EXFO INC.
Form 6-K
March 27, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 6-K

Report of Foreign Private Issuer Pursuant to Rule 13a-16 or 15d-16
Under the Securities Exchange Act of 1934

For the month of March 2015

EXFO Inc.
(Translation of registrant's name into English)

400 Godin Avenue, Quebec, Quebec, Canada G1M 2K2
(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F þForm 40-F o

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes oNo þ

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-______.

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On March 24, 2015, EXFO Inc., a Canadian corporation, reported its results of operations for the second fiscal quarter ended February 28, 2015. This report on Form 6-K sets forth the news release relating to EXFO's announcement and certain information relating to EXFO's financial condition and results of operations for the second fiscal quarter of the 2015 fiscal year. This press release and information relating to EXFO's financial condition and results of operations for the second fiscal quarter of the 2015 fiscal year are hereby incorporated as a document by reference to Form F-3 (Registration Statement under the Securities Act of 1933) declared effective as of July 30, 2001 and to Form F-3 (Registration Statement under the Securities Act of 1933) declared effective as of March 11, 2002 and to amend certain material information as set forth in these two Form F-3 documents.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

EXFO INC.

By: /s/ Germain Lamonde
Name: Germain Lamonde
Title: President and Chief Executive Officer

Date: March 27, 2015

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EXFO Reports Second-Quarter Results for Fiscal 2015

Sales reach US$51.0 million, stable year-over-year
Bookings attain US$54.7 million, book-to-bill ratio of 1.07
Gross margin amounts to 61.7% of sales, up year-over-year
Adjusted EBITDA totals US$1.2 million, up year-over-year

QUEBEC CITY, CANADA, March 24, 2015 — EXFO Inc. (NASDAQ: EXFO; TSX: EXF) reported today financial results for the second quarter ended February 28, 2015.

Sales reached US$51.0 million in the second quarter of fiscal 2015 compared to US$51.2 million in the second quarter of 2014 and US$56.7 million in the first quarter of 2015.

Bookings attained US$54.7 million in the second quarter of fiscal 2015 compared to US$58.7 million in the same period last year and US$54.2 million in the first quarter of 2015. The company's book-to-bill ratio was 1.07 in the second quarter of 2015.

Gross margin before depreciation and amortization* amounted to 61.7% of sales in the second quarter of fiscal 2015 compared to 60.8% in the second quarter of 2014 and 62.6% in the first quarter of 2015.

IFRS net earnings in the second quarter of fiscal 2015 totaled US$0.9 million, or US$0.02 per diluted share, compared to a net loss of US$1.3 million, or US$0.02 per share, in the same period last year and net earnings of US$1.5 million, or US$0.02 per diluted share, in the first quarter of 2015. IFRS net earnings in the second quarter of 2015 included US$1.0 million in after-tax amortization of intangible assets, US$0.4 million in stock-based compensation costs and a foreign exchange gain of US$3.0 million.

Adjusted EBITDA** totaled US$1.2 million, or 2.3% of sales, in the second quarter of fiscal 2015 compared to -US$1.0 million, or -2.0% of sales, in the second quarter of 2014 and US$3.2 million, or 5.6% of sales, in the first quarter of 2015.

"EXFO progressed along its strategic course towards becoming a trusted, end-to-end solutions supplier with a significant bookings increase in this segment during the first half of fiscal 2015," said Germain Lamonde, EXFO's Chairman, President and CEO. "At Mobile World Congress, we showcased several new, high-impact solutions, including our new analytics platform that offers unmatched end-to-end visibility of wireless network performance and service delivery; our subscriber experience analytics solution providing real-time visibility and prioritization of service-impacting issues; and our new test process automation and compliance assurance solution. Judging by the positive response we received for all our new products and solutions, we are in a good position to accelerate revenue in the second half of fiscal 2015."

"I am pleased we completed the first half of 2015 with adjusted EBITDA improving from US$1.3 million to US$4.4 million and gross margin increasing by 60 basis points to 62.1%, despite stable revenue year-over-year," Mr. Lamonde added. "Given our strong funnel of large deals, recently introduced solutions and ongoing cost-reduction initiatives, I am confident we will deliver marked growth in adjusted EBITDA in fiscal 2015 and beyond."

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Selected Financial Information
(In thousands of US dollars)

	Q2 2015	Q1 2015	Q2 2014
Sales	$50,990	$56,724	$51,179
Gross margin*	$31,444	$35,487	$31,106
	61.7 %	62.6 %	60.8 %
Other selected information:			
IFRS net earnings (loss)	$931	$1,481	$(1,339)
Amortization of intangible assets	$1,019	$1,098	$1,074
Stock-based compensation costs	$388	$400	$402
Net income tax effect of the above items	$(53)	$(58)	$(64)
Foreign exchange gain	$2,987	$1,975	$2,292
Adjusted EBITDA**	$1,158	$3,197	$(1,002)

Operating Expenses
Selling and administrative expenses totaled US$20.2 million, or 39.6% of sales in the second quarter of fiscal 2015 compared to US$21.5 million, or 42.1% of sales, in the same period last year and US$21.0 million, or 37.1% of sales, in the first quarter of 2015. In the first half of 2015, SG&A expenses totaled US$41.2 million, or 38.2% of sales.

Gross research and development expenses amounted to US$12.2 million, or 23.9% of sales, in the second quarter of fiscal 2015 compared to US$13.0 million, or 25.5% of sales, in the second quarter of 2014 and US$13.3 million, or 23.5% of sales, in the first quarter of 2015. In the first half of 2015, gross R&D expenses totaled US$25.5 million, or 23.7% of sales.

Net R&D expenses totaled US$10.5 million, or 20.6% of sales, in the second quarter of fiscal 2015 compared to US$11.0 million, or 21.4% of sales, in the same period last year and US$11.7 million, or 20.6% of sales, in the first quarter of 2015. In the first half of 2015, net R&D expenses totaled US$22.2 million, or 20.6% of sales.

Second-Quarter Highlights
Sales. EXFO's revenues were stable year-over-year in the second quarter of 2015 and in the first half of 2015 due to a negative US currency impact and market weakness in Europe, Middle East and Africa (EMEA). Sales increased year-over-year in the Americas, but decreased in EMEA. Geographical split was 53% from the Americas, 25% from EMEA and 22% from Asia-Pacific in the second quarter. EXFO's top customer accounted for 5.6% of sales, while the top three represented 15.2% in the second quarter.

Profitability. EXFO generated adjusted EBITDA of US$1.2 million, or 2.3% of sales, in the second quarter of 2015. The company also delivered US$5.7 million in cash flows from operating activities. Following the completion of a C$30.0 million (US$24.0 million) substantial issuer bid, EXFO had a cash position of US$32.9 million and no debt at the end of the quarter.

Innovation. EXFO launched Xtract, an open analytics platform that provides mobile operators with end-to-end network and service visibility to accelerate and prioritize network optimization, and a quality of experience benchmarking platform that works in tandem with EXFO Mobile Agent, a software application converting smartphones into real-time probes. These solutions leverage technologies from the recent BysteSphere and Aito Technologies acquisitions. The company also introduced common public radio interface (CPRI) software testing options for the FTB-700G and FTB-780 NetBlazer series to simplify fiber-to-the-antenna (FTTA) and distributed antenna system (DAS) deployments; and released iCERT, an added functionality on EXFO's OTDR (optical time domain reflectometry) software, which automatically certifies cable installations in data centers and enterprises. Altogether, the company introduced seven new solutions or major enhancements in the first half of the fiscal year.

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Business Outlook

EXFO forecasts sales between US$56.0 million and US$61.0 million for the third quarter of fiscal 2015, while IFRS net results are expected to range between a net loss of US$0.01 per share and net earnings of US$0.03 per share. IFRS net loss/earnings include US$0.01 per share in after-tax amortization of intangible assets and stock-based compensation costs.

This guidance was established by management based on existing backlog as of the date of this press release, seasonality, expected bookings for the remaining of the quarter, as well as exchange rates as of the day of this press release.

