivering more regional aircraft than last year.

As for the business aircraft market, it was not only affected by the economic health of corporations, but also by the reactions of shareholders to certain financial scandals that have been making headlines for months, in both the United States and Europe. And even so, we delivered more business jets in 2003 than in 2002.

The recovery of the business aircraft sector has been slow, but recent market movements are encouraging.

Along with the rest of the Canadian aerospace industry, our company was hit hard.

The world is, nonetheless, understandably surprised that such a strong aerospace industry has been able to prosper in a country like ours. Some also wonder how Bombardier has been able to hold itself up among leaders like Boeing and Airbus, given the overwhelmingly greater resources upon which they can draw.

Importance and success of the Canadian aerospace industry

Despite the very success of this Canadian industry—found from coast to coast—we seem to have ignored its strategic importance for this country's economy.

See for yourself by considering these figures:

- The Canadian aerospace industry generates annual revenues of more than \$20 billion.

- Not counting those working for airlines, it employs nearly 80,000 individuals, 50,000 of whom work directly on the production of aircraft, parts and aerospace equipment.
- The salaries of these 50,000 workers are 60% higher than the Canadian average.
- 10.4% of these 50,000 employees work in research and development, representing 9.2% of all Canadians employed in R&D in the manufacturing sector.
- By comparison, only 1.4% of employees working in the Canadian auto industry—all major manufacturers of which, I'd like to remind you, have their head offices abroad—are in research and development.
- Bombardier alone has invested \$3.5 billion in research and development in Canada since 1986, the year it entered into the industry.
- The Canadian aerospace industry's manufacturing production creates 51% in added value, compared with 38.9% for the Canadian manufacturing sector as a whole.
- The manufacturing sector of the Canadian aerospace industry generates estimated revenues of more than \$1 billion for the federal and provincial governments.
- The industry exports 89% of its production and makes a substantial contribution to Canada's balance of trade surplus.
- Finally, and to destroy a persistent myth, export financing does not cost the Government of Canada one cent. According to conservative hypotheses, the EDC draws annual estimated revenues of some \$200 million from such activities, which corresponds to the difference between the interest rate at which Export Development Canada borrows and the rate at which it lends to Canadian aerospace industry customers.
- Furthermore, the EDC has pocketed more than \$15 million in fees on Bombardier transactions, just over the past two years.

The Canadian aerospace industry, in short, provides high-quality jobs, creates wealth and contributes to the development of an economy based on knowledge and on the conquering of world markets.

Through this, the industry secures a return on the country's investments, has a positive impact on public finance and asserts Canada's high-tech role on the international scene.

Monumental challenges in aerospace

Ladies and gentlemen, these are glowing achievements.

Governments, provincial and federal, have been supportive of our industry in the past. As an illustration, take the fact that Investissement Québec recently increased its program that provides aircraft financing guarantees to our regional airlines customers by \$600 million.

This past July, the federal government also increased the financing envelope for Canada Account loans by \$1.2 billion.

And while these amounts sound quite large, they appear much smaller when compared to our customers' financing needs. In fact, for the fiscal year just ended, our regional aircraft customers required \$4.1 billion in financing, well over two-thirds of which came from private sector sources.

Ours is a brutally competitive global environment, in which national governments show no hesitation in supporting their national champion or emerging industry.

The industry also faces other fundamental challenges.

Challenge number one: We are up against competitors who benefit from huge military R&D financing. In the United States for instance, the Department of Defense invests \$45 billion US in R&D, some \$6.5 billion of which goes directly to Boeing, Raytheon and United Technologies. Of the international competitors in the field, Canada is the only country in which military investment in R&D is of no real significance.

Challenge number two: The situation is no different in terms of commercial R&D. In 2001, the whole Canadian industry shared 165 million of Canadian R&D dollars provided by the federal government. Airbus' A380 aircraft program can tap into a pool of \$3 billion US of combined public funds from various European countries. Moreover, risk-sharing partners and major suppliers such as Saab and Rolls-Royce also received considerable public funding for their participation in the A380.

Challenge number three: Over the last three years, EDC has financed on average 41% of Bombardier's total regional aircraft deliveries. In comparison, Brazil's Development Bank, BNDES, has financed on average over 80% of Embraer's total deliveries over the same period. Of even greater concern is the fact that EDC's support for 2003 has declined to 37% despite Bombardier's increase in aircraft deliveries, with most of that financing being for existing contracts. Embraer, by comparison, received state support for virtually all of its financing this year.

Challenge number four: 89% of our production is exported, and the rising Canadian dollar will impact the industry's margins.

Challenge number five: If this were not enough competition, ladies and gentlemen, and given that no major industrialized country is indifferent to the economic benefits and spin-offs of a strong aerospace sector, Russia, China and Japan are now entering the fray.