Conference Call and Webcast

EXFO will host a conference call today at 5 p.m. (Eastern time) to review its financial results for the second quarter of fiscal 2015. To listen to the conference call and participate in the question period via telephone, dial 1-416-641-6700. Germain Lamonde, Chairman, President and CEO, and Pierre Plamondon, CPA, CA, Vice-President of Finance and Chief Financial Officer, will participate in the call. An audio replay of the conference call will be available one hour after the event until 11:59 p.m. on March 31, 2015. The replay number is 1-402-977-9141 and the reservation number is 21762798. The audio Webcast and replay of the conference call will also be available on EXFO's Website at www.EXFO.com, under the Investors section.

About EXFO

Listed on the NASDAQ and TSX stock exchanges, EXFO is a leading provider of next-generation test, service assurance and end-to-end quality of experience solutions for mobile and fixed network operators and equipment manufacturers in the global telecommunications industry. EXFO's intelligent solutions with contextually relevant analytics improve end-user quality of experience, enhance network performance and drive operational efficiencies throughout the network and service delivery lifecycle. Key technologies supported include 3G, 4G/LTE, VoLTE, IMS, video, Ethernet/IP, SNMP, OTN, FTTx, xDSL and various optical technologies accounting for more than 38% of the global portable fiber-optic test market. EXFO has a staff of approximately 1600 people in 25 countries, supporting more than 2000 customers worldwide. For more information, visit www.EXFO.com and follow us on the EXFO Blog, Twitter, LinkedIn, Facebook, Google+ and YouTube.

Forward-Looking Statements

This press release contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition. Words such as may, expect, believe, plan, anticipate, intend, could, estimate, continue, or similar expressions or the negative of such expressions are intended to identify forward-looking statements. In addition, any statement that refers to expectations, projections or other characterizations of future events and circumstances are considered forward-looking statements. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including, but not limited to, macroeconomic uncertainty as well as capital spending and network deployment levels in the telecommunications industry (including our ability to quickly adapt cost structures with anticipated levels of business and our ability to manage inventory levels with market demand); future economic, competitive, financial and market conditions; consolidation in the global telecommunications test and service assurance industry and increased competition among vendors; capacity to adapt our future product offering to future technological changes; limited visibility with regards to timing and nature of customer orders; longer sales cycles for complex systems involving customers' acceptances delaying revenue recognition; fluctuating exchange rates; concentration of sales; timely release and market acceptance of our new products and other upcoming products; our ability to successfully expand international operations; our ability to successfully integrate businesses that we acquire; and the retention of key technical and management personnel. Assumptions relating to the foregoing involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. Other risk factors that may affect our future performance and operations are detailed in our Annual Report, on Form 20-F, and our other filings with the U.S. Securities and Exchange Commission and the Canadian securities commissions. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document.

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NON-IFRS MEASURES

EXFO provides non-IFRS measures (gross margin before depreciation and amortization* and adjusted EBITDA**) as supplemental information regarding its operational performance. The company uses these measures for the purpose of evaluating historical and prospective financial performance, as well as its performance relative to competitors. These measures also help the company to plan and forecast for future periods as well as to make operational and strategic decisions. EXFO believes that providing this information, in addition to IFRS measures, allows investors to see the company's results through the eyes of management, and to better understand its historical and future financial performance.

The presentation of this additional information is not prepared in accordance with IFRS. Therefore, the information may not necessarily be comparable to that of other companies and should be considered as a supplement to, not a substitute for, the corresponding measures calculated in accordance with IFRS.

* Gross margin before depreciation and amortization represents sales less cost of sales, excluding depreciation and amortization.

** Adjusted EBITDA represents net earnings (loss) before interest, income taxes, depreciation and amortization, stock-based compensation costs and foreign exchange gain.

The following table summarizes the reconciliation of adjusted EBITDA to IFRS net earnings (loss), in thousands of US dollars:

Adjusted EBITDA (unaudited)

	Q2 2015	Q1 2015	Q2 2014
IFRS net earnings (loss) for the period	$931	$1,481	$(1,339)
Add (deduct):			
Depreciation of property, plant and equipment	1,256	1,245	1,243
Amortization of intangible assets	1,019	1,098	1,074
Interest income	(35)	(217)	(49)
Income taxes	586	1,165	(41)
Stock-based compensation costs	388	400	402
Foreign exchange gain	(2,987)	(1,975)	(2,292)
Adjusted EBITDA for the period	$1,158	$3,197	$(1,002)
Adjusted EBITDA in percentage of sales	2.3%	5.6%	(2.0)%

For more information
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EXFO Inc.
Condensed Unaudited Interim Consolidated Balance Sheets

(in thousands of US dollars)

	As at February 28, 2015	As at August 31, 2014
Assets		
Current assets		
Cash	$30,357	$54,121
Short-term investments	2,582	5,726
Accounts receivable		
Trade	41,308	46,031
Other	1,924	2,001
Income taxes and tax credits recoverable	4,788	3,796
Inventories	32,238	35,232
Prepaid expenses	2,435	2,281
	115,632	149,188
Tax credits recoverable	35,977	41,745
Property, plant and equipment	37,083	42,780
Intangible assets	4,776	7,293
Goodwill	23,003	26,488
Deferred income tax assets	10,826	9,816
Other assets	502	721
	$227,799	$278,031
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	$35,215	$29,553
Provisions	427	532
Income taxes payable	615	840
Deferred revenue	8,359	8,990
	44,616	39,915
Deferred revenue	2,912	3,319
Deferred income tax liabilities	2,503	3,087
Other liabilities	1,308	340
	51,339	46,661
Shareholders’ equity		
Share capital (note 4)	86,527	111,491
Contributed surplus	17,153	16,503

Retained earnings	116,047	113,635
Accumulated other comprehensive loss	(43,267)	(10,259)
	176,460	231,370
	$227,799	$278,031

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EXFO Inc.
Condensed Unaudited Interim Consolidated Statements of Earnings

(in thousands of US dollars, except share and per share data)

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Sales	$50,990	$107,714	$51,179	$107,182
Cost of sales (1) (note 5)	19,546	40,783	20,073	41,258
Selling and administrative (note 5)	20,168	41,200	21,537	43,245
Net research and development (note 5)	10,506	22,164	10,973	22,254
Depreciation of property, plant and equipment (note 5)	1,256	2,501	1,243	2,518
Amortization of intangible assets (note 5)	1,019	2,117	1,074	2,256
Interest income	(35)	(252)	(49)	(76)
Foreign exchange gain	(2,987)	(4,962)	(2,292)	(3,094)
Earnings (loss) before income taxes	1,517	4,163	(1,380)	(1,179)
Income taxes (note 6)	586	1,751	(41)	907
Net earnings (loss) for the period	$931	$2,412	$(1,339)	$(2,086)
Basic and diluted net earnings (loss) per share	$0.02	$0.04	$(0.02)	$(0.03)
Basic weighted average number of shares outstanding (000’s)	59,216	59,775	60,414	60,316
Diluted weighted average number of shares outstanding (000’s) (note 7)	59,813	60,396	60,414	60,316

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

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EXFO Inc.
Condensed Unaudited Interim Consolidated Statements of Comprehensive Loss

(in thousands of US dollars)

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Net earnings (loss) for the period	$931	$2,412	$(1,339)	$(2,086)
Other comprehensive income (loss), net of income taxes				
Items that will not be reclassified subsequently to net earnings				
Foreign currency translation adjustment	(18,566)	(30,301)	(9,580)	(11,528)
Items that may be reclassified subsequently to net earnings				
Unrealized losses on forward exchange contracts	(2,697)	(4,202)	(1,289)	(1,529)
Reclassification of realized losses on forward exchange contracts in net earnings (loss)	338	500	191	365
Deferred income tax effect of losses on forward exchange contracts	622	995	294	312
Other comprehensive loss	(20,303)	(33,008)	(10,384)	(12,380)
Comprehensive loss for the period	$(19,372)	$(30,596)	$(11,723)	$(14,466)

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EXFO Inc.
Condensed Unaudited Interim Consolidated Statements of Changes in Shareholders' Equity

(in thousands of US dollars)

	Six months ended February 28, 2014				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total shareholders' equity
Balance as at September 1, 2013	$109,837	$17,186	$112,852	$ (3,423)	$236,452
Exercise of stock options (note 4)	195	–	–	–	195
Redemption of share capital (note 4)	(831)	(106)	–	–	(937)
Reclassification of stock-based compensation costs (note 4)	2,136	(2,136)	–	–	–
Stock-based compensation costs	–	843	–	–	843
Net loss for the period	–	–	(2,086)	–	(2,086)
Other comprehensive loss					
Foreign currency translation adjustment	–	–	–	(11,528)	(11,528)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes of $312	–	–	–	(852)	(852)
Total comprehensive loss for the period					(14,466)
Balance as at February 28, 2014	$111,337	$15,787	$110,766	$ (15,803)	$222,087

	Six months ended February 28, 2015				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total shareholders' equity
Balance as at September 1, 2014	$111,491	$16,503	$113,635	$ (10,259)	$231,370
Redemption of share capital (note 4)	(26,314)	1,211	–	–	(25,103)
Reclassification of stock-based compensation costs (note 4)	1,350	(1,350)	–	–	–
Stock-based compensation costs	–	789	–	–	789
Net earnings for the period	–	–	2,412	–	2,412
Other comprehensive loss					
Foreign currency translation adjustment	–	–	–	(30,301)	(30,301)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes of $995	–	–	–	(2,707)	(2,707)
Total comprehensive loss for the period					(30,596)

Balance as at February 28, 2015	$86,527	$17,153	$116,047	$ (43,267)	$176,460

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EXFO Inc.
Condensed Unaudited Interim Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Cash flows from operating activities				
Net earnings (loss) for the period	$931	$2,412	$(1,339)	$(2,086)
Add (deduct) items not affecting cash				
Stock-based compensation costs	388	788	402	865
Depreciation and amortization	2,275	4,618	2,317	4,774
Deferred revenue	1,531	504	1,024	(728)
Deferred income taxes	(11)	(343)	(324)	301
Changes in foreign exchange gain/loss	(1,770)	(2,798)	(793)	(901)
	3,344	5,181	1,287	2,225
Changes in non-cash operating items				
Accounts receivable	3,719	(1,317)	6,182	4,525
Income taxes and tax credits	(1,211)	(1,423)	(1,686)	(943)
Inventories	(752)	(1,933)	(1,221)	(3,533)
Prepaid expenses	(165)	(501)	(787)	(616)
Other assets	(2)	(1)	(40)	(34)
Accounts payable, accrued liabilities and provisions	824	7,660	(94)	5,391
Other liabilities	(13)	(32)	(17)	(43)
	5,744	7,634	3,624	6,972
Cash flows from investing activities				
Additions to short-term investments	(5,818)	(19,509)	(4,790)	(14,571)
Proceeds from disposal and maturity of short-term investments	8,300	22,066	4,790	14,562
Additions to capital assets	(2,045)	(2,799)	(1,695)	(2,396)
	437	(242)	(1,695)	(2,405)
Cash flows from financing activities				
Repayment of long-term debt			(307)	(307)
Exercise of stock options			89	195
Redemption of share capital (note 4)	(24,250)	(25,103)	(937)	(937)
	(24,250)	(25,103)	(1,155)	(1,049)
Effect of foreign exchange rate changes on cash	(3,795)	(6,053)	(1,475)	(1,840)
Change in cash	(21,864)	(23,764)	(701)	1,678
Cash – Beginning of the period	52,221	54,121	47,765	45,386

Cash – End of the period	$30,357	$30,357	$47,064	$47,064
Supplementary information				
Income taxes paid	$457	$824	$229	$871
Additions to capital assets	$2,048	$2,938	$1,196	$2,680

As at February 28, 2014 and 2015, unpaid purchases of capital assets amounted to $515 and $495 respectively.

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EXFO Inc.
Notes to Condensed Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

1 Nature of Activities and Incorporation

EXFO Inc. and its subsidiaries (together "EXFO" or the company) design, manufacture and market test, service assurance and quality of experience solutions for wireless and wireline network operators and equipment manufacturers in the global telecommunications industry. The company's core-to-edge solutions assess the performance and reliability of converged Internet protocol (IP) fixed and mobile networks.

EXFO is a company incorporated under the Canada Business Corporations Act and domiciled in Canada. The address of its headquarters is 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2.

These condensed interim consolidated financial statements were authorized for issue by the Board of Directors on March 24, 2015.

2 Basis of Presentation

These condensed interim consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB) applicable to the preparation of interim financial statements, including IAS 34, "Interim Financial Reporting", and using the same accounting policies and methods used in the preparation of the company's most recent annual consolidated financial statements. Consequently, these condensed interim consolidated financial statements should be read in conjunction with the company's most recent annual consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB.

New IFRS Pronouncements

Financial instruments

The final version of IFRS 9, "Financial Instruments", was issued in July 2014 and will replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. Requirements relating to hedge accounting representing a new hedge accounting model have also been added to IFRS 9. The new standard is effective for annual periods beginning on or after January 1, 2018, and must be applied retrospectively. The company has not yet assessed the impact that the new standard will have on its consolidated financial statements.

Revenue from contracts with customers

IFRS 15, "Revenue from Contracts with Customers", was issued in May 2014. The objective of this new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability. This new standard contains principles that an entity will apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. This new standard is effective for annual periods beginning on or after January 1, 2017. Early adoption is permitted. The company has not yet assessed the impact that the new standard will have on its consolidated financial statements or whether or not to early adopt the new standard.

EXFO Inc.
Notes to Condensed Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

3 Financial Instruments

Fair Value of Financial Instruments

The company classifies its derivative and non-derivative financial assets and liabilities measured at fair value using the fair value hierarchy as follows:

Level 1: Quoted prices (unadjusted) in active market for identical assets or liabilities;

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset and liability, either directly or indirectly;

Level 3: Unobservable inputs for the asset or liability.

The company's short-term investments and forward exchange contracts are measured at fair value at each balance sheet date. The company's short-term investments are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices in active markets. The company's forward exchange contracts are classified within Level 2 of the fair value hierarchy because they are valued using quoted prices and forward exchange rates at the balance sheet dates.

The fair value of forward exchange contracts represents the amount at which they could be settled based on estimated current market rates.

The fair value of derivative and non-derivative financial assets and liabilities measured at fair value by level of fair value hierarchy, is as follows:

	As at February 28, 2015		As at August 31, 2014	
	Level 1	Level 2	Level 1	Level 2
Financial assets				
Short-term investments	$2,582	$–	$5,726	$–
Forward exchange contracts	$–	$13	$–	$193
Financial Liabilities				
Forward exchange contracts	$–	$4,545	$–	$690

Derivative Financial Instruments

The functional currency of the company is the Canadian dollar. The company is exposed to currency risk as a result of its export sales of products manufactured in Canada, China and Finland, the majority of which are denominated in US dollars and euros. This risk is partially hedged by forward exchange contracts and certain cost of sales and operating expenses (US dollars and euros). In addition, the company is exposed to currency risk as a result of its research and development activities in India (Indian rupees). This risk is partially hedged by forward exchange contracts. Forward exchange contracts, which are designated as cash flow hedging instruments, qualify for hedge accounting.

As at February 28, 2015, the company held contracts to sell US dollars for Canadian dollars and Indian rupees at various forward rates, which are summarized as follows:

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EXFO Inc.
Notes to Condensed Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

US dollars – Canadian dollars

Expiry dates	Contractual amounts	Weighted average contractual forward rates
March 2015 to August 2015	$ 15,600	1.1027
September 2015 to August 2016	20,200	1.1180
September 2016 to August 2017	8,000	1.1530
September 2017 to December 2017	1,600	1.2135
Total	$ 45,400	1.1223

US dollars – Indian rupees

Expiry dates	Contractual amounts	Weighted average contractual forward rates
March 2015 to August 2015	$ 2,400	64.00
September 2015 to February 2016	1,200	65.32
Total	$ 3,600	64.44

The carrying amount of forward exchange contracts is equal to fair value, which is based on the amount at which they could be settled based on estimated current market rates. The fair value of forward exchange contracts amounted to net losses of $497,000 as at August 31, 2014, and $4,532,000 as at February 28, 2015.