China is single-handedly developing its very own regional jet and is expected to continue to protect its incredibly fast-growing domestic market.

Russia is well experienced in aerospace and has already launched and financed both a regional jet and a medium-range jet program.

Japan has invested in the feasibility study of a Japanese-designed and manufactured twin-engine aircraft. Indeed, Honda has already developed its own jet engine and prototype business jet aircraft.

These countries have the know-how, the resources and the much-needed full government support. They will seek to command their own domestic markets and eventually become formidable competitors worldwide.

Bombardier: a unique market situation

With competition expected to become ever more intense, Bombardier will face greater exposure than its competitors because of the particular context in which it is operating:

- Our market is largely private, while that of our competitors is mostly governmental and benefits from large public sector orders.

- Our market is civil aviation, while that of our competitors is largely military and benefits from significant contributions aimed at developing leading edge technologies.
- Our market is almost entirely international, while that of our competitors is solidly rooted in their heavily populated domestic markets, thereby making us more dependent on export financing.

Ladies and gentlemen, we must contend with the facts.

Unless we promptly develop a well-informed and effective policy in this field, our nation could end up losing its own industry, one of its most highly performing economic assets.

For a Canadian aerospace policy

Such a policy should be based on three key activities in the industry:

1. The design of new products;
2. The manufacture of these products; and, most particularly,
3. The sales financing of these products.

1. In terms of product design

Regarding product design, we believe this policy should include:

- First, the creation of new funding partnerships for research and development, with the sharing of risks and profits between the public and private sectors, such as the Technology Partnerships Canada Program.
- Secondly, the creation of consortiums consisting of local and foreign principal contractors, suppliers and governments for the development of products, derivatives and subsystems. We are quite familiar with this method of operation at Bombardier, which has already allowed us, as well as our competitors, to effectively pool formidable resources.

2. In terms of product manufacturing

When it comes to product manufacturing, the provincial and federal governments have supported the industry well in the past. They must maintain their level of investment support in production facilities and innovate when it comes to creating incentives.

In an ideal world, governments should not be required to intervene in this manner. But the aerospace industry does not necessarily follow the theoretical model of the free market.

By way of example, the State of Washington has committed to setting up an aeronautics training program for Boeing; to creating a workforce development centre; to investing \$4.2 billion US in roadway infrastructure; to hiring eight employees solely assigned to coordinating matters pertaining to Boeing; and to awarding Boeing a 20-year tax holiday worth \$3.2 billion US.

3. In terms of export financing

A Canadian aerospace policy should include a major sales financing assistance component.

This aspect of the policy is of significant importance to Bombardier, because buyers are increasingly making manufacturers responsible for facilitating the financing of their aircraft purchases.

In this respect, Bombardier has agreed to directly provide its customers with \$1 billion US in interim financing, for a maximum of 60 aircraft.

Today, all aircraft manufacturers must count on various financial vehicles that are placed at their disposal by governments to assist in the financing of their sales. Bombardier has long been working in conjunction with Export Development Canada to do this.

Bombardier's experience encourages us to recommend that Canada make a long-term export financing commitment that would include:

- Increased EDC financing capacity;
- Direct or indirect increases of credit limits by product sector as well as by customer and by country; and
- Flexibility permitting the sale and exchange of EDC portfolio components in order to create the necessary room for new transactions.

Ultimately, I believe that in Canada we should create a centre of excellence specializing in the private financing of aircraft sales based on the development of a loan guarantee policy that would encourage private finance sources to provide loans to industry customers.

Such an effort would enable private organizations to gradually serve the market and to develop individual capacities to finance certain transactions on their own.

Need for a well-targeted and concerted effort

Ladies and gentlemen, these are, in my opinion, the essential components of a Canadian aerospace industry policy.

Some of these elements already exist in what I would call a “miniaturized” form. We must not only ensure its continuity, but more importantly, its enrichment.

I am profoundly convinced that such a targeted effort by all public and private stakeholders is essential to the maintenance and to the development of our aerospace industry. Otherwise, we will allow certain nations of Europe, Asia and the Americas—nations more likely to create favourable conditions for development—to benefit from growth in the international aerospace market.

This is one possibility we refuse to contemplate.

The many advantages Canadians draw from their aerospace industry clearly illustrate the need for a Canadian aerospace policy.

That is why Bombardier, one of the leaders of this industry, intends to work with all of its public and private partners to demonstrate this industry’s contribution to the Canadian economy, to the financial health of its governments, as well as to the well-being of multiple regions and of thousands of Canadians working in this state-of-the-art field.

We hope as well to work intensively and relentlessly with the aerospace industry and with governments to draw up a policy aimed at maintaining Canada’s strong presence and its enviable reputation as a world-class knowledge-based economy.

I hope that I can count on the active support of organizations such as yours.

Thank you and good afternoon, Ladies and gentlemen.
Merci, mesdames et messieurs.