As at February 28, 2015, forward exchange contracts in the amount of $13,000 are presented as current assets in other accounts receivable, forward exchange contracts in the amount of $3,392,000 are presented as current liabilities in accounts payable and accrued liabilities, and forward exchange contracts of $1,153,000 are presented as long-term liabilities in other long-term liabilities in the balance sheet. Forward exchange contracts of $618,000, included in accounts payable and accrued liabilities, for which related hedged sales are recognized, are recorded in the statement of earnings; otherwise, other forward exchange contracts are not yet recorded in the statement of earnings.

Based on the portfolio of forward exchange contracts as at February 28, 2015, the company estimates that the portion of the net unrealized losses on these contracts as of that date, which will be realized and reclassified from accumulated other comprehensive income to net earnings over the next 12 months, amounts to $2,761,000.

During the three and six months ended February 28, 2014 and 2015, the company recognized within its sales the following foreign exchange losses on forward exchange contracts:

	Three months ended	Six months ended February 28,	Three months ended	Six months ended February 28,

	February 28, 2015	2015	February 28, 2014	2014
Losses on forward exchange contracts	$600	$892	$285	$369

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EXFO Inc.
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(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

4 Share Capital

On January 7, 2015, the company announced that its Board of Directors had authorized a substantial issuer bid (the "Offer") to purchase for cancellation up to 7,142,857 subordinate voting shares for an aggregate purchase price not to exceed CA$30,000,000. On February 20, 2015, pursuant to the Offer, the company purchased for cancellation 6,521,739 subordinate voting shares for an aggregate purchase price of CA$30,000,000 (US$24,027,000), plus related fees of $223,000. The company used cash to fund the purchase of shares.

The following tables summarize changes in share capital for the six months ended February 28, 2014 and 2015.

	Six months ended February 28, 2014				
	Multiple voting shares		Subordinate voting shares		
	Number	Amount	Number	Amount	Total Amount
Balance as at September 1, 2013	31,643,000	$1	28,401,790	$109,836	$109,837
Exercise of stock options	–	–	25,800	106	106
Redemption of restricted share units	–	–	315,583	–	–
Redemption of deferred share units	–	–	38,010	–	–
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	1,435	1,435
Balance as at November 30, 2013	31,643,000	1	28,781,183	111,377	111,378
Exercise of stock options	–	–	20,500	89	89
Redemption of restricted share units	–	–	95,882	–	–
Redemption of share capital	–	–	(214,470)	(831)	(831)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	701	701
Balance as at February 28, 2014	31,643,000	$1	28,683,095	$111,336	$111,337

	Six months ended February 28, 2015				
	Multiple voting shares		Subordinate voting shares		
	Number	Amount	Number	Amount	Total Amount
Balance as at September 1, 2014	31,643,000	$1	28,703,750	$111,490	$111,491
Redemption of restricted share units	–	–	115,669	–	–
Redemption of share capital	–	–	(236,486)	(919)	(919)
	–	–	–	443	443

Reclassification of stock-based compensation costs to share capital upon exercise of stock awards					
Balance as at November 30, 2014	31,643,000	1	28,582,933	111,014	111,015
Redemption of restricted share units	–	–	107,099	–	–
Redemption of deferred share units	–	–	48,697	–	–
Redemption of share capital	–	–	(6,521,739)	(25,395)	(25,395)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	907	907
Balance as at February 28, 2015	31,643,000	$1	22,216,990	$86,526	$86,527

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EXFO Inc.
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(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

5 Statements of Earnings

Net research and development expenses comprise the following:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Gross research and development expenses	$12,176	$25,485	$13,046	$26,355
Research and development tax credits and grants	(1,670)	(3,321)	(2,073)	(4,101)
Net research and development expenses for the period	$10,506	$22,164	$10,973	$22,254

Inventory write-down is as follows:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Inventory write-down for the period	$1,046	$1,979	$1,251	$2,438

Depreciation and amortization expenses by functional area are as follows:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Cost of sales				
Depreciation of property, plant and equipment	$374	$769	$380	$764
Amortization of intangible assets	441	1,112	497	1,062
	815	1,881	877	1,826
Selling and administrative expenses				
Depreciation of property, plant and equipment	135	277	234	481

Amortization of intangible assets	338	702	380	775
	473	979	614	1,256
Net research and development expenses				
Depreciation of property, plant and equipment	747	1,455	629	1,273
Amortization of intangible assets	240	303	197	419
	987	1,758	826	1,692
	$2,275	$4,618	$2,317	$4,774
Depreciation of property, plant and equipment	$1,256	$2,501	$1,243	$2,518
Amortization of intangible assets	1,019	2,117	1,074	2,256
	$2,275	$4,618	$2,317	$4,774

EXFO Inc.
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(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Employee compensation comprises the following:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Salaries and benefits	$29,097	$59,307	$30,700	$60,720
Stock-based compensation costs	388	788	402	865
Total employee compensation for the period	$29,485	$60,095	$31,102	$61,585

Stock-based compensation costs by functional area are as follows:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Cost of sales	$38	$83	$45	$100
Selling and administrative expenses	260	523	259	592
Net research and development expenses	90	182	98	173
Total stock-based compensation for the period	$388	$788	$402	$865

6 Income Taxes

For the three months and the six months ended February 28, 2014 and 2015, the reconciliation of the income tax provision calculated using the combined Canadian federal and provincial statutory income tax rate with the income tax provision in the financial statements is as follows:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014

Income tax provision (recovery) at combined Canadian federal and provincial statutory tax rate (27%)	$410	$1,124	$(372)	$(318)
Increase (decrease) due to:				
Foreign income taxed at different rates	582	577	(209)	(295)
Non-taxable (income)/loss	243	1,074	(471)	(893)
Non-deductible expenses	172	374	181	407
Foreign exchange effect of translation of foreign subsidiaries in the functional currency	(2,126)	(3,119)	(34)	212
Utilization of previously unrecognized deferred income tax assets	(80)	(80)	12	(3)
Unrecognized deferred income tax assets on temporary deductible differences and unused tax losses	1,379	1,983	974	1,961
Other	6	(182)	(122)	(164)
Income tax provision for the period	$586	$1,751	$(41)	$907

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EXFO Inc.
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The income tax provision (recovery) consists of the following:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Current	$597	$2,094	$283	$606
Deferred	(11)	(343)	(324)	301
	$586	$1,751	$(41)	$907

7 Earnings per Share

The following table summarizes the reconciliation of the basic weighted average number of shares outstanding and the diluted weighted average number of shares outstanding:

	Three months ended February 28, 2015	Six months ended February 28, 2015	Three months ended February 28, 2014	Six months ended February 28, 2014
Basic weighted average number of shares outstanding (000's)	59,216	59,775	60,414	60,316
Plus dilutive effect of (000's):				
Restricted share units	492	510	491	645
Deferred share units	105	111	90	102
Stock options			2	17
Diluted weighted average number of shares outstanding (000's)	59,813	60,396	60,997	61,080
Stock awards excluded from the calculation of diluted weighted average number of shares because their exercise price was greater than the average market price of the common shares (000's)	67	88	259	129

For the three and six months ended February 28, 2014, the diluted amount per share was the same amount as the basic amount per share since the dilutive effect of stock options, restricted share units and deferred share units was not included in the calculation; otherwise, the effect would have been antidilutive. Accordingly, the diluted amount per share for these periods was calculated using the basic weighted average number of shares outstanding.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

This discussion and analysis contains forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Forward-looking statements are statements other than historical information or statements of current condition. Words such as may, expect, believe, plan, anticipate, intend, could, estimate, continue, or similar expressions or the negative of such expressions are intended to identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events and circumstances are considered forward-looking statements. They are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those in forward-looking statements due to various factors including, but not limited to, macroeconomic uncertainty as well as capital spending and network deployment levels in the telecommunications industry (including our ability to quickly adapt cost structures with anticipated levels of business and our ability to manage inventory levels with market demand); future economic, competitive, financial and market conditions; consolidation in the global telecommunications test and service assurance industry and increased competition among vendors; capacity to adapt our future product offering to future technological changes; limited visibility with regards to timing and nature of customer orders; longer sales cycles for complex systems involving customers' acceptance delaying revenue recognition; fluctuating exchange rates; concentration of sales; timely release and market acceptance of our new products and other upcoming products; our ability to successfully expand international operations; our ability to successfully integrate businesses that we acquire; and the retention of key technical and management personnel. Assumptions relating to the foregoing involve judgments and risks, all of which are difficult or impossible to predict and many of which are beyond our control. Other risk factors that may affect our future performance and operations are detailed in our Annual Report, on Form 20-F, and our other filings with the U.S. Securities and Exchange Commission and the Canadian securities commissions. We believe that the expectations reflected in the forward-looking statements are reasonable based on information currently available to us, but we cannot assure that the expectations will prove to have been correct. Accordingly, you should not place undue reliance on these forward-looking statements. These statements speak only as of the date of this document. Unless required by law or applicable regulations, we undertake no obligation to revise or update any of them to reflect events or circumstances that occur after the date of this document. This discussion and analysis should be read in conjunction with the consolidated financial statements.

The following discussion and analysis of financial condition and results of operations is dated March 24, 2015.

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

COMPANY OVERVIEW AND RECENT DEVELOPMENTS

We are a leading provider of next-generation test, service assurance and end-to-end quality of experience solutions for mobile and fixed network operators and equipment manufacturers in the global telecommunications industry. Our intelligent solutions with contextually relevant analytics improve end-user quality of experience, enhance network performance and drive operational efficiencies throughout the network and service delivery lifecycle. We target high-growth market opportunities related to increasing bandwidth and improving quality of experience on network infrastructures: 4G/LTE (long-term evolution), wireless backhaul, small cells and distributed antenna systems (DAS), 100G network upgrades and fiber-to-the-home (FTTH)/fiber-to-the-curb (FTTC)/fiber-to-the-node (FTTN) deployments.

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We launched four new solutions in the second quarter of fiscal 2015, including EXFO Xtract, an open analytics platform that provides mobile operators with end-to-end network and service visibility to accelerate and prioritize network optimization, and a quality of experience benchmarking platform that works in tandem with EXFO Mobile Agent, a software application converting smartphones into real-time probes. These solutions leverage technologies from the recent BysteSphere and Aito Technologies acquisitions. We also introduced common public radio interface (CPRI) software testing options for the FTB-700G and FTB-780 NetBlazer series to simplify fiber-to-the-antenna (FTTA) and distributed antenna system (DAS) deployments; and released iCERT, an added functionality on EXFO's OTDR (optical time domain reflectometry) software, which automatically certifies cable installations in data centers and enterprises. Altogether, we introduced seven new solutions or major enhancements in the first half of fiscal 2015.

We reported sales of $51.0 million in the second quarter of fiscal 2015, stable compared to $51.2 million for the same period last year, despite a significant headwind from a stronger US dollar versus other currencies compared to the same period last year. Bookings decreased 6.9% to $54.7 million in the second quarter of fiscal 2015, for a book-to-bill ratio of 1.07, compared to $58.7 million for the same period last year.

Net earnings amounted to $931,000, or $0.02 per diluted share, in the second quarter of fiscal 2015, compared to a net loss of $1.3 million, or $0.02 per share, for the same period last year. Net earnings for the second quarter of fiscal 2015 included $1.0 million in after-tax amortization of intangible assets, $388,000 in stock-based compensation costs and a foreign exchange gain of $3.0 million.

Adjusted EBITDA (net earnings (loss) before interest, income taxes, depreciation and amortization, stock-based compensation costs and foreign exchange gain) reached $1.2 million, or 2.3% of sales in the second quarter of fiscal 2015, compared to minus $1.0 million, or 2.0% of sales for the same period last year. See page 33 in this document for a complete reconciliation of adjusted EBITDA to IFRS net earnings (loss).

On January 7, 2015, we announced that our Board of Directors had authorized a substantial issuer bid (the "Offer") to purchase for cancellation up to 7,142,857 subordinate voting shares for an aggregate purchase price not to exceed CA$30 million. On February 20, 2015, pursuant to the Offer, we purchased for cancellation 6,521,739 subordinate voting shares for an aggregate purchase price of CA$30 million (US$24.0 million), plus related fees of $223,000. We used cash to fund the purchase of shares.

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RESULTS OF OPERATIONS
(in thousands of US dollars, except per share data, and as a percentage of sales for the periods indicated)

	Three months ended February 28,		Six months ended February 28,	
	2015	2014	2015	2014
Sales	$50,990	$51,179	$107,714	$107,182
Cost of sales (1)	19,546	20,073	40,783	41,258
Selling and administrative	20,168	21,537	41,200	43,245
Net research and development	10,506	10,973	22,164	22,254
Depreciation of property, plant and equipment	1,256	1,243	2,501	2,518
Amortization of intangible assets	1,019	1,074	2,117	2,256
Interest income	(35)	(49)	(252)	(76)
Foreign exchange gain	(2,987)	(2,292)	(4,962)	(3,094)
Earnings (loss) before income taxes	1,517	(1,380)	4,163	(1,179)
Income taxes	586	(41)	1,751	907
Net earnings (loss) for the period	$931	$(1,339)	$2,412	$(2,086)
Basic and diluted net earnings (loss) per share	$0.02	$(0.02)	$0.04	$(0.03)
Other selected information:				
Gross margin before depreciation and amortization (2)	$31,444	$31,106	$66,931	$65,924
Research and development:				
Gross research and development	$12,176	$13,046	$25,485	$26,355
Net research and development	$10,506	$10,973	$22,164	$22,254
Adjusted EBITDA (2)	$1,158	$(1,002)	$4,355	$1,290

(1) The cost of sales is exclusive of depreciation and amortization, shown separately.
(2) Refer to page 33 for non-IFRS measures.

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	Three months ended February 28, 2015		Three months ended February 28, 2014		Six months ended February 28, 2015		Six months ended February 28, 2014	
Sales	100.0	%	100.0	%	100.0	%	100.0	%
Cost of sales (1)	38.3		39.2		37.9		38.5	
Selling and administrative	39.6		42.1		38.2		40.3	
Net research and development	20.6		21.4		20.6		20.8	
Depreciation of property, plant and equipment	2.5		2.4		2.3		2.3	
Amortization of intangible assets	2.0		2.1		2.0		2.1	
Interest income	(0.1	)	(0.1	)	(0.2	)	(0.1	)
Foreign exchange gain	(5.9	)	(4.4	)	(4.6	)	(2.8	)
Earnings (loss) before income taxes	3.0		(2.7	)	3.8		(1.1	)
Income taxes	1.2		(0.1	)	1.6		0.8	
Net earnings (loss) for the period	1.8	%	(2.6	)%	2.2	%	(1.9	)%
Other selected information:								
Gross margin before depreciation and amortization (2)	61.7	%	60.8	%	62.1	%	61.5	%
Research and development:								
Gross research and development	23.9	%	25.5	%	23.7	%	24.6	%
Net research and development	20.6	%	21.4	%	20.6	%	20.8	%
Adjusted EBITDA (2)	2.3	%	(2.0	)%	4.0	%	1.2	%

(1) The cost of sales is exclusive of depreciation and amortization, shown separately.
(2) Refer to page 33 for non-IFRS measures.

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SALES AND BOOKINGS

For the three months ended February 28, 2015, our sales amounted to $51.0 million, stable compared to $51.2 million for the same period last year, and our bookings decreased 6.9% to $54.7 million, from $58.7 million for the same period last year, for a book-to-bill ratio of 1.07.

For the six months ended February 28, 2015, our sales reached $107.7 million, stable compared to $107.2 million for the same period last year. For the first half of fiscal 2015, bookings amounted to $108.9 million, compared to $116.6 million for the same period last year, for a book-to-bill ratio of 1.01.

In the second quarter and the first half of fiscal 2015, we faced a significant headwind from a stronger US dollar versus other currencies compared to the same periods last year, which reduced our sales year-over-year for the second quarter and the first half respectively. Otherwise, we would have reported sales growth year-over-year.

In the second quarter and the first half of fiscal 2015, we reported year-over-year sales growth in the Americas, mainly for our Physical-layer product line, which was offset by the decrease in sales in Europe, Middle-East and Africa (EMEA) and to a lesser extent in Asia-Pacific for both our Physical- and Protocol-layer product lines. It should be noted that in the second quarter and the first half of fiscal 2014, market conditions in the Americas were challenging due to order delays and lower spending levels, especially among key customers, which mainly impacted our Physical-layer product line sales in these periods. Europe remained overall a challenging market affected by a weaker currency and macroeconomic uncertainties.

Moreover, in the second quarter and the first quarter of fiscal 2015, we faced increased competition and pricing pressure compared to the same periods last year, which negatively affected our sales year-over-year.

Booking-wise, in the second quarter and the first half of fiscal 2015, we witnessed the same factors as for our sales, but the booking decrease was more pronounced in both periods, compared to the same periods last year. More precisely, the decrease in bookings in EMEA, especially for our Protocol-layer product line, more than offset the year-over-year increase in bookings in the Americas, which resulted in year-over-year decrease in bookings.

As we gradually evolve from a supplier of dedicated test instruments to a supplier of end-to-end solutions, our quarterly sales and bookings are increasingly subject to quarterly fluctuations, as we are managing more complex, multimillion dollar deals that have prolonged sales and revenue recognition cycles related to our Protocol-layer products; this also explains the year-over-year decrease in sales and bookings in the second quarter and the first half of fiscal 2015 for our Protocol-layer product line.

Geographic distribution

In the second quarter of fiscal 2015, sales to the Americas, EMEA and Asia-Pacific accounted for 53%, 25% and 22% of sales respectively, compared to 45%, 32% and 23% for the same period last year respectively. In the first half of fiscal 2015, sales to the Americas, EMEA and Asia-Pacific accounted for 51%, 28% and 21% of sales respectively, compared to 48%, 31% and 21% for the same period last year respectively.

Customer concentration

We sell our products to a broad range of customers, including network service providers, network equipment manufacturers, wireless operators and cable TV operators. In the second quarters of fiscal 2014 and 2015, no customer accounted for more than 10% of our sales, and our top three customers accounted for 13.1% and 15.2% of sales respectively. In the first halves of fiscal 2014 and 2015, no customer accounted for more than 10% of our sales, and our top three customers accounted for 11.3% and 12.2% of our sales respectively.

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GROSS MARGIN BEFORE DEPRECIATION AND AMORTIZATION (non-IFRS measure — refer to page 33 of this document)

Gross margin before depreciation and amortization (gross margin) reached 61.7% of sales for the three months ended February 28, 2015, compared to 60.8% for the same period last year.

Gross margin reached 62.1% of sales for the six months ended February 28, 2015, compared to 61.5% for the same period last year.

In the second quarter and the first half of fiscal 2015, our gross margin was favorably affected by the product mix, compared to the same periods last year.

In addition, in the second quarter and the first half of fiscal 2015, we reported lower inventory write-down compared to the same periods last year, which increased our gross margin by 0.4% for both periods year-over-year.

However, in the second quarter and the first half of fiscal 2015, foreign exchange losses on our forward exchange contracts reduced our sales and negatively impacted our gross margin by 0.2% for both periods compared to the same periods last year.

Also, in the second quarter and the first half of fiscal 2015, we faced increased competition and pricing pressure for some product lines, compared to the same period last year, which negatively impacted our gross margin year-over-year.

SELLING AND ADMINISTRATIVE EXPENSES

For the three months ended February 28, 2015, selling and administrative expenses were $20.2 million, or 39.6% of sales, compared to $21.5 million, or 42.1% of sales for the same period last year.

For the six months ended February 28, 2015, selling and administrative expenses were $41.2 million, or 38.2% of sales, compared to $43.2 million, or 40.3% of sales for the same period last year.

In the second quarter and the first half of fiscal 2015, our selling and administrative expenses decreased due to tight control on expenses and to the increase in the average value of the US dollar compared to the Canadian dollar and the euro year-over-year, as a portion of our selling and administrative expenses are incurred in these latter two currencies and we report our results in US dollars.

In the second quarter and the first half of fiscal 2015, our selling and administrative expenses decreased as a percentage of sales compared to the same periods last year, as these expenses decreased year-over-year, while our sales were stable.

RESEARCH AND DEVELOPMENT EXPENSES

Gross research and development expenses

For the three months ended February 28, 2015, gross research and development expenses totaled $12.2 million, or 23.9% of sales, compared to $13.0 million, or 25.5% of sales for the same period last year.

For the six months ended February 28, 2015, gross research and development expenses totaled $25.5 million, or 23.7% of sales, compared to $26.4 million, or 24.6% of sales for the same period last year.

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In the second quarter and the first half of fiscal 2015, the year-over-year increase in the average value of the US dollar compared to the Canadian dollar and the euro had a positive impact on our gross research and development expenses as most of these expenses are incurred in these latter two currencies and we report our results in US dollars.

Excluding the positive impact of the year-over-year increase of the average value of the US dollar compared to the Canadian dollar in the second quarter and the first half of fiscal 2015, inflation, salary increases, as well as a shift in the mix and timing of research and development projects slightly increased our gross research and development expenses compared to the same periods last year.

In the second quarter and the first half of fiscal 2015, our gross research and development expenses decreased as a percentage of sales compared to the same periods last year, as these expenses decreased year-over-year, while our sales were stable.

Tax credits and grants

We are entitled to tax credits from the Canadian federal and provincial governments for eligible research and development activities conducted in Canada. We are also eligible to grants by a Finnish technology organization on certain research and development projects conducted in Finland.

For the three months ended February 28, 2015, tax credits and grants for research and development activities were $1.7 million, or 13.7% of gross research and development expenses, compared to $2.1 million, or 15.9% of gross research and development expenses for the same period last year.

For the six months ended February 28, 2015, tax credits and grants for research and development activities were $3.3 million, or 13.0% of gross research and development expenses, compared to $4.1 million, or 15.6% of gross research and development expenses for the same period last year.

The decrease in our tax credits and grants in the second quarter and the first half of fiscal 2015, compared to the same periods last year, results from the decrease in the statutory Canadian federal and provincial research and development tax credit rates, as well as from the increase in the average value of the US dollar, compared to the Canadian dollar year-over-year, as our tax credits are denominated in Canadian dollars and we report our results in US dollars.

In the second quarter and the first half of fiscal 2015, the decrease in tax credits and grants as a percentage of gross research and development expenses, compared to the same periods last year, mainly comes from the decrease in the statutory Canadian federal and provincial research and development tax credit rates.

FOREIGN EXCHANGE GAIN

Foreign exchange gains and losses are mainly the result of the translation of operating activities denominated in currencies other than our functional currency, which is the Canadian dollar. A portion of our foreign exchange gains or losses result from the translation of cash balances and deferred income taxes denominated in US dollars. We manage our exposure to currency risk in part with forward exchange contracts. In addition, some of our entities' operating activities are denominated in US dollars, euros and British pounds, which further hedges this risk. However, we remain exposed to a currency risk; namely, any increase in the value of the Canadian dollar, compared to the US dollar, would have a negative impact on our operating results.

For the three months ended February 28, 2015, we recorded a foreign exchange gain of $3.0 million compared to $2.3 million for the same period last year.

For the six months ended February 28, 2015, we recorded a foreign exchange gain of $5.0 million compared to $3.1 million for the same period last year.

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During the second quarter of fiscal 2015, the period-end value of the Canadian dollar significantly decreased versus the US dollar compared to the previous quarter, which resulted in a foreign exchange gain of $3.0 million during that period. The period-end value of the Canadian dollar decreased 8.5% versus the US dollar to CA$1.2503= US$1.00 in the second quarter of fiscal 2015, compared to CA$1.1440 = US$1.00 at the end of the previous quarter.

During the same period last year, the period-end value of the Canadian dollar decreased versus the US dollar and the euro, compared to the previous quarter, which resulted in a foreign exchange gain of $2.3 million during that period. The period-end value of the Canadian dollar decreased 4.1% versus the US dollar to CA$1.1075= US$1.00 in the second quarter of fiscal 2014, compared to CA$1.0620 = US$1.00 at the end of the previous quarter, and decreased 6.0% versus the euro to CA$1.5291 = €1.00 in the second quarter of fiscal 2014, compared to CA$1.4420 = €1.00 at the end of the previous quarter.

During the first half of fiscal 2015, the period-end value of the Canadian dollar significantly decreased versus the US dollar, compared to the previous year end, which resulted in a foreign exchange gain of $5.0 million during that period. The period-end value of the Canadian dollar decreased 13.2% versus the US dollar to CA$1.2503 = US$1.00 in the first half of fiscal 2015, compared to CA$1.0858 = US$1.00 at the end of the previous year.

During the same period last year, the period-end value of the Canadian dollar significantly decreased versus the US dollar and the euro, compared to the previous year end, which resulted in a foreign exchange gain of $3.1 million during that period. The period-end value of the Canadian dollar decreased 4.9% versus the US dollar to CA$1.1075 = US$1.00 in the first half of fiscal 2014, compared to CA$1.0530 = US$1.00 at the end of the previous year, and decreased 9.7% versus the euro to CA$1.5291 = €1.00 in the first half of fiscal 2014, compared to CA$1.3936 = €1.00 at the end of the previous year.

Foreign-exchange-rate fluctuations also flow through the statement of earnings line items as a portion of our sales and a significant portion of our operating expenses are denominated in Canadian dollars and euros, and we report our results in US dollars. In fact, the average value of the US dollar in the second quarter of fiscal 2015 increased 9.7% and 13.7% respectively year-over-year, compared to the Canadian dollar and the euro. During the first half of fiscal 2015, it increased 8.3% and 9.8% respectively year-over-year, compared to the Canadian dollar and the euro.

INCOME TAXES

For the three months ended February 28, 2015, we reported income tax expenses of $586,000 on earnings before income taxes of $1.5 million. For the corresponding period last year, we reported income tax recovery of $41,000 on a loss before income taxes of $1.4 million.

For the six months ended February 28, 2015, we reported income tax expenses of $1.8 million on earnings before income taxes of $4.2 million. For the corresponding period last year, we reported income tax expenses of $907,000 on a loss before income taxes of $1.2 million.

These situations mainly resulted from the fact that we did not recognize deferred income tax assets for some of our subsidiaries at loss and had some non-deductible losses and expenses, such as stock-based compensation costs. However, a significant portion of our foreign exchange gain was created by the translation of financial statements of our foreign subsidiaries from their local currency to the functional currency, and was therefore non-taxable. Otherwise, our effective tax rate would have been closer to the combined Canadian and provincial statutory tax rate of 27% for both periods.

Please refer to note 6 to our condensed unaudited interim consolidated financial statements for a full reconciliation of our income tax provision.

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LIQUIDITY AND CAPITAL RESOURCES

Cash requirements and capital resources

As at February 28, 2015, cash and short-term investments totaled $32.9 million, while our working capital was at $71.0 million. Our cash and short-term investments decreased $24.7 million in the second quarter of fiscal 2015, compared to the previous quarter. First, in the second quarter of fiscal 2015, we paid a cash payment of $24.3 million for the redemption of share capital under our substantial issuer bid program (including related fees). In addition, during the quarter, we made cash payments of $2.0 million for the purchase of capital assets. Finally, we recorded an unrealized foreign exchange loss on our cash and short-term investments of $4.1 million. This unrealized foreign exchange loss resulted from the translation, in US dollars, of our Canadian-dollar-denominated cash and short-term investments and was included in the accumulated other comprehensive income in the balance sheet. However, operating activities generated $5.7 million in cash.

Our short-term investments consist of debt instruments issued by high-credit quality corporations; therefore, we consider the risk of non-performance of these financial instruments to be limited. These debt instruments are not expected to be affected by a significant liquidity risk. For the purpose of managing our cash position, we have established a cash management policy, which we follow and monitor on a regular basis. Our cash and short-term investments will be used for working capital and other general corporate purposes, as well as potential acquisitions. As at February 28, 2015, cash balances included an amount of $16.0 million that bears interest at an annual rate of 1.3%.

We believe that our cash balances and short-term investments in the amount of $32.9 million will be sufficient to meet our liquidity and capital requirements for the foreseeable future. In addition to these assets, we have unused available lines of credit totaling $13.6 million for working capital and other general corporate purposes, and unused lines of credit of $15.5 million for foreign currency exposure related to forward exchange contracts. However, possible operating losses, restructuring costs and/or possible investments in or acquisitions of complementary businesses, products or technologies may require additional financing. There can be no assurance that additional debt or equity financing will be available when required or, if available, that it can be secured on satisfactory terms.

Sources and uses of cash

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

Operating activities

Cash flows provided by operating activities were $5.7 million for the three months ended February 28, 2015, compared to $3.6 million for the same period last year.

Cash flows provided by operating activities were $7.6 million for the six months ended February 28, 2015, compared to $7.0 million for the same period last year.

Cash flows provided by operating activities in the second quarter of fiscal 2015 were attributable to the net earnings after items not affecting cash of $3.3 million, and the positive net change in non-cash operating items of $2.4 million; this was mainly due to the positive effect on cash of the decrease of $3.7 million in our accounts receivable due to the sequential decrease in sales as well as the timing of receipts and sales during the quarter, and the positive effect on cash of the increase of $824,000 in our accounts payable and accrued liabilities due to timing of purchases and payments during the period. These positive effects on cash were offset in part by the negative effect on cash of the increase of $1.2 million in our income tax and tax credits recoverable due to tax credits earned during the quarter not yet recovered, and the negative effect on cash of the increase of $752,000 in our inventories to meet future demand.

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Cash flows provided by operating activities in the second quarter of fiscal 2014 were attributable to the net earnings after items not affecting cash of $1.3 million, and the positive net change in non-cash operating items of $2.3 million; this was mainly due to the positive effect on cash of the decrease of $6.2 million in our accounts receivable due to the timing of receipts and sales during the quarter. This positive effect on cash was offset in part by the negative effect on cash of the increase of $1.7 million in our income tax and tax credits recoverable due to tax credits earned during the quarter not yet recovered, the negative effect on cash of the increase of $1.2 million in our inventories to meet future demand, as well as the negative effect on cash of the increase of $787,000 in our prepaid expenses due to timing of payments during the quarter.

Cash flows provided by operating activities in the first half of fiscal 2015 were attributable to the net earnings after items not affecting cash of $5.2 million, and the positive net change in non-cash operating items of $2.4 million; this was mainly due to the positive effect on cash of the increase of $7.7 million in our accounts payable and accrued liabilities due to timing of purchases and payments during the period. This positive effect on cash was offset in part by the negative effect on cash of the increase of $1.3 million in our accounts receivable due to the timing of receipts and sales during the period, the negative effect on cash of the increase of $1.4 million in our income tax and tax credits recoverable due to tax credits earned during the period not yet recovered, the negative effect on cash of the increase of $1.9 million in our inventories to meet future demand, and the negative effect on cash of the increase of $501,000 in our prepaid expenses due to timing of payments during the period.

Cash flows provided by operating activities in the first half of fiscal 2014 were attributable to the net earnings after items not affecting cash of $2.2 million, and the positive net change in non-cash operating items of $4.8 million; this was mainly due to the positive effect on cash of the decrease of $4.5 million in our accounts receivable due to the timing of receipts and sales during the period and the positive effect on cash of the increase of $5.4 million in our accounts payable and accrued liabilities due to timing of purchases and payments during the period. These positive effects on cash were offset in part by the negative effect on cash of the increase of $943,000 in our income tax and tax credits recoverable due to tax credits earned during the period not yet recovered, the negative effect on cash of the increase of $3.5 million in our inventories to meet future demand as well as the negative effect on cash of the increase of $616,000 in our prepaid expenses due to timing of payments during the period.

Investing activities

Cash flows provided by investing activities were $437,000 for the three months ended February 28, 2015, compared to cash flows used of $1.7 million for the same period last year.

Cash flows used by investing activities were $242,000 for the six months ended February 28, 2015, compared to $2.4 million for the same period last year.

In the second quarter of fiscal 2015, we disposed (net of acquisitions) of $2.5 million worth of short-term investments, but we paid $2.0 million for the purchase of capital assets.

For the corresponding last year, we paid $1.7 million for the purchase of capital assets.

In the first half of fiscal 2015, we paid $2.8 million for the purchase of capital assets, but we disposed (net of acquisitions) of $2.6 million worth of short-term investments.

For the corresponding period last year, we paid $2.4 million for the purchase of capital assets.

Financing activities

Cash flows used by financing activities were $24.3 million for the three months ended February 28, 2015, compared to $1.2 million for the same period last year.

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Cash flows used by financing activities were $25.1 million for the six months ended February 28, 2015, compared to $1.0 million for the same period last year.

In the second quarter of fiscal 2015, we redeemed share capital under our substantial issuer bid for a cash consideration of $24.3 million.

For the corresponding period last year, we redeemed share capital for a cash consideration of $937,000 and we made a repayment of $307,000 of our long-term debt. However, we received $89,000 from the exercise of stock options.

In the first half of fiscal 2015, we redeemed share capital under our share repurchase programs (namely our substantial issuer bid) for a cash consideration of $25.1 million.

For the corresponding period last year, we redeemed share capital for a cash consideration of $937,000 and we made a repayment of $307,000 of our long-term debt. However, we received $195,000 from the exercise of stock options.

FORWARD EXCHANGE CONTRACTS

We are exposed to a currency risk as a result of our export sales of products manufactured in Canada, China and Finland, the majority of which are denominated in US dollars and euros. In addition, we are exposed to a currency risk as a result of our research and development activities in India (Indian rupees). These risks are partially hedged by forward exchange contracts. Forward exchange contracts, which are designated as cash flow hedging instruments, qualify for hedge accounting.

As at February 28, 2015, we held forward exchange contracts to sell US dollars for Canadian dollars and Indian rupees at various forward rates, which are summarized as follows:

US dollars – Canadian dollars

Expiry dates	Contractual amounts	Weighted average contractual forward rates
March 2015 to August 2015	$15,600,000	1.1027
September 2015 to August 2016	20,200,000	1.1180
September 2016 to August 2017	8,000,000	1.1530
September 2017 to December 2017	1,600,000	1.2135
Total	$45,400,000	1.1223

US dollars – Indian rupees

Expiry dates	Contractual amounts	Weighted average contractual forward rates
March 2015 to August 2015	$2,400,000	64.00
September 2015 to February 2016	1,200,000	65.32
Total	$3,600,000	64.44

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The carrying amount of forward exchange contracts is equal to fair value, which is based on the amount at which they could be settled based on estimated current market rates. The fair value of forward exchange contracts amounted to net losses of $497,000 as at August 31, 2014 and $4.5 million as at February 28, 2015, mainly for our US/Canadian dollars forward exchange contracts. The quarter-end exchange rate was CA$1.2503 = US$1.00 as at February 28, 2015.

SHARE CAPITAL

Share capital

As at March 24, 2015, EXFO had 31,643,000 multiple voting shares outstanding, entitling to 10 votes each and 22,221,590 subordinate voting shares outstanding. The multiple voting shares and the subordinate voting shares are unlimited as to number and without par value.

OFF-BALANCE SHEET ARRANGEMENTS

As at February 28, 2015, our off-balance sheet arrangements consisted of letters of guarantee amounting to $358,000 for our own selling and purchasing requirements, which were reserved from our lines of credit; these letters of guarantee expire at various dates through fiscal 2017.

STRUCTURED ENTITIES

As at February 28, 2015, we did not have interests in any structured entities.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

For a description of the critical accounting policies, judgments in applying accounting policies as well as estimates and assumptions used in the preparation of our consolidated financial statements, refer to our Annual Report on Form 20-F for the year ended August 31, 2014, filed with the U.S. Securities and Exchange Commission and the Canadian securities commissions.

NEW IFRS PRONOUNCEMENTS AND AMENDMENTS

Refer to note 2 to our condensed unaudited interim consolidated financial statements for the three and six months ended February 28, 2015 and to our consolidated financial statements for the year ended August 31, 2014 for the effect of certain recent accounting pronouncements on our consolidated financial statements.

RISKS AND UNCERTAINTIES

For the first half of fiscal 2015, there have been no material changes from the risk factors disclosed in our Annual Report on Form 20-F for the year ended August 31, 2014.

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NON-IFRS MEASURES

We provide non-IFRS measures (gross margin before depreciation and amortization* and adjusted EBITDA**) as supplemental information regarding our operational performance. We use these measures for the purpose of evaluating our historical and prospective financial performance, as well as our performance relative to our competitors. These measures also help us to plan and forecast future periods as well as to make operational and strategic decisions. We believe that providing this information to our investors, in addition to the IFRS measures, allows them to see the company's results through the eyes of management, and to better understand our historical and future financial performance.

The presentation of this additional information is not prepared in accordance with IFRS. Therefore, the information may not necessarily be comparable to that of other companies and should be considered as a supplement to, not a substitute for, the corresponding measures calculated in accordance with IFRS.

* Gross margin before depreciation and amortization represents sales less cost of sales, excluding depreciation and amortization.

** Adjusted EBITDA represents net earnings (loss) before interest, income taxes, depreciation and amortization, stock-based compensation costs and foreign exchange gain.

The following table summarizes the reconciliation of adjusted EBITDA to IFRS net earnings (loss), in thousands of US dollars:

Adjusted EBITDA (unaudited)

	Three months ended February 28,		Six months ended February 28,	
	2015	2014	2015	2014
IFRS net earnings (loss) for the period	$931	$(1,339)	$2,412	$(2,086)
Add (deduct):				
Depreciation of property, plant and equipment	1,256	1,243	2,501	2,518
Amortization of intangible assets	1,019	1,074	2,117	2,256
Interest income	(35)	(49)	(252)	(76)
Income taxes	586	(41)	1,751	907
Stock-based compensation costs	388	402	788	865
Foreign exchange gain	(2,987)	(2,292)	(4,962)	(3,094)
Adjusted EBITDA for the period	$1,158	$(1,002)	$4,355	$1,290
Adjusted EBITDA in percentage of sales	2.3%	(2.0)%	4.0%	1.2%

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QUARTERLY SUMMARY FINANCIAL INFORMATION (unaudited)
(tabular amounts in thousands of US dollars, except per share data)

	Quarters ended			
	February 28, 2015	November 30, 2014	August 31, 2014	May 31, 2014
Sales	$50,990	$ 56,724	$59,742	$63,882
Cost of sales (1)	$19,546	$ 21,237	$22,109	$23,469
Net earnings	$931	$ 1,481	$1,204	$1,665
Basic and diluted net earnings per share	$0.02	$ 0.02	$0.02	$0.03

	Quarters ended			
	February 28, 2014	November 30, 2013	August 31, 2013	May 31, 2013
Sales	$51,179	$ 56,003	$60,888	$58,865
Cost of sales (1)	$20,073	$ 21,185	$22,574	$22,574
Net earnings (loss)	$(1,339)	$ (747)	$3,802	$(862)
Basic and diluted net earnings (loss) per share	$(0.02)	$ (0.01)	$0.06	$(0.01)

(1) The cost of sales is exclusive of depreciation and amortization.